Study no. 1

ANALYSIS OF ABSORPTION CAPACITY OF THE EU FUNDS IN ROMANIA

Authors:

Gheorghe OPRESCU (coordinator)[1]

Daniela Luminița CONSTANTIN[2]

Florinel ILIE[3]

Dragoş PÎSLARU[4]

Acknowledgements:

The authors would like to thank **Ms. Magda Voinea** for the support and feedback in documenting and elaborating sections of this research.

[1] Professor at the Polytechnical University of Bucharest, Director of the Department of Management, and the Romanian Centre for Economic Policy (CEROPE).

[2] Professor at the Academy of Economic Studies of Bucharest, President of the Romanian Regional Science Association.

[3] Business Manager, ING Group.

[4] University lecturer at the Academy of Economic Studies of Bucharest and member of the Group of Applied Economics (GEA).

SUMMARY

Acronyms

NDP	National Development Plan
EU	European Union
MA	Management Authorities
IB	Intermediate Body
PPP	Public Private Partnership
NUTS	Nomenclature des Unitees Territoriales Statistiques
ERDF	European Regional Development Fund
ESF	European Social Fund
CF	Cohesion Fund
EAGGF – Guidance	European Agricultural Guidance and Guarantee Fund - Guidance section
FIFG	Financial Instrument for Fisheries Guidance
CP	Cohesion policy
EIB	European Investment Bank
SOP	Sectoral Operational Program
ROP	Regional Operational Program
ECT	European Territorial Cooperation
AT	Austria
CZ	Czech Republic
EE	Estonia
HU	Hungary
PL	Poland
SI	Slovenia
SK	Slovakia
DE	Germany
EL	Greece
RO	Romania
BG	Bulgaria
IT	Italy
SME	Small and medium-sized enterprises
NGO	Non-governmental organizations

INTRODUCTION

At the present moment, in the relations with the European Union, the real stake for Romania is not accession. This will certainly take place, sooner, or a little later. The real stake is how well-prepared will Romania be at the time of accession to absorb the significant funds it will have access to. In other words, the real stake is building, in this interval, an adequate absorption capacity of community funds.

This paper attempts to assess, over one year before the likely date of accession, how prepared is Romania from this point of view. However, an *ex-ante* assessment is difficult attempt. Some aspects may actually only be analyzed ex-post. That is why the paper shall only attempt to assess the *administrative* absorption capacity during the planning/creation of systems adequate for the management, programming and implementation.

Chapter 1 introduces the reader into the topic, briefly describing the significance of the cohesion policy, its reform and the restructuring of community funds as of 2007, as well as Romania's eligibility for the cohesion policy. Chapter 2 clarifies the notion of absorption capacity and describes the used methodology. Chapter 3 states the results of the assessment, and Chapter 4 presents some considerations related to the financial absorption capacity. Chapter 5 refers to conclusion and recommendations.

The authors do not claim that this study makes a pharmaceutical assessment of the current absorption capacity. Nevertheless, we believe that we proposed a coherent approach, and succeeded to identify some important elements related to the administrative capacity and suggested viable measures for its development. As a first attempt of its kind in Romania, the paper wishes to be rather an invitation for discussion. That is why, it does not 'lecture' and does not contain undisputable 'statements', only points of view, and it offers recommendations not recipes.

The authors wish to thank all those who facilitated a better understanding of the specific problematics: state administration officials, Romanian and international consultants, officials of the European Commission and its Delegation to Bucharest, other people who take interest in this topic. We need to add that we sent questionnaires and received answers from all Management Authorities and most of the Intermediate Body, and we thank them for it.

Last but not least, we thank the European Institute of Romania for its support during the entire study period and for organizing a rountable with the stakeholders (Group of Interest). We would also like to thank Professor Gabriela Drăgan, for her constant support and kind assistance.

Gheorghe Oprescu

Study coordinator

CHAPTER 1. EU FUNDS AND COHESION POLICY. IMPORTANCE FOR ROMANIA

1.1. Importance of the cohesion policy for Romania

The cohesion policy is defined by its scope, namely to support the process of reducing the gaps between EU's mode developed regions and member states, and those less developed. The *primary legal basis* of the cohesion policy is the Treaty on European Union (Title XVII, Economic and Social Cohesion', and Article 148 on the European Social Fund). The objective to strengthen economic and social cohesion is explicitly mentioned under Article 2 of the Treaty of Amsterdam, as a high level objective of the European Union. More specifically, Article 158 states cohesion as a prerequisite for the harmonious development of the EU, underlining the will of ‚*reducing disparities between the levels of development of the various regions and the backwardness of the least favoured regions or islands, including rural areas*'.

The 25+2 member states and candidate countries of the European Union may be divided into three categories of development, using GDP per capita (in PPS) as an indicator[5]: the first group of 12 old Member States has a GDP/inhabitant largely above the EU25 average (10% and over); the second group, of 7 countries, has a GDP/inhabitant between 68% and 94% of the EU25 average; the third group includes 8 countries (6 new Member States, plus Bulgaria and Romania), with a GDP/inhabitant below 60% of community average.

January 1, 2007 is an important date for Romania: it will probably[6] become a member state of the European Union and it will be the beneficiary of substantial non-reimbursable financial transfers, offered by the European community to support its development. These amounts will be specially channelled through the cohesion policy. Thus, as of the first years of accession (2007-2009), the cohesion policy will bring Romania almost 6 billion Euro, which are funds that must be spent upon well-defined principles: *programming* (planning assistance for a number of 7 years); *partnership* (all programming and operational stages must be accomplished in close cooperation with the Commission and the Member States, and regional, local players and other relevant authorities should be involved); *subsidiarity* (community interventions observe the institutional structure of the member state); *additionality* (structural funds must not replace the national public expenditure); *concentrating* assistance in regions and fields that need most of the support, etc.

[5] GDP per capital is the key indicator to measure regional disparities. PPS = Purchasing Power Standards.

[6] The European Union may decide the postponemtn of Romania's accession if the safeguard clause is activated.

1.2. Reform of the cohesion policy; restructuring of the EU funds - implications for Romania

Less than one year before the date of its likely accession, Romania is in a critical moment: during the negotiations for *Chapter 21 – Regional Policy and Coordination of Structural Instruments*, Romania incurred its commitments based on the body of EU law in force at that moment, as proposed by the European Commission in July 2004. The new regulations purport significant changes in the cohesion policy to which Romanian authorities shall have to adapt quickly and in due time.

The current objectives (1, 2 and 3) and the four community initiatives (INTERREG III, Leader+, Equal and Urban II) will be reorganized after 2007 into **three objectives** only: *Convergence* (support of regions with less developed economy), *Regional competitively and employment* (support for regions, other than those less developed, for the achievement of the Lisbon Agenda) and *European Territorial Cooperation* (promotion of a balanced development of the entire community territory, by encouraging cooperation and exchange of best practices among all EU regions), set up in three axes: transborder, trans-national and inter-regional cooperation. Under the new architecture, **Romanian will be eligible under two objectives: Convergence and European Territorial Cooperation.**

Out of the current five structural instruments (the Cohesion fund and four structural funds: European Regional Development Fund – ERDF, European Social Fund – ESF, European Agricultural Guidance and Guarantee Fund – EAGGF, the Guidance section, and the Financial Instrument for Fisheries Guidance – FIFG, the cohesion policy after 2007 will be structured in **three funds** (ERDF, ESF and the Cohesion Fund). To simplify things, agricultural and fisheries funds were transferred to the related policies, namely the Common Agricultural Policy and Common Fisheries Policy. At the same time, the Cohesion Fund must observe the same rules as Structural Funds (e.g. multi-annual planning, project approval, etc). ***Romania will benefit from all three funds, ERDF, ESF and the Cohesion Fund).***

Another significant modification brought by the reform aims at **planning**: thus, currently, the planning process is organized under three levels: National Development Plan and the Community Support Framework (the first includes the priorities for development of the entire national economy, the second only priorities to be financed from structural instruments), Operational Programs (each develops one priority of the Community Support Framework) and Complementary Programs (detailed documents for the implementation of Operational Programs). The reform maintains the obligation of multi-annual planning (for a period of 7 years), but brings an outlined strategic visions and stresses the Lisbon Strategy priorities, requesting the preparation of **only two programming documents: a strategic one** – National Strategic Reference Framework (harmonizes both the national and community priorities included in the Community Strategic Guidelines for the cohesion policy) and **one operational** – Operational Programs. Thus, the necessity to draft the National Development Plan, the

Complementary Programs and operational character of the Community Support Framework disappears.

In the field of **management,** the main changes brought by the reform related to managing operational programs under the objective Convergence aim at creating an Audit Authority (independent body, bound to check the well-functioning of management and control systems) and a Certification Authority (to certify the statement of expenses and the request for payment before conveyance to the Commission), and the disappearance of the concept of Paying Authority. For operational programs under the objective European Territorial Cooperation, the main amendments consist in the necessity to create a Certification Authority, a Single Control Authority and a group of financial controllers (made up of one controller appointed by each participating member state, having the role of supporting the Authority of Control), and the disappearance of the concept of Paying Authority. ***While the new structures related to the objective of Convergence have been already taken over by the Romanian authorities, there are still significant delays in the design of the new structures related to the objective of European Territorial Cooperation.***

1.3. Romania's eligibility for the cohesion policy

Pursuant to the eligibility rules, Romania will benefit of the cohesion policy under objectives '*Convergence'* and '*European territorial cooperation'*.

There are two types of eligibility for the objective '*Convergence'*: regional eligibility (according to which, in Romania, all of the 8 regions are NUTS II eligible)[7] and national eligibility, for the Cohesion Fund.[8]

Also, for the objective'*European territorial cooperation',* there are three types of eligibility, for each of the three action axis.

For *transborder cooperation,*[9] Romania will be eligible with 19 NUTS III regions, under the following arrangement: eight only at the internal border, with Bulgaria and Hungary (relevant for the transborder cooperation under the new objective *European territorial cooperation;* three regions eligible for transborder cooperation, both internal and external; eight regions only at the external borders, with Serbia and Montenegro (which

[7] The regional eligibility criteria for "Convergence" is interpreted in this way: the regional GDP per capita (in PPS) for NUTS II, available for the three years before the adoption of the Regulation (2000, 2001, 2002) is below 75% of the EU25 average. There are other eligibility criteria as well for this objective but they are not relevant for Romania: ultraperipheral regions, regions statistically affected by enlargment.

[8] The eligibility for the Cohesion Fund is established in this way: Member States whose GDP per capita (PPS) available for the three years before the adoption of the Regulation (2000, 2001, 2002) is below 90% of the community average and which have a program for economic convergence.

[9] Those NUTS III Community regions are financially eligible for trans-border cooperation which are located along the internal ground border and certain external borders, as well as certain NUTS III located along the separated maritime border, and provided, generally, that they have maximum 150 km – adjustments are allowed for coherence and continuity of the cooperation action, *cf. Draft of General Regulation*, Art.7.

will be covered by the new Pre-accession Assistance Tool) and with Moldova and Ukraine (which will be covered by the new Vecinity and Partnership Tool). In addition, Romania will be able to include adjacent NUTS III regions, the entire NUTS II regions where the eligible region[10] is located, and third countries. [11]

Certain regions of Romanian will also be eligible for *transborder cooperation*, according to the final list of transnational regions included in the Community Strategic Guidelines. Based on the Commission's preliminary list, Romania shall be eligible with the entire territory for the Danube-Balkan transnational cooperation space. Moreover, Romania will be able to include in the transnational cooperation program other partners external to the Danube-Balkan space,[12] and third countries.[13]

Also, Romania's regions will be able to participate in the *inter-regional cooperation,* depending on the particular projects to be developed.

There are significant differences among these objectives and their components regarding the financial aspects, planning and operational; these differences will be further explained in this study.

[10] In a percentage of maximum 20% of the budget related to the operational program of transborder cooperation (such decision will be made during the negotiations on the transborder cooperation program).

[11] In a percentage of maximum 10% of ERDF contribution for the operational program of transborder cooperation, and provided that those projects benefit community regions.

[12] Only in justified cases, and limited to 20% of budget for the operational program of transborder cooperation.

[13] In a percentage of maximum 10% of ERDF contribution for the operational program of transborder cooperation, and provided that those projects benefit community regions.

CHAPTER 2. CAPACITY OF ABSORPTION. CONCEPT AND SYSTEM

2.1. Defining the absorption capacity

The absorption capacity stands for the degree in which a country is able to effectively and efficiently spend the financial resources from the Structural Funds. If we considered that, in order to do this, it is necessary, on the one hand, to have a absorption capacity from the institutional system created by the particular state in order to manage the funds at issue and, on the other hand, a absorption capacity from the beneficiaries whom these funds address – then, we could speak of two distinct characteristics, namely the *absorption capacity on the supply side* (of funds) and *absorption capacity on the demand side*. The latter is related to the capacities of potential beneficiaries to design projects and to finance them. However, it is difficult, if not impossible, to make an assessment of these features before the very achievement of the programs involved in the use of European funds. That is why **our paper shall only have in view issues related to the capacity of absorption on the supply side.**

The capacity of absorption on the supply side is determined by **three** main **factors,** namely:[14]

A. *Macro-economic absorption capacity*. This capacity may be defined and measured in relation to the Gross Domestic Product (GDP). Thus, the Council Regulation no. 1260/1999 provides that the annual amount that a Member State may benefit from Structural Funds – together with assistance through the Cohesion Fund – *must not exceed 4% of GDP*. The *necessity to increase budget expenses consequent to accession* is also linked to the macro-economic capacity. There is therefore a consensus regarding the necessity that, as of 2007, Romania should ensure budget expenses of at least 2% of GDP higher than at present; these expenses are strictly determined by the obligations incurred in the context of European integration: Romania's contribution to the EU budget (around 1% of GDP), namely the amounts of the national budget necessary for the priorities and measures that will be co-financed by community funds – (still around 0.8% - 1% of GDP). Finally, the *capacity to absorb macro-economic effects generated by the supplementary expenses that are going to be spent* relates also to the macro-economic absorption capacity. Thus, it is obvious that all of these expenses will entail an increase of the aggregate demand but will also have effects over the aggregate supply, especially on its labour market component (given that the increase in volume of economic activity, generated by the transfer of community funds, could entail insufficient qualified labour force resources in certain sectors and/or areas in the country). All of these issues are related to nominal convergence (price stability, interest rates and currency exchange – massive

[14] Andrej Horvat, *Absorption Problems in the EU Structural Funds*, Ljubljana, 2004.

entries of foreign capital may exert pressure over the latter, and likely have negative influence over competitivity) and to real convergence as well (convergence for the purposes of the cohesion policy, namely social and economic development and reduction of lags against community average. An *ex ante* assessment of the macro-economic impact of structural funds shall be made in the context of drafting the National Development Plan for 2007-2013. **The scope of our paper is not to analyse this aspect of the general absorption capacity.**

B. *Financial absorption capacity*. It stands for the capacity of central and local authorities to co-finance programs and projects assisted by the EU, to plan and guarantee these domestic contributions in multi-annual budgets and to collect them from the various partners involved in a project or program. **This paper makes an introduction to the analysis of the financial absorption capacities, related to local authorities.**

C. *Administrative absorption capacity.* It refers to the capacity of central and local authorities to prepare plans, projects and programs in due time, to select the best, to organize an efficient partnership framework, to observe administrative and reporting duties, and to finance and supervise the implementation process, by avoiding any irregularities. **The administrative absorption capacity is in fact the main topic of this paper.**

2.2. System of assessment of the administrative capacity

We further present the methodology created by the European Commission at the beginning of 2002, which was afterwards used for the assessment of the absorption capacity of the accession countries. To this purpose, the Commission ordered a series of studies which analyzed the absorption capacity both from the viewpoint of some Member States (Ireland, Spain, Portugal, Germany), and sectoral (management, programming, implementation, monitoring & assessment, and, respectively, financial management and control).[15]

Three stages must be taken into account when managing Structural Funds:

- **Programming (Design),** which can be defined as an input variable. The elements that define this stage designs the conditions for the effective and efficient management of structural funds. The planning capacity must be

[15] See NEI, *Key Indicators for Candidate Countries to Effectively Manage the Structural Funds*, *Principal Report*, Final Report prepared by the NEI Regional and Urban Development for the EC DG REGIO/DG ENLARGEMENT, Rotterdam, February 2002.

measured by reporting to the request arising from the regulations on structural funds (Regulations no. 1260/99 and 438/2001).

- **Functioning**, or the extent to which structural funds are effectively and efficiently managed. *This stage cannot be assessed in a candidate country*, such as Romania. However, some indications on the functioning of the future system may arise from the functioning of the pre-accession instruments (Phare, ISPA, SAPARD).

- **Performance,** or the extent to which structural funds were effectively and efficiently managed. This is a output variable that measures results. *Performance can only be determined ex post,* at the end of the programming period. Consequently, for Romania, this stage cannot either be assessed in Romania's case.

The above considerations indicate that all that can be assessed more than one year before the likely date of accession is the planning, the design system of the institutional system which will be dedicated for the implementation of priorities and financial measures from Structural Funds.

The measuring of the administrative capacity involved the assessment of **three elements** (i) structure, (ii) human resources, and (iii) systems and tools:

(i) **Structure** related to the clear assignment of responsibilities and tasks to institutions or better at the level of departments or units within these institutions. This assignment refers to a range of structural funds tasks, including *management, programming, implementation, evaluation & monitoring, and financial management & control.* **Given the stage Romania passes through from the point of view of these phases, the paper intends to assess only the first three of them.** Structure also relates to supervisory and ancillary bodies, such as monitoring committees, auditing tasks, partnership, etc.

(ii) **Human resources** relate to the ability to detail tasks and responsibilities at the level of job descriptions, to estimate the number and qualifications of staff, and to fulfil the recruitment needs. This is due to the fact that securing the timely availability of experienced, skilled and motivated staff is a key success factor in the management of the structural funds, which conditions success of structural funds management.

(iii) **Systems and tools** relate to the availability of instruments, manuals, systems, procedures, forms, etc. In other words, these are all job-aids that can enhance the effectiveness of the functioning of the system. They enable organisations to transform tacit and implicit knowledge (existing within the heads of individual people) into explicit knowledge that can be shared across organisations. The existence of systems and tools reduces the vulnerability of organisations (e.g. when staff is leaving), and enhance the effectiveness of their functioning.

Combining the life-cycle tasks and the elements that define the administrative capacity results in the following Management Capability Grid:

Table 2.1 Management Capability Grid (MCG)

	Design (Programming)			Functioning	Performance
	Structure	Human resources	Systems and tools		
Management					
Programming					
Implementation					
Monitoring and assessment					
Financial management and control					

Given the above consideration, the paper's approach relates only to the hachured area of the grid.

The above MCG creates a systematic basis and provides a the key elements that play a role in implementing the management of structural funds throughout the policy life.

Hence, 9 key indicators that will have to be measured.

a. Management

The system mentioned above identifies three key indicators, corresponding to the three columns (structure, human resources, systems and tools):

1) *Designation of Managing Authorities (8 points)*

   a) Consensus and designation on Community Support Framework Managing Authority (CSF MA) exists

   b) Location of CSFMA in line with administrative structure

   c) Consensus and designation on Sectoral Operational Programming (SOP) Managing Authorities (MA) exists

   d) Location of SOP MAs in line with administrative structure

e) Consensus and designation on Regional Operational Programming (ROP) Management exists

f) Location of ROP MAs in line with administrative structure

g) Consensus and designation on MA Cohesion Fund (CF)

h) Location of MA CF in line with administrative structure

2) Staffing of Management Authorities (7 points)

a) Estimates of staffing requirements available

b) Estimates take account of programme size, characteristics and tasks delegated

c) Responsibilities and tasks assigned to job descriptions

d) Remuneration levels for MA-staff were determined

e) Competitiveness of remuneration levels (in relation to private sector)

f) Proof of sufficient candidates for staffing of vacancies

g) Proven efforts for utilisation of experience and know-how from pre-accession stage (including structural funds training)

3) Arrangements on delegation of tasks (3 points)

a) Arrangement on delegating specific tasks (assessment, monitoring, information)

b) Arrangement on delegating implementing tasks existing in detailed terms (tasks according to Article 34 Regulation 1260/1999)

c) Consensus on delegating arrangements existing among stakeholders

b. Programming

All three indicators are also defined from the programming viewpoint.

1. Partnership already present in existing economic development policy (4 points)

a) Systematic and effective interministerial co-ordination of socio-economic policies

b) Social partners systematically involved in design of socio-economic policies

c) Regional partners systematically involved in design of socio-economic policies

d) NGOs systematically involved in design of socio-economic policies

2. *Capacity to carry out programming is available quantitatively and qualitatively (4 points)*

a) Analytic skills

b) Process skills

c) Expertise to create indicator systems

d) Experience in programming

3. *Guidelines for programme preparation exist and disseminated (2 points)*

a) National programming methodology/process description exists

b) Methods for creating partnership established

c. Implementation

1. *Assignment of intermediate bodies (IB) (7 points)*

(a) List of IB available

(b) IB are well-regarded within their domain of work

(c) Assignment of IB to individual measures already carried out

(d) Agreement from IB obtained

(e) Assignments in line with main responsibilities of IB

(f) Authority of MA over IB in line with national hierarchy

(g) Good working relations between MAs and IBs

2. *Staffing of intermediate bodies (6 points)*

(a) Staffing requirements for intermediate bodies clarified

(b) Staffing for intermediate bodies secured

(c) Proven efforts for utilisation of experience and know-how from pre-accession funds

(d) Experience in project generation and project preparation obtained

(e) Experience in project selection and assessment obtained

(f) Knowledge about EU legislation at operational level (rules on state aid, public procurement, environment, equal opportunities)

3. Existing operational project development and management process (5 points)

(a) A coherent set of project selection criteria exists

(b) Standardised ‚application forms' exist

(c) Cost/benefit manual for large projects exists and is known

(d) Frequent reference to national policies, existing schemes, instruments and concrete projects in Structural Funds-related planning documents (NDP, OPs)

(e) Manual for compliance with EU legislation exists

To conclude, the key indicators in the assessment of the management system of structural funds are:

Table 2.2 Managing structural funds - key indicators for assessment

	DESIGN FUNCTIONING		
	Structure	**Human Resources**	**Systems & Tools**
Management	Designation of MAs	Staffing of MAs	Arrangement on delegating tasks
Programming	Partnership already present	Capacity to carry out programming	Guidelines / manuals for programming exist
Implementation	Assignment of IB	Staffing of IB	Existing operational project development and management process

These indicators have been built on the following key messages:

1. Establish the appropriate structures quickly and precisely; these structures cannot be directly copied from Member states, but need to reflect the existing administrative structures and traditions.

2. Simple management structures (e.g. a small number of OPs) require less administrative capacity than complicated structures.

3. Human resources are vital: detail the staff requirements and provide the conditions for recruiting, retaining and training qualified staff, preferably for all administrative staff but at least for the key staff managing the Structural Funds.

4. Develop systems, procedures, manuals, guidelines and other tools in order to increase productivity, efficiency, consistency and quality of work, while reducing the vulnerability of organisations and their dependence on existing staff.

5. Utilise existing experiences that have been gained in the pre-accession stage, wherever applicable and useful. It is crucial that organisations develop a capacity to learn from their previous experiences.

6. Divide attention to all areas of the policy life cycle, notably on financial management & control and implementation, but also on programming and monitoring & evaluation.

2.3. System of assessment

On the basis of the structural funds management grid, the assessment of the administrative capacity of structural funds can be distinguished in a horizontal and a vertical assessment. Assessments result in assignment to one of four categories:

- category A: strong capacity: ready for Structural Funds (at least 90% of maximum score);
- category B: sufficient capacity, but weaknesses to be addressed (75-90% of maximum score);
- category C: not yet sufficient capacity, various and serious weaknesses to be addressed (50-75% of maximum score);
- category D: insufficient capacity, no basis for administering the Funds (below 50% of maximum score).

The results of assessment may be used in order to obtain information on:

- progress towards building the administrative capacities;
- balance among the various horizontal parts of Structural Funds management; attention should focus on the areas which are relatively weak;
- balance among the various vertical parts of Structural Funds management. In general, structures will first need to be in place prior to human resources and systems & tools.

Also, the system of key indicators may be used for several purposes, namely:

- a checklist, to be used as a tool and a guideline for the further accession preparations;
- tool used to outline the state-of-preparations in view of accession;
- monitor the progress of the preparation over time;
- recognise common patterns of imbalance (strengths and weaknesses) across countries;
- comparison with other countries.

CHAPTER 3. EVALUATION OF ADMINISTRATIVE CAPACITY OF ABSORPTION

The European Commission, through the Comprehensive Monitoring Report on Romania, issued on 25 October 2005, explains the state of the administrative capacity of our country in the field of regional policy and of Structural Instruments coordination (Chapter 21), formulating the following main idea: "*There are serious concerns in relation to the administrative capacity of the institutional structures, and in the area of financial management and control. Immediate action is required to strengthen administrative capacity across all concerned bodies at national, regional and local level...*".

Some of the main conclusions of the Report are as follows:

- measures are needed in order to strengthen the administrative capacity across all main ministries and the other relevant bodies;
- the number of employees and the pace of employment should be increased, in order to recover the backwardness;
- the cooperation between the central and local administration should be substantially strengthened;
- the co-financing mechanisms, especially at local level, should be established and clarified;
- for the programming activity, the partnership principle should be effectively implemented;
- the financial management and the control are still characterised by structural weaknesses and should be considerably strengthen in order to avoid the future irregularities.

In the next paragraphs, we will present the results of the evaluation made on the basis of the survey / questionnaires prepared in conformity with the methodology presented in the preceding chapter and the discussions with officials from the institutions involved, Romanian and foreign consultants, officials of the European Commissions and of the EC Delegation in Romania, as well with other experts in the subject. We will like to remind that the evaluation was made only for the management, programming and implementing and design stages.

Furthermore, we will compare the results obtained for Romania with the results of a study that – using the same methodology – evaluated, in the second semester of 2003, the administrative capacity of absorption for Hungary, Czech Republic, Slovakia, Estonia and Slovenia[16]. The results are comparable from the point of view of the period of time until accession, in the case of the above-mentioned countries it was less than a year and

[16] Andrej Horvat, *Absorption Problems in the EU Structural Funds*, Ljubljana, 2004.

for Romania is a little more than a year. In the final part of this chapter, we will comment the responses and we will present the evaluation substantiation for the three phases, meaning management, programming and implementation.

3.1 Overall evaluation

The next table presents the results of the evaluation conducted. The numbers between brackets represent the maximum score that could have been achieved for each of the indicators

Table no. 3.1. Results of the evaluation of the absorption administrative capacity in Romania

	Design			**Total**
	Structure *(max. 19)*	**Human resources** *(max. 17)*	**Systems and instruments** *(max. 10)*	
Management *(max. 18)*	7,6 (*8*)	3,8 (*7*)	1,5 (*3*)	12,9
Programming *(max. 10)*	2,0 (*4*)	2,0 (*4*)	1,2 (*2*)	5,2
Implementation *(max. 18)*	4,8 (*7*)	2,9 (*6*)	1,8 (*5*)	9,5
Total	14,4	8,7	4,5	

Source: authors evaluation

Even if they have certain relevance, the scores in absolute figures show a picture less relevant than those in relative figures:

Table no. 3.2. Evaluation of the absorption administrative capacity in Romania

	Design			**Total**
	Structure	**Human resources**	**Systems and instruments**	
Management	**A** *(95%)*	**C** *(54%)*	**C** *(50%)*	**C** *(72%)*
Programming	**C** *(50%)*	**C** *(50%)*	**C** *(60%)*	**C** *(52%)*
Implementation	**C** *(69%)*	**D** *(49%)*	**D** *(36%)*	**C** *(53%)*
Total	**B** *(76%)*	**C** *(51%)*	**D** *(45%)*	

NB: A: Strong capacity: system ready for the Structural Funds (at least 90%);

B: Sufficient capacity, but weak points should be addressed (75-90% from the maximum score);

C: Capacity not sufficient yet, serious weaknesses must be addressed (50-75%);

D: Insufficient capacity, there is no base for administrating the Structural Funds.

Source: authors evaluation.

The results obtained suggest that Romania is still at the beginning of building the absorption capacity. As one may see, for the 9 basic indicators, Romania got only an A, at the institutional structure of the managing authorities, where the points are given for the establishing of such authorities (for Community Support Framework, Sectoral Operational Programme and Regional Operational Programme). The slight downgrading of this indicator is due to a certain delay in assigning the MAs for the Cohesion Fund and for Public Administration. For the other 8 basic indicators, the absorption capacity is not yet sufficient (C for six of them) or there is not a base for managing the Structural Funds (D for two of them). Details regarding the evaluation method are given below.

The following table presents some comparisons with some of the ex-candidate countries, at comparable period of times, as mentioned above.

Table no. 3.3. Results of the evaluation of the main indicators by country

	RO	**HU**	**CZ**	**SK**	**EE**	**SLO**
Horizontal evaluation						
Management	**C** *(72%)*	**B** *(87%)*	**B** *(75%)*	**C** *(63%)*	**B** *(87%)*	**C** *(71%)*
Programming	**C** *(52%)*	**B** *(80%)*	**B** *(80%)*	**D** *(40%)*	**B** *(87%)*	**B** *(80%)*
Implementation	**C** (53%)	**C** *(72%)*	**C** (56%)	**C** *(52%)*	**C** *(68%)*	**C** *(52%)*
Vertical evaluation						
Structure	**B** *(76%)*	**B** *(84%)*	**B** *(79%)*	**B** *(79%)*	**A** *(95%)*	**B** *(74%)*
Human resources	**C** *(51%)*	**C** *(74%)*	**C** *(71%)*	**D** *(41%)*	**B** *(82%)*	**C** *(59%)*
Systems and instruments	**D** *(45%)*	**C** *(60%)*	**C** *(50%)*	**D** *(40%)*	**C** *(60%)*	**C** *(50%)*

Source: Authors evaluation for Romania and Horvat (2004)

Bearing in mind that the evaluations have been made by two different teams, the countries comparison shows that Romania is on one of the last places, although not the very last. Nevertheless, it should be mentioned that, in four cases (programming, implementation, structure and human resources), the score is the lowest possible; as the evaluation involves a certain degree of subjectivism, no one can guarantee that – without any significant differences of the analysis method – another evaluator would have come to the conclusion that the three of them are in fact in the inferior category. The same comment, but positive this time, can be made about the scores obtained for management stage, as it is close to the upper limit of the category. At the same time, one can observe that, in all countries, the implementation stage and the building of systems and instruments have the toughest situation.

Within the next paragraphs we will present details concerning the method of analysis and evaluation of the answers.

3.2 Management

The management is one of the essential components, which determine the administrative capacity of absorption of the community funds. The main role for accomplishing this task is played by the managing authorities, even if the Paying Authority (with its key role in the control and financial management stage) or the Intermediate Bodies (with key position in implementation stage) play a part too.

According with Council Regulation 1260/1999, Art. 34, the mandate of the Managing Authority covers the following:

1. establishing of a system capable to gather accurate statistics and financial information concerning the implementation process, in order to facilitate the monitoring and the evaluation procedures;
2. annual reporting (after the Monitoring Committee approval) to the Commission of the implementation status;
3. ensuring that the institutions involved in the management and implementation of financial assistance have a separate book-keeping and that they use an adequate accounting system for the transactions associated with the assistance;
4. guaranteeing the rightfulness of the operations financed by the assistance, especially through internal audit for a sound financial management;
5. ensuring the conformity with the community policies (in fields such as competition, environment, public acquisitions, equality of chances etc.);
6. providing compliance with the obligations of information, promotion, publicity etc.

The first step in preparing for managing the structural instruments is to agree upon the strategic objectives to be achieved and to identify the management solutions in order to attain these objectives. In the case of community funds, optimising the management is done under a series of conditionalities imposed by the European Union, through the Cohesion Policy. Therefore, the framework is set by the *acquis communautaire*, which itself is a mobile target, as it is shown in Chapter 1. The *acquis* provides guidelines for establishing the structure, the personnel scheme and systems, the processes and the instruments for managing the structural funds, and is the very first step for ensuring an efficient absorption.

Using the questionnaires and the methodology described above, a series of clear and useful images could be extracted regarding the absorption capacity from the point of view of managing structural instruments.

Table no. 3.4. Score obtained for administrative absorption capacity for the management – design stage

Components	Score	Maximum score	Percent
● Structure	**7,6**	**8**	**95% (Categ. A)**
● Human resources	**3,8**	**7**	**54% (Categ. C)**
● Systems and instruments	**1,5**	**3**	**50% (Categ. C)**
Total	**12,9**	**18**	**72% (Categ. C)**

Source: Authors evaluation

3.2.1. Institutional structure – management authorities

The institutional framework has been design since 2004, through Government Decision 497. This legal act designates the core management structures involved in structural funds management.

Within the Ministry of Public Finance (MPF) has been created the Managing Authority for Community Support Framework (MACSF), which has the task of supervising Romania's overall preparation for using the structural funds. MACSF has two directorates and two departments, related to its functions as coordinator of the process of community funds management.

At the same time, a Single Action Plan was drawn up so as to improve the management systems for the funds the European Union provides for Romania. The action plan comprises the schedule of preparatory efforts so that, beginning with 1 January 2007, Romania will be able to benefit from support through structural instruments.

The others Managing Authorities have taken over their responsibilities, starting at the same time the preparation of NDP 2007-2013 and the elaboration of Operational Programmes (SOPs + ROP). The process of creating such management structures has not been easy, being a pioneering action, as there was hardly any similar institutional experience.

On one hand, the initial decision of setting up the SOP/ROP structure for Romania was rather formal, as part of the negotiations regarding Chapter 21, without enough time to evaluate the most appropriate institutional framework. On the other hand, making operational the structures related to structural funds management faced a whole series of logistics issues, determining both an endogenous effort within the Government and a mobilisation of exogenous factors, materialised in twinning programmes and in technical assistance programmes. The need to finish the accession preparations in a record time led however to a prioritisation of actions related to setting up the framework for managing structural funds.

In two cases, the set-up / functioning of the management structures was blurred. On one hand, there was a large debate regarding the MA for the Cohesion Fund. On the other hand, a MA for Public Administration was requested. These two uncertain aspects of the management structure did affect only marginally the preparations for structural and cohesion funds management.

Taking into account these explanations, the score for this element was **7.6 points out of a maximum of 8 points (meaning 95%)**.

3.2.2 Human resources – quantity, quality, experience

The quality and the availability of human resources are key factors in building a really efficient management system. The professionalism of the personnel involved in the management of structural funds influences in a determinant way the absorption capacity of community funds.

The preparation for managing the structural funds is rendered difficult by the lack of previous experience in training competent human resources. The only similar experience is the one related to the management of pre-accession funds (PHARE, ISPA, SAPARD). Nevertheless, the differences of concept and structure are noteworthy.

Romania assumed a series of commitments regarding the recruitment of personnel for structural funds management. Following the negotiations for Chapter 21, within the Single Action Plan, some benchmarks for each MA and Intermediate Body' organisational chart have been agreed upon. These charts are very generous, including a several hundred persons to be employed by the end of 2006.

Taking into consideration that the policy of the Ministry of Public Finances was to cap wages in order to limit salary burden on budget and inflation, in 2005 the initial schedule to employ new public servants could not be respected. The percentage of employment, compared to the target set for the end of 2006, varies from a managing authority to another, with a dispersion between a minimum level of 28.3% (MA for Competitiveness SOP) and 67% (MA for Human Resources Development SOP). Calculating the ratio between the number of people employed and the number of people to be employed, one may notice a degree of employment of approximately 53% at the level of October 2005.

Obviously, the organisational charts were planned on the basis of general perception of the activity to be deployed and on the other member states' experience. Such estimation has its limits, given the risk of creating artificial jobs, not based on actual personnel needs. Important adjustments will be unavoidable as more details will be available regarding the programmes dimensions, the characteristics and task to be fulfilled by civil servants involved in the management of MA and of IB. Nevertheless, the questionnaires showed that for the current level of preparedness for managing structural funds, most of the MAs would need additional staff, but below the level of initial commitments.

The MA's perception regarding the *availability of human resources* for employment is a positive one, considering that there are plenty of candidates for the available vacancies. However, there are concerns related to the level of training of the potential candidates, many of the MAs being aware of the need to train on-the-job the new civil servants with no previous experience. All the bodies involved in the structural funds management have set up plans for staff training, and have already organized training sessions, especially under the form of short-term programmes (3-5 days).

The *training* sessions targeted both new and experienced employees, being customised for different levels of preparation. According to MAs estimate, on average, their personnel already benefited from 1 to 4 months of training per institution. This high level is the result of the existence of several technical assistance (TA or Twinning) programmes with a strong training component. The training' content was directly related to community funds management.

For the civil servants already employed, but also for the vacancies, *job descriptions* exist, but defined in a general manner, without clear and specific activity details. The degree of detailing the job description varies among the involved institutions. On one hand, some MAs claimed they could not detail now the job description, but only after the finalisation of the SOP/ROP, when they will know better all the operational aspects. Some MAs even specify their intention to use external technical assistance provided through PHARE 2004 for clarifying job descriptions. On the other hand, other MAs consider that they already have an adequate level of detailing for job descriptions, according to the SOP/ROP management requirements.

As regards the *previous experience* in managing the community funds (pre-accession funds), the MA ROP, the MA SOP Competitiveness and the MA for Community Support Framework currently have the lead with more than 50% of the personnel having over two years of experience. By accumulating previous experience in implementing the PHARE Economic and Social Cohesion programmes at regional level, the MA ROP has reached a level of 75% of personnel with experience in managing community funds. At the other extreme, several MAs have only 20-25% of the personnel with such previous experience. Noteworthy, even if the MAs have a satisfactory level of personnel with experience, at the IBs level, especially in the case of newly created structures, such as the regional offices for environment or for SMEs, the level of experience in managing structural funds is under 5%.

The *level of incentives* for the personnel is considered to be acceptable and the most important variable to quantify this level is the quantum of salaries. The salary is considered to be almost satisfactory, especially after its recent increase of 75% through Law 490/2005, which provides this important raise for all personnel involved in managing structural funds. In relative terms, the salary is less attractive if compared with the equivalent in private sector, but clearly more competitive compared with the average salary in the rest of the public administration.

An important issue is that wages are hardly differentiated according to the responsibilities detailed in the job descriptions, being calculated by using the rather uniform grid applied to all public servants.

The main reasons for which the jobs of public servants responsible with the structural funds management are sought and occupied are their safety and stability, the training opportunities, professional development in a field with future perspective, but also the higher salary compared with other areas of public administration.

The *personnel dynamics* was clearly positive, in net terms, for the last year, as only few civil servants gave up their jobs. On the other hand, as the SOPs/ROP will be effectively implemented, it is possible to witness a strong temptation for civil servants involved in managing the structural funds to shift toward private sector, which will probably offer higher wages for experienced people that can help them to attract European funds.

This risk is more important as *there is no tracking-career system for public servants* employed in MA/IB, for providing additional incentives for key-persons in the structural funds management, as to avoid losing human resources in which significant training investments were made, as their leaving may generate major hindrances in the efficient management of funds.

Bearing in mind all these comments, the score obtained for this element was **3.8 points out of the maximum 7 points (meaning 54%)**.

3.2.3 Systems and instruments – the need to be created

The MA for the Community Support Framework has the role of national coordinator for the process of managing the grants, including the activities of evaluation, monitoring and information of national programmes.

As regards the *evaluation activity*, a Central Evaluation Unity was created to coordinate the evaluation activities (ex-ante, mid-term and ex-post) of projects financed through structural funds. Moreover, the central evaluation unity coordinates the elaboration of the "National strategy for evaluation".

At the current level of readiness for managing the structural funds, the efforts were concentrated on the ex-ante evaluation, made at three levels: the analysis of macro-economic impact of the structural funds, the ex-ante evaluation of the NDP and, respectively, the ex-ante evaluation of each OP.

The three levels of ex-ante evaluation will benefit or have already benefited from technical assistance through the PHARE programme. The ex-ante evaluation of the NDP was finished in the autumn of 2005, the analysis of the macro-economic impact is foreseen to be finalised until the end of 2005, while the ex-ante evaluation of the SOP/ROP will be finished at the beginning of 2006.

Concerning the *monitoring* activity, in conformity with the commitments assumed within the Chapter 21, a functional integrated system will be created for collecting and processing information, statistical and financial data regarding the programme implementation, monitoring and evaluation of the European Union's assistance for Romania through structural instruments. Furthermore, a Monitoring Committee will become fully functional.

For this purpose, a study was made to analyse the development of communications infrastructure for the Single Management Information System (SMIS), the SMIS architecture, as well as the training needs of the personnel, which will use this system. As a result, an analysis report was prepared altogether with scenarios and case studies, as well as a testing framework report and training sessions for the main user. At the same time, a SMIS pilot application was launched for ISPA, and in the next period it will be extended to PHARE. The final target is to create an IT system for supporting the management of structural funds, a system able to address the needs at all levels of management (managing authorities, intermediate bodies, implementation agencies, paying authorities, final beneficiaries etc.) and the needs identified at all stages of programming cycle (programming, tenders, contracting, implementing, audit and control, monitoring and evaluation). Furthermore, the Single Management Information System has to comprise all information regarding the budgetary expenses at central, regional and local level, as well as all expenses linked to measures and priorities from the National Development Plan.

For the *information* activity, information campaigns are on-going at local level or at Romania development regions level, in order to encourage the partnership and to promote the fields targeted by the Structural and Cohesion Funds. At the same time, the workshops organised throughout the country aim at informing the relevant partners at local level, public and private, about the structural funds management, about co-financing aspects, and about the role and responsibilities of the local public administration in implementing these funds.

Likewise, for ensuring the information and publicity concerning the National Development Plan and Structural and Cohesion Funds, the MA for CSF prepared a series of promotional and information materials (CDs with information and relevant materials for the process of programming and the management of Structural Funds) send to all County Councils and Prefectures, in order to establish within their headquarters an “info point regarding the National Development Plan and the Structural and Cohesion Funds”. The objective was to ensure a better territorial coverage for information dissemination.

Besides the general information actions of the MA for the Community Support Framework, each of the other MAs started information and consultation sessions for drawing-up and improving the SOP/ROP.

As concerns, the *delegation of responsibilities*, in conformity with the GD 497/2004 regarding the institutional framework responsible with coordination, management and implementing the structural instruments, the MAs coordination and control tasks and arrangements will be delegated to the IBs.

The Management Authorities are still responsible for accurate fulfilment of the delegated tasks and for the effectiveness and efficiency of operations financed through structural instruments. The Intermediate Bodies will have as main task to manage the priorities and measures set up in the Operational Programmes. The responsibilities delegated from Management Authorities to Intermediate Bodies will take into account the regional character of the programme implementation, the actual capacity and experience of the IBs, as well as the co-financing capacity of the IB.

The evaluation, monitoring and information processes will be described by the MA within the SOP/ROP Implementation Manuals. These Manuals will be design with the help of existing and future technical assistance and will include all details related to the SOP/ROP management.

Bearing in mind the above-mentioned comments, the score for this element was of **1.5 points out of a maximum of 3 points (meaning 50%)**.

3.3. Programming

The evaluation of components defining the administrative capacity of absorption in programming field focused on certain design-related elements, at the level of management authorities (MA) as well as of intermediate bodies (IB).

The evaluation methodology applied to the *design* stage concentrated on: *structure* - quality of existing partnerships, *human resources* – programme elaboration capacity, quality and quantity-wise*, systems and instruments* - existence of programming guides/manuals.

The following table shows the results obtained from applying the evaluation grid and provides a comparison between actual and highest possible scores.

Table no. 3.5. Scores obtained for absorption management capacity in programming – design stage

Components	Actual score	Maximum score	Percentage
● Structure	**2**	**4**	**50% (Category C)**
● Human resources	**2**	**4**	**50% (Category C)**
● Systems and instruments	**1,2**	**2**	**60% (Category C)**
Total	**5,2**	**10**	**52%**

Source: Authors' evaluation.

The 52% in the maximum score column indicates that conditions have been created for sufficient absorption capacity in the design stage. Some weak points remain however, which left unresolved could severely affect the success of the entire programming activity. One of the conclusions drawn after the general evaluation, also valid in this particular case, namely that structure and human resources-related elements obtained minimum scores, make it possible in other words for a different evaluator to rank them in the lower category while strictly observing the same evaluation methodology.

Consequently, the following analysis by components will take into account achievements as well as sensitive areas requiring greater attention and finding short, medium and long-term viable solutions.

3.3.1. Institutional structure – existing partnerships

A major aspect of management capacity is the need to have the entire programming activity out-in-the-open, both at the level of the coordinating institution and within an expanded partnership framework.

In the first case we are referring to *cooperation relationships between the programming department and the other departments in the institution*, as in our opinion these relationships are essential for efficient programming, in line with the existing means of implementation and monitoring. Consequently, the setting up of workgroups with the participation of representatives from the other departments in the institution and the organisation of meetings on a regular basis are the two prerequisites of successful programming.

In this sense, the answers to the queries in the questionnaire indicate the fact that in all MAs and IBs the planning/programming department cooperates with the other departments in the institution that carry out relevant activities in terms of planning/programming. As a rule, the programming department communicates with the other departments in formally or informally established workgroups. Workgroup size ranges from very small (2-4 persons), to relatively large (26 persons). In most cases, in-house workgroup meetings do not follow a regular time pattern. Meetings are held only occasionally in order to solve particular issues that come up during planning and programming processes.

In addition to cooperation relationships between the various institutional departments, another prerequisite of efficient programming is *the use of an extended partnership framework*, otherwise a mandatory requirement for programming Structural and Cohesion Funds.

At present, only 50% of MAs currently use extended partnership structures, while the remaining institutions are in an advanced stage of setting up structures of this type.

Existing partnership structures include both representatives of public administration institutions and various economic and social partners, most participants being officially designated by the institutions and bodies they represent. Partnership structures are made up of 20 persons on average and usually meet on a monthly basis or depending on the need to discuss various elements in the planning and programming documents (analysis, priorities, measures, activities, eligibility and selection criteria, identification of projects, etc.) and to make recommendations on the themes approached. In addition to these "effective" partnerships, in some cases management authorities also organise wide scale consultative processes attended by a large number of economic and social partners (100 – 300 persons).

In terms of quality, when setting up partnership structures, most MAs select their partners from relevant institutions and organisations in the areas of activity covered by the operational plan or programme.

Insofar as the contribution of partners to the design of operational programmes is concerned, although all MAs consider their partners' activity useful, several issues occasionally arise owing to lack of experience and insufficient knowledge in programming Structural and Cohesion Funds, which impairs the process of communication between MAs and their partners.

Besides participation in workgroups set up to design the operational programme under coordination, all MAs must take part in the workgroups that design other operational programmes, as well as the workgroups for the holistic planning of national development (for example: the Inter-Institutional Committee for the NDP elaboration), thus achieving a coherent programming, free of any overlap or divergence. IBs are also involved in these partnership structures.

All MAs take part in the workgroups set up to coordinate the overall planning of national development, yet only 50% of MAs participate in the workgroups organised to draw up other operational programmes.

Taking into account both the positive and negative aspects resulting from the analysis of answers received from MAs and IBs, the existence and quality of partnerships set up for planning and programming **scored only 2 of the maximum points (in other words just 50%**), which reveals the progress made in this direction and the need to continue to expand the partnership framework and increase its efficiency.

3.3.2. Human resources – programme-design capacity

If in the area of national and regional development planning in line with EU requirements Romania has made significant progress in the period 1999-2005, the programming activity is quite another matter as no multi-annual programming documents on structural and cohesion funds have been drawn up so far.

Furthermore, most MAs have limited experience in coordinating the development of planning and programming documents similar to those devised in the EU. The main planning and programming documents devised so far are the National Development Plan, National Plan for Agriculture and Rural Development, ISPA Strategy and the Phare Programming Document for Economic and Social Cohesion. As for the evaluation of planning and programming documents, although most have undergone an *ex-ante* evaluation only one has also been subjected to a *mid-term* evaluation.

Nonetheless, development strategies have been devised for the all the areas to be covered by structural and cohesion funds programming. In our opinion, the existence of such documents is also extremely important for development planning and programming activities. They ensure on the one hand, that development plans and programmes and the set of development policies at sectoral and regional level make up a coherent whole, and on the other hand that programme priorities and measures fall in line with the proposed strategic directions.

Another key element of good planning and programming activities is the existence of specialised planning/programming departments within MAs and IBs. Our survey indicates that all MAs and IBs include departments specialised in planning/programming, which are responsible for designing the operational programme and coordinating the consultative process and implementing community support respectively. The size of these planning/programming departments differs among MAs, ranging from relatively large (12-18 persons) which is the case of 3 MAs, to relatively small (3 persons) in other 3 MAs.

Judging from the opinions expressed by the MAs that replied to the queries in the questionnaire, the size of existing personnel is insufficient to design the operational programme. All answers stressed the need to increase the number of staff involved in planning and programming activities by another 1-8 people, in other words between 10%-100%. IBs find themselves in a similar situation.

In terms of professional knowledge and training, in all MAs the personnel involved in planning/programming activities is highly trained in the specific area of activity and has an in-depth knowledge of national and EU legislation on planning/programming, state support, public acquisitions, etc. EU requirements in programming as well as in other relevant areas (for instance: equal opportunities for men and women, protection of the environment, promotion of the information technology society) are also well known. The above-mentioned statement is not however applicable to IBs as some of these admit that some personnel working in programming is poorly, insufficiently trained.

On the whole, less than 40% of personnel employed in planning/programming departments have experience in programming, social-economic studies, devising strategies and quantifying development objectives. In MAs, the percentage of experienced personnel ranges between 20% and 40%. There is only a single MA (with just 3 persons in the planning/programming department) in which all the people involved in planning/programming have relevant experience. In the case of IBs, as rule 1–2 people have experience in carrying out surveys, devising strategies and quantifying development objectives and in two cases none of the people working in the departments have relevant experience.

In addition to professional training and experience of personnel, a decisive factor of management capacity in planning and programming is the promotion of a continuing education and training policy at MA and IB level. The process is all the more important since as we have seen, a large number of personnel (about 60%) lack relevant experience in planning and programming activities. In this sense, it is noteworthy that all MAs and IBs are keen on providing professional training for existing personnel in the form of courses, seminars, study visits, etc. organised by the respective units or by other institutions involved in the planning/programming process. Although all MAs and IBs promote professional training, the length of training periods for employees varies significantly from one institution to the next (from one week to one month per year). All MAs and IBs have already planned future training activities *for existing and recently* *employed personnel* to confirm the continuing education and training policy currently promoted.

In the context created by the novelty of operational programming for the use of structural and cohesion funds as well as by the lack of experience in the area *the impact of technical assistance received could be decisive*. We are referring to technical assistance received prior to the development of the operational programme as well as to that currently provided, namely when the operational programme is actually designed.

Most MAs (70%) benefited from technical assistance projects prior to the actual design stage of the operational programme, which indicates that personnel involved in planning and programming activities grew familiar with EU experience and requirements in programming as well as in other relevant areas, which resulted in an higher level of personnel qualifications. A similar effect was noticeable in the case of most IBs benefiting from technical assistance provided by Romanian and foreign experts.

Besides technical assistance projects carried out prior to the design of the operational programme, the greater part of MAs (70%) are granted technical assistance in developing operational programmes. Most management authorities consider it to be high quality assistance, a relevant conclusion, as it has direct impact on the actual operational programme design.

Finally, it is essential to *provide adequate working conditions*, the absence of which could negatively affect both the development of the activity proper and the satisfaction personnel should derive from their work. In this regard, the *majority* of planning/programming departments have been equipped with *appropriate logistics* for running planning and programming activities. A single MA and two IBs claimed insufficient and outdated equipment.

It is important to keep in mind that the absence of adequate work conditions can lead to greater employee mobility and implicitly to a lower management capacity at institutional level. This is why ensuring adequate workspace, appropriately furnished and equipped with computers, printers, copying machines, etc. and related consumables are major factors that may influence the efficiency of planning or programming.

To these we must add the *wage level of personnel,* which can also result in increased employee mobility thereby reducing administrative capacity. Consequently, in our opinion all institutions involved in planning-programming structural and cohesion funds must ensure a suitable work environment and a satisfactory pay level.

The wage level is usually close to the national average, (about 900 RON). Although the average wage of personnel in planning-programming departments is similar to that of other departments in management authorities, the application of Law no. 490/2004 on financial incentives for personnel who manage community funds, granted a 75% pay increase to the base salary, thus leading to higher wages for employees in MAs and most IBs (planning-programming departments included) compared to both other institutional departments which do not manage community funds, other public administration institutions in Romania.

Taking into account work conditions and pay level, the mobility of employees involved in planning/programming (especially in MAs) remains low, whether towards other departments in the institution responsible for designing operational programmes or towards other local public administration institutions. However, since the wage-based income (especially in the case of young employees) is far below the average pay offered by many private companies, a, increased employee mobility towards the aforementioned companies is quite possible.

Moreover, despite the low employee mobility over the past year – as is the case of MA personnel involved in planning/programming activities (about 2% overall, while in four MAs no employee has left or requested a transfer), as the private sector continues to grow and wages along with it, we consider that the mobility of employees involved in public administration (including planning and programming activities) is likely to increase.

On the whole, the score for the evaluation of the "human resources" component was **2 points out of the maximum 4 (meaning 50%)**, indicating sufficient capacity to develop programmes while requiring a careful approach to weak points and problem-solving.

3.3.3. Systems and instruments – programming guides and manuals

For a fully functional administrative capacity it is essential that the entire planning/programming activity as well as associated activities be well organised by applying a certain methodology to develop operational plans/programmes, by designing work procedures, establishing personnel training plans, etc.

The evaluation of the existing state of programming systems and instruments was based on the answers to questions related to the methodology of designing operational programmes, internal work procedures, and partnerships – cooperation with other departments in the institution covered by the survey.

A noteworthy undertaking for example, is that the Analysis and Programming Department (APD) - in the Ministry of Public Finance, as MA for the Community Support Framework, has developed a *general methodology for Operational Programmes design* which includes a design-calendar. The methodology has been sent to all ministries that play the role of MA for Operational Programmes (OP). The methodology observes the rules and work documents of the European Commission for the 2000-2006 programming period, and takes into account proposals for new regulations corresponding to the period 2007-2013. In turn, MAs disseminated relevant methodologies to IBs according to their area of OP responsibility.

As for the *use of work procedures,* only a single MA has developed a number of work procedures, the rest are only just beginning to establish them. If we corroborate this situation with the fragile structure of some of the planning/programming department in MAs (as already mentioned earlier on, there are cases where the planning/programming department is made up of only 3 employees, of which only one with experience), it is safe to say that the absence of work procedures and detailed methodologies for the design of operational could pose a *major threat* to the actual development of some operational programmes should an experienced employee decide to leave.

Therefore, *it is essential to establish and apply work procedures as soon as possible in order to have efficient planning and programming activities*. Moreover, once in place, work procedures could also partially eliminate the effects of a potential increase in employee mobility and result in more knowledgeable and professional employees

The second requirement – internal partnership framework, cooperation with the other institutional departments has been met to a large extent. All respondents were able to indicate internal collaborators; some even mentioned that workgroup structure changes according to the nature of the issue under discussion, while the number of workgroup members varies as well. In the case of one MA, cooperation with other departments did not take the usual form of meetings but of written consultations (requests for proposals, suggestions, etc.)

Some MAs and IBs hold meetings regularly basis while others meet on a case-by-case basis, when necessary or for follow-up purposes. The meetings cover a broad range of aspects: points of view on new EU structural funds regulations, technical assistance priorities and measures, possible financing schemes, difficulties encountered in applying some of them, analyses, strategies, priorities, measures, financial programming, project portfolios, etc.

According to our study, the preparatory stage for programming systems and instruments was evaluated at **1.2 points out of the maximum 2 (meaning 60%)**. The most sensitive issue that needs to be resolved quickly is the establishment and application of work procedures, an essential condition for the programming activity as a whole.

3.4. Implementiation

The implementation stage is the stage the most close to practice, meaning to the specific activities generated by the use of community funds. From this point of view, many experts consider that it is the most difficult part of the whole mechanism, any malfunction in the management and programming stages having a direct impact on the implementation.

The European regulations do not specific many things regarding the implementing stage. Thus, art. 8(3) of Council Regulation no. 1260/1999 stipulates:

"In application of the principle of subsidiarity, the implementation of assistance shall be the responsibility of the Member State, at the appropriate territorial level according to the arrangements specific to each Member State…"

In other words, according to the principle of subsidiarity, each country organises the implementing institutional structure as it wishes, taking into account the local specificities and having as objective the efficient use of Community Funds.

From the tasks and functions related to the implementation stage we have to mention those referring to the elaboration of selection criteria, reporting activities, observing the

European norms in fields such as public acquisitions, competition, environment or equal opportunities.

The implementation stage has in view especially the intermediate bodies, but not only. An *intermediate body* is a public or private organism, acting under the responsibility of the management or paying authorities or fulfilling tasks on their behalf, in relations with final beneficiaries or other bodies and firms deploying specific operations. In other words, the intermediate bodies are, usually, implementing structures.

The evaluation of preparations related to the implementation stage was made for the three elements, respectively institutional structures, human resources and systems and instruments which will be used in implementing the priorities and measures comprised in the operational programmes.

The scores obtained are presented in the following table.

Table no. 3.6. Scores obtained for absorption administrative capacity in implementation – design stage

Components	Actual score	Maximum score	*Percentage*
● Structure	**4,8**	**7**	**69% (Categ. C)**
● Human resources	**2,9**	**6**	**49% (Categ. C)**
● Systems and instruments	**1,8**	**5**	**36% (Categ. C)**
Total	**9,5**	**18**	**53%**

Source: Authors' evaluation.

3.4.1. Institutional structure – implementation bodies

The evaluation of institutional structures takes into consideration a series of criteria related to the assignment of intermediate bodies, their designation on measures, delegation and division of responsibilities, their public representation, their experience, the existence of formal agreements of implementation with the managing authority, the quality of relations with the managing authority.

Romania has already assigned a large part of the needed intermediate bodies. Some IB have been recently created, for less than a year. Obviously, there is a clear difference between the IBs from the point of view of institutional dynamism, openness and experience in implementing projects financed through community funds. The more dynamic the IB and able to take responsibilities in managing the structural funds, the more easy the MA mission.

The next table shows the list of intermediate bodies involved in the NDP implementation.

Table no. 3.7. Intermediate Bodies

Operational programme	*Intermediate Body*
SOP Competitiveness	**National Agency for Small and Medium Enterprises and Cooperation**
	Ministry of Education and Research – Research and Science National Agency
	Ministry of Communications and Information Technology
	Ministry of Economy and Commerce – Energy Department
SOP Environment Infrastructure	**Regional Agencies for Environment protection (8)**
SOP Human Resources	**National Agency for Employment and Regional Agencies (8)**
Regional OP	**Regional Development Agencies (8)**

As one can see, there are 29 implementation bodies, out of which 24 are local/regional agencies (regional development, environment and employment). It is worth mentioning that, in our opinion, *it is not clear yet if an IB will be involved only in programming (partially), project selection and administration/monitoring or it will also implement directly some programmes.* There is the tendency to "lobby" for both roles – and especially for the implementation one – although it can be taken into account the alternative of IB's role in programming, projects selection and monitoring, even in assistance for the potential beneficiaries.

As an example, Ireland appointed 82 intermediate and implementation bodies, for 5 Operational Programmes (3 sectoral and 2 regional). It should be mentioned that Ireland a dual (multi-level) system of intermediate bodies and implementing agencies. The need to appoint such intermediate bodies, to which all management tasks have been delegated, appeared at the moment when the managing authorities had no clear tasks and specialised personnel for implementing specific sectoral policies.

We believe that a *concentrated* model is more appropriate for Romania, from the point of view of both monitoring and control possibilities and of developing the necessary capacities for managing the European funds. The alternative for such a system is an approach much more dispersed, and – we have to admit – can be found in many European countries. Thus, the number of intermediate bodies for *each* operational programme can be of 30-40, given that for larger Member States this number is up to 500.

The intermediate bodies' experience in implementing European programmes is very heterogeneous. Related to this aspect, the survey answers suggest a range of institutions from those with no experience at all (without experience in community funds management), to more experienced institutions, which have already managed a significant number of projects supported by European finance. Nevertheless, we have to make an important clarification in defining the notions of "management experience" and of "implementation experience" of programmes. Thus, a great number of pre-accession programmes, as grant schemes, were based on the principle of "first come, first served", observing, obviously, some eligibility criteria (often, very permissive). In other words, rarely processes such as projects evaluation and selection actually took place. Moreover, besides technical difficulties (limited experience in setting procedures and eligibility criteria), there are often fears and cautions vis-à-vis assuming responsibilities related to this process.

The negotiations and conclusion of agreements between management authorities and intermediate bodies in view of delegating responsibilities have not taken place. According to Art. 34 from the Regulation 1260/1999 the obligations of the managing authority are:

1. put into practice the system of gathering statistical and financial information related to the projects implemented
2. adjust and implement the programme
3. draw up and submit the annual implementation report
4. organise the mid-term evaluation
5. use of a separate accounting system or an adequate accounting code
6. ensure the correctness of operations financed
7. ensure the compliance with Community policies
8. ensure the compliance with obligations concerning information and publicity

The topical issue is which obligations remain the responsibility of the managing authority and which obligations are delegated to the intermediate bodies. For delegating responsibilities, an agreement/contract should be concluded between the Managing Authority and the Intermediate Body, in order to define the tasks of latter. From this point of view, a distinction has to be made between responsibilities and obligations. Thus, the Managing Authority remains fully responsible for the efficiency and accuracy of the programme management and implementation, while the actual implementation is delegated to the intermediate body.

Almost all the answers to the questionnaires reveal that this delegation was not yet made, specifying that the reason is the unfinished status of the operational programmes (SOPs&ROP). Nevertheless, it is obvious that the division of tasks such as the above-mentioned ones can be made even before finalising the operational programmes. After finalising the OPs, the remaining task, indeed challenging, will be the detailed delegation of priorities and measures for each of the IBs.

Taking into account these comments, the scores obtained for this element was of **4.8 points out of maximum 7 (meaning almost 69%)**.

3.4.2. Human resources – implementation capacity

In terms of *figures*, the personnel framework is still in the first stage, most of the intermediate bodies having less than half of the personnel that they need to have at the accession date, in conformity with the commitments assumed. Moreover, the Intermediate Bodies' personnel is involved in other activities specific for the respective institution. From the answers, it is not clear if a clear delimitation is or will be made within these institutions of the tasks related to the implementation of the programmes financed from European funds. This implementation process is an additional task for some institutions which are already functioning.

The awareness regarding the number of needed personnel is acceptable, but some intermediate bodies do not have the control over the employment procedure, as this task is carried by human resources departments from the parent-institution. Moreover, under the current budgetary constraints implying job-freezing and employment restrictions, there is a tendency to occupy vacancies by redistributions within the institutions, which does not provide personnel with required qualifications and knowledge.

A positive element is that *personnel leavings* from he intermediate bodies are few, almost nil. Among the reasons determining this stability is the possibility to work in a new field, to develop the professional training, the possibility to develop an European career, the safety of job, but also the wage level, which after the substantial raise brought by the Law 490/2004, is considered satisfactory in almost all answers received. Another encouraging element is that, with one exception, all institutions – taking into account the previous experience – consider there will be sufficient candidates for the available vacancies.

The situation is no better for *experience and training of the personnel*. Very few intermediate bodies declare having qualified personnel for preparing, selecting, managing, monitoring and evaluating projects. Obviously, the tasks are specified by the job descriptions, but they are defined rather in a general way than on activities types. The training sessions for intermediate bodies representatives seem not to be exclusively for them, being more on general issues (on structural funds, drawn-up of operational programmes) or unfitted with their future tasks (stress management, leadership and motivation, conflict management, external communication etc.).

Many of the training sessions are carried on within the twinning programmes. At the question referring to the quality of the received technical assistance, the majority of answers evaluate it as satisfactory, but there are cases of "weak" or blank questionnaires (probably, based on the principle that the silence is an answer). More aspects are worth mentioning here. In the first place, the twinning projects usually involve a partnership between the two public administration institutions, a Romanian one and a European one. Without being the subject of the present study, we are convinced that, for more than a few cases, the actual implication of the Community institutions is rather formal and the experts residents in Romania have rather past relations with these institutions. In the second place, such a programme is based on an agreement negotiated between the two parties. Nevertheless, in most of the cases, the Romanian party had an irrelevant contribution to drawing up this agreement. In other words, it was difficult for the Romanian party to define what it wanted from the programme. To know what you do not know (and thus to formulate the training needs) is probably one of the most difficult things. Therefore, the technical assistance programme was drawn up by the foreign party, which only in a small number of cases knew beforehand the Romanian environment. In the third place, more than a few times, the content of the training sessions is decided by the qualification of the foreign experts that can come to Romania at specific dates. In a nutshell, the efficiency of the twinning programmes is not the expected one, the guilt being shared by both parties, which have serious problems of communication and involvement.

Bearing in mind all these comments, the score obtained for this element was **2.9 points out of a maximum 6 (meaning 48%)**.

3.4.3. Systems and instruments – the existence of specific procedures

For implementing the programmes concerning the structural funds, various systems and instruments are used, in a rather heterogeneous way. For this purpose, we may mention manuals, procedures, forms and instructions referring to:

- the management of the project cycle and projects portfolio
- the selection and evaluation techniques
- the modalities of projects approval
- the use of IT systems in projects implementation.

Almost all the respondents at the survey mention that there are no such systems and instruments needed in the implementation stage, and some of them even appreciate that such concerns are premature, because the implementation and selection mechanisms are not yet created within the operational programmes. Only few answers are positive, concerning the regional development projects or pre-accession programmes managed by the institutions in question.

Bearing in mind all these comments, the score obtained for this element is **1.8 points out of a maximum 5 (meaning 36%).**

CHAPTER 4. FINANCIAL ABSORPTION CAPACITY

As described in the methodology section, *financial absorption capacity* stands for the capacity of central an local authorities to co-finance programmes and projects supported by EU, to plan and guarantee such contributions within domestic multi-annual budgets and to colect them from the different partners involved in a project or programme.

4.1. Co-financing capacity – key factor influencing financial absorption capacity

One of the main principles of the cohesion policy is the need for co-financing, which implies that member states should contribute with their own financial resources, in addition to EU non-reimbursable assistance. This principle is based on the assumption that the resources allocated through the cohesion policy are considerably lower than domestic governmental expenditure, which have a greater impact on economic and social cohesion. Unfortunatelly, many times, Member State policies involving public spending are mainly directed at providing basic services and income support and on solving immediate social problems. Such policy response only tackles the effects and not the causes generating socio-economic disparities. As a result, the cohesion policy needs the co-financing rule in order to reorient the national expenditure towards the areas where it can have the best leverage effect on the medium term, as well as to develop a greater sense of ownership of the beneficiaries as regards the proposed projects.

In order to be prepared to ensure this co-financing from the very first day of Romania's accession to the EU, it is higly important for the future beneficiaries to be made timely aware of how much their co-financing effort might be. These figures will be available for Romania only once the programming documents have been elaborated and agreed with the European Commission. In the case of Romania, the programming exercise will be finalised in 2006.

Nevertheless, even at the current stage of preparation, there are a series of key factors related to the level of co-financing which can already be identified and analysed, as part of an early warning that may help increase the financial absorption capacity.

4.1.1. Calculating the project co-financing effort

For calculating how much money will get back from the Commission and consequentely, how much it has to contribute for developing a project, the beneficiary should always follow several steps, such as:

- **first stage**: deduction of non-eligible expenses

Within a project prepared for support under the Cohesion Policy objectives, not all expenses may be covered through structural instruments. The process of identifying eligible expenditure is not an easy one. While for the "European Territorial Cooperation" objective, the list of eligible expenditure is established at EU level, for the "Convergence" objective, it is Romania's responsibility to establish its own system of eligible expenditure, subject only to the several EU exceptions of not eligible expenditure, afferent to each Fund[17]. Apart from these, other ineligible expenditure consists in expenditure occurred outside the eligibility period[18] or for operations completed before the starting date for eligibility or for other operations than those decided on by the OP responsible authorities. Therefore, it is most important for Romania to intensify its efforts of setting the list of eligible expenses, so that the preparation of projects (project pipeline) in 2006 would have a solid ground and clear framework.

- **second stage**: deduction of private expenditure[19] from total eligible cost

The beneficiary must apply the co-financing rate only to the ***total eligible public expenditure***[20] for that project. In the case where the project generates revenues, the public expenditure is calculated by deducting from the investment cost, the current value of the net revenue from the investment over a specific reference period.

- **third stage**: applying the co-financing rate

For each Operational Programme it is mandatory to set a EU maximum co-financing rate. This means that Romania may decide to finance some priorities, measures or projects 100% from the community assistance, as long as the balance between the different priorities or measures respect the maximum OP contribution rate agreed with the European Commission. But the authorities should be cautious when making use of this provision, as Romania's aim should not be to simply consume the EU money as fast as possible, but to use it in an efficient way. It is advisable that such a decision should be

---

[17] Art. 55 Draft General Regulation; Art. 7 Draft Regulation on ERDF; Art. 11 Draft Regulation on ESF; Art. 3 Draft Regulation on CF.

[18] The expenditure has to be actually paid between the date of submitting the operational programmes to the Commission or from the 1st January 2007 whichever is the earliest and before 31 December 2015; For major projects, the expenditure occurred before their approval by the Commission is eligible, is respecting the general OP eligibility period.

[19] Expenses borne by private beneficiaries for a project depend on the contractual arrangement between the public-private contracting parties. Where no national public expenditure is involved in the project, the possibility might arise where the public contribution to a given priority could be financed entirely from Community Funds matched by private sources only (including non governmental organisations), provided that there is an offsetting contribution from national public sources in another priority in order to achieve the global co-financing rate set at a programme level.

[20] Any public contribution to the financing of operations whose origin is the budget of the State, of regional and local authorities, of the European Communities related to the Structural Funds and the Cohesion Fund and any similar expenditure. Any contribution to the financing of operations whose origin is the budget of public law bodies or associations of one or more regional or local authorities or public law bodies.

taken either for supporting the sectors that can have a real added-value to the economic development and/or where it is foreseeable that the beneficiaries will have real problems in ensuring their co-financing part.

4.1.2. Calculating the programme co-financing effort

The steps for determining the co-financing effort at project level might prove useful for each beneficiary, but at national level the scope is to find collective, not individual solutions to co-financing problems. As a result, it is critical to analyse the indicative co-financing effort at the level of each operational programme and the predominant type of beneficiaries for each OP.

The co-financing effort at OP level is determined function of three elements: the cohesion policy allocation to each operational programme[21], the estimation of the national public expenditure to each OP and the OP co-financing rates.

The amount of community contribution to each operational programme is decided by Romania in cooperation with the Commission, function of the overall community transfers, the OP financial prioritization and other community rules.

The exact overall amount that Romania will receive for the 2007-2013 period depends on the on-going Brussels negotiations on the next financial perspective[22]. Nevertheless, Romania is sure on the 2007-2009 financial package, as this has been ring-fenced[23] and is stipulated in its Accession Treaty. For the rest of the period 2010-2013, the financial transfers to Romania will depend on the outcome of the Brussels negotiations.

As working hypothesis, if we add the "ring fenced" financial package for 2007-2009 (5 439 million euro) and the indicative financial package for 2010-2013 (12 560 million euro), we will reach an indicative amount of transfers around 17 999 million euro[24].

In order to reach the community amount that will be available for the operational programmes, we must take into account some supplementary community rules:

---

[21] The Commission's decision adopting an operational programme shall fix the maximum rate and the maximum amount of the contribution by Fund for each operational programme and for each priority axis. (see Draft General Regulation)

[22] The EU financial perspective contains the maximum annual expenditure from the Community budget, organized in budgetary headings. The proposal for the 2007-2013 financial perspective was launched by the European Commission in February 2004; eventually, after long delays, a compromise was reached in December 2005, too late to be analysed in the study.

[23] "Ring fenced" means this financial package will be preserved, whatever the 2007-2013 financial perspective might stipulate.

[24] For obtaining this amount, one should start from the total amount for "structural operations" and deduct transfers for agriculture and fishery, which were before within the cohesion policy and are now included in the Common Agricultural Policy. Therefore, the total amount for CAP is the sum between previous funds for CAP and transfers from structural instruments.

- Out of the overall financial amount, Romania has first to allocate 1/3 to the Cohesion Fund (6002 million euro), money that will finance the SOP Transport Infrastructure and SOP Environment; the rest of 2/3 (11997 million euro) remain for ERDF and ESF and will be allocated between all the operational programmes, depending on the established financial prioritization.
- The remaining 2/3 is further brokendown by the Commission between the two objectives "Convergence" and "European Territorial Cooperation" and the total appropriations allocated to Romania under these objectives are not transferable between them.
- From the amount available for "Convergence", Romania may decide first to allocate some funds for the national performance reserve[25] (3% of the total allocation to this objective) and for the national contingency reserve (1% of the Structural Funds annual contribution to this objective)[26].
- Out of the "European Territorial Cooperation" objective, we have to extract an amount representing the ERDF transfer to the new instruments financing the cross-border cooperation at the EU external border (IPA - Instruments for Pre-Accession and ENPI - European Neighbourhood and Partenrship Instrument)[27]. The remaining sum will be split between the three strands: cross-border cooperation (35.61%), transnational cooperation (47.73%) and interregional cooperation (4.54%); Under this objective and taking ito account the length of its frontieres, Romania may decide to transfer some funds from the transnational component to the cross-border cooperation, under a flexibility of 10% of the amounts allocated.
- The funds have to be further split between the different operational programmes. As an example, a preliminary allocation may look, as follows[28]:

Table 4.1. Financial Allocation for the SOPs/ROP, 2007-2013

Financial Allocation 2007-2013	SOP Competitiveness	SOP Human Resources	SOPs Transport and Environment[29]	ROP	OP Technical Assistance	European Territorial Cooperation[30]
%	12	18	48	18	1	3

[25] If Romania has decided to establish such a reserve, it will assess, not later than 30 June 2011 the performance of each of its operational programmes so that the Commission can award the reserve. Using this instrument is advisable as an incentive to increase SOP/ROP performance.

[26] The national contingency reserve is aimed to cover unforeseen local or sectoral crises linked to economic and social restructuring or to the consequences of trade opening.

[27] Corresponding to the current ERDF percentage financing cross-border cooperation at the EU external border.

[28] This may suffer adjustments, following negotiations with the European Commission. Public Administration OP is not taken into consideration in the above example. Final allocation will be known only after the agreement on the financial perspective for 2007-2013 at the EU level;

[29] Funds for Infrastructure OP (Transport and Environment) come both from the Cohesion Fund and from ERDF (33%+15% in the example);

[30] There will be more OPs under the objective of European Territorial Cooperation;

Source: Authors own opinion

Community transfers need to take into account the national public co-financing of Romania, estimated according to the additionality principle.

The co-financing effort is then calculated by applying the co-financing rates to the overall public expenditure for the Operational Programmes, obtained as the sum of Community support and the national co-financing. Such assessment may be done starting with an indicative baseline, using the maximum contributions rate provided by the Regulation; the real contribution rates[31] for each operational programme and for each axis will be established by the Romanian responsible authorities and submitted to the Commission approval[32]. The maximum OP contribution rates provided by the Regulation[33] are:

- *under the "Convergence" objective*: 85% of the public expenditure co-financed by the Cohesion Fund[34]; 75% of the public expenditure cofinanced by the ERDF or the ESF, which may rise to a maximum of 80% in exceptional and duly justified cases; the latter two may rise[35] with 10% for ERDF, for the interregional cooperation actions it finances under Convergence OPs and 10% for ESF, for the transnational and interregional cooperation actions it finances under Convergence objective;

- *under the "European territorial cooperation" objective*: 75% of the public expenditure.

Minimum co-financing rates for each of the development axis are 20% from all public expenditure, in order to preven an unbalanced distribution of funds among different axis.

Within these limits, *real co-financing rates* are modulated according to certain criteria such as: rates should be higher in disadvantaged areas, in poor areas where real problems in providing the necessary public cofinancing can be envisaged, in sectors that can have a real added-value to the economic boost; these rates could be reduced to take account of the application of the polluter-pays principle[36] and of the estimated amount of revenue generated by the project - by promoting increased recourse to private sources of financing, Member States can thus maximise the multiplier effect of the resources of the Fund.

---

[31] The exact contributions rates may be adapted based on the following criteria: the gravity of the specific problems, in particular of an economic, social or territorial nature; the importance of each priority axis for the Community's priorities as set out in the strategic guidelines of the Community, as well as for national and regional priorities; protection and improvement of the environment, principally through the application of the precautionary principle, the principle of preventive action, and the polluter-pays principle; the rate of mobilisation of private financing, in particular under public-private partnerships, in the fields concerned; the inclusion of interregional cooperation under the "Convergence" objective.

[32] For majour projects, it is the Commission who establishes the rate of assistance.

[33] Art. 51 Draft General Regulation.

[34] In order to accommodate the different contribution rates for CF and ERDF, for operational programmes cofinanced jointly by the ERDF and the Cohesion Fund, the decision adopting the operational programme will fix the maximum rate and the maximum amount of the contribution for each fund and allocation separately.

[35] Art. 52 Draft General Regulation.

[36] The Polluter Pays Principle implies that those who cause environmental damage should bear the costs of avoiding it or compensating for it. The transport and energy infrastructure sectors – which account for about ¼ of the Community's financial support to Romania – have the biggest impact on environment; therefore, the application of the Polluter Pays Principle is most relevant in these sectors.

4.1.3. Solutions for increasing the co-financing capacity of Romania

Under the negotiations on chapter 21, the Romanian Government undertook the commitment to ensure the necessary co-financing to the cohesion policy expenditure. Taking into account the outermost importance and impact that the cohesion policy can play in the future development of Romania, it is the responsibility of the Romanian authorities, at both technical and political level, to identify the cofinancing problems that the future beneficiaries might have and take the necessary steps to adequately support them.

For the forthcoming period, Romania should have two objectives: (i) find solutions to ensure the necessary public cofinancing and (ii) create the necessary conditions for attracting private capital investment.

There are certain common challenges for all types of beneficiaries. The reimbursment rule requires the beneficiaries to finance the start of the project and then turn to the Commission for the reimbursement of the money already spent[37].

Another element that could possibly contribute to implementation delays consists in the system of interim payments[38]: the payment applications for each operational programme are grouped together and sent to the Commission, as far as possible, three times a year and then two more month are necessary for the Commission to transfer the money. This could lead to a situation where a beneficiary whose statement of expenditure has been certified at the beginning of January has to wait till end June to receive his money back, because the global payment application for the respective operational programme has been submitted to the Commission at end April.

Public Co-financing

Public cofinancing might come from the budget of the State, of regional and local authorities, of public law bodies or associations of one or more regional or local authorities or public law bodies. If their budgetary revenues are not sufficient, these bodies can turn to domestic (mainly commercial banks) and/or foreign borrowings (mainly European Investment Bank).

The state budget will need to provide on an annual basis the required co-financing for at least the SOP Transport Infrastructure, where the beneficiaried are mainly central public entities; if in the case of ISPA transport – the precursor of SOP Transport – the necessary public co-financing was provided, not without difficulty, from the state budget, after 2007 the pressure on the state budget will be definitely higher, as Romania will face the challenges of accession: three times higher co-financing than it was on ISPA, contribution to EU budget (estimated at around EUR 800 million for the first year of

[37] Expenditure paid by beneficiaries shall be justified by receipted invoices or accounting documents of equivalent probative value (Art. 77 Draft General Regulation).
[38] Art. 86 Draft General Regulation.

accession) as well as the need to maintain the budget deficit within reasonable limits, thus ensuring macroeconomic stability.

Even if the co-financing effort from the central effort is far from being marginal, the biggest cofinancing effort will press on the budgets of local public bodies and especially local authorities (county councils, municipalities), as these will be the main beneficiaries for three very important operational programmes: SOP Environment, SOP Human Resources Development and ROP.

The experience of pre-accession funds absorption shows that local public authorities have encountered significant problems in ensuring the necessary cofinancing. On one hand, the level of fiscal autonomy is severely limiting their revenues. On the other hand their borrowing capacity is reduced, both due to legal provisions and as a result of their precarious financial capacity, in the context of limited state budget guarantees.

The problems of local public authorities related to their financial absorption capacity will be analysed in more detail in the next subchapter.

Stimulating private investment

Taking into account the considerable cofinancing effort and the increased constraints on national public expenditure, it is necessary to maximise the leverage of Community Fund resources by encouraging greater use of private sources of funding. The private capital involvement will mainly appear in the SOP Increasing Economic Competitiveness, where especially SMEs will be the targeted beneficiaries.

Private investment will also be found in the other SOPs/ROP, where it may be established as public-private partnership.

Problems of SMEs

The year 2007 will bring considerable challenges for Romanian SMEs, which will need to cope with the competitive pressures of the Single Market and with the rigurous provisions of the newly adopted *acquis*, especially regarding the conformity with environment and quality standards. Facing such challenges requires significant investment from the SME sector, which might be deprived of the needed resources for developing projects under the framework of the cohesion policy.

SME co-financing is one of the thorniest aspects of absorbing funds in this sector. Firstly, as oposed to pre-accession funds, structural instruments may not be provided in advance, but only following the reimbursment rule. Such procedure implies that SMEs are required to invest from their own (or attracted) resources for covering all expenses related to the proposed development projects.

Secondly, SMEs need to cover from their own resources the non-eligible expediture. Currently, there is a certain degree of uncertainty regarding expenditure eligibility for SMEs, for example, as regards VAT in the case of projects financed through the cohesion policy. There is the risk that VAT will be considered non-eligible, which would seriously undermine the capacity of SMEs to afford co-financing.

Thirdly, private financial institutions are not generally keen to provide credit to SMEs, due to higher risk exposure. Even if active interest rates have fallen lately, the prerequisites demanded by banks for financing SMEs are still harsh.

Therefore, public intervention for improving SME's access to finance may be justified on grounds of redressing market failure. For this end, the Competitiveness SOP provides for the development of guarantee funds and risk capital, as customized instruments for the SME sector. *Nonetheless, all these schemes will be subject to the state aid regulation.*

Private-Public Partnership (PPP)

One possibility to maximize the leverage effect could be financing of Public Private Partnerships. Public Private Partnership schemes (PPP) are arrangements between public and private sector actors for the delivery of a project or services that are traditionally delivered by the public sector. Both public and private parties share investments, risks, rewards and responsibilities in the implementation of PPP projects. The most frequent types of PPP are:

- Design-Built-Operate – the design, build and operate phasis of a facility are done by the private sector for a period of time, then given back to the public sector; the facility is financed by the public sector and stays in its property during the project duration, but the private sector bears the design, build and operate risks
- Design-Build-Operate-Finance – the design, build, operate and finance of a facility are done by the private sector for a period of time then given back to the public sector; the private investor holds the property of the facility during this period, bears the design, build and operate risks and recovers the costs from public subvention
- Concession – similar to the previous one, but the private sector recovers its costs from the tariffs paid by users

The private capital investment in structural operations depends on a strong political commitment at national level to make the necessary reforms sustainable. The application of PPP could be hampered by the lack of general (legal) frameworks, knowledge and experience in the countries and by the (perceived) administrative complications (for instance, the generation of net-revenues by the project reduces the co-financing amount from the CF).

Romania made significant progress in this respect, by revising its whole legislation on public-private partnership. More, it will be able to use the CP technical assistance for planning successful public/private partnerships. It should now ensure a widespread knowledge of this instrument among the players and learn from others's experiences.

4.2. Co-financing capacity of local government

We consider the co-financing capacity of local governments (LG) as a key factor for our analysis. LG display a set of characteristics which can make them the weakest link in the co-financing chain.

4.2.1. Local government

The main authorities of local administration are the Local Council (LC) at regulatory level and the City Hall (CH) as executive entity. However, the complete chart of the local administration includes several public services and utilities companies, subordinated to the LC and CH. For the purpose of this paper we will refer as borrowers only to the LC and CH.

4.2.2. Legal framework

The legal framework that applies to the analysis of the LG cofinancing capacity comprises, by and large:

- Law 339/2004 on Decentralisation
- Law 313/2004 on Public Debt
- Law 571/2003 on Fiscal Code, as amended (all until OUG 24/2005)
- OUG 45/2003 on Local Public Finances, as amended (Law 108/2004, Law 313/2004, OUG 9/2005)
- OUG 146/2002 on Utilisation of State Treasury Funds, as amended (Law 201/2003)
- OUG 22/2002 (Law 288/2002) on Payment Obligations of Public Institutions
- Law 215/2001 on Local Public Administration, as amended (Law 738/2001, Law 216/2002)
- MoF Order 94/2001 on Harmonisation of Accounting Standards with the 4th CEE Directive and the IAS
- Law 213/1998 on Public Property
- Law 99/1999 on Acceleration of Economic Reform
- Law 58/1998 on Banking, as amended (Law 246/2002, Law 437/2001, Law 357/2002, Law 485/2003)
- Law 64/1995 on Reorganisation and Bankruptcy, as amended (Law 192/2004)

In the following, we set out to analyse financing terms and needs for LG, taking inot account the above-mentioned legal framework.

4.2.3. Borrowing needs and financing sources for LGs

Factors that determine an increase in financing needs for LGs are, at present:

- *More responsibilities without matching resources*. Decentralisation process is driven by EU integration requirements, negotiations with the IMF on the deficit, and domestic political imperatives. Ever more responsibilities have been delegated at local level over the past decade. On the other hand, the central government rarely matched newly delegated responsibilities with available resources (education: salaries are negotiated centrally, but paid locally).
- *Limited resources of central government for capital investments*. Transfer and grants from the State budget earmarked for local capital investments (upgrading the plants for local utilities, replacement of the vehicle pools for local transportation or rehabilitation of public roads) have declined dramatically. The overarching need to preserve macroeconomic stability thus affects indirectly the local authorities. Central authorities' strategy towards encouraging the development of the local borrowing consists more in a re-evaluation of the legislation.
- *EU accession requirements*. Accession to the EU will require a massive investment in environmental cleaning (landfills, incinerators, water treatment plants). Municipalities will have to significantly contribute to these investments, helping to meet the twenty-five percent (25%) country match required for obtaining EU (pre-) accession grants.

There are also elements that lead to a downward pressure on the borrowing demand by LGs:

- *Political factors*. Due to political frictions inherent to coalition politics (the Romanian election system is prone to produce coalition governments more often than not), there is persistent inability to reach consensus at local and central level on objectives and means.
- *Technical factors.* As with the entire economy, the vast majority of municipalities lack advanced financial skills. Understaffing and underpayment only compound this major human resources problem.
- *International factors*. Financing from IFIs (EBRD, EIB etc.) is taken into account when calculating leverage for LGs, which leaves little room for extra leverage within the 20% cap (as it will be discussed later in the paper).

Tight budgets are here to stay for Romania as a prerequisite for macro stability, at least in the mid run (given lower taxation and relations with EU/IMF), and therefore transfers from the state budget will probably not be allowed to grow significantly in the coming years. Moreover, state guarantees for LG debt would equal additional public debt, and endanger the deficit target. The two main financing sources left for co-financing by LGs are, inherently:

- increasing own revenues, from recurring fiscal revenues (those are allowed to be used for co-financing), by way of increasing the local tax base (equivalent to local economic power and growth);
- municipal borrowing (borrowing capacity is constrained, basically, by repayment capacity from own revenues).

Financial analysis is a must in order to determine borrowing capacity of LGs. On top of financial analysis results, maximum leverage for LGs is also constrained by a series of legal provisions. We will first scrutinise the later.

4.2.4. LGs access to loans

Facilities requested by municipalities almost invariably refer to longer tenors, for capex, as also do structural funds. Obviously, tenors of such loans could go well beyond 10 years. To take such loans, substantial credit analysis must be conducted, and loans should be collateralised by assignment of receivables or real estate. Capital expenditure in total municipality expenditure varied between 10% and 20% on average over the last years. It decreased along with the delegation of more and more responsibilities at the municipality level, which strained the local resources.

As concerns absorption capacity, two possible situations occur:

- con-financing loans; co-financing can be supported by own revenues or borrowed funds;
- pre-financing of structural funds and, possibly, of transfers from the central budget for projects to be financed by structural funds; in addition to risks normally incurred by lender under normal circumstances, covered by collateral, due diligence and financial analysis, there is the risk that LGs do not get the structural funds or budget transfers in case some of the conditions to release such funds are not met subsequently to the release of loan.

The main aspects regulated by law regarding loans for LGs are:

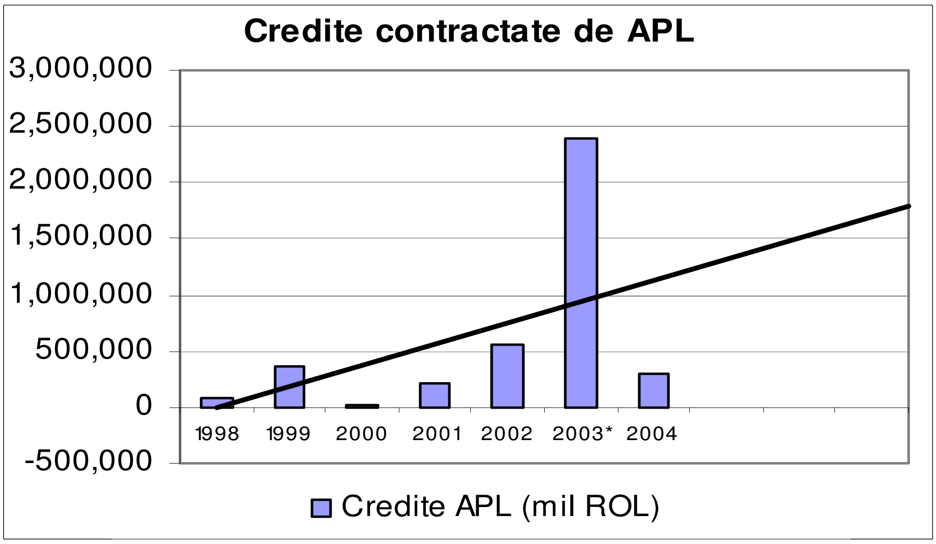
- *Leverage cap*. Municipalities are prohibited from borrowing or guaranteeing loans whose debt service (principal, interest, commissions) per annum is greater than 20% of own revenues (including obligations stemming from municipal debt with state guarantees). The law thus basically caps municipal leverage.

- *Repayment sources*. Repayment can only be made out of own revenues, and repayment of debt has to be included at the top of the other expenses in the local budgets pertaining to the duration of the debt.
- *Interest, tenors, and currency*. There are no specific restrictions, as interest can be fixed or floating, borrowing can be done both in local and foreign currency (with special approval), medium- and long-term.
- *Taxation*. Interest income from municipal bonds is tax-exempt for resident individuals and for non-residents. Similarly, there is no tax on interest made from loans for infrastructure projects.

4.2.4.1. Legal, administrative, financial and guarantee framework

Legal framework has had a major impact on the evolution of municipal borrowing. The graph bellow shows the impact of OUG 45/2003 on municipal borrowing.

Figure 4.2 Credits contracted by LG



* passing of OUG 45/2003.

Source: INSSE, team analysis.

Degree of control over own resources

LGs have control over the level of local taxes, as decided by local and county councils. The weight of own revenues in local budgets has gone up over the last years, mainly due to legislative changes which allowed for a greater decentralisation of revenues sources.

At first sight, own revenues cannot be negatively affected by central government decisions, because transfers from income tax collected centrally can only be adjusted upwards, according to the law. Nevertheless, a significant proportion of own revenues consists in income tax, whose level is set by the central government. Recent history (introduction of 16% flat tax) underscores this issue. Although such a measure is usually accompanied by an increase in the allocation to LGs, redistribution does not offset the revenue loss for the local budgets. More often than not, fiscal responsibilities transfered at local level are nevertheless outside regulatory power of LGs, which translates into a low level of predictability of these sources of own revenues.

It must be mentioned that, as regards cofinancing or pre-financing obligations, as well as loan repayment capacity, earmarked funds cannot be taken into consideration although are included among own revenues, as they are exclusively allocated towards specified public services.

In every situation where, as in Romania, local budgets depend in great measure upon transfers from the central budget (over 50% of total revenues for Romanian LGs) and arrangements governing such transfers are unstable, it is impossible to calculate repayment capacity of LGs. This uncertainty generates credit risk. Finally, LG revenue sources stability can only be ascertained through the analysis of time series.

Legal harmonisation

The harmonisation of the Romanian accounting norms with the 4th Directive of Economic European Communities and with the International Standards Norms might lead to differences between the execution accounts of the municipality and the estimated budgets due to the fact that the contributions of the legal persons to the local budget might be lower than estimated (e.g. companies have to establish inventory provisions which leads to profit diminishment). Revenue volatility will increase.

Tax collection

Until 1999, taxes were collected at county level, by the Treasury. Since then, each city hall has to collect the taxes itself. This has played to the advantage of richer and larger municipalities, which increased their control over revenues. Smaller municipalities lack qualified human resources and this additional responsibility proved to be a burden.

Financial reporting and audit

Unlike companies, municipalities have less practice in terms of disclosure, audit, and financial reporting in a useful manner for creditors. Formation and utilisation of the municipal funds is supervised by the Court of Accounts, which is a Government body. In other words, there is no independently-audited data available. The financial reports that municipalities prepare for the Ministry of Finance rarely present financial information in the reliable, pertinent form that is required to underpin a good credit analysis.

Indebtedness rate

Annual debt service is capped at 20% of estimated amount of own revenues. In case poor collection leads to an excess of the 20% indebtedness rate, the remedies include:

- the LC can decide to increase some local taxes;
- refinancing;
- in case the increased debt service includes municipal guarantees offered by local authorities to third parties, the law provides that a risk fund must be established with the funds resulting from the risk commissions paid by the beneficiary of such municipal guarantees, and interest earned on the account specifically opened with the Treasury.

It is the responsibility of the LC to make sure that the local budget is in compliance with the 20% restriction. The penalties stipulated in the law in case of non-compliance with the 20% cap are insignificant, which could hardly motivate the municipal authorities to take extra precautions in this regard.

In addition, central authorities use to control local leverage through their discretionary powers in approving certain investment plans, accepting financial projections that can prove to be either exceedingly optimistic or conservative. The 20% cap is arbitrary and makes no difference between LGs, despite their very diverse financial standings.

Guarantees

Municipalities can pledge certain receivables (own revenues) as collateral. They can also open escrow accounts with commercial banks, given MoF and creditor consent.

The accounts can be used for collecting revenues or for other available funds, in LCY or FCY, under the specific conditions of the agreements signed by the parties involved. The resources of the escrow accounts can be the budgetary income collected in cash at the local pay-offices, the budgetary income transferred from accounts opened with the Treasury and the borrowed amounts, provided the parties agree this way.

Therefore, escrow accounts somewhat alleviate hindrances caused by central government unavailability for state guarantees. The legal provision which makes them possible was meant expressly to diminish the need for state guarantees. This solution is indeed flexible and feasible. Moreover, once the agreement is concluded, the creditor has priority among general lenders as regards revenues assigned to the escrow account.

State guarantees

While municipal debt is legally part of Romania’s public debt, it can only be repaid from local budget revenues or municipal debt, and it is not an obligation of the central government State guarantees are conditional upon the approval of the Commission for Local Debt Authorisation or the Interministerial Committee for Guarantees and Foreign Trade Loans (in case of FCY borrowing). In case of default, the Ministry of Finance pays from the Risk Fund (risk commissions from the beneficiaries of the guarantee). State guarantees for municipal debt still imply that repayment is made from own revenues only.

Private domain as guarantee

As regards municipal property, the law differentiates between the “public domain” and “private domain”. The property classified as “public domain” is inalienable, not distrainable, and imprescriptible. Property belonging to the “private domain” of the local authority is subject to civil law regulations, meaning that it can be pledged as collateral or sold. The risk for the creditor consists in a lack of clear delimitation between the “public domain” property of the municipalities and their “private domain”. Property belonging to the “private domain” is in certain cases not clearly identified and central authority confirmations of its status can be protracted.

Enforcement of collateral in case of default

There are no specific legal provisions regarding the enforcement of the pledge, with the exception of the above-mentioned.

Insolvabilitatea APL

Lenders’ reluctance is compounded by the absence of legal provisions to regulate municipal insolvency.

Existing regulations do not include municipalities among the entities that can go bankrupt. The risk for the creditor consists in the fact that, in case of insolvency of the municipal borrower, there is little, if any, alternative recourse. As a precautionary measure, municipalities have to report monthly to the Ministry of Finance on the status of their debt repayment schedules.

The problem is indirectly compounded by the unattractiveness of multi-annual financial planning for local authorities. Municipalities cannot deposit money other than with the Treasury, which pays a very low interest rate. In the long run, multi-annual management of local budgets is disincentivised through this requirement.

Temporary illiquidity

Municipalities can be faced with liquidity problems. However, in case of temporary illiquidity, after the exhaustion of working capital, the Treasury may step in with a zero-interest short-term loan, less than 5% of estimated total revenues, guaranteed through the assignment of receivables, other than those pledged as collateral for other municipal debt. In case the municipality still has an overall leverage above 5% by the end of the fiscal year or has not paid its outstanding short-term debt, a special inquiry by the Court of Accounts is triggered, with the drafting of a recovery plan covering a year; further interest-bearing loans can be extended by the Treasury.

However, this procedure is rather reactive in nature, and a better designed algorithm to calculated the leverage cap would much better fit the purpose.

4.2.4.2. Economic context

The local tax base gives the best and most accurate image of the financing capacity of the LGs. Budget transfer mechanisms at national and county levels ensure certain revenue redistribution among LGs, but not with such a magnitude so as to fundamentally alter this image. Tax base analysis can be performed by either considering company sales, or GDP, by regions.

Obviously, tax base is a solid indicators, but no necessarily accurate, of own revenues generation capacity of the LG. Utilities prices hikes (in line with the price liberalisation schedule agreed with the EU, for instance), can generate lower collection rates or unforeseen slides in own revenue sources. The same effect can be generated by an increase in unemployment. Regional development in Romania is asymmetric, with only a handful poles of growth. Besides, unlike other CEECs, Romania's urban population has shown a decreasing trend over the last decade.

]

Table 4.3 Demographic dynamics of Romanian municipalities 1992-2002

Municipality	Population	
	1992	2002
Bucharest	2,067,545	1,926,334
Iasi	344,425	320,888
Cluj-Napoca	328,602	317,953
Timisoara	334,115	317,660
Constanta	350,581	310,471
Craiova	303,959	302,601
Galati	326,141	298,861
Brasov	323,736	284,596
Ploiesti	252,715	232,527
Braila	234,110	216,292
Oradea	222,741	206,614
Bacau	205,029	175,500
Arad	190,114	172,827
Pitesti	179,337	168,458
Sibiu	169,656	154,892
Targu Mures	164,445	150,041
Baia Mare	149,205	137,921
Buzau	148,087	134,227
Satu Mare	131,987	115,142
Botosani	126145	115,070
Ramnicu Valcea	113,624	107,726

Suceava	114,462	105,865
Piatra Neamt	123,360	104,914
Drobeta-Turnu Severin	115,259	104,557
Focsani	101,335	101,854
TOTAL	**7,120,715**	**6,583,791**

Source: INSSE.

Urban population makes up only 52.7% of total population, barely 30% of all inhabitants living in cities above 100,000, which are the local growth centres. The number of employees decreased to 3 million. On the other hand, unemployment stays low, at 6.5% in mid-2005, and real wage growth was above 11% in 2004. Retail credit growth rates of above 50% in 2004 and 2005, alongside real wage growth, led to a significant upsurge in private consumption. This in turn translates into higher revenues from indirect taxes, but in parallel to – an otherwise one-off – decrease in revenue from direct taxes due to the introduction of the flat tax. Even under the scenario of a VAT hike, the increase in indirect tax revenues would still be a one-off, followed, in principle, by a inherent adjustment of consumption. Taxation levels have, thus, effects that can become visible only in time, and the best indicator remains the tax base.

4.2.4.3. Procedural framework

Municipal borrowing is initiated by the mayor (CH) and must be approved by the local council, then get the green light from the Commission for Local Borrowing Authorisation, especially set up for this purpose (comprising several representatives of the central government and one representative of the local administration). Domestic and foreign loan schedules have to get the approval of the local and county councils, with a 2/3 majority. They are mentioned in annexes to the municipal budgets and are approved *in corpore*.

At municipal level, in case the local or county councils do not pass the draft budgets within the legal deadlines (often because of political adversities between the LC and the CH), allocations and transfers from the state budget are discontinued.

At central level, based on the track record – and not at all in line with the legal provisions – the State Budget Act was usually passed late in the first quarter of the year. However, the budget for 2006 has been passed before the end of 2005. Deprived of a clear image of intergovernmental revenues, local budgeting becomes a rather hazardous process. Until one year ago, less than 5% of city halls actually approved their budgets before May.

Apparently, instances mentioned above would lead to default as no sources would be allocated for debt servicing. However, in case the state budget act is not passed three days before year end, previous year budgets will apply, until new budgets come into force. Monthly expenditures cannot be higher than one-twelfth of the previous year total expenditure, except for well-documented exceptions.

4.2.4.4. Political environment

On the face of it, there is no subordination between the central and local authorities, nor among local authorities (between county council, city council and mayor). The law institutes administrative and financial autonomy for municipalities.

Nevertheless, the Chairman of the county council is responsible for the distribution of the equalisation funds to municipalities. The 22% equalisation quota is reallocated as follows: 25% based on the population, area, financial capacity, and the tax base; 75% is largely discretionary, mainly to be geared towards helping municipalities meet their co-financing obligations for the EU structural funds. Among the allocation criteria, the law mentions the "financial capacity" of the respective municipality. Interpretation of this criterion is to a certain extent discretionary and political subjectivism can play an important role. Besides, the Prefect (representative of the central government at county level) has the responsibility to "supervise the legality of the acts of the local authorities". This often translates into political interference, and quasi-arbitration as regards revenue-sharing.

4.2.4.5. Regulatory framework

Municipal rating

Legal provisions do not cover credit analysis or financial capacity evaluation for LGs. Borrowing by LGs so far have been few and far in between, and financial analyses have been rather casual and ad-hoc in nature. Very few LGs have asked for an in-depth scan, and most often for internal use only.

However, in 1998, CNVM granted rating authorisation to a local rating agency, which in 2003 presented a service of credit rating of the municipal debt. The rating evaluates the risk of repayment or of delay in repayment of the municipality bonds. In the first half of 2005, no international rating agency had issued a rating for a Romanian LG, with the notable exception of the City of Bucharest, monitored by Standard & Poor's.

Infrastructure and public utilities regulation

Various sub-sectors of infrastructure or public utilities face different degrees of competition, depending on the nature of the business. Regulatory needs are, therefore, different from sector to sector.

Table 4.4 Ranking of competition intensity among public infrastructure

Competition intensity	**Infrastructure type**
High	Urban transport
	Power plants
	Fixed telephony
	Ports
	Railway
	Underground

	Highways
	Power – distribution
Low	Water and sewage

Source: Gomez-Ibanez, Jose A.; 1998.

The existence or lack thereof of a (well defined) regulatory framework has a major impact on the perceived risk of the capacity of an infrastructure project to generate future cash flows. For instance, the presence of an industry-specific regulatory body and of a clear algorithm for utility prices as a function of inflation, agreed profit margin, and efficiency gain rate, would instil more stability to a business plan for investments in that industry.

Such regulation is still in its infancy in Romania. The Competition Council cannot regulate all industries in detail – there are constraints dictated by, not least, lack of expertise and resources.

CHAPTER 5. CONCLUSIONS AND RECOMMENDATIONS

To simplify, but also to make the reading easier, we chose to present conclusions and recommendations as a list. Recommendations are highlighted in italics.

- The administrative absorption capacity of post-accession funds is still insufficient, due to significant and numerous weaknesses which must be tackled in the period of time before accession. Obviously, this statement should be taken in context; our evaluation has been done one year before scheduled accession. Therefore, there is still time. However, comparison with absorption capacity evaluation in other candidate states (new member states at present), at similar moments in time (approximately one year before accession) raises additional concerns, given the lacklustre performance of Romania.

- There is a joke circulating among economists: the lesser the absorption capacity, the better for macroeconomic stability. Indeed, a massive inflow of funds will have certain effects on aggregate demand, which will in turn put pressure on inflation, exchange rate, balance of payments and current account etc. But keeping macro indicators in check is the responsability of experts other than those writing this paper.

- There is a distinct feeling of lack of authority and coordination in the process of preparation for the administration of EU funds. Until the end of accession negotiations, the Ministry of European Integration played the catalyst of such efforts, in order to push various negotiation chapters forward. Once this process concluded, things got somewhat more relaxed. Surely, Romania took responsibility for a number of aggrements, there is a monitoring mechanism, there are action plans, but the degree of uncertainty regarding decisions by officials in Brussels has receded and everybody feels more comfortable. After all, the safegurard clause can be activated due to well defined areas, and accession will happen anyway. But the real stakes are different. The real objective is that Romania be capable of absorbing as much as possible from the allocated EU funds. In order to spend the most (and the most efficient) of somebody else's money, they will never push you. Besides, more often than not, the political management of institutions involved seems rather less engaged and interested, not least because this topic requires not only discourse, but also technical expertise.

  We are by no means advocates of centralisation. But, while keeping in mind that concepts such as decentralisation or subsidiarity are key ideas of EU philosophy, we nevertheless argue that a certain re-centralisation is necessary. By this we do not mean a re-centralisation of the administration or implementation process, but rather a re-centralisation of the ***institution building of an appropriate absorption capacity****. The set up of a working group, with real powers (authority regarding information collection, but also decision-making powers), at Government level, which should monitor (with a view to accelerate) all aspects related to enhancing the absorption capacity, might prove a good idea.*

- The institutional structure for the administration of structural instruments was defined and was approved by the European Commission during the accession negotiations on Chapter 21. The organisation of Management Authorities and Intermediary Bodies entailed mobilising internal resources within ministries or agencies cooordinating such bodies, resources subsequently accompanied, usually, by twinning or technical assistance projects. Generally speaking, we may conclude that the institutional structure is adequate, with all premises for a good management in place. There are still some institutions (intermediary bodies especially) where the position of the future liaison point with the post-accession fund management mechanism is not yet clearly identified on the organisation chart. This is also due to the fact that specific responsibilities have not yet been devolved at implementation body level.

As regards institutional structure, it would probably be beneficial to have a better connetivity between the entire structural fund managment system at higher levels of the Government. Communication and regular debates, at minister level, on the issues linked to the activation of the structural funds management structures would be highly desirable, in order to better prioritise this process.

- Overall, less than 40% of staff has practical experience in working with EU funds. By „experience" we mean having been involved in a technical assistance programme or having monitored projects financed with EU funds. It has less to do with conducting economic and social analyses, drafting strategies and quantifying development objectives. At MA level, the precentage of staff with practical experience varied between 20% and 40%, with only one MA (whose planning/programming unit comprises only 3 FTEs) being staffed entirely with FTEs deemed to have relevant experience. At IB level, the most frequent situation is having 1-2 FTEs with experience covering analyses, drafting strategies and quantifying objectives, but there are also two situations where no staff has any relevant experience. Under such circumstances, the solution is specialised training for the staff.

Specific trainig focused on structural funds is necessary for staff of all institutions involved, especially IBs. Most of these have benefited from general trainig or trainig on issues totally different from their own activity (stress management, leadership and motivation, conflict management, communication etc.). MA CSC is well positioned to coordinate this trainig.

- It is therefore clear that providing the required human resources and their training is a critical issue for structural fund management. A series of budget constraints has hindered the staff recruitment process, so that understaffing would be the best word to describe the situation as compared to Romania's committments under Chapter 21. On the other hand, organisation charts have been, in some cases, overblown, lacking appropriate level of detail. Besides, for a few years period, pre-accession programmes (PHARE, ISPA, SAPARD) will continue to run in parallel with new post-accession programmes. This means that, in some institutions, staff with certain experience in working with EU funds will continue to work with pre-accession instruments, and post-accession funds would be managed by less skilled staff.

However, it is advisable to avoid another extreme, by making HR policy more flexible. Understaffing should be avoided, but neither is desirable to hire extra civil servants just to tick boxes (see situations where hiring is done mainly through rotation within the same institution, without much preocupation for skills). All MAs and IBs should take responsibility for the optimum number of staff which ensures a maximum of efficiency for POS/POR management. At the same time, MAs and IBs must be directly involved in the hiring process, as they best know the skills they are looking for in new staff. Involvement of MA CSC (or, rather, of the working group we put forward in the above-mentioned), should represent a real support for unlocking financial resources needed for extra staff where necessary, but also for consultations when there is propensity to misuse/waste public funds through overstaffing with no solid justification by MAs/IBs.

- Given the novelty and complexity of topics related to the usage of structural and cohesion funds, as well as the lack of experience in this field, technical assistance may be vital. Most of MAs (70%) and most of IBs have been the beneficiaries of such assistance, which would suggest some exposure of their staff to EU standards and requirements.

- Many of the ongoing technical assistance programmes are twinning projects. There is a number of issues we would like to touch upon in this respect. Firstly, in many instances, real involvement by EU institutions is rather formal. Secondly, technical assistance schedule was established, more often than not, by the foreign counterparty, which only seldomly had had direct contact with the Romanian environment. Thirdly, quite often, the contents of training courses are determined by the qualification of the foreign experts that can be sent to Romania at certain moments in time. In a nutshell, the efficiency of twinning projects does not match expectations, and both sides are to blame for lack of communication and involvement.

Apparently, a thorough analysis of the twinning projects is needed. Such projects can be expected to make a massive contribution to a better absorption capacity. In other words, we must put technical assistance to good work. The Romanian side has to identify the weak spots and formulate a shopping list for training. This evaluation must be done on a case by case basis, as the situation varies among different institutions.

- The implementation of Law 490/2004 on financial incentives for staff managing EU funds, and, consequently, the bonus of 75% of base salary has led to a higher wage in the MAs and most of IBs, above other departments or institutions in the Romanian public administration, which do not have contact with EU funds. Incentives for staff remains a priority, to avoid high personnel turnover when employeed reach a level of expertise better remunerated by the private sector. There are also non-salary incentives which can motivate civil servants, such as career plans, stability, prestige, or EU exposure. It is critical to maintain a high level of involvement of structural funds management staff, by making visible their unique role in the overall progress of the country. Last but not least, salary should be constantly matched to the professional ability and responsability of the respective employee.

Civil servants could be incentivised by corporate-like methods, such as performance-based bonus. While the bonus can be money, it could also be given as incentive trips, gifts, or health insurance etc. Such measures would induce extra flexibility in the civil service remuneration scheme. Besides, career planning must be made a priority as soon as possible, to ensure that employees are aware of the importance the administration places on them and avoid defections. Another recommendation refers to institutional memorty building, so that every document or debate can be archived, preferably in electronic format, and thus create a stable basis in case key staff leaves the insititution.

- As regards the set up of the partnership framework, it has been noticed that only 50% of MAs use extended partnership networks at present, the others being in a relatively advanced stage of preparations. From a qualitative point of view, most MAs already select their partnerns from among the representative organisations relevant for the field covered by the operational plan/programme.

The activity should take place in an open environment, at institution level, as well as through an extended partnership. In the first situation, we refer to the collaboration with other units withing the same institution, while in the second we consider an extended partnership to be a prerequisite for the programming activity (it is, after all, a compulsory condition for structural and cohesion funds programming).

- Coherence, coordination and lack of overlapping between operational programmes, their focus on really important issues, are extremely engrossing imperatives. All these cannot be achieved through desk work or by a top-down coordinating body. The can only be achieved through a bottom-up approach, founded on meaningful and functional partnerships. While all MAs participate in the working groups aimed at nation-wide coordination of planning, only half of the MAs are involved in the working groups for the drafting of other operational programmes.

Aside from the participation in the working groups expressly established to set up the operational programme which they coordinate, all MAs should also participate in the working groups drafting the other operational programmes, as well as in the working groups for nation-wide development planning (e.g. the NDP Inter-Insitutitonal Committee), with a view to achieving coherent programming, and avoiding overlapping and conflicts. IBs should also be involved in these partnerships.

- Systems, procedures, and instruments envisaged for structural funds management will be built in time, on the learning curve. Efforts to implement the Single Management Information System (SIMS) have started to yield results, with signs that it may become fully functional in 2006. Evaluation and monitoring are new processes, with shy beginnings, but with strong support via external technical assistance, funded by PHARE. These two processes will bring more responsibility from the public institutions involved, and will increase their efficiency. Communication and transparency are older challenges for the public administration, which will be affected by the EU requirements to establish a permanent and open partnership with the society.

  Another major challenge for the time ahead is internalising the evaluation and monitoring capacity, to decrease dependency on external technical assistance, which is very expensive and does not favour institutional memory building. A first step is on-the-job training. A second one would be to gradually outsource from domestic research-evaluation-monitoring institutions. This step should not be seen as a second-best, but as a step towards an independent evaluation and monitoring capacity, managed by the private sector or by the non-profit one.

- Regarding the use of instruments, manuals, and procedures, only one MA has put in place a series of procedures, while the other MAs are only now drafting such procedures. Lack of procedures and of detailed methodologies, in connexion with the fragile structure of certain institutions, may represent a serious threat to the absorption process.

  We are convinced that the urgent formulation and implementation of procedures is essential to the efficient roll out of planning and programming processes. In addition, this can – at least in part – eliminate the effects of an amplified staff turnover and can directly contribute to enhance staff skills and professionalism.

  Many of the measures covered by operational programmes will comprise state aid-sensitive issues. This is a very specialised field and the involvement of the Competition Council is required starting with this programming phase.

By financial capacity we meant almost exclusively the credit risk evaluation methodology. From this perspective, as regards borrowing capacity, Romanian LGs are faced with a series of issues, both objective and subjective in nature. Regarding the non-structural issues, we would mention (for further scrutiny and adjustment):

- Lack of an independent audit and low quality of financial data.
- Inappropriate structure of financial reports for a credit risk analysis.
- Insufficient regulation of various infrastructure sectors.
- Arbitrary and non-customised leverage cap.
- Lack of legal provisions on LG insolvency.

- Still problematic enforcement of collateral.

Concerning the rather objective hindrances, they can only be tackled in time, either by the evolution of the overall economic, social and political environment:

- Little or no track record on LG repayment behaviour (no time series).
- Significant uncertainty regarding LG revenues (both own revenues and intergovernmental transfers).
- Political risk is still high.

REFERENCES

I Legislation

√ **România**

1. Law 151/1998 ammended by Law 315/2004 on regional development in Romania;
2. Law 500/2002 on public finance;
3. OUG 45/2003 on local public finance, with subsequent ammendments (Law 108/2004, Law 313/2004, OUG 9/2005);
4. Law 64/1995 on judicial reorganization and bankruptcy with subsequent ammendments (Law 192/2004);
5. Law 58/1998 on banking activity, with subsequent ammendments (Law 246/2002, Law 437/2001, Law 357/2002, Law 485/2003);
6. Law 213/1998 on public property;
7. Law 99/1999 on accelerating economic reform;
8. Law 215/2001 on local public administration, with subsequent ammendments (Law 738/2001, Law 216/2002);
9. Law 571/2003 on the Fiscal Code Codul Fiscal, with subsequent ammendments (last amendment - OUG 24/2005);
10. Law 313/2004 on public debt;
11. Law 339/2004 on decentralization;
12. Ordinul MF 94/2001 on harmonizing accounting standards with the IVth Directive EEC and IAS;
13. OUG 22/2002 (Law 288/2002) on payment obligation due by public institutions;
14. OUG 146/2002 on managing funds from State Treasury, with subsequent ammendments (Law 201/2003);
15. EU Accession Treaty of Romania and Bulgaria, 2005;
16. Complementary Position Paper for Chapter 21 – Regional Policy and the Coordination of Structural Instruments;

√ **European Union**

17. COM(2004) 101 final/2 din 26.02.2004: "Building our common future – Policy challenges and budgetary means of the enlarged UNION 2007-2013"
18. COM(2004) 487 final: "Financial Perspectives 2007-2013"

19. COM(2004) 657 final – "2004 Regular Report on Romania's progress towards accession";

20. Commission regulation setting out detailed rules in application of Council Regulation laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and Regulation of the European Parliament and of the Council on the European Regional Development Fund (COM (2005) 7979 of 12 April 2005);

21. Communication From The Commission To The Member States of 2 September 2004 laying down guidelines for a Community initiative concerning trans-European cooperation intended to encourage harmonious and balanced development of the European territory INTERREG III (2004/C 226/02);

22. Communication from the Commission to the Member States of 7 May 2001 "INTERREGIONAL COOPERATION", Strand C of the Interreg III Community initiative Commission communication C(2001) 1188 final, (2001/C 141/02);

23. European Commission, "Guide to the Cohesion Fund 2000-2006" (February 2000);

24. Proposal for a Council Regulation establishing a Cohesion Fund (COM(2004) 494 of 14 July 2004);

25. Proposal for a Council Regulation laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund (COM (2004) 492 of 14 July 2004);

26. Proposal for a Council Regulation on European Fisheries Fund (COM(2004) 497 of 14 July 2004;

27. Proposal for a Council Regulation on support for rural development by the European Agricultural Fund for Rural Development (COM(2004) 490 final of 14 July 2004);

28. Proposal for a Council Regulation on the financing of the common agricultural policy (COM(2004) 489 final of 14 July 2004);

29. Proposal for a Regulation of the European Parliament and of the Council on the European Regional Development Fund (COM(2004) 495 of 14 July 2004);

30. Proposal for a Regulation of the European Parliament and of the Council on the European Social Fund (COM(2004) 493 of 14 July 2004);

31. Proposal for a Regulation of the European Parliament and of the Council establishing a European grouping of cross-border cooperation (EGCC) (COM (2004) 496 of 14 July 2004).

32. Regulation (EC) No 1059/2003 of the European Parliament and of the Council of 26 May 2003;

II. Books, articles and studies

33. Boncea, M., Caraman, S., Stretean, S., Ştefancu, A. (2003) *Ghid de utilizare a OUG 45/2003 privind finanţele publice locale*, USAID

34. Caluşeru, G., Ghinea, A., Nicola, I., Stretean, S. (2003) *Local Government Borrowing: Regulation and Practice. Country report – Romania*, Institutul pentru Politici Publice

35. Camagni, R. (2004), "*Competitiveness and Territorial Cohesion: The New Challenges for EU 25*", paper presented at the 17th European Advanced Studies Institute in Regional Science, Split, Croatia, June 28 – July 4, 2004

36. Constantin, D.L., Folescu, A. (2004), "*The Impact of the EU Enlargement on Romania's Regional Policy: The Role of Structural Funds*", paper for the 44th Congress of the European Regional Science Association, Porto, August 2004

37. Cojanu V., Pîslaru D., Dima A., Stănculescu M., Muşetescu C. (2004) "*Specific requirements of the EU structural instruments and policy implications for Romania*". Pre-accession impact studies II, study no.6, European Institute of Romania, Bucharest

38. Crothers, J. D. (1995) "*Project Finance in Central and Eastern Europe from a Lender's Perspective: Lessons Learned in Poland and Romania*", McGill Law Journal, 41, pp. 286-295

39. DeAngelis, M., Căluşeru, G., Bulboacă, A. (2002) "*Creditarea şi finanţarea municipală în România – cadrul legal şi strategii în domeniu*", *USAID Policy Paper*

40. EPC/ECFIN/225/2004 - "*The structural challenges facing the candidate countries (Bulgaria, Romania, Turkey) – a comparative perspective*"

41. Filipiak, Ewa (2004) "*Les administrations publiques polonaises face aux fonds structurels et au fonds de cohesion europeens: Quelle capacite d'absorption a la veille de l'adhesion a l'union europeenne?*", DEA Aires Politiques Comparées, Europe post-communiste, Ecole Doctorale de Sciences-Po

42. Giosan, V., Tobă, M. (2004) *Politica de echilibrare a bugetelor locale in România – impactul aplicării OUG nr. 45/2003*, Institutul pentru Politici Publice

43. Gomez-Ibanez, J. A. (1998) "*Commitment and Flexibility: Strategies for Regulating Privatized Infrastructure*", working draft, Harvard University

44. Horvat, A. (2004) *Absorption problems in the EU Structural Funds. Some aspects regarding administrative absorption capacity in the Czech Republic, Estonia, Hungary, Slovakia and Slovenia*, National Agency for Regional Development of Slovenia

45. INS (Institutul Naţional de Statistică) (2004) *Anuarul Statistic al României* – 2003

46. INS (Institutul Naţional de Statistică) (2005) *Anuarul Statistic al României* – 2004

47. IPP & APD (Institutul pentru Politici Publice şi Asociaţia Pro Democraţia) (2001) *Bugetele locale între teorie şi practică*

48. Kehew, R. (2000) *Contractarea unui împrumut pentru a îmbunătăţi piaţa centrală din Focşani*, USAID/RTI, Programul privind Administraţia Publică Locală

49. Kehew, R., Giosan, V. et al (2001) *Manual de evaluare preliminară a credibilității financiare a autorităților publice locale din România utilizând indicatori financiari primari*, USAID/România, Programul privind Administrația Publică Locală

50. LABOUR ASOCIADOS S.L.L, (2003) "*Analysis of the impact of community policies on regional cohesion: Final Report*", DG REGIO, European Commission, Bruxelles

51. Molle, W. (1999), "*The Dynamics of Economic Integration and Cohesion in the EU: Experience from the Past and Challenges for the Future*", in Fischer, M., Njikamp, P. (Eds.), Spatial Dynamics of European Integration, Springer Verlag

52. NEI (2002), "*Key Indicators for Candidate Countries to Effectively Manage the Structural Funds; Principal Report, Final Report*", prepared by the NEI Regional and Urban Development for the EC DG REGIO/DG ENLARGEMENT, Rotterdam

53. NEI (2002a), *Key Indicators for Candidate Countries to Effectively Manage the Structural Funds; Country Reports,* prepared by the NEI Regional and Urben Development for the EC DG REGIO/DG ENLARGEMENT, Rotterdam

54. NEI (2002b) *Key Indicators for Candidate Countries to Effectively Manage the Structural Funds; Sectoral Reports,* prepared by the NEI Regional and Urben Development for the EC DG REGIO/DG ENLARGEMENT, Rotterdam

55. ÖIR in association with LRDP and IDOM (2003) *A Study on the Efficiency of the Implementation Methods for Structural Funds: Final Report*, Vienna

56. Peterson, G. E. (1998) *Measuring Local Government Credit Risk and Improving Creditworthiness*, prepared for World Bank

57. PMAI (Primaria Municipiului Alba Iulia) (2002) *Prospect- obligațiuni municipale*

58. PMB (Primăria Municipiului Bacău) (2004) *Prospect de ofertă publică primară de obligațiuni municipale emise de Municipiul Bacău*

59. PMT (Primăria Municipiului Timişoara) (2003) *Prospect Obligațiuni Municipale*

60. S&P (Standard & Poor's) (1997) "Behind the Ratings – Rating Local and Regional Governments in Emerging Markets", *Standard and Poor's CreditWeek*, August

61. S&P (Standard & Poor's) (1997) *Rating Regional and Local Government*, Global Ratings Criteria: Latin America

62. S&P (Standard & Poor's) (2003) *Public Finance Criteria*

63. S&P (Standard & Poor's) (2004a) *Central and East European Local and Regional Government*, Sector Review

64. S&P (Standard & Poor's) (2004b) *Research: City of Bucharest*, RatingDirect

65. S&P (Standard & Poor's) (2005a) *Central & Eastern European Local Government Review*, International Public Finance Ratings

66. S&P (Standard & Poor's) (2005b) *Western European Local & Regional Government Credit Survey 2005*, International Public Finance Ratings

67. Spofford, T. (2002) *Descentralizare fiscală, creditare municipală şi furnizarea de servicii publice în România – strategii pentru sprijinirea integrării politicilor de reformă*, USAID Policy Paper

III. Web resources

68. http://europa.eu.int/comm/regional_policy/ns_fr.htm.

69. http://europa.eu.int/comm/enlargement/index_en.html

70. http://europa.eu.int/comm/economy_finance/index_en.htm

71. http://www.mie.ro

72. http://www.mfinante.ro