

# **Selected aspects of local and regional development**

Daniel Klimovský, Katarzyna Radzik-Maruszak(editors)

Nova Gorica, 2012

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## INTRODUCTION

In the times of economic crisis that started in 2008 it is important to search for all possible solutions to restart the development in any possible way. In this sense one can differ two basic levels. One is national and it is mainly connected to the macro-economic and budgetary situation where systemic solutions are searched for. This level is burdened with international relations and international politics, different interests and capabilities of government to start right measures. In this manner Slovenia as well as majority of whole EU is from citizens' perspective failing for four years (most visible exemption is Germany and most visible fail is Greece). Despite general failure there is still long list of small local or regional successful stories which give us a hope that after all crisis can be micro defeated when society, economy and politics search for creative solutions and when they are avoiding stereotypical assessments made by geo-economics interests how to sell/buy some country or government for the lowest price possible. On the national level, we are mainly facing disintegration of solidarity and democracy excused by saving economic crisis situation. But on the local level there are often attempts which show how certain positive solutions can be worked out.

With this in mind School of Advanced Social Studies organised summer school on shaping of conditions of local and regional development under partial financing of the EU from European social fond within the frame of Operative program for development of human resources 2007-2013 and development priority 3 "Human resource development and life long learning, priority goal 3.3 ; quality, competitiveness and responsiveness of higher education. Project was initiated by, supported and belongs to longer term activities of POLLOC.EU initiative (Policy Making and Politics at the Local Level) which is responsible of promotion of local and regional development as main research focus in Central and Eastern European countries.

Uroš Pinterič, PhD.



# POLITICAL SYSTEMS AS GENERATOR OF LOCAL AND REGIONAL DEVELOPMENT

Michaela Bátorová<sup>1</sup>

## INTRODUCTION

When developing something – in this book it is a territory settled by people –, one usually focuses on specifying *what* to develop and *how* to develop it. The “what question” deals with clarifying one’s interests and needs of particular development object. The “how question” deals with methods and materials articulated in possession of technical knowledge and (human, financial, and technological) resources that one needs for accomplishing development objectives. These two preconditions are unconditionally framed by political system within which the exercise of development activities takes place. Political system is often defined as a set of institutions and interest groups, relationship between those institutions and the political norms and rules that govern their functions. In other words, based on particular set of values and beliefs shared in the society, political system defines distribution of formal powers (authority) between its members. Applying this definition to the topic of local and regional development, the political system determines which interests and needs are chosen as priorities in the development process, who is in charge of the development, or which resources can be used or are available for the development. Assuming that each nation state, region, or town and city has its specific interests and needs (due to specific geographical conditions, culture, socio-economic situation, demography, etc.) maintained by various set of institutions with particular authorities, it can be stated that *local and regional development* is a highly context-dependent process following a variety of different developmental paths in different territories and different time periods.

In relation to mentioned, there is no singularly agreed, homogeneous definition of local and regional development. Historically, local and regional development has been dominated by economic concerns such as growth, income and employment, and sometimes it was wholly equated with this relatively narrow focus upon *economic development*. Dissatisfaction with this technocratic, non-human approach caused emergence of alternative, more socially-oriented approaches to local and regional development. The pure economic focus was broadened in an attempt to address also social, political, ecological and cultural concerns (Pike, Pose, & Tomaney, 2007) – basic features shaping social system of a society. Recognizing social inequalities, promoting environmental sustainability, encouraging inclusive government and governance and

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recognizing cultural diversity have been emphasized to varying degrees within broadened definitions of local and regional development (Haughton & Counsell, 2004 quoted in Pike et al., 2007). This broader understanding of development, however, provides challenges in defining what the local and regional is, could be and should be. Since particular notions of development are socially determined by particular interests of groups in charge, in specific places and time periods, or particular political systems, the definition of and approaches to local and regional development have number of different alternatives. The most important is that the local and regional development focuses on improving the people's quality of life within the boundaries of social system and the questions of "what" and "how" are dependent on the combination of all the components framing that particular social system.

The purpose of this chapter is to compare briefly an assortment of European political systems – sub-system of the social system –, and discuss their potential for improving the quality of life of their citizens. The potential is discussed with reflection on four components of the political system: a) institutional component – defining the main formal actors involved in local and regional development; b) regulative component – defining the formal competences – authority to conduct local and regional development, c) ideological component – defining the set of values prevailing in the political system and d) functional components – defining the character of political regime. For illustrative purposes, the focus is on employment strategies as one of the objectives in the sustainable development of the countries in the European Union.

Data for the comparison of different European systems are taken from the secondary sources – official documents, reports, and comparative researchers.

In the first part, general characteristics of the political systems are presented. This section is followed by four descriptive sections with specification of components of the political system. These general characteristics are enriched by empirical examples from the European Countries. In the last section, the general conclusions are provided.

## **BASIC CHARACTERISTICS OF THE POLITICAL SYSTEMS**

According to Parsons, political system is one of the sub-systems of the social system (the other sub-systems are economic, cultural, and legal). Political sub-system ensures function of generalization, which helps to define goals and objectives, mobilize resources and energies in order to achieve social goals and determine priorities between them.

For surviving, political system needs five basic features:

- a) **components** – having institutional, regulative, ideological and functional character;
- b) **relationships** – short-tem, long-term, bilateral, multilateral, cooperation, confrontation, etc.);
- c) **environment** – it is defined by boundaries and it is separating it from the

internal and external environment of the society; the external environment of the political system is formed by other sub-systems of the social system, political systems of other states, and natural environment of other society;

- d) **interactions** between all the components of the political system, but also between the political system and its external environment;
- e) **reaction** on inputs and outputs, which may cause changes in the political system or in the external environment. This change may have quantitative or qualitative character. The qualitative change is followed by striking jump, dramatic, turbulent, or revolutionary events (e.g., replacement of the non-democratic by democratic political regime). The quantitative character is accompanied by incremental, evolutionary process in order to achieve change in the potential of the political system (e.g., increment or decrement of institutional components, etc.) (Barát, 2005)

For the purposes of the local and regional development the most important features of the political system are the specific combinations of group of components and their mutual supplementation, because they create specific character of the political system of particular nation-state. Therefore, in the rest of the paper, via those institutional, regulative, ideological and functional components I will discuss the potentials for the local and regional development.

#### *INSTITUTIONAL AND REGULATIVE COMPONENTS*

The institutional components represent mainly organs of the state (national) and sub-national (self-) government, interest groups and initiatives. The state organs and organs of the self-governments dispose with various competences, apply horizontal and vertical distribution of powers and mechanisms of control, and assure governance of public affairs in its authority. This distribution of powers is normally legitimatised by regulative component which determines boundaries of desirable and respectable behaviour of individual institutional elements. In their sphere of action, regulative components control expected behaviour and they have various legal power and character (Barát, 2005). According to this we distinguish following regulative framework:

- a) international agreements – for example, the state organs and state are bounded by international duties (agreements about EU, super-ordination of the European law over the national law, etc.)
- b) national legal norms (constitution, laws, departmental regulations, orders, etc.);
- c) statutes and memorandums of the civic associations;

In practice, the institutional components together with regulative framework, applied on various governmental levels, can be determined from three perspectives. From the first perspective, they determine whether decision-making organs (either state or sub-national government) can freely act in implementing their assigned competences, or they have to follow strict instructions from above. For example, even if in some countries the local



governments are in charge of delivering pro-employment services, in the constitution, departmental regulations or orders, the state or other superior organ may regulate the content or the extent of the services. For example, the state can define how much money local governments can use for those services, which target groups have to be prioritized, or which activities are eligible for financial support. The regulations may also treat whether certain services are implemented on the obligatory or voluntary bases, or whether some services have original or decentralized characters. Thus these frameworks define the degree of autonomy exercised by specific public organs and hierarchical relations between various governmental levels. In the literature this autonomy and the relations are often studied by analysing vertical (central-local) power relations. From the second perspective, the institutional and regulative components also outline who exactly from within the (sub-national) governmental body is responsible for particular functions – for example, either elected political representatives have full charge in deciding how the local and regional development would look like, or the non-elected civil servants are given a big power to shape the character of the development. This distribution of responsibilities is often studied via analysing horizontal (intra-governmental) relations. From the third perspective, the institutional and regulative components adjust relations between the governmental bodies and citizens by specifying (inter alia) selection of the local representatives who are supposed to carry and defend the developmental interests and needs of its electorates. The selection process of local representatives predetermines whether politicians are directly or indirectly accountable for their decisions, or citizens' ability to influence the developmental decisions affecting their lives. In the following sections, these three perspectives on institutional and regulative components of political systems are elaborated in reflection to different political systems applied in EU.

### *POLITICAL SYSTEMS BASED ON THE STATE STRUCTURE*

Analysis of the political system usually starts on the highest – nation-state – level. Depending on the character of the supreme decision-making body, governing the assigned territory, in general we recognize two types of political systems – authoritarian and republic. The authoritarian system refers to the concentration of powers to the hands of one person or a small group of decision-makers. Traditionally, monarchies are the most common representatives of this system. Important feature of this system is that the leadership is transferred by the means of heredity. Recently, monarchies in the Europe have a character of constitutional monarchy, which means that the monarch does not influence the politics of the monarch's country; rather it fulfils the role of ceremonial leader. The executive and political powers are usually devoted to the elected parliament and government. There are seven constitutional monarchies in the European Union (Belgium, Denmark, Luxemburg, the Netherlands, Spain, Sweden, and United Kingdom). The other members of the European Union apply republic as their political system. According to the Free Merriam-Webster dictionary republic is a government having a

chief of state who is not a monarch and who in modern times is usually a president. Republic often refers to the government in which supreme power resides in a body of citizens entitled to vote and is exercised by elected officers and representatives responsible to them and governing according to law.

In both (constitutional) monarchy and republic the governing powers are further distributed between other – sub-national – decision-making organs for better reflection of the local interests and needs. In this respect, we can recognize three types of the states: unitary, federal and confederal (quasi-federal) states. Most of the European Union's member states are unitary states. That means that most of the competences lie with the central government and only minor or local issues are within the authority of sub-national governments (regions, provinces, counties, districts, or municipalities). Three states are federations (Austria, Belgium and Germany) of states or regions with equal competences, and seven other states have confederal (quasi-federal) character (Denmark, Finland, France, United Kingdom, the Netherland, Spain, and Italy) with devoted competences to regions or autonomous areas. Not surprisingly, this different territorial distribution of authorities among the European member states has several reasons. Often specific historical events, natural conditions, size of the country, or requirements connected to the European Union regulations participated in miscellaneous nature of the member-state structures.

In relation to the local and regional development, these general characteristics of political systems implemented in the European member states could determine, that in the constitutional monarchies the parliament with its president are in charge of setting the character of the local and regional development; in the republic the parliament or the president (or both) have the overall responsibility; alternatively, in the unitary states these authority is centralized, while in the federal and quasi-federal states the autonomous regions or autonomous areas take the lead in local and regional development. This would mean that this development has mainly centralized (or region-centred – as for example in Spain) character.

However, the current comparative studies, analysing the distribution of competences for local and regional development, show that local and regional (self-) governments (also in the unitary states) play very strong role in this development process. This trend is supported also by recent decentralization actions guided by stronger democratization of political systems – bringing citizens closer to the decision-making about their public lives and improving the often criticized inefficiency and inflexibility of overloaded state bureaucracy.

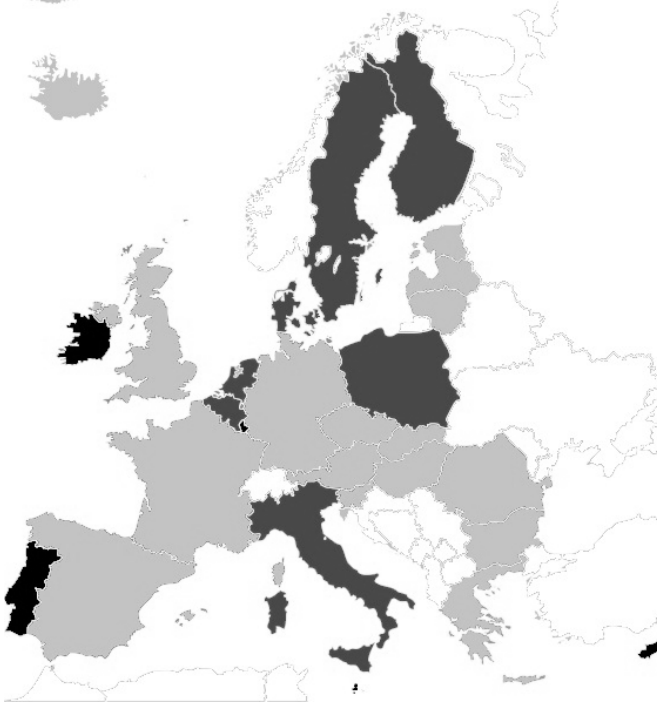
Monné (2004) provides several arguments towards keeping the role of local and regional governments strong in dealing with local and regional development activities in general and employment strategies in particular. Author mentions that the success in the fight against the unemployment in Europe is “dependent on the mobilisation and support of all resources available, including, and especially, at regional and local level. For it is

localities that are best placed to translate national and regional strategies into action on the ground. And are local actors that best understand local conditions, aspirations and needs,” (Monné, 2004: 2). Monné further stresses that it is at local level that the potential for job creation can be tapped. It is at the local level that education and training is organised, developed and delivered. And it is at the local level where services are provided to help integrate the most vulnerable into our societies.

“Thus, local authorities are among the most important players in the development of employment at local level. As the first level of democratically elected government and thus the level closest to the people and the local economy, local authorities clearly have an important role in developing partnerships to promote employment that bring together all the local public and private players. Local authorities have powers in many areas that are potential sources of new jobs, so their actions are likely to structure a considerable portion of the local labour market.” (Monné, 2004: 2-4).

Unfortunately, it seems that most of the European member states have not taken into the consideration Monné’s suggestions for decentralization of competences related to the employment strategies. According to the data gathered by the Council of European Municipalities and Regions (CEMR), in year 2011 only in Belgium, Denmark, Finland, Italy, Netherlands, Poland and Sweden the sub-national governments (either local and/or regional authorities) are explicitly responsible for the employment policies in their territories (CEMR, 2011). On the other hand, in Cyprus, Ireland, Portugal Luxembourg, Malta and Portugal, the sub-national governments do not take responsibility for employment services or services related to it. In the rest of the member states, it is difficult to define if they do or do not have competences for applying employment strategies, because these activities might be included within the category of social services, social protection, social welfare or local and regional development. Some sub-national governments might exhibit the employment strategies also within the economic development functions.

Picture: EU member states based on the delegation of competences related to the employment strategies.



Notes: In countries with dark grey colour, the sub-national governments are explicitly responsible for activities fostering the employment. In countries with black colour, the sub-national governments are not responsible for those activities. And in countries with the light grey colour, sub-national government might be responsible for discussed activities via other more general functions (social services, social welfare, local and regional development, etc.).

One of the ways how to investigate the reasons, why only few local governments in the European Union are directly responsible for employment strategies can be searched in deeper analysis of the central-local (vertical) relations.

### *POLITICAL SYSTEMS BASED ON VERTICAL RELATIONS*

Vertical distribution of powers between the central and local governments, or determination of the local governments' autonomy let several researchers to define various models of central-local relations in EU countries. For example, Robert J. Bennett in 1993 distinguished European nation-states in the following three groups:

- The Napoleonic *fused system* was typical for most west European unitary and quasi-federal states. The provision of services is decided by local as well as upper-level governments and Mayor (head of the local government) takes the overall responsibility for implementation of these functions. The “new

democracies” from the Central Eastern Europe were classified as moving towards this system. In accordance to the previously mentioned map (Picture 1), sub-national governments of some countries within this group are explicitly responsible also for the employment strategies (e.g. Italy, the Netherlands, or Poland); majority of them (with high probability) exercises those strategies as part of other general social policies (e.g. Slovakia, Greece, or France).

- The Anglo-Saxon *dual system* with detached state hierarchy was typical only for Britain and Ireland. The central government agencies and municipalities existed on the local level side by side but with different competences providing for the powerful local executive boards or committees a relative freedom in delivery of services. The state, however, kept overall supervision of the local functions. Therefore it is not surprising, that according to previously mentioned results the local governments within these countries are not responsible for employment strategies.
- *Split hierarchy systems* or mixed systems were typical for Nordic countries, where the state kept the dominance as described in the fused systems, but the executive powers were in the hands of collective bodies, which were expected to coordinate, supervise, and develop major strategies. This is reflected also in the results from the previously mentioned map, that all the sub-national governments in Denmark, Finland, and Sweden are responsible for employment strategies.

Slightly different approach to analyse central-local relations presented Hesse and Sharpe (1991). These authors came up with three governmental groups in Europe: Franco group (Spain, Italy, France, Greece, Belgium, and Portugal), Anglo-Saxon group (UK, Ireland, Canada, New Zealand, Australia, and partly USA) and the North and Central European group (Scandinavia, Germany, the Netherlands). Similarly to their colleague, Hesse and Sharpe also focused on the distribution of competences between the state and local governments, but they added factor of political influence of the local level in relation to upper-level government.

Results of their study showed that fewer competences (smaller authority) the local government had, the higher involvement of “politics” was needed for the run of the municipality. For example in the Franco group, municipal representatives focused more on building or maintaining the community identity, while leaving management of services to the upper level governments. For ensuring particular local interests, municipal political representatives were expected to be good negotiators at the higher governmental level, which consequently empowered their position on the local governments. In the Anglo-group, local governments had weak legal and political role, but they played important actors in delivering public services. Therefore, functional role dominated over the political one, which was enabled also by quite high local government discretion. In addition, weak position of political leaders left room for bigger visibility and involvement

of executive officers in the run of the municipality. Hence, even if the British or Irish local governments are not responsible for politically-driven creation of employment strategies, they play very important role in their implementation.

Finally, for the North and Central European group was also typical big amount of assigned services and high level of autonomy. This one, however, was assured also in the constitution. Consequently, in comparison to the previous groups, municipalities in the North and Central European group had better possibilities for acting as political entities, which put political and executive (administrative) officers on relatively equal level of influence. This means that Nordic local governments seem to have full autonomy in creating and also in implementing strategies for employment policies in their territories. However, it needs to be reminded, that even if the constitution guarantees the local government autonomy and the local governments are the main providers of public services, the state administration often keeps tight control over the egalitarian approach to the provision of services and dictates the conditions under which these services should be implemented (Finland is a very good example, see Haveri, 2009).

Hesse and Sharpe did not include post-communist countries to their comparison. Additionally, both mentioned typologies were created prior to the fundamental changes in central-local relations – before the decentralization movement; therefore, their applicability in current circumstances might not be appropriate anymore. Although, in reflection to the current data about the distributed responsibility for the employment services (CEMR, 2011), this typology still has its significance.

In their relatively recent comparative study, Heinelt and Hlepas (2006) tied-up on shortcomings of all previously discussed studies. Authors created an updated typology containing among all Western countries also some countries from the Central Eastern Europe (Hungary, Poland, and Czech Republic). Their main inspiration was Hesse and Sharpe's model, though as comparative indicators authors focused on a) whether local governments provide social services, b) what is the financial autonomy of municipalities, and c) what is the level of municipal public spending measured by its proportion of GDP.

Heinelt and Hlepas's analysis confirmed the Hesse and Sharpe's division of Western countries between the old three categories (though probably due to recent governmental reforms Belgium and Italy are now closer to the Anglo-Saxon countries, rather than to the Franco group). Interestingly enough, after few years of transformation from the communist to the democratic regime, Czech Republic seemed to incline now more to the Franco group, Poland to the Anglo-Saxon group and Hungary to the North and Central European group. This acknowledges what some critics were pointing out, that many post-communist countries might not move only towards the Bennett's fused systems, rather they will transform with more divergent patterns. And the current reality shows that decentralization of functions, level of discretion (autonomy), territorial structures, electoral systems, as well as actual management of (social) services all became very heterogeneous in this post-communist world (see Baldersheim, Gejza, Horváth, Illner, &

Swianiewicz, 1996; Swianiewicz, 2005; Klimovsky, 2009; Swianiewicz, 2010). Also in relation to the employment strategies or responsibilities for their provision, the differences are visible. For example, only in Poland, this responsibility is explicitly assigned to the sub-national governments (inter-mediary and regional level); in Hungary only the local level and in Romania only the regional level are responsible for the territorial development policies (within which are expected to be treated also employment strategies); or in Slovakia and Czech republic both local and regional governmental levels are responsible for the territorial development policies, while in the rest of the post-countries (Bulgaria, Estonia, Latvia, Lithuania, Slovenia) only the local governments deal with social policies, because the regional level does not exist. Thus, even if the CEE countries share the same history and similar cultural patterns, their recent development, reflected in taken political decisions about the character of the implemented political systems – especially its regulative components, varies significantly.

One of the explanations why these differences between EU countries are so significant, and why the development has taken different paths (even if the European Union strives for unification of the political systems of the member states) could be found also in identifying those who were responsible for taking certain political decisions and those who have the biggest influence on the character of those decisions. Thus in practice, it is necessary to identify who has the biggest and the loudest voice in defining development priorities, whether political interests prevail over the technocratic ones or vice versa and what kind of relations are between the political leaders and citizens or how citizens can influence their own lives. Thus, it is not enough to describe only the government's formal position and role towards the other administrative organs (or other members of the political system), but it is important to uncover also particular intra-governmental (or politico-administrative) relations within the walls of the political body and with the outside world. The following sections thus elaborate the second (horizontal relations) and third (selection process of leaders) perspectives in describing institutional and regulative components of the political systems. The main focus is on sub-national governments since they have big importance on local and regional development in currently quite decentralized nation states, as mentioned earlier.

### *POLITICAL SYSTEMS BASED ON HORIZONTAL RELATIONS*

Due to already discussed heterogeneous distribution of competences between the state and sub-national authorities, the approaches in defining intra-governmental relations in sub-national governments are more complicated and still without one generally accepted typology. One of the first scholars elaborating the intra-governmental relations at local governments were Mouritzen & Svava (2002). Authors were interested in different power relations between Mayor, council, and municipal administration – constantly present elements in municipal organization. They wanted to show to what extent is the council

controlled by one or more political actors and to what extent is the control over the executive in the hands of one or more political actors. Thus, by analysing 14 different governmental systems, authors created four governmental models: a) the strong Mayor form, b) the committee-leader form, c) the collective form, and d) the council-manager form.

- For the strong Mayor form is typical “elected Mayor who controls council and is legally and in actuality in full charge of executive functions. The head of the administrative office serves at the Mayor’s will and can be hired and fired without the consent of any other politicians or political bodies. The Mayor can hire appointees to help with any functions. Countries in this group are Spain, Italy, France, and Portugal (with Mayor-council governments).
- In the committee leader form, one person is clearly “the political leader” of the municipality – with or without the title of Mayor. He or she may or may not control the council. Executive powers are shared. The political leader may have responsibilities for some executive functions but other will rest with collegiate bodies, which is, standing committees composed of elected politicians, and with the head of the administrative office. Countries in this group are Denmark, Sweden, and UK.
- The collective form is represented by the central decision-making collegiate body - the executive committee, which is responsible for all the executive functions. The executive committee consists of locally elected politicians and the Mayor, who presides. Countries involved in this group are Belgium, and The Netherlands.
- In the council-manager form, all the executive functions are in the hands of a professional administrator – the city manager – who is appointed by the city council, which has general authority over policy but is restricted from involvement in administrative matters. The council is a relatively small body, headed by a Mayor who formally has presiding and ceremonial functions only. Countries representing this group are Finland, Ireland, and Norway (Mouritzen & Svava, 2002, p. 55-63).

In connection to previously discussed central-local relations, and by comparing the distribution of countries within above described four categories one can observe one important attribute: countries with weak local government units (countries from the Franco group) seem to have strong political leaders not only due to requested strong relations with the upper-governmental authorities, or thanks to their societal function of “identity builders” (Stoker, 2011), but also due to the institutional system shaping the intragovernmental relations. In comparison to the other groups of countries, this system provides most of the formal powers to individual political leaders, who have a possibility to perform one-man (political) leadership. This means that these political (elected) leaders have strong authority to decide how employment strategies (either they are fully



created on the state level or upper-governmental levels, or this function is directly delegated to the local authorities) will be implemented without a strong intervention from the collective decision-making body or (non-elected) civil servants.

On the contrary, in countries with strong independent communities (countries from the North-Central Europe) whose societal function is mainly to assure “welfare” system (Stoker, 2011) the attention is not on defining strong formal powers for political leaders, but on providing enough executive authority to executive (administrative non-elected) leaders. These executive leaders have also possibility to perform one-man (professional) leadership. That means that even if the collective decision-making body creates (employment) strategies and define priorities, the administrative leaders can and often are expected to contribute to and influence the character of those (employment) strategies as well as their appropriate execution.

In the middle categories, one can find countries which are typical service providers (Sweden, UK, Denmark, the Netherlands), but the influence of politicians is as significant as the influence of civil servants, since politicians play important role in executive functions. The main distinction in these “in-between” categories is that instead of individual (one-man) leadership, the leadership of collective decision-making bodies dominates.

Mouritzen & Svava’s typology gained honours by number of citations and in the following years, it became a base for other comparative studies dealing with the intragovernmental relations (Steyvers, et. al. 2005; or Bäck et. al. 2006; Berg, 2006). A well as in the previous cases, one of the critiques, which this study received, is that it does not reflect the recent changes in studied local governments; hence, it is only a static description of the status quo in studied cases. In addition to this, it does not include all the countries of the European Union for the comparison (Heinelt and Hlepas, 2006); therefore, it might not cover all the nuances of not included – mainly Central Eastern European – countries. In addition, in the description of particular governmental forms, authors do not reflect on different ways of Mayoral selections, even if they possess those kinds of information. However indicators provided by Mouritzen and Svava can be applicable to any country, and in case other researchers applying these indicators find some significant deviations from this model, this can only enrich the knowledge of different governmental systems.

There is also Wollmann’s (2004) study focusing on the intra-governmental relations of local governments. Author deals with the distribution of legislative and executive functions between municipal organs and consequently defines two different governmental models: monistic and dualistic. In the monistic model, the council is regarded as the only decision-making body and the local administration acts under the instruction and scrutiny of the council without own decision-making powers. This model is typical for Britain and Scandinavian countries (Wollmann, 2004, 2008). In contrast, in the dual model, the decision-making powers are shared between two main actors: Mayor and the collective

body. Collective body is ‘recognized as the prime decision-making body of local government, but the head/chief executive of the local administration is seen as possessing some (‘executive’) decision-making powers of his or her own that are not derived from the local council. This system is typical for continental Europe – represented by France and Germany (Wollmann, 2004: 151, and 2008: 283), but also Slovakia, Spain or Hungary. Although this typology interestingly deals with basic division of politico-administrative functions in local governments, unfortunately this distinction between the monistic and dualistic system is not always very clear in practice. This is especially in case when the executive functions are spread in various forms of committees; or in the dual model, when the council intervenes to the work of administrators by which it actually exercises the executive functions (Heinelt & Hlepas, 2006).

### *SYSTEMS FOR SELECTING (LOCAL) LEADERS*

The third perspective to the institutional and regulative components focuses on the selection process of the main local representatives – those who take the overall responsibility over local or regional development decisions. The selection process of local leader is a very important feature defining leaders’ position and role in the organization as well as leaders’ relationship with and accountability to electorates. It defines the creation of virtual connections between those who are in charge of selection and the one how is selected. In practice one can usually recognize three basic models of leaders’ selection in European local governments: direct election, indirect election by a collective organ, and process of appointment by higher governmental authority. Each of these models has its positive as well as negative features, though in the last decades many countries, originally with indirect elections, have turned their attention to the implementation of direct (Mayoral) elections model. In the following paragraphs I will focus on description of these two models.

#### *Indirectly Elected Leader*

Practice shows that usage of indirectly elected leader model varies in many countries. On the municipal level, it can be found in the “old” European countries (Spain, Denmark, France, Finland), but also in the “new” European democracies (Czech Republic, Latvia, or Malta). This model requires consensus among councillors who elect their leader to the leadership position. In case the consensus is not reached, other (most-likely governmentally higher) authority appoints the incumbent to this position. For example in the Czech Republic, director of the regional office appoints from among the employees of this office an officer who becomes responsible for guiding the municipal administration. In France the situation is similar, but here the prefect from the state administration defines who will be in charge of the run of the municipality. Specific situation is also in Spain. Here the law says that if the municipal council is not able to reach consensus,

Mayor becomes the one who leads the political party with the most seats in the municipal parliament. The same system applies for the state government.

In principle, members of the collective representative body select leader from among themselves. However, one can find also countries where selected leader is not member of this collective organ. Typical example is from Poland (before the implementation of the direct Mayoral election), where Mayor was selected by the executive board (rada gminy) from among its members or from among citizens (Klimovsky, 2009).

Also the selection procedures for choosing the leader vary quite much. Principle of simple majority is used for example in Ukraine, or in France (if the Mayor is not selected in the first two rounds during which the absolute majority is used) (Copus, 2006). Absolute majority is needed also in Denmark, and qualified majority was before needed in Poland.

One of the most positive features of indirectly elected leader is a lower possibility to select incompetent leader. Most of the candidates have assured at least some political skills gained by affiliation to the political party which nominated them. That means that it is expected that the leader would also foster interests and reflect on needs, which the representatives of certain political party presented in their electoral programs. If the candidate is selected from among non-councillors, then it is expected that he or she has some professional experiences in leading the governments. In addition, this model also enables that leader has strong connection with governmental collective organ, which assures that leader can find support among the majority of councillors in enforcing his or her policy proposals. However, the same feature is also a drawback, because it can yield to the situation when leader is just a ceremonial figure with set of responsibilities controlled by the powerful political party which is through this leadership position enforcing its political interests in more heterogeneous governments without taking direct accountability for its decisions.

#### *Directly Elected Leader*

The models of directly elected leader enable citizens to directly vote for their political master in elections. Candidate who obtains the biggest number of votes wins the battle. During last two-three decades, many countries (e.g. United Kingdom, Austria, Switzerland, or Hungary) implemented this system (Klimovsky, 2009) on the local level as an alternative to the indirect or the appointment model of creating Mayor's position. The most important reason for applying this model is requested growth of legitimacy of leading politician in connection to citizens (Swianiewicz, 2005). In addition, many countries applied this model in order to improve the efficiency of decision-making practices while transferring number of executive responsibilities to Mayor's hands. Powerful executive leader is often considered as a means for providing better management of local and national affairs and more effective representation of the local community (Fenwick & Elcock, 2005). However, what is often missed, this model tends to diminish position of (municipal) councils composed of representatives of various

political parties (Magre & Bertrana, 2007: 191) in which the plurality of options is often restrained. Thus, there is a threat that needs and interests of many inferior groups of people might not be heard off.

From the leader's position point of view, this model of directly elected leader has also some negative characteristics. The first one is mostly related to the possibility of electing "incompetent" person (Klimovsky, 2009). It comes from the assumption that the affiliation to the political party does not play a significant role in the elections (e.g., according to the communal elections in year 2006, 30% of elected Slovak Mayors were independent candidates). In this sense, citizens elect leader mostly based on other, more personal indicators). Thus, this may drive to the situation when citizens may elect person only based on good "marketing skills" (charisma, populist visions, good communication skills, expected ability to fulfil citizens' needs, expected ability to implement presented visions, etc.), but political or managerial skills needed for fulfilling all the administrative and political tasks are not guaranteed (for further discussion see Copus, 2004).

Alternatively, the second problem related to leader's direct election, is that the collective decision-making body (e.g., municipal council) does not need to accept newly elected leader. Direct elections do not guarantee political majority in the council. Thus, when leader has to face a big opposition in the council it might strongly weaken his or her, otherwise, very strong formal position. Such circumstances can consequently harm the overall run of the state or the municipality. In the worst scenario, there might be a constant pat situation, when leader is not able to pass any of his or her proposals and in turn, he or she might not be willing to sign any of council's proposals. The only solution for this situation is probably leader's abdication.

In spite of several negative features of directly elected leaders, Copus (2004) mentioned that this system makes "the politics in some areas uncertain and exciting, but the democracy has become more encompassing and inclusive" This representative democracy entailed to direct accountability to citizens, which is assured in the model of directly elected leader, is often lacking in all the other electoral models.

It is evident that central-local, intra-governmental relations and the selection process of its leaders from the comparative perspective provide more specific information about who is charge of local and regional development and in which degree this associated activities can be executed in a sovereign or dependent way. It also show where the citizens can apply their requests, or with who the non-governmental actors, civic associations and private business can negotiate their local and regional development projects.

But the political system is not only about the distribution of formal powers between various organs. Political system is also about determining the ideologies, expressed by selection of specific priorities of interests and needs in the development process. These ideologies represent another component of the political system.

## *IDEOLOGICAL COMPONENTS OF THE POLITICAL SYSTEM*

Ideological components represent specific ideologies, which they take part in the creation of public opinions and influence the selection of particular political goals, tools and mechanisms. Ideology is a set of opinions and conceptions about the world. According to Marx, it is a blurred picture of the reality. According to Weber, it is a tool of those in power for manipulating the masses (Barát, 2005).

Political environment of the European Union is influenced and shaped by following five ideologies:

- liberalism – freedom and political, economic and social responsibility for everybody without exceptions is a core motto of the current liberalism. Political parties, which follow this ideology, strive for achieving: decreasing the state expenditures, decreasing the taxation, developing privatization, cancelling minimal salary, cancelling barriers on the labour market, privatization of the state companies, etc. According to liberals, invisible hand of the market will arrange everything and the state should behave only as watchdog and to individual social spheres should intervene as little as possible.
- conservatism – is an ideology, which strives to secure traditional values and pillars of the society. In political life, conservatism situates in a role of defender of:
  - traditional historical values and not rapid changes
  - public interests and not interests of the individual
  - the state and state institutions as a protector of the citizen and creator of the legal framework (the division of power is unavoidable)
- socialism – is an ideology defending collective ownership of produced product, control of the entire production, distribution and trade as a fair means on the participation on the national wealth. It stresses a social function of the state, position of the state as a strong organization, supports socially oriented economy, preferring interests of the entire society before the interests of the individual, etc. In practice, socialism is performed in two streams:
  - socio-democratic stream;
  - communist stream – with more radical values;
- Nationalism – it is an ideology preferring interests and needs of concrete ethnic group and by following this optic, it judges and evaluates all the relations with other ethnic groups.
- Catholicism – it is an ideology emphasizing authenticity and correctness of Christian conceptions, values, and ideals, trying to subordinate the secular society under the Christian religion.

In the current political spectrum in European member states, it is hard to find a political party, which would strictly follow principles of one of these mentioned ideologies. Instead, we can find a combination of various values, and approaches, helping the

political parties to grasp the needs and interests of their electorate. Very common are political parties following conservative socialism, social conservatism, liberal socialism, or social liberalism, etc. Such diversity of ideologies and associated values can predict that also approaches to local and regional development and employment strategies are very diverse. Social democratic parties might support stronger control over the creation of employment strategies and their implementation, while social liberals might be more willing to let the market decide about the most appropriate tools and mechanisms for solving the unemployment problems. Moreover, taking into the consideration fact, that many European countries follow the multi-party system<sup>2</sup>, the government strategies thus needs to search for compromises, which would satisfy the interests of (at least the) governing majority.

### *FUNCTIONAL COMPONENTS OF THE POLITICAL SYSTEM*

The last components of the political system are the functional components. The functional components are the models of political activity, which creates political regime. They take into the consideration political traditions and cultures. Political regime is in general defined as a means, by which the society deals the relationship between those who govern and those who are governed.

As examples of this group of components, the literature refers to the usage of political consensus, confrontations, or conflicts among the political actors. In other words, the functional components treat also the decision-making styles prevailing in particular political systems.

### *POLITICAL SYSTEMS BASED ON FUNCTIONAL COMPONENTS*

One interesting typology focusing on decision-making practices in local government is Bäck's (2005) typology. Bäck used Wollmann's typology for describing "new" political systems, which combines and compare monistic versus dualistic organizations with a majoritarian versus consociational (power-sharing) form of democratic decision making. In very general terms, for majoritarian decision making is typical that decisions are based on the principle of majority rule – a solution attracting the majority of participants wins. On the contrary in the consociational decision-making process, participants are trying to achieve consensus by any means. The Bäck's typology is additionally mirrored with the Mouritzen and Svava's governmental forms and it is valid on the local as well as state-governmental level:

- "Assembly Government: is presented by situations where executive power is in the hands of a proportionally composed committee of the council, i.e. monism in combination with consociationalism. This is very close to what Mouritzen

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<sup>2</sup> See: [http://en.wikipedia.org/wiki/List\\_of\\_ruling\\_political\\_parties\\_by\\_country#5](http://en.wikipedia.org/wiki/List_of_ruling_political_parties_by_country#5)

and Svara term ‘the committee leader form’. According to Bäck, countries within this group are Sweden, Norway, Britain and Poland (before the implementation of direct Mayoral elections);

- **Parliamentarism:** is a combination of monism with majoritarianism, i.e. situations featuring a collective executive, appointed by the council not using proportional techniques but some variations on the majority principle. Mouritzen and Svara would probably also classify the parliamentarism as ‘committee leader form’. Countries in this group are Denmark and the Netherlands;
- In presidentialism there is a separately elected Mayor, appointing his own cabinet of deputies without consideration of the party-political composition of the council. In this form the dualistic and majoritarian principles are combined. Countries in this group are Italy, Greece, New Zealand, and Poland (after the direct Mayoral elections);
- In semi-presidentialism the Mayor is surrounded by a council-appointed collective executive. Here the dualism is combined with consociationalisms or majoritarianism depending on how the collective executive is appointed by the council. This model strongly reminds Mouritzen’s and Svara’s strong-mayor form,” (Bäck, 2005: 82-83). According to Bäck’s findings Germany is the main representative of this group.

This description shows, that by his typology, Bäck did not cover two of the Mouritzen and Svara’s model: council-manager form and collective form. However, the author claims that both forms could be included under “parliamentarism system” (see Bäck, 2005: 87). Another shortcoming of Bäck’s model is that majoritarian and consociational types of decision making do not only depend on the formal (legal) rules laid down in the municipal constitution or local governmental acts. Rather, they depend on, “a socially determined and locally embedded ‘logic of appropriateness’ or even a pragmatically driven political ‘logic of consequentiality’, taking certain actual local (power) constellations into account,” (Heinelt & Hlepas, 2006, p.30). Thus, it happens that in municipalities where one would expect consociational decision making, local representatives can follow principles of majoritarian decision making; and in municipalities where one would expect majoritarian decision making, local representative can drive for consociational solutions depending on the situation.

## CONCLUSIONS

Political systems in Europe differ. These differences are based on set of components framing the environment of the political system. The institutional components define various structures, distribution of powers and control over public affairs; regulative components define various regulative frameworks within which the political organs can

exercise their assigned competences; ideological components provide miscellaneous nature of visions, objectives, and priorities of the political system shaped by specific values and beliefs of those in power; and functional components determine political regimes – decision-making styles – used by those in charge.

All these components in combination with other economic, cultural, geographical, legal, or social systems create endless variations in the character of implemented local and regional development as well as potential for that development. For these reasons, there is not one universal and objective model of local and regional development or a priority in employment strategies which should be developed first. Rather politicians (either on the national, regional or local level) are required constantly to deliberate, negotiate, or compromise opposing priorities. And instead of top-down ordering, process of governance – inter-governmental coordination, decentralization and multi-level institutional structures – is an essentiality in achieving development with a potential of improving the quality of life of its citizens. Thus, when talking about political systems as generator for local and regional development, we have to start the discussion with two words: “it depends...”.

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## LOCAL POLICY MAKING: ACTORS AND TOOLS

Daniel Klimovský<sup>1</sup> and Zuzana Lackova<sup>2</sup>

Regional level and local level represent the political levels which tend to be underestimated in comparison with national and international levels. More or less it is only the matter of approach not regarding even the theoretically specified hierarchy of relatively independent on one side but full value levels of politics on the other side, neither the political reality considered as the basement of high heterogeneity. All the mentioned political levels are interrelated with the key words of this chapter. Its main goal is to theoretically introduce basic political issues related to regional and local development; issues related to policy actors and policy tools in particular.

### POLITICAL DIMENSIONS ON REGIONAL AND LOCAL LEVEL

Politics as societal phenomenon exists at all the levels of the social life. On the one hand it is presented as an object – an object of scientific inquiry, called political science or politology, and on the other one it functions as social reality being changed in time and space whether it is or not inquired.

While speaking about the politics as about social phenomenon presented at all the levels of social life (Pinterič 2009), then the highest level of politics is the international level. Politics is presented by more levels within the particular state forms. It is possible to state there are these political levels with the state forms:

- federal level;
- national level;
- regional level;
- local level.

Federal level is the highest level of politics within the state form. It is the politics which refers to several independent (totally or partially) functioning national political levels. This level is connected with the existence of state forms with the character of federation or confederation. National level can be the highest level of politics within the state form but only if we speak about the unitary state.

Regional level of politics functions as some intermediary between national and local levels of politics. For the citizens of particular regions this level is more closer with its content and impact but also distant as the local one. Its main goal is solving the local

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matters or issues but also overlapping the capacity of particular residential units, e.g. municipalities as the smallest political and administrative units.

Local (communal) level of politics presents the effort of moving the politics closer to inhabitants within their residential units. Resolutions accepted at this level are in the immediate interaction between inhabitants and local politically-administrative authorities what finally causes greater interdependence with ideas and interests of individuals (Klimovský 2006b: 103) – it is not possible at the national level of democratically consolidated states/countries, or there exist such mechanisms preventing those situations.

By Fiala and Schubert (2000), there are three basic semantic political dimensions as polity, politics and policy.

## **POLITY AND ITS REGIONAL AND LOCAL LEVELS**

Polity expresses the normative or institutional aspect of politics. It reflects already existing political order of the organised society (Malíková 2003: 7). As it was mentioned, the basic assumption to make polity as real term is the organised society. If we want to speak about polity at the regional as well as local level it is necessary to understand by the organised society the political community (it means the organised group of people) binding to definitely restricted area. This area responds to the municipality (in most European countries the political community is the association of more municipalities) or the region as the basic element of political organisation of the country.

Inevitably it is to stress that polity has its own structure with several qualitatively as well as quantitatively different parts. They differ in more criteria. It has three basic parts (Klimovský 2006a):

### **Normative part**

It is the complex of acts and other generally binding regulations valid within the actual period of time and place. These include mainly a summary of laws and other generally binding regulations valid in a certain time and place. They make the frame to be directed by and which must not be exceeded (under penalty) at local as well as regional political-administrative authorities, then inhabitants of particular political communities, where all those authorities do operate. The normative framework of the regional and local levels is in comparison with the normative framework of the national level more rich due to the fact that at these levels they are covered not only by the legal rules bonded at the national level but also those ones applying for the specific territory (substatutory generally binding regulations agreed by the competent authorities of regional or

local politically-administrative authorities).

- Economical part                      This part is formed by the existing economic ties, relations and processes which are more or less repeated within the mentioned bonds. These relations are formed:
- a) between political-administrative authorities within each other;
  - b) between political-administrative authorities and the citizens of particular political communities;
  - c) between political-administrative authorities and the objects created by the citizens of the particular political communities because of various reasons (e.g. legal entity of profit or nonprofit character).
  - d) between the citizens of political communities where particular political-administrative authorities operate.

Social part                              It is the main demographic and socio-economic structure of already existing organized community – already existing political community (age, race, nationality, education, etc.).

All the mentioned levels are not determined or given lets say forever. Otherwise, they may change within time and space and this may cause variety and dynamics of polity. Of course these changes are rarely short-timed or immediate. More often it happens, that the status of polity in the specific place and the specific time changes only gradually by the influence of different factors on its qualitative and quantitative character. So polity tends to perpetuate but there cannot be stated any constancy.

Very good example of the polity dynamics at the local and regional level are some reform efforts leading to centralisation or decentralisation of the administrative-political system at those levels. This effort brings potentially not only new actors (e.g. new administrative-political system) but also new legislative review of already existing relations and bonds (e.g. form the point of view of subordination, responsibility, control, etc.) or even the termination of already existing actors.

## **POLITICS AND ITS REGIONAL AND LOCAL LEVEL**

Politics in its meaning expresses the processual aspect of politics – it means the process of meeting the opinions of different interest groups sharing the ideas within the particular political system (Malíková 2003: 8). The above mentioned groups exist at all the levels of politics of course. Its essential feature is that some of them act at all the levels and some just specialize on a certain level or just one level. As the example of the interest group acting at all the levels is an organization dealing with the environment protection. This kind of group may act at the state level (acting against the parliament passing the laws of environment protection) as well as regional and local level (by some project realisation

focused on environment protection in some particular area). The example of an interest group acting at the regional or local level are the nonprofit organisations in different areas of public life (e.g. inhabitants of more municipalities establish a civic association offering help to seniors or sick citizens of particular municipalities).

These interest groups present their ideas externally and it is followed by their mutual clashes and rivalry. The most significantly it is when their different ideas are met at the elections which finally lead to forming of new legitimate administrative-political authorities. Promoting these ideas depends on various factors, the most important ones are:

- political power of these groups;
- degree of organization of these groups;
- possibility to integrate the citizens' requests into the specific ideas;
- quality of ideas presented by those groups;
- the way of promoting of the mentioned ideas;
- ability to fulfill those ideas.

Also within the regional and local level of politics there appears political rivalry. This rivalry is specific in the specific features different from that one at the state level. At the regional and local level it is rivalry among the individuals. Political parties have some influence but regarding the tightness of connections among the politicians at the regional and local level and their coinhabitants, the important role is played by their immediate interactions. So the politicians operating at those levels are not removed far from the citizens as it is usually with the politicians at the national level. That is why the citizens of smaller political communities are not bound while making decisions by the political criteria of the political affiliation of their deputies. From this may be concluded that from the increasing political community rises also the influence of political parties and vice versa, the smaller political community is, the smaller influence the political parties have.

It is typical for the regional and local level of politics the simple control of fulfilling the election promises. Citizens of those political communities may immediately check and control fulfilling of what the politicians at the regional and local level had bound before elections. This possibility of control exists as well as at the state level but we cannot speak about the immediate way of control only mediatedly. In this connection there must be concerned one essential factor, it means capacity of correct information to be disposed by the citizens. This one of the main reasons why the politicians operating at the lower levels should have legally agreed duty to inform the citizens adequately about their activities that are, and will be realised.

## **POLICY AND ITS REGIONAL AND LOCAL LEVEL**

The newest area of research within the politics is the field of policy. There are more definitions currently but each of them contains different elements and stresses different

matters. Simple definition is offered for instance by Dye who notes that public policy is anything what the government decides to do or not to do (Dye 1972: 2). Jenkins offers more comprehensive definition of public policy – term means the sum of mutually connected decisions of the political actors or groups of those stakeholders, their target selection and reaching them within the specific situations where all the decisions should be in responsibility of those already mentioned actors (Jenkins 1978: 15). Other definition is by Fiala and Schubert, where they note that public policy makes not only the content of politics but it becomes also its result, its material and its target. At this level political ideas and decisions become specific remedy, developing programs, issues with the specific material, results directly related to the citizens but on the other side they may circumvent the citizens or may share only the symbolic function (Schubert In: Fiala, Schubert 2000: 19). Nearly identical definition is offered by Malíková, who defines the term policy as a result or specific strategy by which there are realised ideas as well as need to solve already existing public problems (Malíková 2003: 8). These are the best ideas of the interest groups that won in the competitive area. The result itself depends on criteria used in evaluation of particular presented ideas. Otherwise it may happen that one selected idea or proposal will not be economically efficient but from the long-time view it will function effectively or that proposal is to win, within which there will be ensured more financial sources (even though the implementation itself will be financially more demanding).

Reasoning the need of policy at regional and local level is really simple. As it is noted by Bussfeld, problems of the municipalities need to be solved in the municipalities themselves either to minimize some potential problems (Bussfeld 1986: 49). This could be analogically transferred to the regional level.

Hereby appears the question what is the difference between public policy and public administration at regional and local level. Answer is offered by Potůček a LeLoup (2003) who stresses the fact that public administration is characterized by the routine processes and public policy is defined by creating new untested posts. Even though there was described so strict separation of public administration from the public policy, so it is to point out that local and regional level offer more possibilities of the mutual interconnection of administrative elements. There are more reasons but the most significant is territorial self-government and its basement of working. It is a part of administrative-political system where are met administrative and political matters.

## **SUBSTANCE OF POLITICS AT REGIONAL AND LOCAL LEVEL**

“Power to people!” it was the most daring challenge discovered in the USA as well as in some West European countries during 1960s and 1970s. The same request was submitted in the Central Europe after dramatic events at the end of 1980s and the beginning of 1990s (Kimball 1998: 1). Even though the communist regimes were successfully

overthrown in many Central and Eastern European countries, former satellites of the Soviet Union encountered the problems connected with forming new democratic political systems (Horaničová, Klimovský 2005: 1). Moreover all those events appeared in the similar time in the Central and Eastern European countries, they significantly differed among each other. It is possible to say that in all those countries soon appeared the political discussions dealing with proper and effective transformation of administrative and political responsibility. In relation with this transformation it is necessary to deal with the quests of decentralisation because democratic and decentralisation reforms or let's say its first stage were the fundamental part of the whole political transformation in this part of Europe after the year 1989 (Illner 1999: 17) and had strong influence on the current shape and position of the politics at regional and local levels.

## **PRINCIPLES OF CONSTRUCTION OF REGIONAL AND LOCAL ADMINISTRATIVE-POLITICAL SUBSYSTEM**

Each administrative-political system if to be functional, needs to respect certain conditions or principles keeping which finally enables its own existence.

Hendrych (2003) defines several important organization principles related to organization or to the construction of administrative-political systems. Considering the dichotomic position, there is possibility of the rate of mutual combination determining the overall appearance of administrative-political system at the particular level.

- territorial principle – includes unambiguous determination of territory borders within which the particular administrative-political system will work;
- functional principle – while constructing any administrative-political system there appears the definition of competence and division of functions;
- centralization principle – stresses the fact of forming the politics (in its whole range and content); it undergoes only the decisions of political-administrative centres;
- principle of decentralization – contains the matter of importance of more subcentres or more administrative-political units (municipalities or regions) with the approved rights and with participation on policymaking;
- principle of concentration – it means there are such legal rights which effect cannot be transformed on the lower units by administrative-political units (does not matter if they are directly subordinated or just related units).
- principle of deconcentration – it takes into account the possibility of such legal rights which allow the administrative-political units to move its effect/effort to lower subordinated units;
- collective principle – it contains the necessity of collective impacts more often in the process of forming the particular politics leading to collective decision making process into the politics creation.;



- monocratic principle – it is the opposite of collective principle and its substance lies in fact that in more cases it is an individual who is responsible for a particular policy and this means he/she should make decisions autonomously (relativity of autonomy relies to the fact that an individual does not act in political vacuum and his/her position is weakened by official and not official subordinated units that may interrupt the process of acting/working);
- election principle – it stresses the implementation of individuals into their functions via the act of election (direct or indirect);
- appointing principle – enables personnel occupation of some functions specified for political-administrative unit ignoring the electoral process.

Recently there has been implemented the principle of subsidiarity. The phenomenon of subsidiarity is implied mostly between higher and lower administrative and political units (including also EU). Subsidiarity positively expresses the idea about each act of higher unit shall help the lower ones as well individuals. Negatively speaking subsidiarity asks from the higher unit some alternative way of act in case it may help the lower unit or the individual in problem situations (Hendrych, Hoós, Jenei, Vass 2005: 125).

## **DECENTRALIZATION AS THE CONDITION OF REGIONAL AND LOCAL DEVELOPMENT**

With the fact that politics exists at the regional and local level may be supposed that at the mentioned levels do work relevant political actors and the particular political-administrative authorities dispose some amount of legal rights. It is only possible in case when political-administrative centres reject those legal rights in their favor. And it is the process by which such centre delegates the legal right independently providing decisionmaking process to lower unit where political – administrative center rejects in favor of these units, can be termed as decentralization.

Focusing on basic targets there are four key forms of decentralisation – political, territorial, market and administrative – as they were defined by Cohen and Peterson (1999). Political decentralization means traditionally the transfer, or moving the decisionmaking rights to citizens or to their elected representatives on lower units. Territorial decentralization is connected with the realization of regional and legal policy in the specific area/territory because this form of decentralisation determines that territory (it is not only the question of space or borders but also its socio-economic character). Market decentralization helps to create such conditions that help the producers of products and services to identify the goods references of individuals or communities according to their local conditions and other specifications and then modify their production. It is followed by diversion and practically it may happen that public assets (mostly those serviced at the regional and communal level) are provided not only by the subjects belonging to system of public administration but also profit organizations or

nonprofit organizations focusing on interest of local unit citizens. Last but not less important form of decentralisation is administrative decentralization focusing on legal rights distribution and its functions within the hierarchical as well as functional meaning. Most oftenly it is connected with the political decentralization and there is no exception that it is connected with the local decentralization.

Theoretically as well as practically there are three basic types of decentralization – deconcentration, delegation and devolution. Each of this type determines some relations between administrative-political centre and the units sharing the lower level of politics.

Deconcentration presents the transfer of the legal rights to the lower level belonging into the jurisdiction rights of political-administrative centre. Essentially the point is to keep the key roles and receiving bound solutions preserved at the central level as well as achieving the state where the government deconcentrates are responsible for implementation of accepted solutions, in other words lower political-administrative units directly subordinated to the central government having the immediate possibility to know the local situation and needs. If to generalize, deconcentration can be defined as a situation where the central government takes the full responsibility but the individual steps of particular policies implement various political-administrative units of the state character that are directly subordinated to the central government and then fully and directly controlled.

Delegation responds the situation in which runs the transfer of powers from central government to the lower political-administrative authorities with no state character so there is no direct subjection towards the central government. And this government may provide control only indirectly. Delegation is mostly used by central government in relation to semi-autonomous agencies respectively to political-administrative units of local municipalities. An essential feature of the delegation is that the delegated subject in most cases bears the entire amount of financial costs connected with an effect of transferred competences.

It is possible to speak about devolution if there is a situation when political-administrative centre (central government) transmits the part of powers of relatively autonomous political-administrative units of territorial self-government or others political-administrative units independent from the central government. Devolution itself entails a number of conditions without satisfying which is not feasible. Among the basic units belong those on which there are transformed certain powers within devolution and those should be legislatively modified scope, as well as they must be provided with the opportunity to raise their own revenues and affect their amount by their own actions, and it is also necessary to introduce such mechanism of control on the one side independent from the central government but on the other one which is able to guarantee not only the legality but also the accuracy (mainly in terms of economy, efficiency and effectiveness) of its procedure.

Each type of decentralization contains in addition to real benefits, also some risks.

Therefore there cannot be achieved the awaited results by decentralization policy. As McDowell (1999) states, the problem in this area is caused by the fact that currently there is not sufficiently developed problem why in some cases decentralization policy brings the effect and in some no. Regarding the risks of decentralization in connection with it there should be an answer for question as for the capacities of regional or communal political-administrative units sufficient from the personal, material and functional point of view. Hereby Kimball (1999) states the most common problem as insufficient tax basement consequently the relevant political-administrative unit fails to meet the needs and tasks by their own financial sources. Secondly, the politics forming in the decentralized units cannot be considered as independent because those units causing a synergy effect need to coordinate their policies but limiting their own independence. Thirdly, decentralization entails the need for comprehensive and integrated management activities of various actors – from the state organizational units to self-government political-administrative units up to NGOs and private organizations.

In accordance with the existence of ethnically heterogeneous areas there cannot be ignored the risk of ethnic tension which could be bound by the nationalistic actors on the decentralization policy in all its forms. Moreover as Hesse (1986), mentions the decentralized politics and administration stress the existence of such facts at the regional and local level like proximity towards the problems, orientation on target groups or regional or sector targeting. Otherwise, there is the question if local and regional policy are those in which it is possible to motivate all participating actors for innovations.

## **POLICY ACTORS AT REGIONAL AND LOCAL LEVEL**

In the political reality there are many actors at regional and local level. Their number increases in case there are no those actors who really act and implement their activities at those levels but also these actors who may potentially act at these levels.

From the functional point of view all the political actors may be classified into two big groups. The first group are those actors who enter the process of policy forming obligatory, based on post they share – political and administrative actors at regional and local level of policy. It is in fact of all political-administrative units of public character presented by administrative workers (clerks) or regional or local political representatives.

The second group is created by variety of other actors at the regional and local level of policy among which belong profit oriented private subjects or companies, media, or citizens themselves or their associations of apolitical character (NGO's).

## **POLITICAL AND ADMINISTRATIVE ACTORS OF THE REGIONAL AND LOCAL POLICIES**

When talking about political and administrative actors at the regional and local level of policy we understand by that it is a part of political and administrative system in addition to political parties.

Regarding the organization of political parties and movements they have fixed organization at all the levels of politics or their organizational hierarchy limits only for national or regional level (if there are regional political parties or movements) and at the other levels of politics act actively without their fixed organizational hierarchy. It is really interesting that in more Post-Communist countries prevailed the second stage of organization (after revealing the political atmosphere and removal of Communist prior) that one which particular political parties or movements tried to set the fixed organizational structure at the national level, while there were neglected building of regional and local components. This paradox development was associated mainly with an attempt to democratize quickly in the countries and the affect was in weakening the Communist powers at the national level and creating of institutional alternative ready to represent the interests of voters.

Organizational units of political parties and movements in the regions and municipalities fulfill several important tasks (as well as if those organizational units do not exist, fulfilling those tasks will be undertaken by the party centres) among which belong those who help to:

- identify problems of regional and local character and to select those to be dealt by the party centres;
- solve those problems of regional or local character which are not that serious to be dealt by the party centres;
- get new members and look for new sympathizers of given political party or movement;
- identify the members who have potential to become a part of the party elite and then to help to enforce those identified members (e.g. in the inter-party primary elections).

The most important role is that those organizational units offer the individuals (except the politicians) who represent the voters and to whom the voters may address their proposals, comments or complaints.

System of public administration (administrative system), stands on three pillars, or in other words system of public administration contains three basic subsystems (Klimovský 2008):

- subsystem of state administration;
- subsystem of self-government;
- subsystem of public corporations (specific agencies).

Each of these subsystems has its own specifics but on the other side there are some common features appeared in other two subsystems.

In relation to regional and local level of policy play the most important role the actors who are organizationally included into the subsystem of the state administration as well as into the subsystem of self-government.

It is necessary to specify further facts as for the extraordinary place of territorial self-government in subsystem of self-government and its political-administrative units.

The state government and territorial self-government could be organized in so called linked (common) model or dual model. As it is mentioned by Konečný (2004) in the common model there exists only one system of public administrative bodies ensuring state as well as self-government competences and then in parallel in the dual model exist two organization systems which units do not stand in opposition but their competences do not overlap. The common model is typical for Anglo-American administrative-political culture respectively for small unitary states, dual model for bigger countries of continental Europe. This is not fully valid because in some countries it is possible to identify wide range of elements combination of both models.

Subsystem of state administration is organized strictly within hierarchy, so the organizational units at the lower levels are always subordinated to higher ones. Analogically it means that all the organizational units of subsystem of the state administration are directed and controlled by the government centre determining not only their goals and tasks but also the way how they will be accomplished.

Organizational units of the subsystem of state administration are represented by the administrators working in the state employment entitled by the central government or other higher political-administrative authority. Very important role plays the political affiliation at the state administrators and joining new government there are rotated new administrators as well. This phenomenon is connected with the question of power policy, mainly in case of ministers, the members of government. The ministerial unreliability is then defined as the behavior of the government member who does not implement or implements only in the slow pace or implements only partially those government decisions included into his/her competence or accepts the decisions that are in opposition with policy of the given government (Blondel, Manning 2002: 456).

From the institutional point of view the state role and its bodies is limited by the number of increased functions of the self-government. This increasing is differentiated in the individual states but nevertheless it leads in some cases to blurring the boundaries among federalism, autonomy and decentralization itself (Matula 2005: 135). It is connected with the fact that self-government is attributed with such public skills but the truth is that self-government may perform them in the same quality as the state and it is not precluded by other limits such as control and division of power and efficiency of performance (Matula 2004: 94).

Self-government represents within the system of public administration powerful effect and influence on public life by means of non-state character. This government is not understood and cannot be identical with the state government regarding the state power action of the subsystem of the state administration. In parallel with the state administration, the self-government participates in the solving of public affairs (Průcha 1998: 244) and hence in implementation of public policy at regional or local levels. In this context the specific position shares mainly the area of organizational units included into the territorial self-government.

Basic political-administrative units of subsystem of territorial/local self-government are municipalities. By the Art No. 3 of the European Charter of Local Self-government, municipality presents the existence of local territorial self-government; local municipal authorities implement the law of its bodies to administrate and direct the essential part of public affairs within their own responsibilities defined by law in accordance with the interests of residents/citizens of particular local unit. This right shall be exercised by the councils or assemblies whose members are freely elected by direct, fair and general election law by secret ballot which may be responsible to them or to executive bodies of an advisory character. All the bodies of the local self-government may independently determine their own administrative structure regarding the local needs mainly and effective arrangement of administration. The competences by the local authorities are on origin character and they cannot be restricted or withdrawn by any other entity belonging into the system of public administration except the situation when it is provided with the special law. This does not necessarily mean that there cannot be delegated the originally belonging competences into the other subsystems of public administration system. This delegation is allowed when it is based on law and financing of such performed competences should be carried out by the subject that delegated the competences. Regarding the financing of the original competences of the organizational units of the subsystem of territorial self-government, it must be adapted to the scope of competences wherein at least the part of the fund should come from the local taxes and fees which the amount or rate the competent authority of local government units may influence by their own decisions. For an effective performance of local self-government it is necessary to financially weaker local units have secured additional funding through the mechanisms of financial compensation. Beside this the bodies of the local/territorial self-government may obtain resources by loans from the state subsidies or other appropriate resources. The bodies of the local self-governments cooperate not only with the subjects operating in their area but also among each other. The forms of such cooperation are modified by the legislation of particular countries which does not exclude the association and cooperation between local government bodies in different countries (e.g. in the form of cross-border cooperation).

Next type of political administrative units of subsystem of territorial government are the regions (in the European countries such regions are called different names as province,

region, district, county, voivodships, etc.) These units operate at a level which is a kind of intermediate level between local and national levels.

The reasons for the regional level of territorial government existence are more but most often mentioned one is the fact that the political and administrative reality raises problems of existence by which nature there are not prior for the state which also exceed the limits and possibilities of political-administrative units established for the lowest, i.e. local level.

By Škultéty et alli (2002) by the term corporation (agency) we may understand the legally modified association of individuals which is established for the purpose of tracking the particular target. Unlike the other forms of associations, the corporate associations have legal personality that differs from the legal status of associated entities. In order for any corporation to be considered a public corporation there must be accomplished several criteria:

- public corporations arise from the manifested intension of the legislature;
- public corporations arise directly from the law or from the decision of the particular decision and competent body of public administration (based on law);
- public corporations are funded partially or completely from the public budgets ;
- public corporations not only pursue public goals but also provide a real public service;
- public corporations dispose with certain elements of public authority.

Very similar public corporation is defined by Průcha (1998). He especially emphasizes their status and personal component. By him the public corporations are focused on achieving certain objectives in implementing the public interest and are granted legal personality and their action is a priori approved by the state. From the organizational point of view the bodies of public corporations usually do not subdivide into the lower organizational units so it means the bodies of public corporations have relatively independent position exclusively confined to the legislative framework of the certain public corporation. Although the public corporations act under the law and their subjectivity is derived from the state, they always act in their name (even if that particular case represents the body) within their own competences and to achieve the public interest which is set more freely, as it is in the case of state administration.

## **OTHER ACTORS OF THE REGIONAL AND LOCAL POLICIES**

Naturally, in addition to political and administrative actors in policy making at the regional or local level there is an affect by the other actors. This involves a large group of different entities from which there are mentioned mainly the companies/enterprises (firms), mass media and organizations of civic sector.

By the enterprises we may understand the profit oriented companies who achieve by their

activities their own profits. Their activity that occurs mainly in production may have productive or nonproductive character. Next important feature of these entities is the fact their results (goods and services) are offered via the market or directly to the customer or to the other companies who will mediate the transfer of goods or services from the producers to customers.

According to fact that some companies create in economically developed countries the number of work posts, their requirements play vital role in public policy. Another important fact is that the companies help by their products to satisfy needs of citizens and finally the state's as well (Filip, Grzebyk, Kaliszczak 2010). At this point arises the questions on how the way of requirement formulation, or the way of company representation in this process. Rather than searching the answer for this question, should be realised that the differences that exist between particular companies are really significant and serious that it is not possible to unify their requests (within the process of policy making). As for the aspect of influence, there are the enterprises which have:

- local character – mostly there are small companies of nonproductive character whose employees come from the certain area and whose services are directed to the customers living in that area;
- regional character – mostly there are small or middle companies whose production is for the market within a certain area and whose seats and headquarters are often found in the socioeconomic centre of that region;
- national character – almost all large companies have that kind of character and they tend be placed in the bigger seats and whose production is directed to the majority of regional and local markets within the given country;
- transnational character – there are large companies presented in more countries, trying to use the competitive advantages of the countries where they are represented (e.g. by placing their seats into the countries who have pro-business tax policy and in which there is cheap work force or proper material basement), and which are able to influence the policy making process from the side of central governments of more countries.

The specific role within the policymaking process is played by mass media. Mostly they are owned by private owners and their attempt is to gain their profits. However they act as mediators between political and civic spheres. The role of mass media within policymaking at local and regional level is usually referring to the position of intermediary entities because their activities create space or arena where ideas meet relevant actor of policymaking process.

Local and regional levels are typical by the fact they operate alongside the nationwide mass media as well as mass media of local or regional character. Their attitude to politics and its levels is analogous to – the local as well as regional mass media provide more space to policymaking at local or regional levels. Conversely, the national mass media deal with policymaking at the national level. This, naturally, does not prevent a local or



regional media offering information on policymaking at national level or the national media to offer information on policies at lower levels.

Mass media are rarely considered as apolitical (such apolitical nature is required in the developed democratic countries from the media of public character, activities which are partially or fully financed from the public budgets). Indeed many of them explicitly state their relationship to politics and in their comments and contributions often is followed by defence of such political statements corresponding with their relationship to politics (it can be most clearly discerned in daily newspapers).

Perhaps one of the most important issues related to the role of mass media in the politics (as well as in the policy at local and regional levels) is the question of fairness and accuracy in informing the public. Mass media act as one and only mediator to inform the citizens about the policymaking process in its width. Therefore in terms of citizens' orientation it may look more dangerously, if some of the mass media declare their apolitical nature using the way of fulfilling their activities but ignoring it more than the fact when some mass media prefer their political status in informing the citizens but also they report openly to such political attitudes openly reported, allowing the recipients of their information (citizens) in order to separate possible tendentious way of communicating information to be proved correct within this knowledge.

The most heterogeneous group created by other actors of regional and local levels of policy is the group marked as organization of civic sector. Just in at the introduction of the notes of organization of civic sector (also marked as nongovernment or nonprofit organizations) it is worth to note that the importance of civic sector in the world within past fifteen years is continuously growing in the world.

The growth of huge number of nongovernment organizations, development of associating and voluntary work belong into big social innovations (Bútora, Frič 2005: 151) that appeared at the turn of the 20th and 21st centuries.

Civil society by Ondrušek et alli (2001) fulfills ten basic functions via its subjects:

- forms and translates the ideas and requirements of the citizens via their active participation;
- saves and develops heterogeneous and plural character of society;
- co-creates and modifies public meaning;
- acts in favour of social integration based on presented and identified interests;
- acts in the position of important factor of political socialization;
- interacts within the social control mechanism;
- offers those goods that are not offered by public nor by private profit sector;
- offers the space for implementation of social innovations;
- interacts in conflicts solving and implementing preventive tools to prevent them from;
- creates new values and fulfills in advance defined social objectives.

Different independent associations and interest groups create mechanism via which the citizens may influence the actual political decision and by this limit and control those who reached/gained powerful positions in the state. To fulfill this task there must be two mutually complementing conditions to be guaranteed. On the one hand they need to be independent from the state on the other hand the state should support them or at least guarantee their legal and legitimate acting. Problem is that a kind of balanced relation could be considered as ideal in the stable and consolidated democracies often occurs in this area open and closed conflicts marked by varying degrees of intensity (Čambáliková, Malová 1998: 4).

## **POLICY TOOLS AT REGIONAL AND LOCAL LEVEL**

The basic predisposition of public policymaking at any level is the choice of proper tools to reach the policy objectives (Malíková 2003: 28).

Each implemented element may be considered to be the policy tool/instrument into the process of policy making which should serve the changes or maintenance of status quo. As it is stated by Malíková (2003), there are such tools helping to direct the activities within the public life and serving the solutions for the particular problems or problem situations.

Analogically as it is in the case of political actors as well as at the public policy tools, the truth is that some of them can be used at all the levels of policy and the part only at some levels.

### *CLASSIFICATION OF POLITICAL TOOLS USED AT REGIONAL AND LOCAL LEVEL*

From the time point of view the policy tools can be divided into long-term, medium-term and short-term tools. If public policy is seen not only as a solution of the particular problem but also as the mechanism implementation for preventing, then it is clear that the highest representation among the tools belongs to the group of tools with long-term or at least medium-term nature.

Political tools from the nature point of view are divided by Malíkova (2003):

- normative-legislative;
- economic;
- informative;
- administrative-organizational.

Of course such of policymaking tools classification cannot be absolute due to the overlapping at each level of policy, and sometimes it is difficult to differ that overlapping nature of implemented tools (very good example of prevailing overlapping nature are the local taxes and fees causing the fiscal changes) (Hudec et alli 2009).

Normative-legislative tools arise the rights and rules of political actors or regulate the political process itself. Their basic feature is that they bound a particular actor (if it is an individual legal act, e.g. decision in some mater) or they modify the position of each actor in the similar situation of not defined number (if it is a normative legal act e.g. an issue of generally binding regulation by the municipality of using the public space area within one municipality). Mainly the second group, normative legal acts makes the framework conditions for operating and functioning of the political actors, regardless whether it is the policy tool holder itself or not.

Economic tools are policy tools causing various fiscal consequences and their main objective is to ensure the financial or material tool for successful realization of particular policies or only the selected entities. In case of economic tools it is clear that not all the tools may be connected to the particular level because the political level where runs implementation and the political where are issues brought, they do not need to be identical (e.g. the grant structure directed/managed by the central public authority-ministry may offer the financial sources to the applicants at the local level and it means that the economic tool implemented et the national level brings finally the issues with the local character).

Implementation of the economic tools is not problematic but sometimes it meets the capacity problem (e.g. financial means from the particular grant structure are more applicants than it is possible to satisfy them or potential allocations do not go/are not directed to all possible areas but only some of them).

Informative tools are connected with the need to widespread the certain amount of information among the political actors. This amount can be seen in two positions – on the one hand there is so called obligatory amount of information (available for everybody) – and on the other hand there is so called selective amount of information, not published across the board, available only for certain predetermined range of political actors (it is only in case to keep the confidentiality –of business, state, etc.). The main problem of information tools is their quantity and quality as well. Not each political actor is capable of good and right way to decipher the content of shared data or to filter the amount of information from their total.

Administrative-organizational tools are connected with organizing and administration of the particular policy. This may be provided in direction of political-administrative authority or under the contracting this can be moved to another entity or is triggered by the political actors provided by a private nature.

From the formal point of view the policy tools can be divided by Doern and Phidd (1992), into three big groups. The first group contains the obligatory tools implemented on a certain regulation, and the interest parties cannot avoid their exposure. The second group contains of the voluntary tools. These are not based on coercive nature and their effect will be only felt though the willingness of entities affected by. The space between these two groups is filled by the group of so called mixed tools similar with obligatory

tools but also sharing some signs of voluntary tools. In their case it is about the situation when some element is not implemented obligatory but when implemented, the concerned subjects must respect it in full range.

## **CYCLE OF POLICYMAKING AT REGIONAL AND LOCAL LEVEL**

The first stage of policymaking (initiation) is considered to be that part of political cycle where it is found, there exists socio-economic problem to be solved and where this kind of problem is identified and defined (Fiala, Schubert 2000: 79). The emergence of socio-economic problem usually occurs spontaneously, based on reality.

In the next stage called as estimation, runs the analysis of the problem situation coming from the first stage (from initiation) and it is about proposing the possible solutions of a particular problem (Fiala, Schubert 2000: 80). This stage is for the final success definitely important because just the amount of information may ensure the right decision. Any other decisionmaking could approach the decision based on intuition leading finally to disaster situation. This is one of the main reasons why in this stage there must be selected that one subject (actor) to provide the analysis. For the local level as well as for the regional one, it is typical that while analysing the problem, as well as searching the right solutions, there cooperate more actors. As an example could be used an effort to solve the environmental problem where do participate not only the municipality representatives but also the representatives of company/ies located in the local area and also the citizens themselves and other NGOs dealing with the environment protection as well as regional political-administrative units.

Selection is the stage where is accepted the final decision about the discussed problem situation (Fiala, Schubert 2000: 81). In any selection the dominant attitude towards any mater does not necessarily belong to the majority attitudes (Kaplan, Lasswell 1982: 40). Miller (1982) in this context thinks about the relation between power and ability to influence the decisionmaking process or an ability to reach the wished issues. He stresses the fact that not everybody who reaches the wished issue is that powerful actor from the power distribution point of view. In this case of accepting the decisions may become a successful actor that one:

- has preferences similar with those of other powerful actors;
- has preferences similar with those who also the actors have;
- has preferences, considered being of “average“;
- keeps in his/her hands “balanced status of power distribution“, when there are two powerful/strong but in opposition standing groups, and he/she may alternate one side for another due to his/her preferences;
- he/she holds the majority preference but due to the existence of many preference groups and cyclic preference voting may get the best benefit from all rest preferences.

Next option is when successful political actor does not need to be strong from the power distribution point of view, and when this success does not stand on preferences. Based on this the successful actor in the acceptance process may become that one who:

- has strategically important skills or abilities, while most of them do not have;
- has relevant and important information, while most of them do not have;
- may freely cooperate with the others, while most of them cannot;
- is active and uses all the occasions while the most of them are passive.

The third possibility is when the political actor could be considered as a successful one in terms of outcomes of decisionmaking process, is then the situation when this actor:

- is able to modify the preferences of the others as well as their activities;
- is able to modify the activities of other actors without changing their preferences (e.g. via threats or promises);
- is able to (may be also sometimes in cooperation with others) to reach the wished issues and prevent the unwished outputs regardless the preferences or activities of other actors (or those who stand out of this mentioned cooperation).

By implementation it is called that stage of political cycle in which the intentions are converted into the measurable activities (Fiala, Schubert 2000: 82). It means the decisions accepted in the stage of selection are then listed into the life. However, in this stage as well comes the decisionmaking. "The game" is entered by new actors and there appear also new facts or problems. This may or not lead to certain changes/modifications in the decisions accepted within the previous stages of the policymaking cycle.

The question when the implementation starts and when does it finish, is really difficult. It is connected with the statement by Dowding (1991), by whom there are three mutually connected statements:

- any act, potentially conflicted is considered to be also a political act;
- considering unlimited amount of individual preferences we may state that each act is potentially conflicted;
- according to the above mentioned statements, every act is potentially considered to be political act.

Implementation as the stage of political cycle may have several phases. It depends mainly on the difficulty and complexity of problem situation. These phases may follow one another, may overlap and there comes superposition of implementation activities. For the local and regional level is important that the decisionmakers are closer to the performance of their decisions than it was the case with decisionmakers at the national level. This also includes the simplification of determination of liability relationships.

Evaluation investigates the effects of exposure tools that have been used in the implementation stage. In particular they compare the results with the expected results

with those that were actually received.

Finishing as the stage of political cycle is not typical and appears only rarely. There is not often the situation when the problem is resolved so that it could not be further addressed. Practically, much more frequent closure of the political cycle is via the repeated problem reformulation. By the policy implementation there are solved certain problems but there may float out some other facts which are within the evaluation evaluated and then they are able to initiate the whole political cycle again.

There is one more problem-semantic problem that is connected with the matter of finishing policy. By finishing, as it is stated by Howlett and Ramesh (1995), we cannot understand an absolute finish of particular policy. By this idea with the finishing policy there should be finished also the tools used for the particular policy. It is just hard to imagine the use of normative tool (e.g. the legal norm) in the exactly set time. Politics can be finished but some tools need to function further on to prevent the problem situation.

Although the presented theoretical models of policymaking process share the principle of rationality and try to respect the empiric nature of need specification of particular municipalities or regions and then accepting of particular regulations, it is reminded by Staroňová (2001) that the practice often brings a lack of sense of those elements resulting in performed steps below the expectations.

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# **BUDGETARY INTERVENTIONS FOR REGIONAL DEVELOPMENT**

Saša Drezgic<sup>1</sup>

## **INTRODUCTION**

In the last two decades in particular there is a hot debate on the efficiency of sub-national governments and the extent of effects of their activities on regional (local) economic development. In this paper, the key factors of sub-national government efficiency will be thoroughly discussed with special emphasis on territorial-administrative formation of local governments which defines the level of democracy and the economies of scale of particular local governments.

In addition to the issue of efficiency the effects of economic crises that propagated through all levels of government present one of the most important topics in the field of fiscal federalism nowadays. This is not surprising because the crisis is still ongoing phenomena and regional and local governments worldwide are engaged in creating novel approaches for reducing the harmful impacts. Numerous questions arise. To what extent can regional and local governments provide support to citizens and local businesses? What are the repercussions of the crisis to the regional and local budget? How to increase revenues? Hard choices of cutting government spending are also included.

First part of the paper, after introduction, elaborates some important lessons on key factors of regional (local) government efficiency. Second part focuses on position of local government sector in terms of potential for conducting the countercyclical fiscal policy. We can observe that such policy is mainly present in developed decentralized economies. Third part of the paper deals with position of regional (local) governments within the system of intergovernmental relations. This position defines potentials of subnational governments to conduct proactive measures in mitigating the effects of economic crises. Fourth part presents an example of response of Croatian regional (local) governments as an attempt of countercyclical budgetary measures.

## **REGIONAL (LOCAL) GOVERNMENT EFFICIENCY**

Regional (local) government efficiency comes from many sources. However, we can address three pillars which should enable increasing the efficiency in sub-national public spending (Hemmings, 2006):

- opportunities to encourage greater economies of scale in service provision
- adjustment of sub-national government financing to further increase transparency

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and provide the right balance between autonomy for the regions and municipalities and the central-government power

- improvements in accountability – in the form of oversight and transparency in public procurement process, strengthening the benchmarking processes, and improvement of e-government particularly in the sense of better coordination between government databases

In this part, we deal with the issue of achieving greater economies of scale in provision of regional (local) public goods and services. This is the first and fundamental step towards exploiting the advantages of other categories that improve the outcomes of regional (local) government activities. Questioning the optimal level of government size, as was mentioned, has many layers (given as criteria in the next section). When we focus on economic efficiency, besides average (marginal) costs which decrease with the size of the local government, we have to aggregate these layers into one that is beneficial in terms of optimal size. There is a general consensus that the level of citizens' participation (which does not refer only to voting) and the level of democracy (in terms of better information and accessibility given to the citizens) negatively correlates with the government size. This comes from the fact that as the government gets larger, the more the individual preferences towards regional (local) public goods and services are blended into aggregate preferences of the whole community. At some point of the government size, there is a possibility that aggregate preferences and the distribution of individual preferences do not match closely. It is highly unlikely that a sample of numerous distributions of preferences for many local public goods and services would follow a normal distribution (which would guarantee that most of the citizens' preferences are satisfied). Therefore, local government representatives have to be more responsible towards individual voters in smaller governments simply because they are more accessible and their actions are more visible.

Larger governments can improve territorial equality by combining rich and poor areas (inhabitants) and eliminating differences between available resources and expenditures per capita. The smaller the governments are, the larger the fluctuation of individual local government expenditure standards from the average expenditure standard of local governments. Of course, such a situation intensifies the needs for central government transfers in order to preserve an acceptable level of provision of local goods and services. This is a sort of a paradox. Despite the fact that smaller governments have a greater potential for improving the level of local democracy, they demand a greater intervention of the central government to resolve inequalities in resources necessary for satisfying citizens' needs. Usually, the central government does not provide a sufficient level of transfers, which means that a possible level of democracy expressed through the provision of requested regional (local) public goods and service is never reached. On the contrary, over-fragmented territorial formation usually creates a local government able to

finance only administrative costs without any space for satisfying public needs. This particularly happens in less developed countries with a lower level of fiscal capacities.

A formal model of optimal government size was presented by King (1996). Even though this model relies on restrictive assumptions, it brings interesting considerations into the fore. King argues that the optimal size of the government changes through time, and despite the significant costs of structural reforms, the size has to be periodically revised if we want to preserve an appropriate level of allocative efficiency.

Usually, the optimal government size concept is given by the trade-off between the economies of scale brought by decreasing costs of larger government and burden of overcrowding of particular government territory. Having in mind that the high level of quality of life in large cities in Europe, we can relax the boundary related to number of inhabitants as the burden which provides incentives for smaller government. The reason for such relaxation is due to the fact that amalgamation procedures go from the local government with lowest number of inhabitants and in this way respect the government size from bottom up. The more important aspect is the level of democracy on the local level that should be on the higher level given the smaller government. However, the question is what kind of democracy is valid in case of small governments that are not able to finance any outlays other than administrative ones. This is more the truth the more country is less developed.

The advantage of having fragmented subnational governments is in matching local residents preferences as close as possible to provision of local public goods and services. If there is such a match, we can say that there is optimal allocative efficiency and the welfare of local inhabitants is maximized. However, there are several obstacles that prevent the occurrence of such ideal case. There are inter-jurisdictional costs of benefit externalities (or spillovers), economies of scale and administration and compliance costs of the government that make argument for more consolidated local governments. Therefore, there is an optimal size of government defined by the intersection of these two opposing principles.

In addition, there is a clear relationship between the degree of decentralization and the level of economic growth. The more the country is developed, the more it can enjoy in the benefits of decentralization. Due to the abundance of the resources and higher level of mobility of local residents, specific local preferences will more diversify among local governments. On the contrary, when the economy is poor, there is not much difference between the local governments because, and, due to the lack of resources, they can provide only minimum level of local goods and services.

The table 1 presents an overview of local government size in EU-27 countries. In 2010, the average European municipality had 5592 inhabitants over a surface area of 49 km<sup>2</sup>. However, across the countries we can observe significant disparities both in terms of population and surface area in per capita terms.

Table 1: Population, surface area and number of 1level local governments in the EU-27 Member States in 2010

|   | Population<br>(thousands) | Surface<br>area (km <sup>2</sup> ) | 1st Level<br>(municipalities<br>and local<br>authorities) | Population<br>(thousands)<br>/number of local<br>governments | Surface<br>area/number<br>of local<br>governments |
|---|---------------------------|------------------------------------|---|--|---|
| <b>Countries with one subnational government level</b>    |                           |                                    |   |  |   |
| <b>Bulgaria</b>   | 7,547                     | 111,002                            | 264   | 28,6   | 420,5   |
| <b>Cyprus</b>   | 804                       | 5,695                              | 378   | 2,1  | 15,1  |
| <b>Estonia</b>  | 1,340                     | 45,227                             | 226   | 0,6  | 200,1   |
| <b>Finland</b>  | 5,363                     | 338,145                            | 342   | 15,7   | 988,7   |
| <b>Ireland</b>  | 4,476                     | 69,797                             | 114   | 39,3   | 612,3   |
| <b>Latvia</b>   | 2,239                     | 64,589                             | 119   | 18,8   | 542,8   |
| <b>Lithuania</b>  | 3,287                     | 65,300                             | 60  | 54,8   | 10,9  |
| <b>Luxembourg</b>   | 507                       | 2,586                              | 105   | 4,8  | 24,6  |
| <b>Malta</b>  | 414                       | 316                                | 68  | 6,1  | 4,6   |
| <b>Portugal</b>   | 10,636                    | 92,152                             | 308   | 34,5   | 299,2   |
| <b>Slovenia</b>   | 2,049                     | 20,273                             | 210   | 9,8  | 96,5  |
| <b>Countries with two subnational government levels</b>   |                           |                                    |   |  |   |
| <b>Austria</b>  | 8,370                     | 83,871                             | 2,357   | 0,4  | 35,6  |
| <b>Czech Republic</b>                                     | 10,538                    | 78,868                             | 6,250   | 16,9   | 126,2   |
| <b>Denmark</b>  | 5,546                     | 43,098                             | 98  | 56,6   | 439,8   |
| <b>Greece</b>   | 11,305                    | 131,957                            | 325   | 34,8   | 406,0   |
| <b>Hungary</b>  | 10,000                    | 93,029                             | 3,177   | 3,15   | 29,3  |
| <b>Netherlands</b>  | 16,611                    | 41,528                             | 430   | 38,6   | 96,6  |
| <b>Romania</b>  | 21,431                    | 238,391                            | 3180  | 6,7  | 75,0  |
| <b>Slovakia</b>   | 5,430                     | 49,034                             | 2,928   | 185,5  | 16,7  |
| <b>Sweden</b>   | 9,378                     | 449,964                            | 290   | 32,3   | 1551,6  |
| <b>Countries with three subnational government levels</b> |                           |                                    |   |  |   |
| <b>Belgium</b>  | 10,883                    | 30,528                             | 589   | 18,5   | 51,8  |
| <b>France</b>   | 64,812                    | 632,834                            | 36,682  | 1,8  | 17,3  |
| <b>Germany</b>  | 81,744                    | 357,027                            | 12,104  | 6,8  | 29,5  |
| <b>Italy</b>  | 60,468                    | 301,336                            | 8,094   | 7,5  | 37,2  |
| <b>Poland</b>   | 38,191                    | 312,685                            | 2,479   | 15,4   | 126,1   |
| <b>Spain</b>  | 46,073                    | 505,997                            | 8,116   | 5,7  | 62,3  |
| <b>United Kingdom</b>                                     | 62,195                    | 243,820                            | 406   | 153,2  | 60,1  |
| <b>TOTAL EU 27</b>  | 501,636                   | 4,409,047                          | 89,699  | 5,6  | 49,2  |

Source: Dexia, 2010

In the cases where maximum number of inhabitants does not reach minimum level of economic efficiency, and there is no political will to introduce amalgamation reforms, there are two possible alternatives to overcome to costs of fragmentation. First, cooperation between governments in many activities can enable reaching the optimum economic level. This refers to voluntary creation of federations of several smaller

governments or creation of intermunicipal enterprises that usually offer communal services such as public transport, energy sector, water and sewer. Second solution refers to outsourcing of part of activities to private sector companies.

Such processes can be noticed for the last several years through the reforms at the municipal level that has encouraged inter-municipal cooperation and municipalities to merge. Cooperation between municipalities for some time is in the process in many different European countries (Hungary, Finland, Austria, Estonia, Bulgaria, Portugal, etc.). In addition, several countries amalgamated their local governments in rather voluntary manner such as in Denmark in 2007 where the number of municipalities dropped from 270 to 98, Latvia in 2009 where they went from 524 to 119, and Greece in 2010 with a rather aggressive approach to reform (from 1,034 to 325). Such municipal reforms are also set in England, Northern Ireland, Finland, Netherlands, Germany, Luxembourg and France (Dexia, 2011).

One of the consequences of sub-national government territorial fragmentation was the fact that there were substantial differences between municipalities and cities in terms of territorial size, number of inhabitants, and technical, economical and financial capabilities of these governments to deliver standard level of local goods and services. The problem is that, at the beginning, the functions and responsibilities given to the same layer of government were equal besides these obvious differences. Later, these differences had to be overcome by formation of new entities and levels of government which introduced different levels of responsibilities depending on the real possibilities of sub-national governments (this refers to “independent competencies” and “delegate powers” in Czech system or “large” cities in Croatia, for example). Despite of such attempts to overcome the problems of lack of economies of scale, research on the optimal size of local governments determine that the costs and quality of delivery of local goods and services are severely compromised in case of local governments with less than 500 inhabitants (Ladner and Steiner, 2003, acc. to Hemmings, 2006).

Surprisingly, the research on the impact of mergers provides evidence for improved quality of local government service but does not find evidence on significant cost savings (Hemmings, 2006). This might be explained by the fact that measures that stimulate mergers usually come with increased level of resources given to the local government which decreases incentives to reduce costs. It is also possible that large governments take over additional responsibilities that have to be financed.

## **LOCAL GOVERNMENT EFFICIENCY IN CEE COUNTRIES**

Most of the CEE countries followed the similar path of the decentralisation process. From the establishment of intergovernmental systems in 1990s in most of the countries there was a too large number of municipalities and regions. The common feature was continuation of territorial fragmentation which lead to creation of additional local governments which imposed problems to extending autonomy and legal power to the local governments.

The Czech Republic provides a good example of such common process. After territorial reform that established subnational territorial boundaries in early 1990s, in year 2000 there was a further decentralisation process that created 14 regional governments which replaced a network of 76 administrative districts (okresy). Despite this reform these regions were still not large enough to qualify as th “NUTS2” regions for EU-regional funding purposes. The population of these regions ranges from 300000 to 1.3 million. The problem is that the subnational government is even more fragmented in regards to municipalities. There are 6243 municipalities with large differences in terms of population (Hemmings, 2006).

The same scenario is noticeable, for example, in Croatia where there are 21 regions formed (same as in Czech Republic, the capital of Croatia, Zagreb, has a dual powers of region and city) with more than 400 cities and municipalities. This number in time has grown to 570 municipalities. Even though this number is quite lower than the number of municipalities in Czech Republic there are continuous discussions in last several years about the need of amalgamation of these government to much lower number.

One of the key drivers of latest revival of amalgamation debates is in effects of economic crisis that spill-over to central and local government budgets. The need for central government transfers is increasing in times when central government budgets are under pressure towards fiscal consolidation i.e. reduction of deficit financing.

One of the consequences of subnational government territorial fragmentation was the fact that there were substantial differences between municipalities and cities in terms of territorial size, number of inhabitants, but technical, economical and financial capabilities of these governments to deliver standard level of local goods and services. The problem is that, at the beginning, the functions and responsibilities given to the same layer of government were equal besides these obvious differences. Later, these differences had to be overcome by formation of new forms and levels of government which introduced different levels of responsibilities depending on the real possibilities of subnational governments (this refers to “independent competencies” and “delegate powers” in Czech system or “large” cities in Croatia, for example). Despite of such attempts to overcome the problems of lack of economies of scale, research on the optimal size of local governments determine that the costs and quality of delivery of local goods and services are severely compromised in case of local governments with less that 500 inhabitants (Ladner and Steiner, 2003, according to Hemmings, 2006). Over half of Czech

municipalities have population below 500.

In order to overcome the problem of fragmentation, the changes of municipalities' tax allocation formula are introduced in 2001 – the governments are motivated to merge due to higher portion of allocation to larger governments. Due to such incentives such municipalities could gain 40% higher tax revenues by merging with other government. However, there are still no records on merger of governments which shows high level of political benefits in hands of political representatives that govern municipalities.

Surprisingly the research on the impact of mergers provides evidence for improved quality of local government service but does not find evidence on significant cost savings (Hemmings, 2006). This might be explained by the fact that measures that stimulate mergers usually come with increased level of resources given to the local government which decreases incentives to reduce costs. It is also possible that large governments take over additional responsibilities that have to be financed.

Interesting phenomena is visible in countries when it comes to region formation. Even though the countries were fully aware of the EU regulations and regional system of funding which requires regions between 0.8 and 3 million inhabitants (NUTS2), they constructed regions that did not comply with these demands. Together with statistical implications this made regional administration and policymaking more complicated.

Interestingly, the level of sub-national government indebtedness in all of the SEE countries is very low (usually averages 1 % of GDP). The reasons for such state is that in most of the countries there are hard budget constraints (balanced budget rule) imposed with control of central government in form of approvals for deficit financing. The low level of local government debt is particularly positive in these times of fiscal stress; however, the question remains what is the effect on local government investments. In addition, there are many benefits of financing investments through borrowing particularly in terms of efficiency and impact on local economic growth.

So far, the tax autonomy in SEE countries was very limited relative to western decentralised economies. Intergovernmental systems in SEE countries heavily rely on central government transfers towards subnational levels – either through the transfer of revenues from major taxes (Value added tax - VAT, Personal income tax - PIT and Corporate income tax - CIT) or conditional or unconditional grants.

## **FISCAL POLICY AND LOCAL GOVERNMENTS IN TIMES OF CRISES**

Usual framework of public finances considers the process decentralization in terms of function of allocation. However, contemporary research more and more attention devotes to the issues of fiscal federalism and macroeconomic stability (Shah, 2008). Common notion that regional (local) governments do not have role in stabilization policy is abandoned. This is particularly the case in recent economic crises where local governments in many countries are not any more passive observers and, on contrary, took

proactive measures (see Clark, 2009). Regional (local) government employment is by itself a stabilizer of the economic cycle. In times of crises it is not easy to lay off government employees and some studies show that while employment of the private sector decreases sharply, employment in the regional/local government even increased (see Boyd, 2009).

However, such countercyclical activities are not common feature of all countries. They usually occur in developed economies. Less developed economies both on central and regional/local level engage in procyclical behavior. Procyclical fiscal policy and its impact on macro-stabilization and economic growth have been extensively studied. On the other hand, the effects of the imbalance between levels of government are much less studied. It is assumed that because there is a vertical imbalance in the federal system, local authorities have incentives to increase spending above the socially optimal level and have high deficits. Such a situation is definitely confirmed by cases of Argentina and Brazil. (Struzennegger and Werneck, p. 124).

In federal countries regional and local sector share responsibility for conducting of fiscal policy and thus mitigate economic shocks. The allocation of responsibility focuses on the distribution of stable and cyclically less sensitive revenue sources and expenditure responsibilities for local authorities. This becomes a bit difficult for regions in case that they have some responsibility that is cyclically sensitive, such as social assistance (Shah, 2008, p. 119). In addition, there is still not clear whether the fiscal risks are greater in decentralized systems.

Both Keynesian and neoliberal theories agree in the fact that during recession the authorities need to use deficit financing and lower taxes, and during the expansion have budgetary surpluses and raise taxes. These same recommendations come from different reasons. Neoliberals argue that such approach raises allocative efficiency, and Keynesians point out positive effects of short-term stabilization of aggregate demand management policies (Struzennegger and Werneck, p.126).

Subnational governments in developed countries were strongly pressured towards fiscal consolidation effort by imposing "hard" budget constraints, and at the same time to additional efforts to increase the efficiency of their activities. It is believed that long-term fiscal sustainability is possible only in this way through the introduction of strict fiscal rules. More importantly such efforts should reduce negative effects of fiscal shocks (Sutherland, Price, Joumard, 2006). However, the fact is that pressures to reduce expenditures of the local sector comes more as a consequence of the increasing spending of the central government and extrabudgetary funds.

Regarding the effects of economic crises on local governments there are several important issues that define the scope and extent of these effects and possible outcomes of local government responses for mitigating the crises:

1. fiscal rules that bind the autonomy of local government spending



2. level of local tax autonomy and structure of local government revenues
3. institutional factor – fiscal transparency

Fiscal rules should prevent the unsustainable growth of debt and spending at the local level. Most commonly used fiscal policy is a policy of balanced budgets. Besides that, the usual tools are restrictions on borrowing and limits on tax rates. However, the general problem is that fiscal rules essentially do not succeed to restrain local spending. Local government spending is a result of numerous factors and politically sensitive programs that are difficult to connect with the objectives of budgetary spending limits (Sutherland, Price, Joumard, 2006, p. 6). This problem is even intensified in cases where there is insufficient awareness of the need for long-term planning of revenues and expenditures and program spending.

Nevertheless, studies show that the rule of balanced budgets and borrowing constraints lead to long-term sustainability of local fiscal policy<sup>2</sup>. Local governments under these rules experience faster adjustment of fiscal shocks, especially by reducing expenditure. (Sutherland, Price, Joumard, 2006, p. 38). There are five criteria necessary for setting up the appropriate fiscal rules (Sutherland, Price, Joumard, 2006, p. 7):

1. long-term fiscal sustainability
2. short-term economic stability
3. aggregate efficiency - in the sense of equalizing marginal benefits from public spending to limit the damages caused by taxation
4. allocative efficiency of public spending, which is manifested in matching quantity and quality of public services with local preferences
5. possibility to maintain the redistributive elements within the system, it should not come into question - the minimum standards should remain the same

The level of the tax autonomy is one of the crucial issues when analyzing possible effects of economic crises on local governments. Higher tax autonomy will give more power in hands of local government in combating the effects of crises. This is especially the case in federal countries with high level of fiscal transparency and high level of tax competition. In both cases local governments will try to keep the taxes low. Also, the distribution of tax revenues, which exposes the local communities who are vulnerable to cyclical fluctuations, will reduce the tendency to conducting the procyclical fiscal policy (Sutherland, Price, Joumard, 2006, p. 6). In any case, regardless of the way to curb excessive spending and taxes at the local level, fiscal transparency helps the sustainability of the budgets of local governments.

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2 However, the majority of research is related to the USA economy.

Table 2: Coping with the cycle

| Sub-central governments |                            |                  |                               |                                 |               |                                   |
|-------------------------|----------------------------|------------------|-------------------------------|---------------------------------|---------------|-----------------------------------|
|                         | Can draw on                |                  | Can cut mandated expenditures | Revenues are adjusted to        |               | Receive special financial support |
|                         | Rainy day or reserve funds | Off-budget funds |                               | Projected cyclical fluctuations | Actual shocks |                                   |
| <b>Canada state</b>     | +                          | +                |                               | +                               |               |                                   |
| <b>Canada local</b>     | +                          |                  |                               |                                 |               |                                   |
| <b>Czech Republic</b>   |                            | +                |                               |                                 |               |                                   |
| <b>Denmark</b>          |                            |                  |                               | +                               |               |                                   |
| <b>Finland</b>          | +                          | +                | +                             |                                 | +             | +                                 |
| <b>France</b>           |                            |                  |                               |                                 |               | +                                 |
| <b>Germany state</b>    |                            |                  | +                             |                                 |               |                                   |
| <b>Germany local</b>    |                            |                  |                               |                                 | +             |                                   |
| <b>Japan</b>            | +                          |                  |                               |                                 |               |                                   |
| <b>Netherlands</b>      | +                          |                  |                               |                                 |               |                                   |

Source: Sutherland, Price, Joumard, 2006, p. 28, adapted by the author

Many countries have developed procedures to ensure budget balance in the range of consultations with central authorities in case of realization of the deficit or making consolidation plans. There are also more strict measures, such as drafting of a new budget. However, in the event of a crisis rigid rules constitute an aggravating circumstance for countercyclical action of local governments. In majority of countries there are no measures envisaged in the case of the fiscal crisis caused by the economic shock. However, there are some exceptions (see table 2).

Additional problem for less developed economies is that their local governments are prone to conduct procyclical fiscal policy. A strand of contemporary literature tries to provide an answer why that happens. There are several potential explanations. In addition to argument of severe credit constraints in less developed economies during crises, some authors claim that the main reason for that is the so-called “voracity effect” proposed by Lane and Tornell (1999). They argue that during the period of boom some groups try to appropriate the surplus of resources. The competition between groups is more fierce the larger is the amount of available resources. Because of that the common pool problem is more intensified during the expansion (Struzennegger and Werneck, p.126).

The more decentralized country is, it is harder to maintain countercyclical fiscal policy. Particularly in case where local authorities have a greater part of government spending in their jurisdictions. Since they have no responsibility for stabilization policy there is an increased likelihood that in time of economic expansion they will set off in procyclical spending (Perry at al., 2008, p. 17). For example, case of Argentina provides example of such procyclical behavior of local governments. It is interesting that smaller local governments conducted more procyclical policy. Furthermore, it was shown that tax

revenues are more procyclical than transfers of central government (particularly local sales taxes).

Finally, the effects of financial markets are not irrelevant. It is well known that in times of crisis the cost of financing in developed countries fell, while in Eastern Europe significantly increased. Moreover, banks were not willing to finance the local community in order to ensure their own credibility and to isolate themselves in case of potential new financial shocks. Thus, the possibilities of refinancing of obligations are reduced and together with the additional pressure for reduction of transfers from the central government, it became hard to service the commitments from previous periods. Therefore, the local governments are not able to conduct countercyclical policies in their jurisdiction. Even if the local government has a flawless history in terms of fiscal credibility they might have problems with financing provision of goods or services. In time of crisis interest rates are rising and banks refrain from lending which has procyclical effect.

It has to be stated that existing fiscal rules are still far from being perfect, especially in context of mitigating the effects of economic crises. These rules depend on the objectives of fiscal policy of local governments which can be directed towards debt sustainability and short-term stabilization, reducing inequality, etc. There is certainly great need for establishing better rules that would contain elements of stabilization policy. Two important features of these rules that one should consider are: countercyclical transfers from the central government to ensure the smooth functioning of local authorities and use of stabilization funds (rainy-day funds).

## **RESPONSE OF LOCAL GOVERNMENTS**

As it was already noted, the possibility of regional (local) government units in proactive behavior towards mitigating the effects of economic crises depend largely on the given tax autonomy. Since the tax autonomy of local governments in Croatia is very limited one cannot expect significant measures conducted by the local sector. The only form of taxation which may have important effect is the change of rate of local surtax on personal income tax. Other possible sources are communal fees. Therefore, majority of measures that can be conducted fall in the area of local government spending.

Regarding the local government spending, majority of governments didn't conduct any proactive measures in combating the economic cycle. However some measures of limited scope and extent can be listed<sup>3</sup>:

- Some units adopted measures to reduce expenditures. Guidelines were sent to budget users to save up to 20% of revenues based on clearly defined priorities of

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3 This part is based on interviews with local government officials and official documents of local governments.

financing. These savings were partly related to expected effects of fall of revenues and budget deficits caused by excessive spending in previous period (mainly by financing infrastructure from current revenues);

- Some units decreased and other increased communal fees;
- In many local governments tax revenues did not fall significantly. However, some units postponed planned sale of property due to lower prices of assets which decreased total revenues;
- Some units experience high level of repayments for the infrastructure financed in recent period and are forced to cut other expenditures. In many cases these objects exert high costs of maintenance;
- Certain local taxes are reduced. However, due to low rates this effect is negligible in terms of decreasing the tax burden for the local businesses;
- Numerous local government conduct minor spending cuts more oriented towards showing fiscal discipline to the citizens (i.e. cutting the spending of city departments). However, these spending cuts are also negligible in terms of economic effects;
- In some cases the wages of local government employees are decreased;
- Grants and subsidies are increased in lesser extent.

The effects of economic crises on regional (local) governments in Croatia can be observed through fall of revenues and expenditures. In that sense, subnational public sector just follows the economic shock and does not have any significant countercyclical potential. There is no systematic behavior. Some measures are conducted in certain jurisdictions and motivated by gaining political points. It seems that overall effect of local government is procyclical but it cannot have significant effects on macroeconomic stability due to low level of decentralization and limited tax and expenditure autonomy of the local sector.

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# THE ROLE OF TAX AUTONOMY IN MUNICIPAL AND REGIONAL DEVELOPMENT

Olga Sharapova<sup>1</sup>

## INTRODUCTION

### *1. Significance of financial and tax autonomy for local self-government*

As early as 2000 the Steering Committee on Local and Regional Democracy of the Council of Europe highlighted in its opinion<sup>2</sup> the involving of a certain degree of financial autonomy in local self-government, the connection of local authorities' financial resources with their responsibilities, as well as the necessity of adaptation of local taxation, financial equalization mechanisms and state grants to the needs of municipalities. Not only politicians but also a doctrine demonstrates a strong link between local self-government and financial autonomy. Thus, under A. Guengant and J.-M. Josselin<sup>3</sup>, a local autonomy involves three main components: decision autonomy, management autonomy and executed competences. Actually the dimension of local autonomy depends on regional and local decisional freedom, a degree of participation of regions and municipalities in public affairs, a volume of their competences. Each of three mentioned components is consisted of its own elements but for us the inclusion of financial autonomy into autonomy of management is the most interesting question. Of course, this division is quite relative because a managerial process supposes also a decision-making. The classical (economic) vision examines the financial autonomy in two aspects – autonomy of expenditures and autonomy of revenues. An alternative structure of financial autonomy proposed by French senators<sup>4</sup> (legal approach) includes autonomy of financial management and autonomy of tax decision. In both cases the first type of autonomy is not possible without the second one. The Congress of local and regional authorities reminds that the competences granted by Constitution and/or legislation to the local self-government/regions should be relevant to the level of own resources<sup>5</sup>.

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2 Opinion 14 (2000) [HYPERLINK "https://wcd.coe.int/ViewDoc.jsp?Ref=OPI\(2000\)014&Language=lanEnglish&Ver=original&Site=COE&BackColorInternet=DBDCF2&BackColorIntranet=FDC864&BackColorLogged=FDC864"](https://wcd.coe.int/ViewDoc.jsp?Ref=OPI(2000)014&Language=lanEnglish&Ver=original&Site=COE&BackColorInternet=DBDCF2&BackColorIntranet=FDC864&BackColorLogged=FDC864) (25.07.2012)

3 Guengant et Josselin, 2005 : 148.

4 Hervé, 2011 : 134.

5 Opinion 14 (2000), *ibid*.

Even if there is no common comprehension of financial autonomy, tax autonomy is anyway considered as a part of financial autonomy. Tax revenue is recognized as the most important own resource because of its stable character in the long-term perspective which allows to the local authorities to assess the volume of future revenues and to pursue a sustainable socio-economic policy. Consequently, the tax autonomy represents an indicator of independence of local self-government not only in federations, but also in unitary countries. Thus the senators recognize that in France the financial autonomy of regions, departments and municipalities is inseparable from vast tax autonomy<sup>6</sup>. This trend is typical not only for French context but it is widespread, also for Russia. However, the tax autonomy does not ensure automatically the financial autonomy. Why? Because even if the local authorities are authorized to establish a rate for certain tax (legal capacity), it does not entail a mobilization of necessary resources (economic capacity) when a base for this tax is weak/insufficient. A striking illustration is a property tax for physical persons in Russia. Nevertheless a municipality/region can really, not nominally, take a decision only if its management autonomy combines with the tax autonomy. Thus the tax autonomy stipulates the financial autonomy.

## *2. Interconnection of tax autonomy and tax potential*

The constitutional reform of 2003 in France demonstrates a desire of French legislator to grant a real financial basis to local self-government. At the same time a financial autonomy is accompanied by a requirement of equalization (vertical and horizontal) in order to reduce negative impacts of tax autonomy and to respect the principles of solidarity and equality of municipalities and regions concerning their finances. We do not find any mention of equalization principle in the Russian Constitution but it is represented in the Budgetary Code and in the acts of Government. Thus according to the Concept of the interbudgetary relations and the organization of the budgetary process in regions and local government until 2013<sup>7</sup> the mechanism of equalization of local and regional budgets allows to ensure a certain level of revenues sufficient for financing of attributed responsibilities and *ultima analysi* to provide a comparable range and level of public services. The European experts of local self-government put a substantial degree of equalization in the same row with the tax autonomy as a necessary condition of fiscal decentralization and a strong local government<sup>8</sup> because it can potentially favor the achievement of the goals of economic stability and become a tool of sustainable and balanced policy of sub-national development. An implementation of equalization's mechanism is possible due to the assessment of tax potential of regions and municipalities. At the same time at least in theory we can observe that the increasing of

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6 Krattinger, Gourault, 2008-2009: 152.

7 Ordinance of the Russian Federation Government no 1123-r, p. 4.

8 Opinion 14 (2000), *ibid*.

tax autonomy level fosters the development of sub-national tax potential. However, such equalization may entail some negative consequences for the local authorities by forcing them to establish the same tax rates and therefore to prejudice a tax competition.

The French institutional system is characterized by a strong fragmentation of the municipal map. With the existence of tax autonomy this fragmentation entails firstly and potentially a horizontal tax competition between municipalities despite of the State policy of intermunicipal cooperation and secondly a tax sharing between the various administrative levels<sup>9</sup>. There are two main kinds of tax competition according to its effects – positive and negative (harmful). On the one hand, the tax competition may contribute to the principle of subsidiarity placing regional/local tax decision-making closer to citizen's preferences, to the improvement of public finances' management, to the prevention of tax and expenditure excesses, to increasing public sector's efficiency and finally to regional/municipal development. On the other hand, the tax competition may lead to the growth of tax rate disparities, to an under-provision of public services and finally to the slowdown or absence of regional/municipal development. Despite of a real significance of tax competition for local and regional development, we should take into consideration that the French legal science uses extremely rarely the notion of tax competition, that conception is more proper to the papers of US researchers. That American tradition expands to the European economic studies. The Russian legal science does not contain any significant studies of tax competition as well. Some references to this notion can be found in few governmental acts. The Russian government traditionally stresses on the prevention of unfair tax competition at the sub-national level and the ensuring of common tax space<sup>10</sup>; at the same time the main objective of the Center was and remains an extension of tax powers of regional and local authorities, i.e. tax autonomy.

### *3. Historical development of financial and tax autonomy and tax potential in France and in Russia*

The notions of financial and tax autonomy and tax potential did not appear simultaneously and recently.

Firstly we will examine briefly a legal development of financial and tax autonomy in Russia and in France. In its Ordinance<sup>11</sup> of April 28<sup>th</sup>, 1995 the Government noted that in 1994 strengthening of regional tax autonomy took place and redistribution of budgetary revenues for benefit of local budgets continued. However short-term actual improvement of the situation with regional tax autonomy was not significantly efficient for socio-

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9 Madiès, 2007: 218-230.

10 Ordinance of the Russian Federation Government no 584 of August 15th, 2001, p. 8.

11 Ordinance of the Russian Federation Government no 439 of April 28th, 1995, p. 23.



economic development at the sub-national level. In the Ordinance<sup>12</sup> of August 15<sup>th</sup>, 2001 the Government underlined that until regional and local authorities did not have legislatively fixed tax-budgetary autonomy, they would not be interested in efficient control of public finances and creation of favorable conditions for development of tax potential. The principle of autonomy of regions and municipalities in budgetary field is provided by the article 31 of the Russian Budgetary Code, whereas the principle of tax autonomy is not clearly expressed in any legal act till now. As of financial autonomy, for its strengthening the stable tax legislation and interbudgetary relations are necessary; that was also recognized by Government in 2006<sup>13</sup>. During last six years the significant results were reached in this area. Monitoring of local budgets in 2009 revealed a decrease of municipal own revenues on 4% in comparison with 2008, however in 2011 the 14% increase of their own incomes in comparison with 2010 was noted<sup>14</sup>. Thus, there are neither definitions of financial and tax autonomy, nor substantial statements about it in Russian legislation and Constitution. Only several governmental regulations touch these questions.

In contrast to Russia, French Constitution by the article 72-2 provides a financial autonomy's principle. This article resulted from the constitutional reform of 2003. The last one based on a declaration of general policy provided by French prime-minister J.-P. Raffarin at July 2002 in the Parliament<sup>15</sup>. A general objective announced in the declaration was a construction of unitary and decentralized Republic. According to the constitutional revision of March 28<sup>th</sup>, 2003 the guaranty of financial autonomy of sub-national government was fixed at the constitutional level. The most interesting for us provision of the article 72-2 is the following: tax resources and other own revenues of territorial entities for each category of them should represent a determinative share of their revenue. About the share different proposals were made during elaboration of the article 72-2. Thus ones considered that tax resources and other own revenues should represent preponderant share of their revenues. Others assessed such statement as unclear and suggested that tax resources and other own revenues should represent more than half of their revenues<sup>16</sup>. It was the most important point of discussions. The members of Parliament hesitated because on the one hand they wanted to grant a real financial autonomy and on the other hand they saw a sad situation with the local taxation<sup>17</sup>. Finally a word «determinative» was chosen as a consensus. Thus, the actual constitutional wording of sub-national governments' financial autonomy needs to be specified. The

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12 Ordinance of the Russian Federation Government no 584, *ibid*.

13 Ordinance of the Russian Federation Government no 467-r, p. 4

14 Information about the results of local budgets' monitoring in 2009 and 2011, [http://www1.minfin.ru/ru/reforms/local\\_government/monitoring/](http://www1.minfin.ru/ru/reforms/local_government/monitoring/) (01.08.2012).

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17 Dechaux, 2008 : 4.



of regions, their tax potential and budgetary provision. All that required the centralization of budgetary resources not only in short- and medium-term perspective, as it was provided initially by the Government, but also in long-term perspective. For purposes of incentives of regions and municipalities to develop their tax potential and to improve the quality of regional finances administration, diverse requirements to budgetary process for regions and municipalities were provided by the Budgetary Code. These requirements depended on the share of interbudgetary transfers (except subventions) in the own revenues of regional and local budgets. Unlike to financial and tax autonomy, a tax potential is defined by Russian legislation which provides also enough details about it. Concerning the development of notion «tax potential»<sup>24</sup> in French legislation, we found the traces of municipal tax potential in the Code of Municipalities (does not exist now). The article L234-4 of version abolished in 1996 determined a tax potential of municipality by quite laconic way. Thus it was calculated by an application of the national average tax rate to each of municipal bases of four local direct taxes (without specification). After the abolishment of mentioned article a definition of municipal tax potential became more detailed and was provided by the GCTE. As of departmental tax potential, a first mention of its structure was in the law of 1985 about a general grant of functioning. The article 33 of this law was also laconic and determined a departmental tax potential as an amount of bases of four local direct taxes multiplied by national average tax rate to each of them. This article was abrogated in 1996, but the same statement was kept in the article L3334-6 of the GCTE. In 1999 a composition of departmental tax potential expanded by the compensation according to the law of finances of that year. Since 2005 such compensation was replaced by a fixed grant and the article L3334-6 added the average of five last exercises through registration fees or a tax of real estate transactions' publicity (under certain conditions). The version of December 30<sup>th</sup>, 2011 provided the fullest determination of departmental tax potential. It will be examined in the first part of the paper.

#### *4. Definitions of tax autonomy and tax potential*

Before continuing with the study of tax potential and tax competition in their connection with tax autonomy, we will attempt to elaborate the definitions of these initially economic notions from legal point of view.

According to the OECD approach<sup>25</sup>, the notion of tax autonomy embraces different aspects of liberty of sub-national governments to dispose of their own taxes. These

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24 Different versions of articles concerning a sub-national tax potential are available at the web-site of French legislation

<http://www.legifrance.gouv.fr/affichCode.do?cidTexte=LEGITEXT000006070633&dateTexte=20120804> (02.08.2012).

25 Blöchliger, King, 2006: 9.

aspects include capacity of regions and municipalities to introduce or to abolish a tax, to set tax rates, to determine the tax base, or to grant tax abatements. Sometimes the tax autonomy is linked not only with own local/regional taxes but also with tax sharing between different state-administrative levels. We can refer to the shared taxes as a component of tax autonomy if the tax rates or/and bases of these taxes are not defined by the Center or any other unique level, but there are municipalities or regions that influence on these elements and may negotiate the sharing formula with central government (Russian and French case). Thus the tax autonomy can be defined as a legal and economic capacity of regions/municipalities to mobilize independently their own revenues of tax nature in order to cover expenditures resulted from the attributed responsibilities. If we replace «the own revenues of tax nature» by «the own revenues and the transferred resources» in this definition, we obtain the financial autonomy.

For determining the tax potential we will use some statements of the Russian Budgetary Code (articles 131 and 137) and of the French Report prepared jointly by the Ministry of Economics, Industry and Employment, the Ministry of Budget, Public Accountants and the State reform and the Ministry of Home Affairs, Overseas Territories and Territorial Entities in May 2010 during the elaboration of local finances reform in France<sup>26</sup>. So we can define the tax potential as an aggregate of tax bases attributed by Constitution and/or legislation to region/municipality which serves as a measure of tax wealth in order to determine a level of budgetary provision of regions/municipalities, to assess the differences of tax bases' distribution and to neutralize the economic disparities at the sub-national level.

### *5. Key question*

In this article we will try to determine how legal and regulative provisions influence on the sub-national tax potential and tax autonomy in view of their significance for regional and local development in France and in Russia.

### *6. Delimitation of topic*

We have chosen these countries for several reasons. France is a representative of the old-democratic West European countries with relatively recent tradition of decentralization; Russia is a representative of the young-democratic East European countries with recent tradition of decentralization and strong trend towards a consolidation of State power. Besides they represent different conception of local autonomy in connection with financial autonomy. In France such conception focuses mainly on the budgetary autonomy, which deals not only with management autonomy (i.e. to set partially local

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26 Durieux, 2010: 16

taxes) but also with the possibility for local self-government to apply their certain powers (i.e. to finance themselves due to the other local resources, and in particular loans)<sup>27</sup>. Such approach to the financial autonomy supposes that the regional/local financial autonomy may be restricted by the Center through several tools such as compulsory expenditures and the framing of the tax competence of local authorities. In Russia this conception essentially stresses or pretends to stress on the tax autonomy which refers to a real power in tax field at the sub-national level.

Our framework is legal and economic. Traditionally the notion of tax potential is the subject of economic researches but only a few studies from legal point of view exist. We propose mainly an analysis of legislation and regulative acts; we will attempt to examine how this economic phenomenon is «wrapped» in a law.

We will focus on sub-national tax potential and tax autonomy as a tool of its increasing, firstly we will examine the application and composition of regions' and municipalities' tax potential (I) and secondly – the measures of increasing of regions' and municipalities' tax potential by contributing to the tax autonomy (II) taking into consideration their significance for development of regions and municipalities.

## **APPLICATION AND COMPOSITION OF REGIONS' AND MUNICIPALITIES' TAX POTENTIAL**

The main influence on tax potential at the sub-national level is exerted by two factors – legal (legislative and regulative acts, primarily in budgetary and tax field) and economic. Within this article our attention will be concentrated on the first factor. First of all we will study the legal framework of tax potential and field of its using (A), and then – the elements of tax potential and influence of its determination on sub-national tax autonomy and development (B).

### *A. Legal framework of tax potential and field of its using*

1. For a start we should define a *legal framework of tax potential*, a level and a type of legal sources.

In France, as in an unitary State, this is a competence of Parliament which adopted the main texts for all level of territorial entities (departments, municipalities, intermunicipal groups\*) – the General Code of Territorial Entities (GCTE) and the General Code of Taxes. The executive acts in this field can be adopted by decrees of the State Council.

In Russia, federative State, there are three levels of relevant legislation and regulation. The first one is a federal. We can find a few mentions of tax potential in the Budgetary

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27 Gilles, 2012: 99-100.

\* There is no indicator of tax potential for equalization mechanism at the third level – for regions (see chapter II of Section III in the 4th Part of GCTE).

Code, a main information contains in the Tax Code which sets the elements influencing on tax potential: tax rates (the most important), competence of the Tax service and system of tax control. Tax potential itself is a subject of the Federal Government competence which through the Ordinances (legal acts of regulative nature) elaborates the main provisions about tax potential of regions. Besides, the framing of interbudgetary strategy which includes a tax potential development is also provided by the Government. The second level is regional. Regions by their laws determine the own methodology of tax potential calculating for municipalities situated on their territory. The third and last level is local. Municipalities elaborate the measures of increasing of their tax potential and provide the terms of its implementation. Normally this is a field of executive power, a mayor and an administrative body of municipality.

2. Both in Russia and in France the tool of *tax potential is used for equalization's mechanism at the sub-national level*. However in France a tax potential is the most appropriate indicator for a horizontal equalization as a measure of tax bases independent from tax rate policy<sup>28</sup>, whereas in Russia a tax potential plays the most important role in a vertical equalization.

There are two main types of federal grants to the Russian regions that use a tax potential as a determinant – for equalization of budgetary provision<sup>29</sup> and for maintaining of measures for ensuring of budgets' balance in regions reached the best results in increasing of their tax potential<sup>30</sup>. There were also some state grants for departments in France distributed according to their tax potential<sup>31</sup> – general grant of functioning (grant of equalization, is not provided by the GCTE now), general grant of equipment (*dotation globale d'équipement*, still exists); these grants represent a vertical equalization mechanism.

There are certain special grants for some entities of intermunicipal cooperation (*établissements publics de coopération intercommunale dotés d'une fiscalité propre*) also under the criteria of tax potential, but it is out of our scrutiny within this paper. For Russian municipalities there are regional grants for equalization of budgetary provision; in this case a local tax potential is applied for calculating of the grants. In France there are two main kinds of grants for municipalities (*communes*) using the criteria of tax potential<sup>32</sup> – general grant of functioning (*dotation globale de fonctionnement*) and grant of equipment of rural territories (*dotation d'équipement des territoires ruraux*). The first type of grants is divided into development grant (*dotation d'aménagement*) (which includes national grant of equalization (*dotation nationale de péréquation*) and grant of

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28 Durieux, 2010: 29.

29 Provided by the articles 131 and 138 of the Russian Federation Budgetary Code and by the Ordinance of the Russian Federation Government no 670.

30 Ordinance of the Russian Federation Government no 798.

31 See the article L3334-6 of GCTE.

32 See the articles L2334-4, L2334-7, L2334-14-1, L2334-21, L2334-33, L2336-2, L2336-3 of GCTE.

rural solidarity (*dotation de solidarité rurale*), and fixed grant (*dotation forfaitaire*). Both kinds of grants for municipalities in France are provided by the Fund of equalization of intermunicipal and municipal resources existing due to the contributions of intermunicipal group with cumulative financial potential per inhabitant exceeding 90% of average cumulative financial potential per inhabitant and the contributions of municipalities out of any group of own taxation with cumulative financial potential per inhabitant exceeding 90% of average cumulative financial potential per inhabitant. We should underline that a financial potential and the tax one are not the same tool. A financial potential includes a tax potential and state grants.

If the legal sources and a field of application of tax potential at the sub-national level are more or less similar in France and in Russia, it is not the same for its structure.

### *B. Elements of tax potential and influence of its determination on sub-national tax autonomy and development*

1. In both countries a tax potential is calculated per inhabitant but there are some significant differences between a *composition of tax potential* in Russia and France.

In Russia a tax potential of the region is calculated by extremely difficult formula<sup>33</sup>. In a summary this formula includes:

(a) the forecast of revenues of regional budgets for the next financial year provided by tax on moral persons' profits, personal income tax, property tax for moral persons, tax applied within a simplified system of taxation, single tax on a fixed income, excises, tax on mining operations;

(b) indicators characterizing a tax potential of the region during 2 years before the current year and on the last day of current year. Such indicators include assigned salary, retail turnover, volume of paid services rendered to the population through all channels of realization, residual book value of capital assets of commercial enterprises, cost of mineral products production, volume of spirit production shipped by enterprises.

In France the departmental tax potential was till recently determined by adding the following amounts:

(a) product determined by an application of the national average tax rate to the departmental bases of land tax on a built property (*taxe foncière sur les propriétés bâties*);

(b) sum of departmental products collected through a contribution on an added value of enterprises – *CAVE (cotisation sur la valeur ajoutée)* and a fixed taxation for network companies (electricity, water supply);

(c) sum of positive or negative amounts resulting from the application of compensation grant entailed by the reform of professional tax and application of national

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33 Ordinance of the Russian Federation Government no 670.

fund of departmental resources' individual guaranty;

(d) average sum of products collected by the department during the last five exercises through registration fees or a tax of real estate transactions' publicity (under certain conditions) and products collected through a special tax on insurance contracts by the department during the previous year;

(e) amount collected during the previous year through a part of fixed grant.

Concerning the municipal tax potential in France, it is calculated for one municipality by adding the following amounts<sup>34</sup>:

(a) product determined by an application of the national average tax rate to the municipal bases of residence tax, of land tax on a built property and land tax on a unbuilt property;

(b) sum of:

(a.a) product determined by an application of the national average tax rate to the municipal bases of enterprises' land contribution;

(a.b) municipal and intermunicipal products collected through a CAVE, an additional tax of the land tax on a unbuilt property and fixed taxation for network companies (electricity, water supply) as well as tax on commercial spaces;

(c) sum of positive or negative amounts resulting from the application of compensation grant entailed by the reform of professional tax and application of national fund of municipal and intermunicipal resources' individual guaranty;

(d) sum of products collected by the municipality through a gambling charge, a surtax on mineral waters and mine fee;

(e) amount collected during the previous year through a part of fixed grant.

Unlike France where the methodology of tax potential determination is provided by the GCTE, in other words by the Center, in Russia there are regions that elaborate such methodology through their own legislation. We will examine the Methodology of tax potential calculating of municipal districts (urban counties) provided by the Law of Kaluzhsky region<sup>35</sup>. We have chosen this region because it demonstrated the best results of tax potential increasing in 2011 (first place from 83 regions).

Tax potential of municipal district (urban county) is calculated by the formula, no less difficult, than formula for regions. In summary a local tax potential is equal to tax resources per inhabitant. The last one is the amount of tax resources provided by representative taxes – taxes which reflect a total tax potential in the most realistic way. In municipalities of Kaluzhsky region representative taxes embrace the personal income tax, the property tax for moral persons, the single tax on fixed income and the tax applied

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34 Article L2334-4 of GCTE

35 Law of the Kaluzhsky region no 79-OZ.



within a simplified system of taxation. It is interesting that this group does not include any local taxes. An amount of tax resources provided by each type of representative taxes is determined as an average tax base for each tax (salary, residual book value of capital assets of enterprises, retail turnover and turnover of catering, receipts from realization of goods, works and services of small enterprises) multiplied by several following ratings: representative tax rate, ratio of allocations to the budget of municipal districts (urban counties) set by the Budgetary Code, single ratio of allocations set by the legislation of Kaluzhsky region, coefficient of current situation in particular municipal district (urban county). An average tax base is calculated according to the indicators of current year and two previous years (medium-term indicators). A representative tax rate is determined on the basis of forecast concerning personal income tax and salary next financial year in the whole region. A coefficient of current situation is the indicator reflecting average speed of growth of the tax for 7 months during current financial year.

For urban and rural settlements a calculation of tax potential is provided by resolutions of the mayor of the municipal districts, on which territory these settlements are situated. Analysis of the Resolution<sup>36</sup> of the mayor of municipal district Borovskoj (Kaluzhsky region) allows to distinguish similarities and differences in determination of tax potential of settlements and municipal districts (urban county). In both cases representative taxes and representative tax rate are used. However settlements' tax potential is determined on the basis of indicators next financial year, including local taxes.

Less than year ago the Russian Government adopted the ordinance<sup>37</sup> in order to foster regions to increase their own tax potential. Thus, the regions which reached the best results in increasing of regional tax potential, obtain grants for maintaining measures of budgetary balance' ensuring. The results of regional activity of their tax potential increasing is assessed according to the population size at the end of year, taxation, reached level and dynamics of indicators in investment activity, and industrial production. Indicator «taxation» represents volume of tax revenues of budgets except the tax on mining operations, the tax on moral persons' profits and regional taxes provided by economic activities «Production of minerals». These tax revenues were excluded from the indicators of tax potential increasing because it is a question of regional natural resources, in other words a revenue source which is at the disposal of particular region independently from its economical policy. It is too early to talk about positive or negative effect of this legal act to tax potential of the Russian regions, therefore we pass to already accepted measures of tax potential's increase at the sub-national level and their efficiency for development of regions and municipalities in France and Russia.

2. So what is the *influence of calculating methods for regional and local tax potential on their tax autonomy and development?* In Russia a regional tax potential

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36 Resolution of the mayor of municipal district «Borovskoj district» no 3193.

37 Ordinance of the Russian Federation Government no 798.

represents a combination of predicted and actual receipts multiplied by 0.3 for the last year indicator and by 0.35 for two previous years' indicators (almost an average tax rate for medium-term indicators). Local tax potential is determined according to weighted average tax bases depending on indicators for current year and for two previous years and to certain predicted and actual indicators. In France for calculating departmental and local tax potential an average rate is applied directly to tax bases, both these elements are mainly fixed for last year (short-term indicator). On the one hand, the French methodology seems to be more exact by using the factual indicators. On the other hand, the Russian methodology by using more often medium-term indicators seems to be more suitable to requirements of stable character of formulae for the assessment of local and regional revenues, first of all the tax ones. Stability is an extremely important factor for a tax autonomy because the application of medium-term and long-term indicators allows to observe an evolution of the regional/local taxes and other revenues, to predict its future development and hence a further situation with tax autonomy and to take the necessary measures. It is curious that in Russia the basis of regional and local tax potential (except rural and urban settlements) are federal and regional taxes and special tax regimes whereas in France – departmental and local taxes. Thus, *a priori* a tax potential at the sub-national level in Russia depends mainly on federal taxes. This is a conspicuous indicator of local and regional tax autonomy development.

## **MEASURES OF INCREASING OF REGIONS' AND MUNICIPALITIES' TAX POTENTIAL BY CONTRIBUTING TO TAX AUTONOMY**

By extending local and regional tax autonomy it is possible to increase their tax potential which represents one of the main indicators of economic development which is a basis of regional/local development in whole. We will stress on the legal arrangements improving the situation with sub-national tax potential level taken by regions and municipalities themselves (A) and by the Center (B).

### *A. Legal measures of tax potential increasing provided the regional and local level*

1. First of all, the article 12 of the Russian Tax Code provides a capacity of regions and municipalities to introduce and abolish through a regional/local legislation their own taxes enumerated at the Tax Code. For such taxes representative bodies of regions and municipalities normally set the rates, scheme and terms of tax payment if these elements are not determined by the Tax Code. Tax reliefs could be set at the both levels within the limits stipulated by the Tax Code. Also representative bodies of municipal districts, urban counties and two cities of federal importance (their status is similar to other regions) – Moscow and St. Petersburg can introduce a special system of simplified tax on the fixed income for certain kinds of activity. Such system is provided by the Tax Code (chapter 26.3) and applied at the same time with a usual taxation. Thus, *the first step of*

*municipalities and regions within legal framework towards increasing of their tax autonomy and tax potential* is an application of optional tools like introduction of the regional and effective local taxes, special tax regimes, abolishment of unproductive and difficult for administration local taxes. Provision of tax reliefs may be useful as well for tax potential and tax autonomy, because normally this measure fosters a creation of new enterprises and hence new job, what means new tax bases. Regions and municipalities should use these possibilities even if their degree of freedom is quite limited by the federal legislation.

*2. The second step of sub-national representative and executive bodies towards expansion of their tax autonomy and tax potential by using legal capacities* is an elaboration of own derivative measures with the aims of increasing of the tax collection's level, strengthening of tax discipline, expanding of tax base, improvement of tax administration's quality. Normally regional legislation determines the directions of tax potential's increasing, whereas the practical measures are provided, as a rule, by municipal legal acts, because exactly local authorities are capable to choose those tools that will be the most effective depending on specific characteristics of particular municipality. For example, the resolution of the Administration of Aleksandrovsky municipal district of Stavropolsky region stipulates that the following measures in order to expand a tax base and increase tax revenues of the local budget should be taken:

(a) creation of conditions for start-up of new producing capacity and factories in the district,

(b) analysis of actual amounts of base profitability's coefficients (K2) applied within a single tax on fixed income in order to increase,

(c) analysis of the total sum of tax debt to the budget of Aleksandrovsky municipal district,

(d) meetings of joint commission on increasing of the overall performance of salary's legalization (problem of so-called «black» and «grey» salary) and commission on improvement of the payments and calculations' system within the administration of Aleksandrovsky municipal district.

However some practical measures of increasing of the sub-national tax potential can be determined by regional legal acts on the basis of suitability of their application on all territory of the region. For example, the resolutions of the mayor of Belgorodsky region (22<sup>nd</sup> place from 83 regions) provide a passport system of municipal, state and other enterprises<sup>38</sup>. Enterprise's tax passport represents complete information about its main social and economic indices of activity, its structure, the main indicators used for calculation of tax base, data affecting tax base on profits' tax, the dynamics of taxing payments to the budgets of different levels, tax debt and burden<sup>39</sup>. Analysis of economic potential of enterprises and relevant municipality, as well as revealing of the reasons of growth or

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38 Resolutions of the Mayor of the Belgorodsky region' s administration no 603 and no 267.

39 Voloshina, Fedorova, Klimenko, 2002.

decrease of tax receipts are facilitated considerably due to tax passports.

What is an efficiency of implementation of such measures? In 2011 the budget of Kaluzhsky region (1<sup>st</sup> place from 83 regions) receives by 17,5% tax revenues more than in 2010, the budget of Murmansk region (68<sup>th</sup> place from 83 regions) – by 13,1% more, the budget of Ulyanovsky region (17<sup>th</sup> place from 83 regions) – by 11,3% more in comparison with 2010<sup>40</sup>.

It is interesting that we can find some regional/municipal legal acts about measures of increasing of their tax autonomy and tax potential in Belgium, in Switzerland, in Russia, *i.e.* in federations, but we did not reveal anything similar in French sources. Nevertheless in both countries, France and Russia, the main influence on sub-national tax potential is reached by the Center through national legislation.

### *B. Legal measures of tax potential increasing provided the national level*

Mainly we mean modifications in budgetary and tax legal acts.

Thus by the example of Belgorodsky region we can observe an impact of federal budgetary-tax policy through the modifications of tax sharing's ratios for different levels of budgets. In 2001 the second part of Russia Tax Code shortened the list of local taxes fixed by the Law about the bases of tax system, instead of 23 local taxes 5 taxes were provided: land tax, property tax for physical persons, advertising tax, succession tax, license tax. At the same time the abolition of Federal road fund<sup>41</sup> influenced on the taxes for benefit of territorial road fund. Besides, the budgetary legislation changed the ratios of tax revenues' sharing between different budgets. As a result of these changes the revenues of federal budget increased at one and half times, the regional budget had 30% more tax receipts and revenues of local budgets and territorial road fund<sup>42</sup> decreased respectively by 90% and 60%. If a federal legislator kept the rates at the level of previous year (2000) for tax payments to the territorial road fund, tax revenues would be three times more. Because of the collecting of 100% VAT for profit of federal budget, the losses of regional budget were 9% of revenues of whole regional budget<sup>43</sup>.

In France one of the reforms of local taxation comparable by its effect on the tax potential with the putting into force of the Tax Code in Russia became the abolition from 2010 of professional tax for companies and its replacement by the land contribution of enterprises (LCE) and CAVE. We can make following conclusions resulting from the work of the mission Durieux<sup>\*\*</sup>:

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40 Statistics data are available at the web-sites of these regions:  
[http://www.kalugaonline.ru/news/153/news153\\_6970.html](http://www.kalugaonline.ru/news/153/news153_6970.html) (29.07.2012), <http://m51.ru/?p=4624>  
(29.07.2012), <http://ulgov.ru/news/regional/2012.03.01/21809/> (29.07.2012).

41 Abolished by the Federal law n° 150-FZ of December 27th, 2000.

42 Does not exist at present.

43 Voloshina, Fedorova, Klimenko, 2002.

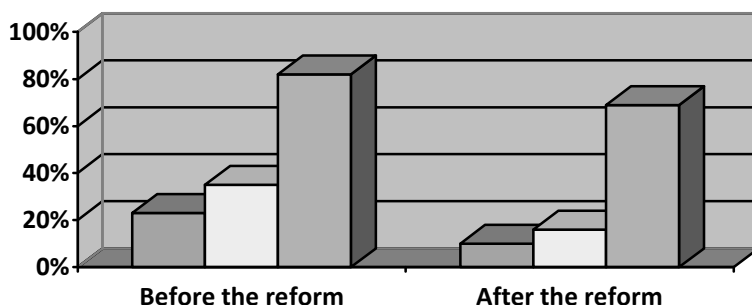
\*\* Group of state financial inspectors asked by the French Government to provide a report about the influence of the reform of professional on the local taxation and enterprises.

(a) tax autonomy at the sub-national level may strengthen because a part of tax revenues should increase again in total resources of municipalities<sup>44</sup>;

(b) the reform contributes to the tax autonomy because in a long-term prospect of 2015 the reform should increase somewhat a financial autonomy of municipalities<sup>45</sup>. In a short-term perspective a local financial autonomy degrades slightly but remains over the limit fixed by the organic law (60,8 % for municipalities, 58,6 % for departments, 41,7 % for regions);

(c) the consequences of this reform on the tax potential of municipalities are also positive because «the dynamics of new tax bases of CAVE and LCE should be stronger than that of the bases of professional tax»<sup>46</sup>.

The works of the mission Durieux represent essentially forecasts and simulations of evolution. This report stresses on the impact of legislative changes in the field of sub-national finances on the reduction of inequalities of tax potential per inhabitant between municipalities, departments, regions. After the realization of this reform, first appreciations of practical results appeared. Thus Alain Guengant, President of the CNRS (National center for scientific research), demonstrates that it entailed a back-off of the tax autonomy at the sub-national level<sup>47</sup>. According to Guengant and senators<sup>48</sup>, «the regions lost a totality of powers of tax rate voting within a new tax system and kept it only for three indirect taxes: share of internal tax on petroleum products, tax on car registration and apprenticeship tax».



■ Tax autonomy of regions    □ Tax autonomy of departments    ■ Rate power of municipalities

44 Durieux, 2010 : 15.

45 Durieux, 2010 : 14.

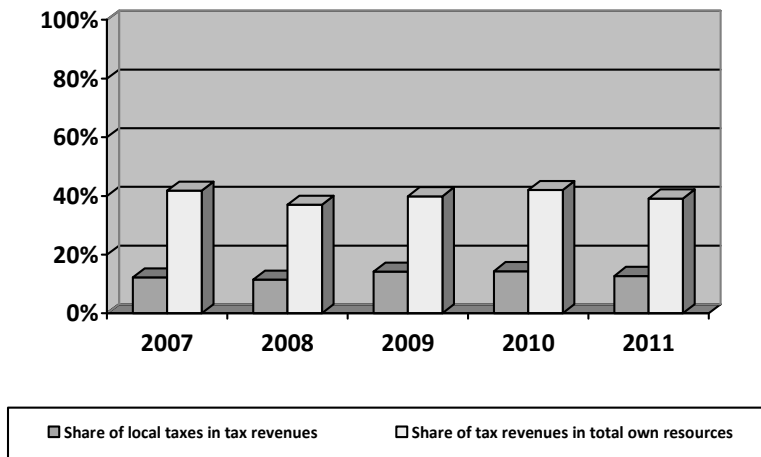
46 Durieux, 2010 : 2.

47 Guengant, 2010 : 177.

48 Hervé, 2011 : 135.

However if for us the tax autonomy is an inseparable part of financial autonomy and an element extremely important for a local autonomy, the French Constitutional Council considered in view of this reform that «it results neither from the article 72-2 of the Constitution of 1958, nor from other constitutional statement that the territorial entities benefit from a tax autonomy»<sup>49</sup>. This article is considered as constitutional principle of financial autonomy, it provides that territorial entities can enjoy resources freely within the conditions determined by law. They may receive all or part of taxes of all kinds and may be authorized by law to determine tax base and rates within the limits set by such law. Tax resources and other own revenue of territorial entities for each category of them should represent a determinative share of their revenue. If we refer to the approach to tax autonomy used by the OCDE, this position of French Constitutional Council does not seem clear. However we can remember an expression of Édouard Balladur, president of the Committee for the reform of local entities created by the former president of France Nicolas Sarkozy in 2008, who wrote in his report that «the territorial administration is an eminently political question in France»<sup>50</sup>. It is also fair for Russia.

Thus, on the one hand, various Concepts and Programs developed by federal government, considered and considers increasing of tax autonomy and hence tax potential of municipalities among the main tasks of tax-budgetary policy in Russia. On the other hand, practical implementation of such policy demonstrates quite average results<sup>51</sup>:



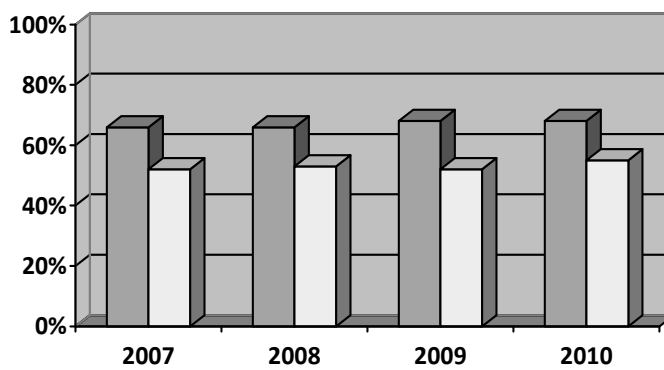
49 Décision du Conseil constitutionnel n° 2009-599 DC, <http://www.conseil-constitutionnel.fr/decision/2009/2009-599-dc/decision-n-2009-599-dc-du-29-decembre-2009.46804.html> (27.07.2012)

50 Hervé, 2011: 136.

51 Information about the results of local budgets' monitoring in 2007-2011, *ibid.*

We can see little (from 12,2% to 14,4% for local taxes and from 38,1% to 42% for tax revenues) but stable growth of local taxes' share and municipal tax revenues in total from 2007 till 2010, than in 2011 a decrease reached a level of 2007 (even below for tax revenues).

For comparison we cite the same data for France (see below)<sup>52</sup>:



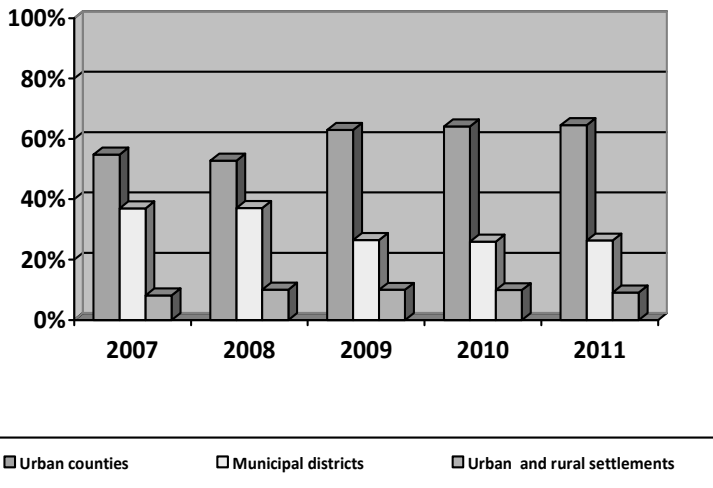
■ Share of municipal taxes in revenues of municipalities  
 □ Share of tax revenues in total own revenues of municipalities

We have not had yet the data for 2011, so we cannot see an impact of the reform of professional tax. Last 4 years a share of municipal taxes in local tax revenues and a share of tax revenues in total own resources of municipal budgets remain almost the same (~52% and 66% respectively).

Concerning the equalization mechanism, the main tool of which is tax potential, Russian situation should also be improved. It is typical the unequal distribution of tax revenues at the local level which can be explained by significant differences on the social and economic plan between the different types of local entities and by the tradition (established in 2001 by the Program of development of the budgetary federalism in Russia until 2005) of high ratios of the sharing of the federal and regional taxes for the benefit of urban districts. The following picture shows this inequality.

<sup>52</sup> Les collectivités locales en chiffres 2012,

[http://www.dgcl.interieur.gouv.fr/workspaces/members/desl/documents/clench/2012/les\\_collectivites\\_lo8798/downloadFile/file/05\\_chapitre-4.pdf?nocache=1334926106.21](http://www.dgcl.interieur.gouv.fr/workspaces/members/desl/documents/clench/2012/les_collectivites_lo8798/downloadFile/file/05_chapitre-4.pdf?nocache=1334926106.21) (03.08.2012).



Thus, approximately only 10% of tax revenues come to the budgets of urban and rural settlements, between 27 and 37% – to the municipal districts’ budgets and over 60% are received by urban counties.

That situation can be also explained by the fact that the methodology of tax potential evaluation should take into account the changes of tax base of municipalities due to the economic crisis. There are also some problems in vertical equalization linked with shortcoming of tax potential determination as well. Actual mechanism<sup>53</sup> of allocations of grants to regional budgets from the budgets of settlements and/or municipal districts (urban counties) does not ensure any significant decreasing of disparities of municipal tax revenues in the regions where municipalities have excessively high tax potential created independently from the local self-governments' efforts. This «from-bottom-to-top» vertical equalization concerns the municipalities where calculated local tax revenues exceeded a level set by regional laws. Such mechanism does not stimulate local authorities to take measures of tax potential's increasing. That is why the Government noted in its resolution<sup>54</sup> from August 8<sup>th</sup>, 2009 a necessity of updating of actual mechanism through a skimming of excess income and creation of additional incentives to increase local tax potential by the way of establishing of progressive schedule of skimming.

As we could observe, in Russia a sub-national tax potential is mainly used as an indicator for vertical equalization. When there are some defects in tax potential's determination, receipts are redistributed unequally hence regions and municipalities can be demotivated

53 Methodology of calculating and allocations of grants according to the article 142.2 of the Budgetary Code, [http://www.minfin.ru/common/img/uploaded/library/2008/09/NPA\\_Otritsatelnye\\_transfery.doc](http://www.minfin.ru/common/img/uploaded/library/2008/09/NPA_Otritsatelnye_transfery.doc) (03.08.2012).

54 Ordinance of the Russian Federation Government no 1123-r, *ibid*.



to develop their tax potential and fostered to strengthen a tax competition between them. As we mentioned in the introduction, there are two types of tax competition – positive and harmful. In the middle of 1990's some regions in Russia created internal offshore zones that were considered as negative tax competition. A horizontal equalization may serve a solution of this problem and to reorientate the regions and municipalities toward the cooperation instead of pure competition. In France both kinds of equalization are applied. This is a possible explanation why in French legislation we did not find any mention about interterritorial tax competition. Besides, a vertical equalization deepens a financial dependence of regional/local (self)government from national authorities. Such dependence fosters localities not to make any efforts for developing their tax potential and increasing a level of tax collection.

## CONCLUSION

In this paper we attempted to determine how legislation and regulation affects on the tax potential and tax autonomy of regions and municipalities in France and in Russia taking into consideration a strong importance of these phenomena for regional and local development.

It was observed that in Russia there are regulative acts (work of Government) that normally contain some details about the tax potential (mostly calculating methodology) of regions and municipalities, but their financial (and tax) autonomy, one of the main tools of contribution in increasing of tax potential, even is not defined at the legislative or constitutional level. In France all these questions are at least set by the legislation (work of Parliament) and the cornerstone of local self-government – financial autonomy – is provided by the Constitution (article 72-2). Remainder that the Constitution disposes the highest legal force and then there are legislative and regulative acts in hierarchical order. Thus, the more a problem is important, the higher a level of its solution. At the same, Russian regions and municipalities are freer than in France concerning the measures of their tax potential and tax autonomy increasing. It can be explained by the federative character of Russia and the unitary decentralized nature of France.

We can conclude as well, that different calculating methods for regional and local tax potential chosen by the legislator/ the Government influence differently on the sub-national tax autonomy and development. The application of mostly actual indicators instead of forecasts (French case) makes an assessment of tax potential more exact. At the same time the using of long- and medium term indicators (Russian case) makes an evaluation of tax potential more stable. That allows to regions and municipalities to follow the development of their taxes and other revenues, to predict a future situation with the tax autonomy and to take the necessary measures. An extremely weakness of local taxation in Russia entails the fact that the basis of regional and local tax potential (except rural and urban settlements) are federal and regional taxes and special tax

regimes whereas in France – departmental and local taxes.

Concerning the application of tax potential, we can note that in Russia a sub-national tax potential is mainly used for vertical equalization's purposes. Hence some shortcomings in tax potential's calculating due to the methodology adopted by the federal Government endows an unequal redistribution of the revenues for benefit of the budgets of different levels. In its turn these inequalities foster regions and municipalities not to make any efforts for increasing of their tax potential, but to strengthen a tax competition between them. In France a horizontal equalization is also applied. It can prevent a harmful tax competition at the sub-national level and reorientate the regions and municipalities toward a cooperation instead of pure competition. Besides, an application of only vertical equalization increases a financial and hence a common dependence of regional/local authorities from the Center.

We can not and should not determine which legal framing of tax potential in its interconnection with the tax autonomy – the French one or the Russian one – is more efficient. Each of them is more or less adapted to each country's specificity such as its traditions, political structure, territorial-administrative organization, distribution of competences between different levels of government and etc. But there is some positive and negative experience in each state, which could be taken into consideration by the legislators/governments of these countries.

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# ROLE OF PRIVATE SECTOR IN LOCAL AND REGIONAL DEVELOPMENT

Lea Prijon<sup>1</sup>

## INTRODUCTION

Local and regional development is becoming an increasingly important issue all over the world. There are many agencies and commissions dealing with it, by developing strategies and implicating measurements which could enable development of poorer localities and regions which are lagging behind. In this, private sector plays an important role, since is precisely entrepreneurship, which may significantly contribute to region's growth and prosperity. Developmental actions and strategies cannot be generalized and equally applied to all localities and regions in every country. Only well planned strategies and practices, which take into account all opportunities and potentials of the region can generate its development and raise the general standard of inhabitants. Thus, in different localities and regions within countries, the developmental approach of public sector is different.

By achieving local and regional development, strategies of the letter are formed in terms of sustainable development, which is also becoming an increasingly important issue in our time. The crucial point of sustainable development is to achieve locality and region's progress, growth and development, but not (only) in quantitative terms (development with resource depletion and environmental pollution). The aim of such development is thus a focus in preserving and respecting (bio)diversity of localities, regions, countries and nations.

In this paper we focus on the role of the private sector (enterprises) for local and regional development, where on the one hand regions can contribute to successful entrepreneurship, while on the other entrepreneurship generates prosperity of the region. We start from the position that entrepreneurship is a key factor for progress in terms of job creation, economic growth (GDP growth), standard improving, etc. Companies of different localities and regions may be organized and operate in different ways, from their association in clusters, business incubators, to different ways of investments, e.g. networks of business angels, or innovation (diaspora entrepreneurs).

The present contribution does not go into details in analyzing the role of private sector (enterprises) in specific field or matter. It is intended as a general insight into the topic with highlighted key points form theoretical review on the issue.

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## LOCAL AND REGIONAL DEVELOPMENT

*Development* is a complex term, a geographical phenomenon, since it is linked to a specific space (Castells, 1983 in Pike et al., 2007: 1258). As such it requires the recognition of; geographical concepts of space, territory, place and scale (see Pike et al., 2007). Sen (see 1999) describes development as a process of expanding the real freedoms of people and links it with the growth of GDP, the rise in personal incomes, industrialization, technological advance or social modernization. In terms of "local" (localities) and "regional" (regions), these are socially constructed spatial scales (see Hudson, 2007 or Swyngedouw, 1997 in Pike et al., 2007: 1254) and are territorially bounded units with particular administrative, political, social and cultural identities, even though boundaries keep changing at different spatial scales (Pike et al., 2007: 1255). With adoption of state roles, the region is not treated as a territorial or historical unit, but it can perform as a semi-independent unit on state's level or in the world economy. In addition a region retains "an identity redefined from the regional identity of the inhabitants of the little homeland into a pragmatic identity of the region, which can be translated into economic acts and marketing attractiveness for investors and which can create a new image of the region" (Szajnowska-Wysocka, 2009: 76).

Before proceeding towards the focus of this contribution it is essential to highlight how can local and regional development begin. In this regard regional policy and regional planning are a starting point to understand local and regional development. *Regional policy* includes strategies of national government in terms of activity distribution between different regions. In general terms focuses on inter-regional issues and includes distribution of economic activities, within regions in poorer economic conditions. On the other hand, *regional planning* focuses on a region as a whole and includes coordinated decision making through a specific strategy. Regional planning may be performed by administrative bodies of central government, which were decentralized, or by elected regional governments, which depend on the institutional framework (Adams and Harris, 2005: 12).

Regional economic development and growth can be defined as a *holistic approach*, which is participatory and action oriented. Which implicates the mobilization of people to effect changes, needed for region's improvement (Adapon, 2008: 2). Local and regional development has been defined as: "..." / a broad term but can be seen as a general effort to reduce regional disparities by supporting (employment and wealth-generating) economic activities in regions" (OECD, 2012). Thierstein and Walser (1999: 4) define regional development as a "socially complex process" which allows local actors form and implement innovative programs based on synergistic utilization of endogenous (internal) resources. In addition, regional development works as a supplement for national macroeconomic and structural policies. The OECD also emphasizes the importance of

competitive and dynamic regions in every country for economic and social objectives to be achieved. Past experiences of reducing regional disparities, in terms of large-scale infrastructure and inward investment, show a failure of such policies, since the result is under-used economic potential and weakened social cohesion. Thus, a new approach was needed for development of lagging regions to catch up and develop, involving attempts to exploit unused economic potential, unnoticed to outside agencies. With such an approach all parts of cities and regions can contribute to national development. The strategy of this approach is oriented towards an increase of the competitiveness of all regions. Some of the crucial measurements are (hereinafter OECD, 2012 and Tomaney, 2010: 10):

- a) A strategic concept (development strategy), which should cover a wider range of direct and indirect factors, which affect the performance of local enterprises.
- b) A greater emphasis on the identification and mobilization of endogenous potential (region's skills and innovation capabilities) and assets rather than on exogenous investments and transfers. This measurement includes the ability of places to grow on their own resources.
- c) An emphasis on opportunities rather on disadvantages.
- d) A collective/negotiated governance approach, which involves national, regional and local government in addition to other stakeholders, with reduction of centralism of central government.

The OECD (in Tomaney, 2010) called this approach the "*new paradigm*", which presupposes that opportunities and potentials for growth are spread across all types of regions. This paradigm is focused on maximizing the national output through encouraging a region to reach its growth potential from within. Nevertheless, this paradigm cannot be applied to all localities and regions at the same terms. In remote rural areas, where a declining share of employment in agriculture is observed, it shift from sectorial policies towards promoting local competitiveness based on sustainable development and resource management, diversifying around natural resource endowments, introducing new skills and technologies into traditional sectors, and reform of local governments which enables the achievement of scale economies in service provision (Tomaney, 2010: 15). In the table below (Table 1), a comparison between the "*old paradigm*" and "*new paradigm*" is given, to highlight differences between them.



TABLE 1: Comparing old and new paradigm of regional policy

|                             | <b>Old Paradigm</b>  | <b>New Paradigm</b>   |
|-----------------------------|--|---|
| <b>Objectives</b>           | Compensating temporarily for location disadvantages of lagging regions | Tapping underutilized potential in all regions for enhancing regional competitiveness                         |
| <b>Unit of intervention</b> | Administrative units   | Functional economic areas   |
| <b>Strategies</b>           | Sectorial approach   | Integrated development programmes   |
| <b>Tools</b>                | Subsidies and state aids   | Mix of soft and hard capital (capital stock, labor market, business environment, social capital and networks) |
| Actors                      | Central government   | Different levels of government  |

Source: Tomaney, 2010: 13 (adapted from OECD, 2009)

Globalization has raised the importance of regions, thus the current common tendency in Europe (and also in the global sense) is to *regionalize* the national space. With this trend regions are gaining on importance in terms of creating socio-economic systems (Castells, 2000 and Parysek, 1997 in Szajnowska-Wysocka, 2009: 75). An important momentum in regional and local development was the accession of ten new member states<sup>2</sup> to European Union in 2004, which gave a further impetus in the importance and the need of reducing regional economic disparities. The 174 Article of the Treaty on the Functioning of the European Union states (hereinafter Communities and Local Government Committee, 2012: 5):

*"In order to promote its overall harmonious development, the Union shall develop and pursue its actions leading to the strengthening of its economic, social and territorial cohesion".*

*"In particular, the Union shall aim at reducing disparities between the levels of development of the various regions and the backwardness of the least favored regions".*

Whenever speaking of local and regional development, the main question is: *"Local and regional development for whom?"* (Pike et al., 2007: 1261). In accordance with this Pike et al. (2007) gave a practical view on the objects and subjects of local and regional development, summarized in table below (Table 2).

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<sup>2</sup> Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia, Slovenia, Cyprus and Malta.

TABLE 2: The objects and subjects of local and regional development

| Scale/level                    | Objects              | Subjects                        |
|--------------------------------|----------------------|---------------------------------|
| People                         | Individuals          | Education and training          |
|                                | Households           | Homecare services               |
|                                | Families             | Childcare                       |
|                                | Neighborhoods        | Neighborhood renewal            |
| Spaces, places and territories | Communities          | Community regeneration          |
|                                | Villages             | Rural diversification           |
|                                | Localities           | Strategic partnerships          |
|                                | Towns                | Market town revival             |
|                                | Cities               | Growth strategies               |
|                                | City-regions         | Local authority collaboration   |
|                                | Sub-regions          | Spatial strategies              |
|                                | Regions              | Regional economic strategies    |
|                                | Sub-nations          | Economic development strategies |
|                                | Nations              | Regional development            |
|                                | Macro-regions        | Economic and social cohesion    |
| International                  | Aid distribution     |                                 |
| Global                         | Trade liberalization |                                 |

Source: Pike et al., 2007: 1261

Although different regions have different developmental potentials and possibilities Adams and Harris (2005) highlight some common weaknesses and shortcomings of regional development strategies (RDS), which resulted from the review of their case studies (hereinafter Adams and Harris, 2005: 14):

- Regional development strategies do not focus enough on crucial features of regional development strategies.
- Even in some of successful cases, a limited success in engaging stakeholders, some interest groups (business representatives) has been noticed in preparing the RDS, from what is evident that the RDS does not therefore enjoy a high profile.
- Strategies often fail to adequately address problematics and risks, and are often being criticized as overly optimistic.
- Many RDS documents are seen as unclear, since they fail to adequately explain how the strategy and its related actions have been arrived at.

There are three main EU funds intended to achieve greater economic cohesion, reduce regional disparities and promote economic growth across the EU. Among these the *European Regional Development Fund (ERDF)* is the largest one, which was established in 1975. The European Regional Development Fund (ERDF) aims to reduce economic disparities between the EU's regions by generating economic growth, increasing the employment and achieving a balanced distribution of prosperity between the regions).

Most of the money, which amounts of 201 billion €<sup>3</sup>, for the period between 2007–2013, is intended for the poorer regions in Eastern and Southern Europe. ERDF's strategy is participating in region's development and structural adjustment, where development is lagging behind and in the conversion of declining industrial regions. ERDF supports financially<sup>4</sup> public sector's projects (projects promoted by government departments, local authorities, higher education establishments) whenever there are no other sources of funding. The ERDF found also supplies voluntary sector organizations or helps small and medium-sized enterprises in their development (but in a smaller extent). In its financing the ERDF found does not include or allow replacement of the offered resources with public spending by a member country under a principle known as "additionality" (Communities and Local Government Committee, 2012: 5 - 9). Table 3 shows the objectives of European Regional Development Fund as the largest of the three Structural and Cohesion funds.

Table 3: EU Structural and Cohesion Funds, 2007–2013

| Fund                              | Value                | Purpose  |
|-----------------------------------|----------------------|--|
| <b>ERDF</b>                       | <b>201 billion €</b> | Investment in companies (particularly small and medium-sized enterprises), infrastructure, financial instruments and technical assistance measures. Allocated on a regional basis. |
| <b>European Social Fund (ESF)</b> | <b>76 billion €</b>  | Supports for projects to provide training, improve skills, and open up access to employment opportunities. Allocated on a regional basis.  |
| <b>Cohesion Fund</b>              | <b>70 billion €</b>  | Finances trans-European transport networks and environmental projects. Allocated to Member States whose Gross National Income per inhabitant is less than 90% of the EU average.   |
| <b>TOTAL</b>                      | <b>347 billion €</b> |  |

Source: Communities and Local Government Committee, 2012: 9

Specific "problem" represent countries (and thus regions) that are less developed or already in developmental phase, in this regard the OECD has developed several regional approaches, which address common, relevant topics. In our context this especially concerns countries of Central and Eastern Europe which were/are experiencing transition form centrally planned to market economy. Many of these countries are still, after more than two decades, struggling to implement macroeconomic stabilization, basic

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3 The level of eligible public spending is defined in advance by the European Commission which usually amounts at least in the same quantity, in real terms, as was spent in the previous period. Defined found of sources is maintained throughout the programming period for each country. Afterwards, the Commission verifies for compliance with the additionality rule with each country during and after the programming period. The regional funding forms an increasingly large proportion of the whole found (European Regional Development Fund: 2012: 5 – 10).

4 The share of funding per project varies according to the region's needs, the least developed regions can receive up to 85% of the value of the project (European Regional Development Fund: 2012: 5 - 9).

institutional and policy reforms. In this regard the OECD tries to support institution building and structural reform by highlighting several crucial issues, for example anti-corruption, pension reform, financial sector reform, corporate governance and tax policy (OECD, 2012). In these countries, the biggest achievement of Entrepreneur Cooperatives, is economic integration of their members into regional, national and export markets (Göler von Ravensburg, 2009: 10).

All regions, whether in developed or undeveloped countries, should have a vision of its development and a short-, mid- and long term strategy and concrete aims, which should be measurable by quantitative indicators (Pinterič, 2009: 1236), and nevertheless local and regional development is determined also by qualitative nature. The quantitative aspect concerns numeric measures (GDP p.c., productivity rate/increase, available jobs vacancies, investment project, number of tax-payers etc.) and focuses objectively on the absolute or relative change in indicators in a specific time periods and localities/regions (see Mccann, 2007 in Pike et al., 2007: 1260 and Pinterič, 2009: 1236) and is rather easy to determine. On the other hand qualitative dimension are more complex and "excellence" oriented. It concerns basics of local and regional features and development (sustainability, forms of growth, type and 'quality' of jobs, sustainability of investments, growth potentials, social diversity of new enterprises etc.). Qualitative approaches are oriented in specifics of local and regional development, which are socially determined and are thus more subjective (see Sen, 1999). It is crucial to act attentive while determining local and regional development and to consider both, its quantitative and qualitative aspects. Consequently, these two aspects can be linked but are not necessarily complementary, since localities and regions can be developing in quantitative terms while its qualitative dimension could be problematic<sup>5</sup> (Pike et al., 2007: 1260).

### *Sustainable development as a crucial factor of local and regional development*

Nowadays, local and regional development is bounded to sustainable development, defined as: "development which meets the needs of the present without compromising the ability of future generations to meet their own needs" (World Commission on Environment and Development, 1987 in Harrison, 2003: 1). Sustainable development is a very long-term community goal, constituted by (hereinafter see Thierstein and Walser, 1999; Galliano, 2003; Harris, 2003; Cox and Cusick, 2006):

- Economic sustainability,
- Environmental/ecological sustainability,
- Social sustainability,
- Institutional sustainability (Galliano, 2003)

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5 For example a locality/region is experiencing low level and weak growth, which is perhaps more sustainable; an insufficient share of jobs, which are perhaps good in quality etc.

Sustainability seeks to achieve the interaction balance between these systems (Cox and Cusick, 2006: 1). Thierstein and Walser (1999) call it the *"flower of sustainability"* which is based on organizational characteristics and systemic principles of sustainability<sup>6</sup>. The concept of sustainable development focuses on *what it specifically seeks to achieve* and implies certain limitations, which are *"imposed by the present state of technology and social organization on environmental resources and by the ability of the biosphere to absorb the effects of human activities"* (Kates et al., 2005: 11). The most important aspect of sustainability are social interrelationships, communication patterns and institutional settings, which strongly differ from one region to another. Sustainable regional development can be achieved in different ways since it is based on the question *"how to act"* which is unique for every region and depends on specific situation, interests and/or needs of the actors involved. More parallel or contradictory goals and strategies may exist at the same time. Thus, the crucial point is oriented towards the process of *how the goals have to be formulated and measures designed and implemented* (see Thierstein and Walser, 1999).

In terms of the role of private sector (enterprises) for economic development of localities and regions, from neo-classical economic theory perspective, sustainability can mean the maximization of welfare over time. Economic sustainability requires the maintenance or growth of different kinds of complementary capitals (manufactured capital, natural capital, human capital, and social capital), which enable make economic production (Harrison, 2003: 2). Strategies of sustainable economic growth need to improve business environment, with public funds, but in a way it does not distort business stimulations. Government can use public funds for provide adequate infrastructure which supports profitable enterprises, but not in the sense of redistribution of wealth. The aim of such policies should be, according to Porter, identifying and making the full use of the competitive advantages of inner cities, to later result as profitable business (Porter, 1995: 56-67).

## **COOPERATION OF REGIONS (PUBLIC SECTOR) AND ENTERPRISES (PRIVATE SECTOR)**

Cooperation between public and private sector is crucial for the success of both. If, on the one hand, public sector, in terms of local and regional environment, is important for the establishment of new businesses and stimulation of already established firms, enterprises, on the other hand, are of a great importance for local and regional development. The public overall opinion is that public institutions are expected to provide business development and entrepreneurship through various measures and subsidies. Nevertheless,

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6 Ethical framework and policy (and politics)

it is of vital importance the private sector's contribution for any local and regional community, especially for the less developed ones.

Successful participation means the success of both areas (sectors), which can occur in different ways. With public funding of establishment of new businesses, assistance in preservation of old ones, with founding of incubators, technological parks, etc. regions (localities) contribute to job creation, being of extreme importance for local and region development. On the other hand, enterprises (private sector) contribute to the development of regions and local communities with good performance and possible sponsoring of regional events and needs in terms of region's reinforcement and/or progress. Marchese and Potter state: "*It is widely acknowledged that entrepreneurship plays a key role in relation to economic development and that entrepreneurs are key agents of change in market economies*" (Marchese and Potter, 2011: 115).

*Enrollment of public sector in local and regional development through promotion of private sector (enterprises)*

Local and regional support of enterprises is important, as Robinson et al. state: "*Many social scientists believe that supporting entrepreneurship development within low-income communities is a plausible development strategy to combat poverty*" (see Acs and Malecki, 2003; Lichtenstein and Lyons, 2001; Smilor, 1997; Winters, 1997 in Robinson et al., 2004: 3). Promoting entrepreneurship and enterprises in underdeveloped and poorer localities and regions, generates economic efficiency. New businesses in low-income localities, which are promoted through local initiatives and are locally controlled, can help determine a community's prosperity or deterioration, since they most probably represent a rural, local or regional development strategy. Interests, in the (positive) impact of entrepreneurship for local and regional development and cooperation between public and private sector are constantly growing. Implementation of more entrepreneurship-led development policies could have a positive impact on deprived localities and regions, by creating new jobs and thus increase wealth through locally owned businesses. In addition, development scholars indicate that social relations and a strong local social structure may positively affect on regions that are lagging behind in development. Social relations may, in fact increase entrepreneurship-led development bodes in small rural communities, in which limited factors of production and few economic opportunities are rooted (Robinson et al., 2004: 3, 25).

Local and regional development depend heavily on entrepreneurship, therefore a fertile and stimulating entrepreneurial environment with values and orientation towards entrepreneurship is of vital importance (Braun and Diensberg, 2007: XII). The structural perspective research, which considers features of financial, human, social capital and structural exogenous conditions, aims to explain the relation between new firms and regional economic growth and development (see Moreno et al., 2007). Structural reform

indices cover a variety of three surfaces of reform: trade and outward orientation, business and regulatory reform, and governance. All these areas generally correspond to the key areas of change, which are required to create more open, private sector-driven, and diversified economies in a region (Structural Reform for Long-Term Growth: 71). In local and regional developmental strategies, government programs should aim towards joining the micro, small, medium-size and large, high-value-added enterprises (Newland and Tanaka, 2010: 1). What concerns surveys on linkage between the establishment of new enterprises, their job creation and growth and their positive trends on local and region's development, discrepancies can be found. Some authors (see Reynolds, 1994; Acs and Armington, 2002 in Fritsch, 2008: 6 or Bates, 1995; Birch, 1979; Acs, 1999 in Robinson et al., 2004: 4) find a positive effect between the level of new business formation and regional employment. Nevertheless, some other authors (see Audretsch and Fritsch, 1996; Fritsch, 1996; EIM, 1994 in Fritsch, 2008: 6) did not identify a positive trend and relationship between the share of new firms and regional employment growth. Assumptions about sustainability of small enterprise development compared to already established and old business attraction are also emerging.

Such examples can be found in Slovenian Goriška region, in the case of HIT<sup>7</sup>, although the latter is a semi-state enterprise, which was sponsoring sport, entertainment and tourism events and various needs over the locality near to Nova Gorica. HIT is also an example of combining public and private sector, for example setting up tourist associations is an important contribution to added value of both.

Another example of cooperation can be found in linking the municipality of Nova Gorica as a public sector and various (private) faculties in this region. Examples of such successful practices can be found in the US (the example of Silicon Valley in San Francisco Bay Area)<sup>8</sup>. Even though, comparisons between the Silicon Valley and Goriška region has to be understood in modified context of capacity and volume of USA and Slovenia, the case of Silicon Valley is an example of possible contribution of the private sector for local and regional development. The smart specialization approach highlights the opportunities and possibilities that university research base can have for technological diversification strategies of major locally embedded industries. Thus, university spinouts can contribute substantially to regional entrepreneurial activity and to the attraction/retention of global businesses by the assets (physical and human) that the university has to offer (Connecting Universities to Regional Growth: A Practical Guide, 2011: 2).

Despite, region's crucial role in promoting and enabling enterprises for development of both, public and private sector, this contribution focuses on the role and importance of

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7 HIT - Hoteli, Igralnice, Turizem d.d., Nova Gorica (Hotels, Casino, Tourism). Web page: .

8 Public support for engaging universities in regional development has followed the US experience of Silicon Valley, which focuses on high-tech knowledge areas and bio-technology and fostering spin outs of businesses from research labs by using science parks as a key mechanism (see Connecting Universities to Regional Growth: A Practical Guide, 2011: 2).

private sector (enterprises) for local development.

Local and regional development consists of cooperation between regions, state(s), associations of capital, labor and civil society, etc. and in its different stages depends on local, regional and national economic and political interests (Pike et al., 2007: 1255). In this sense, local and regional development can be compared to economic development and economic concerns; growth, income, employment etc., which are geographically and culturally relative, since well-being standards differ among countries (Canzanelli, 2001 in Pike et al., 2007: 1259). Employment creation and stabilization (in formal and informal economies) are the best strategy in helping promoting the development and preventing poverty (Göler von Ravensburg, 2009: 11), since it improves regional's standard of living and economy (Couture, 2003: 43). But, as it was stated by Local government commission: *"One of the biggest myths is that in order to foster economic development, a community must accept growth"* (Local government commission, 2004 in Pike et al., 2007: 1254). Alternative approaches are emerging; local and socially oriented ones, are questioning the dominant economic focus of local and regional development on firms in (inter)national economic context (Geddes and Newman, 1999 in Pike et al., 2007: 1254). In the following paragraphs we will examine, how can local and regional authorities (public sector) contribute to enterprise's development (private sector) and vice versa.

## **ROLE, IMPORTANCE AND IMPACT OF ENTERPRISES FOR LOCAL AND REGIONAL DEVELOPMENT**

Before continuing to the issue of this paragraph, a definition of *private sector* is necessary to understand its role and contribution to local and regional development. The (rural) private sector, which differs within countries, regions and localities, consists of economic agents, represented by subsistence or smallholder farmers, rural wage-earners, livestock herders, small-scale traders, micro entrepreneurs (to medium-sized enterprises), local private operators (input suppliers, transporters, microfinance institutions, etc.), bigger market players (including local or international commodity buyers and sellers), commercial banks, supermarkets, etc. In addition, rural private sector includes also associations of farmers, herders, water users or traders (Private sector development and partnership strategy, 2007: 6). Local development corporations are also a part of private sector and are private, not-for-profit corporations, generally established by<sup>9</sup> local governments with the aim of economic development or other public purposes. They are present in many counties, cities, towns, villages, and fire districts to finance local government operations and projects. In many cases they "serve" for avoiding constitutional or statutory provisions, which would apply to local government's projects (e.g. referendum requirements, competitive bidding, limitations on the issuance of debt,

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9 Or for their benefit.



etc.) (Di Napoli, 2011: 3).

Enterprise is a sociocultural phenomenon and its establishment and performance (success or failure) are linked and dependent on the environment where enterprise is operating. Environment, which can stimulate or demotivate enterprise's activity, is crucial in determining conditions under which an enterprise will function. The connection of region's development and entrepreneurial capabilities are linked with "*entrepreneurship capital*"<sup>10</sup>, which is manifested in the number of startups, which are considered as the most suitable measure of entrepreneurship capital. Thus, entrepreneurship capital is greater in regions, which display a stronger economic performance (see Audretsch and Keilbach, 2004). In addition to entrepreneurship capital, also human capital is crucial for regional development and implicates, that regional growth lies also in intensifying highly educated and productive people in a specific region (Florida, 2003). Several studies have shown a correlation between human capital and regional growth (Glaeser in Florida, 2003).

Deriving from Porter, Robinson et al. (2004: 8-9) consider three key points as being fundamental for entrepreneurship-led rural development policy:

- An economic social focus, emphasizing the creation rather than redistribution of wealth within economically disadvantaged rural communities.
- An emphasis on the private sector as opposed to the government and social service sector; but highlights the supportive role of government and social services.
- An emphasis on having skilled and experienced individuals engaged in entrepreneurial activities.

Nolan (2003: 77) states that entrepreneurship is a critical component of local development. There are several examples of program types of innovation (hereinafter Nolan, 2003: 81 – 85):

- a) Business Networks, which is an important part of business, since there are assumptions that entrepreneurs involved in formal networks perform better than those who are not. Some aim at general sharing of information, while others tackle more specific goals. Networks facilitate rapid learning, information flow, reconfiguration of relationships with suppliers, in some cases they led to a new division of labor in a group of firms, they are an incentive for cooperation, for technological development, exporting etc.

Nolan (2003) gives various recommendations for the development of business networks, such as:

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10 Represented by agents and legal, institutional and social factors, which provide positive and stimulating environment

- *implementing broad campaigns to introduce the networking concept to businesses,*
  - *providing financial support for feasibility work, start-up activities, and the costs of network brokerage,*
  - *work with realistic time frames,*
  - *ensuring experienced network brokers,*
- b) Networks of Business Angels, concern the access to institutional equity investment, since formal venture capital is linked with geographical area. The main problem with ensuring formal venture capital lies in the fact that there is less or none, in less developed and dynamic regions and areas without substantial activity in financial services. Business angels are crucial for local and regional territorial development since they are geographically dispersed and they invest locally. Business angel networks are non-distortionary and as such attractive for local development policy, they pay particular attention to market imperfections, mobilize local savings and know-how. These networks of business angels seek to match informal investors with ventures, who are looking for small and thus uncertain amounts of equity finance. Informal investors work on bases of acquaintances (see Mason and Harrison, 1997 in Nolan, 2003: 83). Usually business angels networks are publicly supported on not-for-profit basis. Nevertheless, privately operated initiatives on this field have emerged, experiences indicate critical limitations in running these networks on a for-profit basis.
- c) Aiming for Visible Points of Referral to Professional Advisers. Business advisory services policies of public provisions, in many countries, have moved toward greater prominence on ensuring entrepreneurs an easy access to private-sector sources of information and advice. Generally, private sources are used in these cases, such predominance can be due to specialist knowledge private sources constitute. Or may regard confidence risen by the self-regulation of professions like banking or accounting (see Bennett and Robson, 1999 in Nolan, 2003: 84). There are different information sources for reviewing different business purposes; using customers opinions for product development or selling in new markets or a highly valued information source gained from network of small firms with other (small or big) firms (see Malecki and Poehling, 1999 in Nolan, 2003: 84). A recent survey discovered that growth of recipient firms is linked more with private sources of advice; lawyers, accountants, networks of friendship in business etc. (see Bennett and Robson, 1999 in Nolan, 2003: 84). A referral system of advisory agencies, which should be placed in locations frequented by potential and actual business people, could include; industry

associations, mainstream for-profit providers, chambers of commerce, nongovernmental organizations, and business mentors. Advisor/development agencies might help businessman with failed loan applications to improve the quality of application, their business plans, help them with financial forecasts etc. These agencies should also facilitate information flow (about job vacancies) or access to a one-stop function for potential entrepreneurs, ease procedures for paperwork or finding advice.

In addition of Nolan's (2003) several examples of program types of innovation, a few more examples can be added:

1. *Diaspora entrepreneurs*, who are the "first movers" in exploiting economic developmental opportunities and contribute to job creation and economic growth. The latter has been reviled by a recent research, where diaspora entrepreneurship has been defined as a crucial contributor to development by stimulating innovation, creating social capital across borders, and channeling political and financial capital toward their countries of origin. Attracting diaspora direct investors and entrepreneurs is difficult in many countries in development (Newland and Tanaka, 2010: 1).
2. *Business incubators*, which represent the way of "mutual assistance" between public sector (governmental policies) and private sector (business) in their development and grow. Small and microenterprises tend to move from undersupplied localities to more developed ones. These enterprises operate on basis of "easy-in and easy-out" of tenure and they need conditions which allow them to graduate into different sizes of accommodation. Prospective tenants seek flexible accommodation, which is more important compared to price (Nolan, 2003: 88). Incubators in small communities should be treated carefully, in this regard past OECD work on incubation emphasized; the importance of scale in incubation schemes, since greater scale reduces costs and risks, and also arises possibilities for the leveraging of private finance. Government investments in incubator-type buildings and estates could be a public policy response to imperfections in the market for industrial real estate, which is a capital-intensive use of public funds, with limited possibilities of reimbursement through with further property sale. "Virtual incubators", could also be a way of reducing costs and effective in providing non-property-based services in less populated areas and territories with small numbers of potential tenants.
3. *Clusters*, have been observed in regions with many excellent businesses in strategic alliances in an industry or along a value chain. "Clusters are (regional) concentrations of businesses including their service providers along a value chain – We also speak of networks of complementary businesses in this situation" (GTZ, 2007: 3). Clusters are an implement for further development of a region's (or entrepreneurial) strengths. Nevertheless, clusters emerge through

location decisions by businesses and are self-reinforcing, they cannot represent a short-term solution to overcome structural weaknesses. For such a structure, corresponding service providers (e.g. as engineers, technical agencies, lawyers, tax advisers, universities and advanced training institutions, etc.) should also exist to supply and support the functioning of this structure and regional development (GTZ, 2007: 5 – 8). Besides, their important role in new business formation and region's development, cluster's crucial feature is also their dynamic external economies (see Porter, 1997).

## CONCLUSION

Described practices, strategies and measurements taken by public sector (agencies, commissions, founds) in promoting entrepreneurship and the contribution of the latter to local and regional development show that such an aim is possible. Local and regional policies (strategies) should be oriented to a specific locality and region since their potentials and developmental opportunities vary greatly among countries. Private sector (enterprises) is the crucial generator of region's development, growth and prosperity. If enterprises are supported by local and regional policy makers, which have a well-designed strategy, region's development is possible.

Nevertheless, such policies, measurements and strategies should be oriented towards sustainable development and value added goal. Enabling, promoting and supporting new business, small and medium-sized companies and implementing them in joint cooperation with large, already well-established businesses can be a recipe for local and regional's success. Enterprises contribute to development with clustering, innovation is brought in regions by diaspora entrepreneurs, incubators facilitate efficient entrepreneurship and investments are gained by business angels. All these crucial elements are mutually connected and form crucial networks, which may contribute to local and regional development.

Practices from the past show that cooperation between public and private sector is of vital importance for sustainable economic development for a certain locality or region and that such development is possible. One good example is the Silicon Valley, which is know for its world's largest technology corporations and a great amount of small innovative business. Such practices can be find all over the world, where there is interest in investment in startups, small and medium sized business and where governmental policies are interested in helping already established business. On the other hand, interest in the private sector in contributing to local and regional development, should also exist and aim towards sustainable development, based on qualitative strategies.

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# FINANCING INFRASTRUCTURE: PPP MODELS TO DATE AND FIRST RESULTS OF PPP PROJECTS EXECUTION IN RUSSIA

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## INTRODUCTION

Investments in infrastructure are typically scaled and characterized by high initial investments and long payback period [Pethe, Ghodke, 2002]. According to the company, "Renaissance Capital" for 2020 - 2030 years Russia would need 752.5 billion U.S. dollars to invest in infrastructure. The volume of investment required is huge, and without the cooperation of state and business, and therefore, without searching for new models of interaction between the two sectors it won't be achievable.

Among the key features that are available to the government to finance public sector infrastructure, the following can be outlined [Akitoby, Hemming, Schwartz, 2007]:

4. attracting financing through public borrowing, increasing public savings, or relocating government spending in other sectors;
5. more efficient use of investment by improving planning and evaluation process of projects;
6. involvement of private capital.

Selecting one of these strategies will depend on the state budget of a country. States use different strategies for financing public sector infrastructure to meet basic needs. Today, with limited investment opportunities from the government and the unwillingness of governments to increase public debt, governments are increasingly turning to the private sector in search of opportunities to transfer a certain public services under private responsibility.

Limitation of financing resources in the world that we see today requires government to have greater openness to private sector involvement in creating public infrastructure. Governments today should more carefully consider all financial resources available in the market and pursue a work towards selecting new innovative methods of infrastructure financing with incorporation of fair risks and awards allocation. As other countries Russia is competing with the rest of the world for scarce financing resources requested for infrastructure projects procurement.

The difficulties faced by Russia in connection with the global financial crisis and stimulate the government and private sector to find the most effective ways of working to support economic development. Competitiveness and development of the country in times of crisis depends primarily on the ability of the government to modernize the economy, as well as maintain and develop the basic infrastructure of the public sector. In

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2008, Russia has invested 4.7% of GDP on infrastructure, already in 2009 this figure decreased significantly reaching 2.8% of GDP [Sberbank, 2010]. Obviously, government cannot provide the necessary funds for infrastructure creation. One of the most promising forms of private sector involvement for the creation, financing public infrastructure and services based on them is a public-private partnership (hereinafter – PPP).

Current tendencies of development in Russia show substantial growth in demand for modern infrastructure. According to official estimates only sustainable development of transport infrastructure requires 1 trillion USD of investments before 2020. It is obvious that this amount of funds cannot be raised only from budget sources. This is a precondition for development of PPP which allows the government to implement infrastructure projects without reducing funding for other areas of spending.

Experience of other countries shows that new public sector infrastructure is the first object for the application of PPPs due to a clear view of the government of the need for an object and possibility to predict revenue and expenses more accurately when it is created. The effectiveness of the PPP in comparison with the public procurement confirms the experience of advanced countries in the application of PPPs, namely the UK and Australia (see Table 1). In this case, the efficient use of PPP models in comparison with public procurement is seen from two sides:

- compare planned and actual time for the project implementation;
- comparison of planned and actual costs for the project.

Table 1. Comparison of results of projects for the traditional method and the state through the use of PPPs

|                     | Research of «MottMacDonald» (Great Britain), 2002 |                 | Research of Ministry of Finance of Great Britain, 2003 |                 | National Audit Office (Great Britain), 2003 |                 | Research of «Allen» (Australia), 2007 |                  |
|---------------------|---|-----------------|--|-----------------|---|-----------------|---------------------------------------|------------------|
|                     | Time overrun, %                                   | Cost overrun, % | Time overrun, %  | Cost overrun, % | Time overrun, %                             | Cost overrun, % | Time overrun, %                       | Costs overrun, % |
| Public procure ment | 17%   | 47%             | -  | -               | 70%   | 73%             | 23,5%                                 | 14,8%            |
| PPP                 | -   | 1%              | 11%  | 0%              | 24%*  | 22%             | 0%**                                  | 1,2%             |

Source: составлено на основе: Performance of PPPs and Traditional Procurement in Australia, Allen Consulting Group, 2007, p. 63; PFI: Construction performance, National Audit Office, 2003, p.26; PFI: Meeting the Investment Challenge, HM Treasury, 2003, p.134; Review of Large Public Procurement in the UK, Mott MacDonald, 2002, p.92.

Note: \* - 8% of the projects exceeded the scheduled time over two months;

\*\* - in 3,4% of completed projects construction stage was completed ahead of schedule.

According to the data presented above, the costs overrun for the investigated projects

implemented under public procurement varies from 14.8% to 73%, while the use of PPPs cost overrun ranged from 1% to 22%.

Under public procurement of a project, despite the source of unexpected cost increase or raising costs of providing services and operating costs when compared with planned, the government bears the risk associated with these and thus all expenses. In case of PPP, the government is able to record the final cost of providing services through PPP contract, transferring the risks of cost overruns to the private sector [Tiong, Anderson, 2003].

Key value of private sector involvement via PPP mechanism is the ability to do more projects in parallel rather than sequentially because one is less reliant on ‘just’ the state or regional budget. In the same it is important to note that PPP doesn’t create free solution for a government of creating infrastructure. At the end of the day, there are really only two funding sources – “user pay” or general taxation (state funding) – this is different to financing structures that PPP suggests and which are about meeting cash flow needs during project construction, operation. PPP structures should provide better flexibility to tie the contractors into service quality and delivery standards with appropriate penalties through payment mechanisms etc.

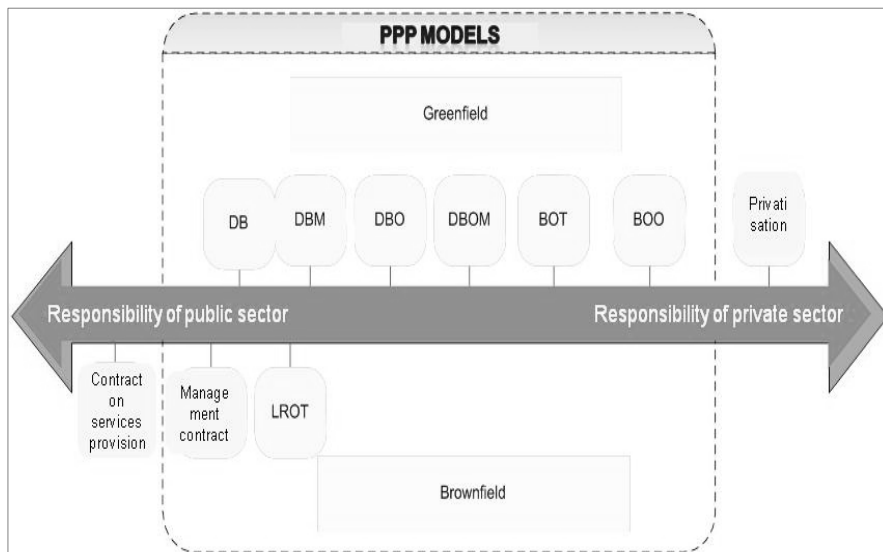
Due to the fact that PPP is not a solution for all public infrastructure project special attention should be put on criteria selecting the model of project implementation. Among criteria of selecting a procurement root are used such as project’s size, project’s contract duration, opportunity to gain yield, opportunity to use quality criteria for project implementation and service provision, ability to reallocate risks on private sector, innovation of project and other.

## **SELECTING PPP MODEL FOR INFRASTRUCTURE FINANCING**

It should be noted that even in times of crisis infrastructure is a relatively stable asset for investment by the private sector, which generates most of the predictable cash flows, which are often backed by government guarantees. In terms of government infrastructure, which refers to the main scope of PPP, is a recognized driver support and promote economic growth, which makes the implementation of projects in this area for the benefit of the state.

In selecting PPP model government has to consider legal restrictions that current PPP legislation implies, financial and budget efficiencies that selected PPP model brings, ownership for asset (whether government would like to remain it or not), and also assess bankability of selected procurement model. The variety of PPP models presented in a figure 1 below.

Figure 1. PPP models



Source: designed by author based on Closing the infrastructure Gap..., 2006; Booz, 2007; New opportunities..., 2008.

The figure 1 depicting the continuum of diverse forms of interaction government and business, PPP models lies between simple public contracting with the private sector to provide certain services and privatization. To disclose the content of these models we can use so-called alphabet, where letters correspond to activities that are transmitted to responsibility private sector in PPP and thus consist PPP models in the title:

- B — Build;
- O — Own or Operate;
- T — Transfer;
- D — Design;
- M — Maintainance;
- F — Finance;
- L — Lease;
- R — Rehabilitate.

Today PPP is widely used for completion of tasks of regional and local governments in respect of infrastructure creation and rehabilitation, including schools [Ball, Heafey, King, 2000; Akintoye, Beck, Hardcastle, 2003], public transport [Klijn, Teisman, 2003], healthcare [Froud, Shaoul, 2001; Ennis, 2005; McKee, Edwards, Atun, 2006], roads [Reeves, 2003], airports [Goodliffe, 2002], prisons [Schneider, 2000], water supply [Hodge, Greve, 2005], tunnels, sea ports, bridges, museums, libraries, social houses and

other infrastructure assets [Grimsey, Lewis, 2004].

Each of presented above PPP models can be procured with the use of the following payment mechanisms:

- a. Toll – payment goes directly from users. Revenue stream generated by the project provides requested equity IRR for investor. Demand risk of the project is taken by investor;
- b. Minimum guaranteed income (hereinafter – MGI) – government takes a responsibility to pay to investor defined minimum guaranteed payment. It means that in case of revenues of the project will be less than defined in advance MGI, then government compensate the difference between actual revenue and MGI. In case if project revenue exceeds MGI, part of the revenue in excess of MGI is distributed between public and private sectors. In this case demand risk is shared between government and private sector.
- c. Availability payment – is a fixed payment that governments pay to investor during operation period of the project. This payment is subject to quality of services provision by private sector. Demand risk is taken by public side in this case.

Thus each of existing PPP models can be implemented with one of payment mechanisms described above. Selection of payment mechanism will directly impact on requirement of investor on equity IRR in the project. The required equity IRR will fall in case we're moving in selection of payment mechanism from toll to availability payment. On the contrary government support requested for a project will raise going from toll to availability payment project structure.

Selection of PPP model should be based on value for money assessment. In a table 2 presented a simplified comparison of main PPP models.

Table 2. Overview of PPP models groups

|                                  | PPP models without transferring ownership right to private sector (for ex. BOT/DBFO/BOOT)   |   |  | PPP models with transferring ownership right to private sector (ex. BOO)   |   |  |
|----------------------------------|---|---|--|--|---|--|
| Payment mechanism                | <i>Toll</i>   | <i>MGI</i>  | <i>Availability payment</i>  | <i>Toll</i>  | <i>MGI</i>  | <i>Availability payment</i>  |
| Equity IRR                       | 30%*  |   |  | 15%*   |   |  |
|                                  | ← Decreasing →  |   |  |  |   |  |
| Senior debt rate                 | 15%*  |   |  | 12%*   |   |  |
|                                  | ← Decreasing →  |   |  |  |   |  |
| Cashflow for public sector       | = Direct tax cashflow + indirect tax effect – capital grant (if applicable) + TV** of the project   | = Direct tax cashflow + indirect tax effect + part of revenues which exceeds MGI –MGI + TV** of the project | = Direct tax cashflow + indirect tax effect + toll collection (if applicable) – availability payment + TV** of the project | = Direct tax cashflow + indirect tax effect – capital grant (if applicable)  | = Direct tax cashflow + indirect tax effect + part of revenues which exceeds MGI –MGI | = Direct tax cashflow + indirect tax effect + toll collection (if applicable) – availability payment |
| Advantages for public sector     | a) Government will remain ownership right on infrastructure asset.<br>b) Reduced burden on public budget due to reallocation of maintenance costs to private sector<br>c) Better risk sharing compare to public procurement<br>d) Payment mechanism allows better quality control   |   |  | a) Reduced burden on public budget<br>b) Better risk sharing compare to public procurement<br>c) Payment mechanism allows better quality control during PPP contract period<br>In post PPP contract period asset operation is at expense of private sector                           |   |  |
| Disadvantages for private sector | e) More difficult to reach financial closure due to the fact that private sector does not have ownership right on the asset<br>f) Long process of structuring and preparation of a project to tender<br>g) High cost of financing (compare to public procurement) and complex process of financial closure (depending on payment mechanism) |   |  | h) Easier process of financial closure due to private sector holds ownership right for the asset<br>i) Government loses control over the asset and ownership right<br>There are no clear standards of quality and quantity of services provision after PPP contract will be expired. |   |  |

Note: \* - figures are indicative for Russia;

\*\* TV – terminal value. Under these PPP models ownership right for infrastructure asset will belong to the government. Due to this after completion of the contract government will have terminal value of the infrastructure asset.

As any developing PPP country to prepare PPP project that will be able to attract investors and bank and remain attractive for government itself Russia should understand key requirements of each side in the project that predetermines viability of use PPP model for the project. The main consideration of lenders is to receive money back with return that will require having a control over key decisions of the project and possibility to have step in rights when the project will go wrong. Lenders are really conservative in making the decision on providing a debt which means they are risks averse and will look for securing their position in PPP contract. Investors from other side are stepping up in a PPP project to gain a profit (equity IRR). They do expect from the government first of all a “balanced” risk sharing in the project. Government is interested in provision a long-term public service on the basis of created infrastructure asset. Thus it is interested to have a control under quality of project implementation through setting an efficient rewards and penalty system (payment on performance, i.e. less risk of delay and cost

overrun) and transferring some projects risks to private sector.

The complex structure of financing PPP project is explained by a high proportion of debt in the financing structure. Use of different types of debt and equity defines allocation of risks between funding sources for the project.

Providers of senior debt financing usually from 60-80% of the project total funding requirements. Thus they have priority in receiving payment of obligations by availability for them net project cash flow. The qualities of collateral for lenders are PPP agreement for the project, assets, equity, and revenue, net of operational costs.

Subordinated debt financing usually from 10 to 20% of the project total funding requirements, and it served only after the fulfillment of obligations of the senior debt. The quality of collateral for subordinated debt will be cash flow after fulfillment of senior debt requirements.

Equity capital covers the remainder of the funding requirements which usually is 10-25%. Equity takes the main project risks and in particular profitability risk. Due to this investor will require fair compensation (as equity IRR) for project procurement. In Russia this figure can vary from 15% to 40%.

Due to all these factors government should carefully assess from legal, financial viability perspectives along with taking into consideration socio-economic and budget efficiencies of each procurement option in selecting method of project realisation.

Public procurement should be used in cases where there are no restrictions on possibilities of public funding, as well as risks carefully analyzed and government is able to handle them, and also capable to develop an effective methods of quality control of construction as well as services provision.

Management contract is effective in cases where the initial investment of construction or reconstruction of asset is relatively low, since cost of building is a fully funded from the budget. As well as in public procurement most of project's risks are handled by the government, so this model should be used only when the government is ready to take all risks of the project and capable to manage them.

PPP models like BTO, BOT, BOOT, DBFOM, DBO, and others provide most preferred option for project due to possibility of allocation risks and responsibilities between public and private sectors. This approach reduces burden on public budget by reallocating costs of facility to private sector. PPP models incorporate mechanism of quality control during construction and operation phases.

## **PPP PROJECTS EXECUTION IN RUSSIA**

Russia is one of the PPP developing countries which prefer new procurement method as PPP for procuring infrastructure projects. Russia is beginning to take the first steps in preparing and implementing projects through the PPP mechanism. In 2005 Russia and accepted first legislative act dedicated to PPP - Federal Law № 115 "On Concession

Agreements" and in the same year launched one of the largest PPP programs in the world. After 7 years after the Federal Law "On Concession Agreements" and 6 years after the first regional law of the PPP in 2010, only three PPP project reached financial closure: road projects "Moscow – St. Petersburg (15-58 km)" and M-1 "Moscow-Minsk around Odintsovo" as well as the project of reconstruction and development of Pulkovo airport. These three financial closes have brought Russia on a different level of PPP market maturity. In 2012 another transport project reached financial closure which is Western High Speed Diameter (hereinafter - WHSD), also school project in Slavyanka district in St. Petersburg was closed. Today, at the stage of financial closure there is a project of construction waste recycling plant in Levashovo (St. Petersburg). Quasi-PPP projects are being implemented today in the field of healthcare (for example, in Kazan, St. Petersburg, Petrozavodsk cities), water / wastewater treatment (for example, in Moscow, St. Petersburg).

One of the first PPP project announced, was WHSD in St. Petersburg. A year after the announcement of the project it became clear that its implementation is difficult to achieve based on the federal law on concessions due to limitations imposed by law. For example, the project required the involvement in WHSD two public bodies from government side - Ministry of Transport of Russia and government of St. Petersburg, which was impossible under the act. Another issue was connected with Article 11 of the concession law, which sets unrealistic deadlines (i.e. 60 days) for the registration of plots of land which are necessary for the closure of the concession agreement. In practice, a compulsory purchase of land can take from 2.5 to 3 years, and bearing in mind the grantor issue in the WHSD project it required even more time. These were some of the examples of legal problems WHSD project had met. It was a first test for PPP legal framework which had showed its pitfalls and created difficulties for the first PPP projects in Russia. Only in 2012 the project reached financial close.

Other limitations of the project related to macroeconomic and financial environment. The project was huge in terms of required investments - almost U.S. \$ 2 billion. In 2006 for a country that had no experience in implementing PPP projects, without readiness in that moment of national financial market, with a high currency risk WHSD implementation was an ambitious task. Almost the only one of the essential success factors for launching the first PPP project at that time was the presence of political support for the project. Three times tender was announced for the project and twice it was postponed because of the emergence of certain problems, the third competition was held before the financial crisis, where the winner was chosen, but deal wasn't financially closed due to significant raise of cost of financing. These problems explain why the project WHSD took so long and so many resources for its preparation. WHSD became the first project on which government has learned to understand the requirements of banks, investors, and public sector itself for the successful financial close of the project. Even if the financial crisis would not have been in 2008, the project WHSD could be financed at that time only by

major foreign banks because of lack of development of the local financial market. Then it would have been a problem with foreign capital in the project due to high foreign exchange risk, to cover which there were no available hedging instruments, and the project generated a whole stream of income in local currency. Three years after the announcement of the project, it has been modified and put up for a tender. In 2011 project won of "Highway of the Northern Capital" (formed by "VTB Capital", Gazprombank, an Italian construction company Astaldi and Turkish Ictas Insaat and Mega Yapi). The company will build a central section of WHSD within 36 months and will receive a guaranteed annual income from the city of \$ 9.67 billion [Vedomosti, 8/9/11].

Setting not realistic requirements by the government to private sector on PPP projects lead always to raise of costs of the project for the government and thus disseminate all benefits PPP mechanism can bring.

The main problem in implementing the first PPP project is the absence of thorough legislation on PPP and the minimum experience in implementing similar projects. For instance federal law on concessions still allows to use only one PPP model - BTO where investor construct and operate an asset while government retain ownership right for it.

In 2010 situation in PPP market in Russia dramatically changed. More than 50% of regional governments introduced its own legislation on PPPs, main public bodies for PPP procurement were established, Russian development bank “Vnesheconombank” was introduced, domestic capital market introduced its appetite for PPP projects showing existing over liquidity.

Financial crisis has worked as a trigger for Russian government to look on PPP implementation more serious. Three major financial closes in Russia has proved it where two of them were “quick-win” solutions (see table 3).

Table 3. Three financially closed projects in Russia in 2010

| billion, USD                        | Sources of financing |                                       |                        |       |                    |
|-------------------------------------|----------------------|---------------------------------------|------------------------|-------|--------------------|
|                                     | Public budget        | Investment fund of Russian Federation | Private sector capital | Total | Government sources |
| Pulkovo airport                     | -                    | -                                     | 1,5                    | 1,5   | Partial guarantees |
| Moscow-St Petersburg road, 15-58 km | 0,77                 | -                                     | 1,23                   | 2     | 38,3%              |
| Moscow-Minsk M1 (Odintsovo bypass)  | -                    | 0,37                                  | 0,49                   | 0,86  | 42,8%              |

Source: based on Sberbank, 2010; Infrastructure Journal, 2011

Only one financial closes based on project financing, it is Pulkovo airport. The real



challenge of PPP projects is that they can be paid only through general taxation or via pay mechanism. Thus financial structure of the project can tell a lot about their effectiveness in respect of project costs for the government and society. Table 2 showed that the great amount of capital contributed in the road projects by government that raises the question of affordability of the projects and raises a question on their ability to ensure VFM for the government.

Success and ability of Pulkovo project to reach financial close on the basis of project finance is partially linked to predictability of cash flow generation by the project and existence of revenues in foreign currency that blocks the exchange risk.

In two projects out of three (except Pulkovo airport) government guarantees redemption of the debt of private sector (see table 4).

Table 4. Three major closes: key facts

|   | <b>Pulkovo airport</b>  | <b>Moscow-St Petersburg road, 15-58 km</b>  | <b>Moscow-Minsk M1 (Odintsovo bypass)</b>               |
|---|---|---|---|
| <b>PPP model</b>                              | BOOT  | BTO   | BTO   |
| <b>Payment mechanism</b>                      | No payments   | minimum revenue guarantee   | minimum revenue guarantee                               |
| <b>Government support</b>                     | Reconstruction of two runways<br>Partial guarantees for banks | Grant from Investment Fund of Russian Federation<br>Government guarantees (loan)<br>Minimum revenue guarantee | Government guarantees on corporate infrastructure bonds |
| <b>Demand risk on private sector</b>          | Yes   | Above level of minimum revenue guarantee  | Above level of minimum revenue guarantee                |
| <b>Impact on public budget / fiscal risks</b> | Low risk  | High risk   | High risk   |

Source: based on Infrastructure Journal, 2011,

In two roads projects government didn't succeed to ensure competition on a tender. During prequalification on Moscow – St. Petersburg road, 15 – 58 km and Moscow – Minsk were presented only 2 bidders, and only one bidder was prequalified in both projects. Thus in the beginning there were no preconditions created for PPP projects to be efficient for government. In comparison in Pulkovo airport project on a prequalification

stage were introduced 7 bidders and 3 of them submitted their bids. As a result mentioned above road projects didn't ensure condition which are essential for capital expenditure decrease in comparison with the conventional procurement.

It is important to highlight the positive effect of participation in the projects foreign experienced private companies such as Alpine Bau, Vinci, Fraport which has brought new technologies and better management. Nevertheless rescheduling the construction beginning due to protests of population and social organizations (road Moscow – St. Petersburg, 15 – 58 km) and organizational problems (road Moscow – Minsk) decreased significantly positive effect from foreign companies attraction.

Having considered the above key PPP projects in Russia, we can conclude that the cause of failure and long-term projects preparation is not due to financial crisis but due inexperience of all market participants that are involved in PPP project. In the first place legal, financial and institutional environments were not ready for first PPP projects. This situation is typical for all PPP emerging markets. The creation of the legal, institutional and macroeconomic environment, as well as developing an understanding of all members of the PPP project of the conditions that must be fulfilled to enable PPP project implementation takes time.

At the moment, the effective implementation of big capital PPP projects, PPP is most likely in case of infrastructure, where demand risk is absent or minimized, or in cases where the project is able to generate a steady income (as it is a case in the airport "Pulkovo" project).

Despite the importance of financial closure occurred, the continued success of the expansion areas of PPPs in Russia, as well as the increase in investor interest in participating in such projects depends largely on the approach of the government on preparation of future projects. First of all, we are talking about realistic expectations and requirements of the government to investor, as well as the optimal risk-sharing between the private and public sectors, as potential attempts by the state to shift more risks to the private sector will lead to a rise in the cost of the project to the public budget and make it impossible to achieve value-for-money in the project.

## **CONCLUSION**

Key value of private sector involvement via PPP mechanism is a ability to do more projects in parallel rather than sequentially because one is less reliant on 'just' the state or regional budget.

PPP models provide better flexibility to tie the contractors into service quality and delivery standards with appropriate penalties through payment mechanisms etc. The major advantage of PPP comparing to public procurement is opportunity to allocate risks efficiently between project participants. Particularly risks connected by investor and lenders in a project, in conclusion determine chances of reaching financial closure. Hence

optimal risk allocation and PPP project financing structure is set as key from all available success factors.

The success of a country's PPP programme depends on the quality of investors it is able to attract and the availability of finance. Development of a transparent investment regime coupled with the removal of barriers to investment (such as currency exchange controls or restrictions on repatriation of dividends) will assist in attracting potential foreign investors, which will in turn have the effect of increasing competition.

A robust security package is essential for lenders (including creditworthy public sector covenants (or some form of guarantee or support of the public sector's obligations), the ability to pledge project receivables, charges/mortgages, direct agreements and step-in rights).

The main sources of financing of PPP projects in developed PPP markets before the crisis were equity investors in conjunction with the credit resources of private banks. Government support in these countries is rarely used and is more common in countries with emerging PPP market, where minimum guarantees of the government stimulates the interest of investors and contributes to the development of PPP market. Almost all PPP structures, and certainly in emerging markets, rely to greater or lesser extent on public sector support.

PPP is not a panacea for all projects and it should be carefully considered. Choosing PPP model depends on the goals and objectives of the government, as well as his willingness to transfer certain functions to private partner. The choice of the model will depend on several important parameters, namely the impact on the effectiveness of the project, the possibility of shifting risks to private partner, to improve the quality of services and opportunities for innovations.

On the other hand, the choice of the PPP model by the government depends on requirements of private sector that should be taken into account to make the project be procured. Important factors for private sector for participation in PPP projects are the following:

- profit;  
premium for risk-taking;
- governance mechanism prescribed in the contract;
- possible expansion;
- government support;
- political stability.

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# ROLE OF COMMUNICATION IN POLICY MAKING

Viera Žúborová<sup>1</sup>

The third age of political communication not only open the space for new opportunities for political actors to target and influences the opinions of potential voters, but also open the channels for citizens to influences the relevant actors in the political area, created new communication tools within there are able to communicate with politicians, there are able to present their issues, approaches and visions in the political area and at the end influences the decision – process in it. In other words, the third age of political communication expanded the political participation and the two – way flow, this leads to the object that we nowadays described as “direct communication” in the political area which create an open space for citizens to improve and influence “direct” the dialogue over the policy matters.

This leads to the fact, that government “upgrade” their ways to communicate with the citizens, from the basic level – the need to communicate information to the citizens – to high participative and interactive communication.

The aim of the text (article) is to provide a guide of the communication ways of the relevant (non) political actors in the policy making area. To understanding the importance of political communication in the policy making we need to explain not only the whole scale of political participation as a multidimensional phenomenon<sup>2</sup> (Verba-Norman: 1972), but also the communication architecture that is visible between the actors in the political system. In this context this article will observe the communication network structure and position among the political participant and how influences the information aggregation through communication and the whole scale of efficiency of governing and policy making in general.

## PRINCIPLES OF POLICY-MAKING

Also in these days the term policy-making is difficult to describe. There are many theoretical frameworks that try to attempt to put boundaries around part of the policy process. We can also observe that there is a common pattern that explains when a policy is made. In other words the term refers to ongoing stages of decision-making of ideas, visions, opinion through space and different levels. The traditional model of policy process that separates policy-making into specific and different stages: agenda-setting,

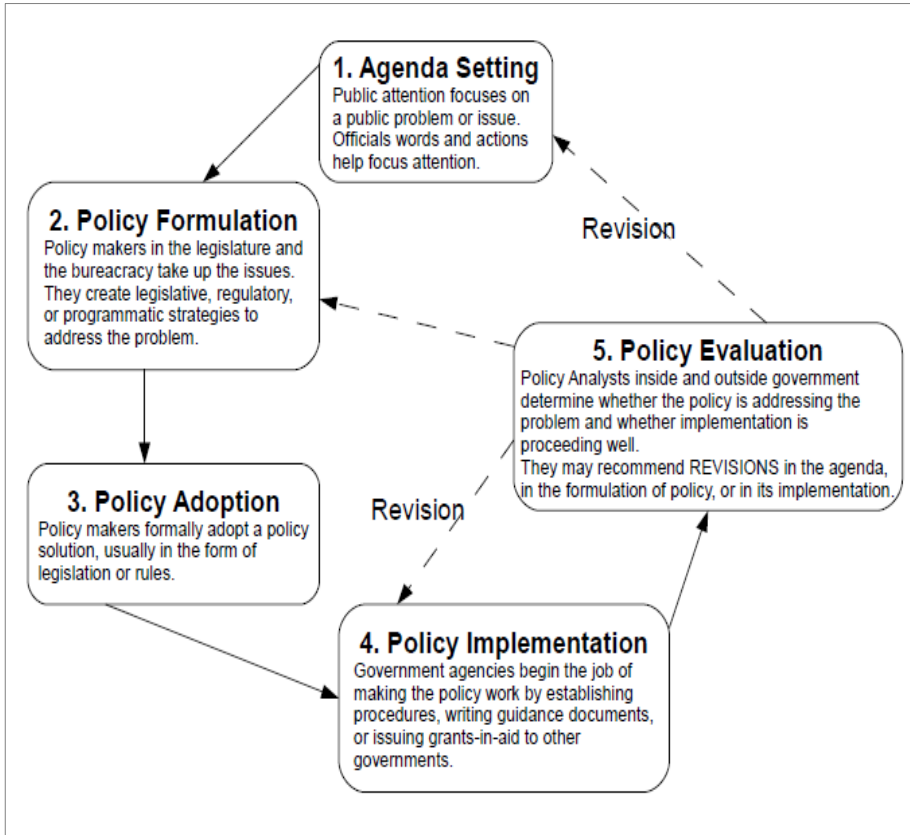
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2 As Verba has demonstrated, there are different types and forms of political participation and cost and benefits that are associated with it.

policy formulation, decision-making, implementation and evaluation (Neilson: 2001).

Figure 1: Model of policy-making and policy implementation



Source: Maetz M., Balié J. (2008)

This “traditional” model of policy making is useful tool to help clarify the processes in the political area and identify the steps of complex events that highlight features of political life and outputs to the environment (society). In other words, it creates an idealistic view on policy, in reality of course policy-making and policy implementation is more unpredictable and also now always rational oriented.

The study of policy-making not only involves to explain and to follow “traditional” models which describes the processes in it, but also different perspectives on understanding policy change. Sumner and Jones (2008) noted that there are three domains of interest based around specific types of power relations: actors, institutions and discourses. In other words, we can observe three approaches to understanding policy processes.

For the goal of this article we will focus on the first approach – policy actors and networks, which involves also communication as a general pattern in it. As Wolmer noted: “In any given policy domain actor networks are not exclusively confined to state institutions....This means that on the other hand the existence of actor-networks can make for pluralist policy-making involving a range of different stakeholders or actors. Processes of negotiating and bargaining between competing interest groups are central to policy making. And networks can also gradually change narratives as well as reinforcing them – as they bring people together who strategies and catch the attention of the right people.”

So we can observe that the general pattern to create such actor-network is a particular issue problem, aspect for public policy, what means that the first phase “agenda setting” is active. The next actor-network is active in the second phase “policy formulation” as called “epistemic communities” consisting of professionals in particular domain of issue problem which was presented in the agenda-setting. The last actor-network “policy communities” is visible in the following phases of adoption, implementation and evaluation of policy, who are integrated with the processes, which play a vital role “in the developing, testing and refining policy ideas”. (Jones: 2009)

As we can observe, the policy-making model is create of sets of communication network of relevant actors that are in a permanent communication flow. This means that the communication networks are viewed as an important influences alongside individuals, it goes from the fact that policy-making does not take place in a vacuum:political, economic and social factors influence the inputs and outputs of how specific policies are made, and also what kind of actors makes them and in what levels.

Another view on the policy-making process and the involvement of different actors could be seen in the works of Sabatier and Jenkins-Smith (1993) and Perkin and Court (2005). They recognize 4 stages of policy process: agenda setting, policy formulation, implementation and evaluation. As they note, in every stage of the policy-making process different actors of the networks could take the leading role, alone or together. For example the civil society and the media are visible and involved at the agenda-setting level. But also in the policy formulation, the civil society could be involved, they can established new values and effective debates or providing supplies to their own community or play a crucial role as a bridge between governors and local people. (Lavis et al.: 2002).

## **THE (IDEAL) COMMUNICATION FLOW IN THE (POLITICAL) SYSTEM**

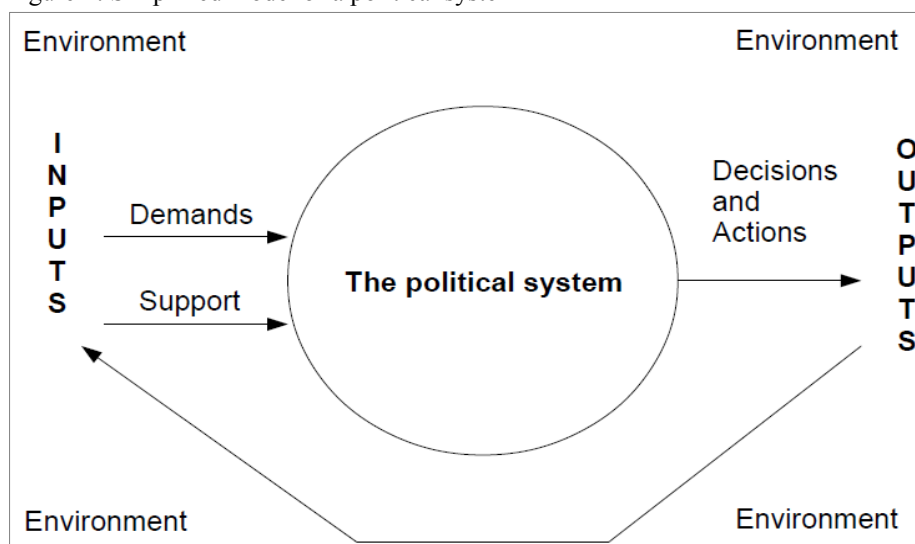
The traditional communication flow which was represent in the current decades in the political sphere between political and other actors usually point the election as the decade of “changes” where the political actors pull their visions, opinion the the society and target the potential voters to gain the seats in the parliament, or to govern. In other words,



political participation was taken to the end, where the policy making and decision making begins. The traditional view on the political system, where only inputs and outputs were active changed to a multidimensional communication flow, which also added lateral and participative flow. In these decades we can not only observe inputs whose aggregated into outputs, but also flows that are visible in every level and stages of (political) participation and policy making.

This view presented above is observe also in the Easton model of political system. Easton observe that all social systems are created by interactions among actors – persons, and these interactions are in general the basic patterns of such systems. But he also specifies the political system from other according the specific set of interactions “what distinguishes political interactions from all other social interactions is that they are predominately oriented toward the authoritative allocation of values for a society” (Easton: 1965, 50).

Figure 1: Simplified model of a political system



Source: Easton, 1965, 112

Easton portrayed the political system as a dynamic feedback system, where the position and success of political actors are influence and depends on the support of society (voters). As Easton observes, “political systems accumulate large repertoires of mechanisms through which they may seek the cope with their environments. Through they may regulate their own behaviour, transform their internal structure, and eve go so far as to remodel their fundamental goals” (Easton: 1965, 19).

In general we can characterise the input-output approach or Easton (1965) concept through specific features of political system:

16. implies a set of interaction vice versa values are authoritatively allocated;
17. system of regularised persistent patterns of relationship (among people and institutions);
18. self-regulating system, which have potential to change, correct;
19. dynamic system which is improving through the feedback mechanism;
20. inputs put the political system at work and outputs (policies and decisions) throw back what is not accepted.

In common view, the same mechanism can be observe in the concept of political communication, which give us an other complex view of the development of the society. In other words, it goes from the fact that any changes in one component (Eastons unit) of the society causes changes in the behaviour and the action of the other components in the society (Votmer: 2008).

Through Easton “terms” political communication is a system of common interactions between the main actors (political – media – society) in the political system and the environment around it. These interactions are provide on a special place called political market, were the political parties try to sell their goods and consumers – voters try to “buy” a good that could be able to fill full their interest, believes. (Žúborová: 2010)

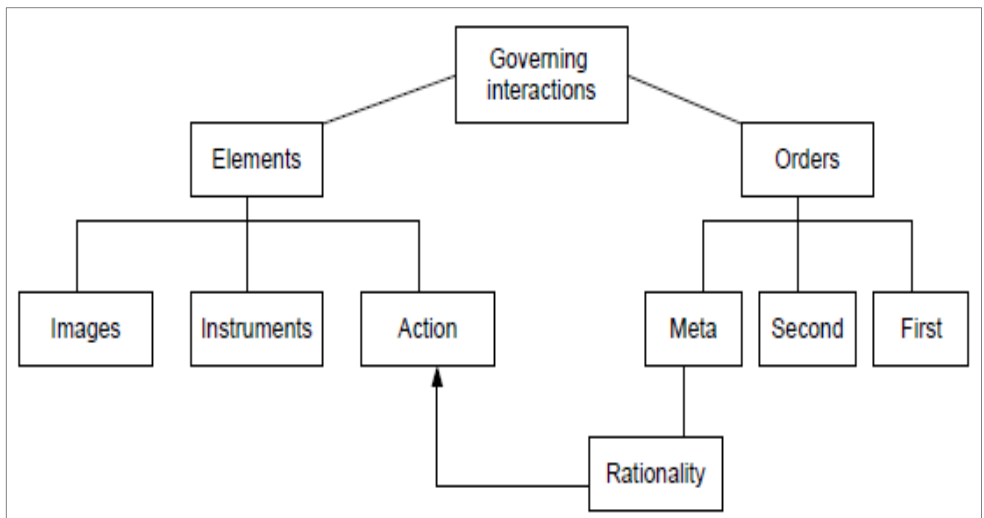
As in the Easton concept, the outputs are also concerned with the flowing from the behaviour of the actors of the system rather than from actions in the environment (Easton: 1965, p. 27), also we can observe the same pattern in the political communication, where actors design their strategies and behaviour to target the potential voters, not vice versa. This whole process of interactions build a huge networks of messages. There are exchanging between these two main actors. It is a on – going process of creation, modification and development which never ends. (Žúborová: 2010).

As for Easton is crucial the feedback, which lies in the production of outputs and response by the society to it, further of communication of information about the response and finally the reactions of the authorities. As John R. Fisher (2010) observe, the feedback loop are “actions to be taken to satisfy demands or create conditions that will do so, information must be provided to authorities (those people who speak on behalf of the system) about the effect of each round of outputs, since a drop in support is an important source of stress (Ishiyama-Breuning: 2011, 74)...so they can bolster the input of support for themselves or for the system (Easton: 1966, 152)”. Also in the political communication concept we can observe this specific unit. The feedback in the political communication deal with the communication flow of the political actors with the voters. If their pack it as a explicit or implicit message, and through which mass media channels are the political messages send, and also if the messages are modified through the channels. And at the end how the voters – citizens understanding the messages and the

way in which they act after receiving the messages.

More specifically, than Easton system theory is the Kooiman concept of governing interactions, which explain us the intentional level of interactions within the governors and governed. He conceptualise this model through which he consider the analyse of governing and governance, including policy making.

Figure 2: Governing interactions



Source: Kooiman, p. 80

Kooiman in his text not only consider “governance to be the totality of all interactions within the social – political arenas”, but also he explain and characterise the main units of this dynamic process, where governors are able to fulfil their goals, beliefs and visions only through specific instruments, images and actions. (Kooiman: 2003) The governing interactions could be described as all these activities that are able to influence the way in which political actors formulate their decisions and execute then for the society.

As regards to the term feedback or feedback loop (Easton), Kooiman in his text define this dynamic interaction with the term “reactive”. He goes from the fact, that every action related to the governing “can often be said to take a more reactive character, while initiatives for such action are located more in the social sphere and society” (Koomina: 2003, p. 83).

## THE (IDEAL) COMMUNICATION FLOW IN POLICY MAKING

Policy-making is a complex phenomenon that play a central role in every stage of legislative bodies of the country. Policies which are created in these dynamic processes affect everyone in the political and societal community. But these outputs are affected but many interests from the beginning of initiation of the policy, their formulation, creation, adoption and implementation. We can say that the inputs of the policy-making are permanently in a competing and conflicting clash of interest following the main (central) goal to balances the public values in it.

Figure 3: Key policy-making activities



Source: Local government policy-making process, MRSC Report No. 45, 1999

The central key of every policy-making at the initial phase is the summary of variables that mirror every values, opinion and vision in the societal environment and that is relevant to the political. In other words, any activities of the society are mirrored, summarized and brought upon the the political like of the community and legislative body. As for example, Easton observe, there can be different types of demands or supports (Easton: 1965). An effective policy-making process is measurable not only by the public support in the political and societal system but also the it's relevant and the ability of policy implementation in the community.

If we look at the key policy-making activities we must realize that without a relevant communication a specific policy would not arises. For example at the first stage “creating a community vision” political actors create such values and future plans at the beginning

of the campaign period, or through initiatives in the electoral period, these messages are broadcasting through various communication channels in the society. The same communication pattern and tools could be observe also the the second stage “community goals and objectives”. But in the practice, we must say that these phases are likely more closer to the community that other coming, that are communicated only through resolutions, specific policies, annual report, etc. (Local government policy-making process...1999)

As we write above, the main phase of the communication flow between the political actors and society is visible in the first two stages, and therefore we will give thes two stages the highest priority.

As we mentioned, the creation of a vision is in majority visible in the campaign period, where political actors starting communication on a particular issue, includes using public debate, consultation, while such tools have also effect on the outcome of promoted “product”. The communication that is using should be in the theoretical framework rise from acknowledges and responds to the common demands and concerns of the society. As many research conducted, that a successful campaign and in the end a potential (target) voter group will be promote and image in the political messages of the candidate include also their environment. (McNair: 2003, 108)

This specific clue could be associated also with the Concept of Lees-Marshment’s Market oriented party. We goes from the fact that political communication flows through a special communication channels, where the political marketing “acts”. In another words political marketing have the potential to influence the consumer behaviour for his/her own property. It include a number of tools, strategies which could – are able to influence the whole spectrum of political communication, especially the communication channels. (Žuborová: 2010) So the segmentation of potential voters (targeting) and the location of the candidate in it create the main strategy which should be communicate to the society of the candidate. (Less Marshment: 2003)

## **ADVANTAGES AND DISADVANTAGES OF COMMUNICATION IN POLICY-MAKING**

Every citizen in democratic country have the right to know the steps, the policies and decision, activities of authorities at the legislative body. In a well functioning system, the authorities provides reliable information to the society. The society so rely heavily on modern communication channels (radio, television, internet, newspapers) to rise the specific information that concern them and their lives. The central key of this opened information flow is the friendship and good relations between the political actors and media. So not only media but especially the political sphere need to learn to tolerate the role of an independent media in the system, and learn to use them not only as a feedback tool but also as a communication channel.

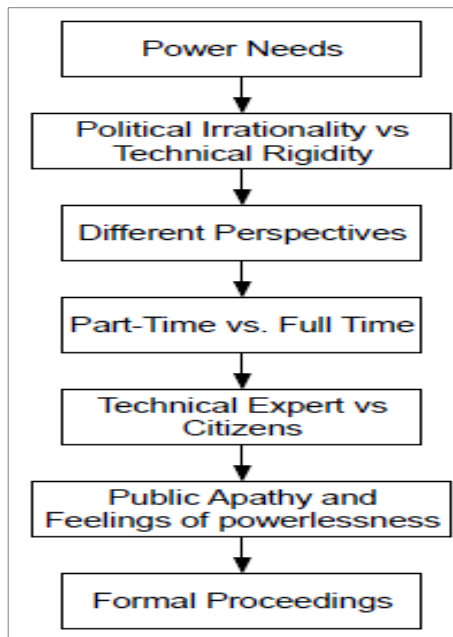
The main disadvantages of the communication in general is the fact, that every individual have different goals, visions, interest, and this simple create the main barriers in the policy-making process and also in the communication within the society.

In the first unit “power needs” the disadvantage is visible in the lack of information between the civil society and policy makers, for example to support for improving strategies for citizens and of their living. In other words, in this unit is visible a huge gap between the general knowledge and diversified needs of the society and the communication barriers for the improving is very strong and blocked by bureaucratic needs of policy makers (Gupta: 1992). The second barrier is dealing with the relation between technical and political staff in the public office (Local government policy-making process..1999).

The third barrier in the communication between policy makers and society, including media, is the “difference” not only in the communication style, but also in the language that is using by the main actors in the political and societal system. Every one of the main actors have their own vision, their own ways to deal with different situation, and this could leads to a lack of communication in the system.

The following to unit – barriers are visible in the technical support of the communication and the human resources of elected authorities and their willingness and potential to communicate permanent.

Figure 4: Communications Barriers



Source: Local government policy-making process, MRSC Report No. 45, 1999

The sixth barrier of effective communication is presented by the “public apathy and feelings of powerlessness” which is associated with the decisions making of the governors and the inability of the society to force the policies as the outputs of the system. This could be the result of inadequate communication of the authorities to the society or the result of the “untouchable” position of the policy makers in the public sphere, which could leads to an apathy of the society and to the Nixon phenomenon of “silent majority” as the who are not willing to express their opinions publicly.

Information, consultation and participation are the main tools that could be added to the advantages of communication in policy-making, if we speak in the ideal constellation. The policy-making process cover a broad spectrum of interaction between government and citizens. This interaction are built up from information – consultation and participation which we mentioned above. Also the policy – making process must consider how policy will be communicated with the public and in how range should – must be the society involved in these processes.

The first and general pattern which is characterise for the communication in the policy-making process is the “information”, which could be seen as one way relation on one hand it covers passive access to information from the citizens (as newsletters, reports, etc.) and active access of information (web pages, social media, public meetings, etc.).

The second stage of the relation between government and citizens “consultation” is characterise by two way relation where the governors are seeking the feedback from the “users” of public policies, government services as outputs of policy-making.

The third stage “active participation” is the general goal of every of modern and opened government. It’s describe by the a relation based on partnership, where citizens are played an active role in the policy-making processes through active dialogue in the proposing of new policies, but the final step and decision by implementation and formulation rest in the hands of the government.

Through these general communication stages in the policy-making government are following the goal to strengthen the relation within the society and potential voters. As the OECD working paper observe that the driving forces to built up such strong relationship (and in some cases partnership as it is visible in the active participation of society) are:

4. improve the quality of policy;
5. meet the challenges of the emerging information society;
6. integrate public input into the policy-making process;
7. respond to calls for greater government transparency and accountability;
8. strengthen public trust in government (Citizens as Partners....2001)

These powerful communication platforms or stages are viewed as information clearing house allow to share information between the main actors in the political and societal

system. We must observe that these stages need sufficient tools through which are permanently transmitted information.

## **THE POTENTIAL OF NEW COMMUNICATION TECHNOLOGIES IN THE POLICY-MAKING**

The new communication technologies in the current decades are viewed as the effective tool that should be able to strengthen the common interactions and relations between the society and authorities. The new communication technologies can make easier effort for citizens to searching, collecting, updating information that are important in their every day living, or information that help their to get closer to the decision making process and monitor the steps of their elected politicians.

As also Mosca in his article note that democratic potential of new communication technologies: “on one side it is horizontal, bi-directional, interactive, and cheap, and it empowers resource poor collective actors and individuals. On the other side, the problem of the digital divide raises a discussion on the democratic nature of this medium” (Mosca, 2007, p. 16)

If we try to observe the position and influence of the new communication technologies in the policy-making processes we must appoint reasons why the main actors in the societal and political sphere are more and more using modern communication technologies. From the side of governors the main reasons for using modern communication technologies are:

- establish a presence,
- act as a demonstrator,
- deliver information;
- deliver online services,
- to enable consultation with citizens,
- to facilitate participation by citizens,
- to sale their information resources to public and private sphere including society (Citizens as Partners....2001)

From the side of the society, the reason for using modern communication technologies, or in other words, the importance of involving the society to use these communication channels are:

- active participation in the public sphere,
- providing local knowledge to the authorities about what should be done and what not,
- to create a feedback for authorities, from seeking to improve the delivery service of policies,
- create an effective interaction with the authorities to problem solve issues,



- education role by providing an opportunity to explain problems, issues,
- measurement the range of public opinion about vision, beliefs (Curtain: 2003).

We yet know that the new communication technologies have a great affect on the main interaction in the political and societal sphere, including the policy-making, and mainly the decentralised nature of these communication technologies. We can also observe that in general the impact of new communication technologies in the policy-making process have not only positive but also negative impact. In other words, the „internet creates a new public sphere, which influences the policy making arena and reduces comparative physical resource advantages of experts and governors over citizens“ (Yang - Zhiyoung: 2010, 432).

## REMARKS

The core element of good governance means a effective and interactive communication in the relations between citizens and policy makers. The communication not only allow governors to develop new sources of policy ideas, but also gave them relevant information and resources when it comes to making decisions. The aim of this article was to explain, briefly, the main advantages and disadvantages of the policy-making processes and the role of communication in these processes. As we observe, the main pattern of the communication in the policy-making is the „interaction“ which play a crucial role in every stage of making policies. So in this view, the political actors, if they would built up a functional and stable system, they must strengthening their relations and networks with the society and ensure that the messages or outputs which are sending to the environment are complete, objective and relevant and also to easy to understand (one way communication). They must open a new network of interaction, where the role of citizens in the policy-making have a clear goal and rulers defining the limits of the exercise and authorities obligation to account for its use of societal inputs (two way communication- consultation). And also, if it still is rare in the policy-making, governors should create space for an active participation of the citizens in the decision-making processes. They must built up such communication channels that allowed for society to present their ideas and proposals into the policy-making processes. Which could be fulfil with the new communication technologies, as internet, which as the text mentioned above decentralised the processes of policy-making.

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# EXPLORING THE LIMITS OF PUBLIC PARTICIPATION. LESSONS FROM LOCAL GOVERNMENT IN POLAND (1990-2010)

Katarzyna Radzik-Maruszak<sup>1</sup>

## INTRODUCTION

The transformation of the system that took place in many Central and Eastern European countries in 1989/1990 caused the fundamental changes at the local level. The objective of the decentralization reform was to establish strong, autonomous from central control, local government. The administrative, fiscal, and political decentralization were supposed to change drastically the role of the central state by providing local authorities with a new set of responsibilities, fiscal resources, and the decision-making power to implement them (Regulska 2009:537). What is more, decentralization became an important element of participatory democracy that had a potential to improve the accountability of local government.

In the case of Poland the introduction of the wider mechanisms of public participation was one of the proofs of 'local independence' as it allowed citizens to make decisions and to be involved in the process of local governing. Gradually traditional forms of participation (elections, referenda, consultations) were supplemented by the active cooperation of local government units with non-governmental organisations and the informational policy conducted by local administration. Recently some local authorities have started to experiment with new forms of involvement e.g. those characteristic of participatory and deliberative democracy (participatory budgeting, citizens' juries, consensus conferences, deliberative forums); (McLaverly 2011:406-408).

Though, while analysing the level of public engagement after 1990 it seems that the phenomenon of the lack of support for actions undertaken by local government is becoming more and more common. The turnout in local elections not only never exceeds 50% but in some local units is constantly around 20%. Moreover, the practice applied so far indicates that in some cases elections or referenda are not the ways of solving issues crucial for local communities, but they are rather the institutions by means of which local political elites compete with each other.

The aim of the paper is to analyze local participation in Poland (1990-2010). The article poses the following questions: What are the reasons of the citizens' indifference and weak engagement in local issues (1990-2010)?; How can citizens' apathy be explained in the context of local relations?; Is, e.g. poor voting turnout, a proof of the lack of acceptance

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of activities and policy conducted by local authorities or are there other reasons?; Is the low level of local participation the result of already established relations between local authorities and citizens?

The paper is organized as follows: the first section elaborates the decentralization and participation issues; the second focuses on local participation in Poland, its forms and practice; finally the conclusion tries to identify the reasons of citizens' apathy and discusses the possible reforms.

The theoretical study is supported by the objective data e.g. official statistics in local elections, referenda etc. obtained from the State Electoral Commission (Państwowa Komisja Wyborcza – PKW) and the Public Research Centre (Centrum Badania Opinii Społecznej - CBOS).

## **THE BASIC NOTIONS: DECENTRALIZATION & PARTICIPATION**

Decentralization is a process that reallocates resources from a higher, more central authority to a lower one. At present at least three types of decentralization can be distinguished: administrative, political and fiscal one (Bevir 2011:64). However building the decentralized system is not a one-time procedure, but rather the process that needs time and establishments of lasting cooperation and collaboration between numerous actors (institutions, organizations, social groups etc.). In many countries decentralization constitutes an important issue. Firstly, as Treisman points out 'the question of how governments should be organized must be as old as the study of politics', therefore discussion over the level of centralization/decentralization is never outdated (Treisman 2007:6 cited in Saito 2011: 486). Secondly, in some cases citizens showed their disappointment to a disfunctional, inefficient structures of the central administration which led for searching new solutions.

Concerning the relation between central state and local government many arguments in favour of decentralization can be found in the literature (see e.g. Saito 2011:486-488; de Vries 2000: 197-198; Bevir 2011:64-67)

Firstly, decentralization is supposed to reinforce the efficiency. It is said that local government is located closer to people and because of that is better suited than central government to identify what kinds of services people need. The presence of many organizations can lead to the technical efficiency, through learning from diversity and therefore justify the decentralization of the production (Walsh 1996:71 cited in de Vries 2000:197). Moreover, some scholars indicate that decentralized institutions are more efficient, flexible and can adjust themselves much quicker to changing circumstances. They are also more innovative and generate higher morale (Osborne 1993:253ff cited in M.S. de Vries 2000:198).

Secondly, decentralization has an impact of responsiveness. Local authorities can produce and provide services that are more responsive to public aspirations. This quite old

argument is linked to the principle of subsidiarity that says that provision of public services should be located at the lowest level of government, encompassing, in a spatial sense, the relevant benefits and costs (Oates 1999:1122). The advocates of this attitude indicate also that there is nothing as ‘tailor-made’ solutions and therefore local government is better suited than central government to identify what kinds of services people need (J.S. Mill 1861; de Vries 2000:197).

Thirdly, many believe that decentralization influences service’s development. Citizens are more likely to share the costs of services if they feel the improvement. Moreover the use of inhabitants for provision of local services would render this service cheaper and more efficient. However this gives also a foundation for the empowerment of local communities (de Vries 2000:197).

Fourthly, decentralization is often linked with the level of participation. Participation means that citizens have a legitimate right to voice concerns in affairs that influence their lives (Saito 2011). The decentralists believe that the process of sharing the power can enhance civic participation and it may neutralize entrenched local elites who are often unsympathetic to national or local policies (de Vries 2000:197). Local authorities are more likely to reflect peoples’ preferences than the central government.

Moreover, decentralization influences scrutiny and accountability of local institutions. On the one hand political power is located closer to citizens, on the other politicians are less remote and more visible. People can scrutinize them closer than central power. In addition, if local authorities are elected by popular mandate, relations between leaders and the population become more intense, which in turn contribute to more trusting and accountable relations between leaders and followers. During these processes civil values are noticed, which is more than important in young democracies (Saito 2011:486-488).

Finally, the transfer of power from central state to local government might increase ethnic harmony and national unity. Local democratization is a precondition for building national unity in multi-ethnic and multi-religious societies, or in industrialized as in developing countries. Local autonomy better accommodate the competing interests of diverse social groups, including ethnic and religious minorities (Saito 2011:487)

What is important as regards the topic of the paper, decentralization can influence the level of public participation. It seems, that at present in many democracies enhancing public participation became a central agenda. However, in most cases, this is not just an impact of the decentralization discussion but also a result of other matters.

Firstly, the decline in civic participation and the growing distance between citizens and state institutions can be observed. Some authors warn of the emergence of ‘diminished democracy’, in which public involvement has lost its link to political life and where political engagement has become more dominant of professional bodies (Skocpol 2003:11; Gaventa 2004:5). In Western democracies, the roots of this phenomenon could be found in the 1980s when the role and position of local authorities were influenced by the concept of New Public Management (Pollitt, Bouckaert 2011). In many states

unelected, and also unaccountable, bodies were established (executive agencies, boards, quangos etc.). NPM called attention to efficiency and effectiveness and obliged local government to operate in a new manner, e.g. to find and apply innovative methods of service delivery and for financing them. Nevertheless, the paradigm has managerialised local authorities' and citizens' role by putting them in the perspective of the service providers and service users.

Secondly, the emergence of new actors at local level and the fragmentation of decision-making powers in the 1980s and 1990s contributed to a shift from local government to local governance (John 2001). Despite the importance of efficacy, governance focussed more on the improvements in the quality of local democracy. In a consequence, the recent reforms brought pressure to include to the decision-making process, not only entrepreneurs and executive agencies but also citizens and NGOs. In many countries local authorities were almost forced to move, by government exhortation and citizen pressure, from representative towards participative and deliberative democracy and use new forms of civil engagement.

Thirdly, what refers to the argument above, in many countries the discussion was conducted over the crisis of efficiency of traditional mechanism of democracy. In Great Britain the Labour government launched in 1997 the programme of 'democratic renewal' that was about adjusting the institutions of local government to make them more democratic (Pratchett 1999:2) In this context, some governments decided to supplement traditional methods of participation (local elections, referenda, consultations) by the new forms of civic involvement (participatory budgeting, citizens' juries etc.) Moreover, a number of countries especially those that suffered the authoritarian governments and carried out the political transformation identified the introduction of varied mechanism of participation with enhancing the democratization process.

## **THE CONTEXT AND PRACTICE OF LOCAL PARTICIPATION IN POLAND**

However, both issues decentralization and participation have a different meaning and value in countries with communist past. Between 1944 and 1989 Poland was under this regime's rule. The political system was adjusted to Soviet pattern. Though the system was coherent, it was based on the assumptions that were strange to the basic rules of the democratic state. The preamble of the Constitution of 1952 (amended in 1976) contained a statement that the main role of the state was the implementation of 'the great socialist ideas'. While formally the power belonged to 'the working people of the towns and villages', through parliament and the peoples' council, in fact all the decisions were made by the party. Society was to head in the direction set by the official ideology. The will of the people was unimportant as those who ruled the country assumed that the nation was and would remain against the existing political system. In practice it also meant the central bodies decided about everything and any form of civic control over their activities

was only formal (Kulesza 2002:191).

When the communist regime collapsed in 1989 a significant effort was put to re-establish free, independent and elected local government. It was a strong belief that self-government might be an antidote to the centralized state and the institution through the people could gain control over their lives, regenerate and revitalise their communities (Campbell & Coulson 2006:543). In many cases the restitution of local government and establishment of elected local authorities were perceived as a value on its own (Swianiewicz 2002:53).

What distinguishes decentralization reform in Poland from other CEE countries' experiences is the perfect use of the historic 'five minutes'. As Jerzy Regulski and Michał Kulesza, the founding-fathers of the reform indicate the system's reform is possible only when particular conditions allow it to take place. It is crucial to use this opportunity because such favorable circumstances may never happen again (Regulski 2010: 24; see also Kulesza 2000:205).

The first wave of decentralization started just in 1990. On the basis of the Act of 8 March 1990 on Local Self-Government independent municipal government was established. However, the solution was perceived as a provisional one. It was argued that the existence of 49 small regions (*województwa*) introduced by the communist administration in the mid-seventies was disfunctional and required modification. It was assumed that newly elected regional governments should be introduced along with reforms in territorial division. However, for a number of reasons, the introduction of upper tiers of local governments had been postponed until the end of 1998 (Swianiewicz, Herbst 2002:223-224). In that year on the basis of the Act of 5 June 1998 on Counties and the Act of 5 June 1998 on Regions the three tier local government's system was established<sup>2</sup>. That was stated as a second wave of decentralization (for details see e.g. Radzik 2010; Swianiewicz 2005:101-102).

What is important, the decentralization process and the establishment of local government with elected authorities opened new possibilities for participation. On each level of government elected councils were introduced. In addition in 2002 the directly elected mayors were established in all municipalities. The important step in the broadening of participatory mechanisms was also the passing of the Act of 11 October 1991 on Municipal Referendum (changed in 2000, amended in 2005). Finally the local consultations were introduced. Moreover some local authorities decided to enlarge number of participatory opportunities and supplement representative and participative democracy by deliberative mechanisms.

After twenty years of democratic rule and the implementation of decentralization principle it is worth to focus on participation and the transformation of civic engagement at local level. In this section I will elaborate local elections, referenda, citizens'

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2 The reform started to operate on 1st January 1999.



initiatives, consultations and other forms of civic engagement more deeply.

### *LOCAL ELECTIONS*

Local elections can be defined as the simplest manifestation of citizens' participation in the functioning of local government units. They are important in terms of their function – legitimisation, aggregation and diagnosis. The first one not only legitimises the selection of authorities, but also shows whether citizens accept the power relations being formed and whether they believe in the idea of local government, whereas the aggregation function allows the reflection for current interests of local communities. Finally, the last one - the diagnostic function - makes it possible to determine the alienation level of citizens (Michałowski 2009:73). Poor voting turnout may prove the lack of acceptance of activities and policy conducted by local authorities.

The first local elections took place on 27 May 1990. In the municipalities up to 40 000 of inhabitant the majority rule was in force, whereas in bigger units the elections were organized under the proportional rule. The voting turnout was 42.27%, and even though it was not an impressive result, the huge activeness of civil committees coming into existence and social trust in the possibility of changing reality are worth noting. Moreover, the results of voting indicated that party affiliation played more than a very limited role. As Swianiewicz indicates just a few months after the fall of the past regime, there was simply not enough time for new parties to organize themselves. Furthermore, the parties connected with communism were compromised and had a minor support of the electorate (Swianiewicz 2005: 106).

Regarding the second local elections that were organized in 1994, two things seems to be worth mentioning. First, the turnout comparing to 1990 dropped and was only 33.75%. Second, there was a visible increase in party dependence. Emerging political divisions had an impact on the issue of personnel choices – councillors, chairs of councils, their deputies, mayors. It might have been a result of the “war at the top” – the conflict between ‘Solidarity’ leaders who before used to act together. What is more, 1994 local campaign introduced for the first time an interesting phenomenon – the ‘hidden partisan candidates’. Four years of democratic rule already brought the disillusionment with party politics and many candidates decided to suspend their party affiliation and stand for the election either as a ‘independent’ or with a support of a not-very revealing names of electoral committees (Swianiewicz 2005:107). However, it seems that since 1994 the trend is becoming more popular.

The third local elections took place in 1998. The campaign and voting were significant because of at least three reasons. Firstly, the second decentralization reform was introduced and people for the first time were able to vote not only for municipal but also county and regional councillors. Secondly, the electoral law was amended. In municipalities above 20 000 inhabitants and at county and regional levels the

proportional rule was introduced. Also the level of support for the list of candidates were established. Thirdly, the results of the elections showed that a further step in the advance of political parties in municipal politics was taken (further details see Swianiewicz, *ibid.*). The local turnout was 45.45% in municipal councils, 47.76% in county councils and 45.35% in regional councils (Słobodzian 2011: 247).

The 2002 elections brought expectations for a revitalization of local politics and a higher turnout as for the first time mayors were supposed to be elected directly at the municipal level. The hopes failed, however as the turnout on municipal level was 44.12%, 49.48% at county level and 44.23% at regional level. Moreover, it should be stressed that the least interested in local affairs turned out to be residents of large cities – in many units the participation of citizens did not exceed 20% (Michałowski 2009:78). Also in the first mayoral elections took part only 44.24% of those entitled to vote.

The fifth elections after the democratic break took place in 2006 and were based on the significantly changed electoral law. Just two months before the voting, by the votes of the governmental coalition of Law and Justice (Prawo i Sprawiedliwość), populist Self-Defense of the Republic of Poland (Samoobrona RP) and nationalist League of Polish Families (Liga Polskich Rodzin) the local election law was altered. The possibility of creation the block of lists and forming the agreements concerning the seats division before the elections was introduced. The changes had an impact at least on two things. Firstly, the new regulations fostered the formations that were grouped into blocks; for the others it was much more difficult to obtain the seats. Secondly, new law made the voting rules illegible for ordinary citizens<sup>3</sup>. The general turnout was 39.56% (Radzik-Maruszak:2012). The last local elections took place in 2010. Again the turnout was not significant, as only 47.32% entitled to vote went to the polls.

On the basis of conducted analysis of local elections (1990-2010) some issues are worth to be underlined. Firstly, the Public Opinion Research Centre's (CBOS) survey from September 2010 revealed that two thirds of respondents described local elections as important (68%), whereas 38% among them as very important (CBOS 2010:2). Moreover, two months before the last local elections, 65% of people declared that were interested in local voting and one respondent out of six was very interested (17%). For one third of people local elections were not important (CBOS 2010:3). 71% of those who were tested declared that they would take part in voting, 53% declared to do that for certain (CBOS 2010:5). However, in the end the turnout was only 47.32%. This shows that on the one hand people feel obliged to vote and consider taking part in elections as crucial and socially approved, however on the other it does not translate to real actions.

Secondly, the results of elections showed the tendency of partisanship of local politics. The highest number of candidates for mayors that had a party affiliation and support was presented in 2010 election. It seems that parties gave a clear signal to the society: local

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3 The possibility of blocking the lists was abolished in 2008.

government is the next political battlefield (Michałowski 2012:28). However, still if comparing the presence of political parties in local governments, Poland is far behind countries like Sweden, Norway, Switzerland or the Netherlands (Swianiewicz 2010:19). Though, what happens in Western democracies rather rarely and what exists in Poland is a number of candidates for councillors and mayors who hides the fact of party support during campaign or even afterward. Many of them declare to be 'independent' or to have a support of a not-very revealing electoral committees. Unfortunately, the phenomenon is very difficult to be tested among mayors and even impossible to verify among councillors.

Thirdly, it seems that the party or quasi-party presence has impact on another electoral behaviors and causes the negative-voting phenomena. The voters more and more frequently vote against the particular political option, than they actually articulate real support. Furthermore, the politicization, partisanship, negative image and the progressive brutality of local politics discourage certain groups from the deeper involvement. The statistics revealed that after the 2010 elections, women constitute only 25% of councillors and 9% of directly elected mayors on the municipal level (Grochal 2011: 4).

### *LOCAL REFERENDA*

Undoubtedly, the introduction of local referenda and consultations were to serve the development of the participatory society. Initially, in the 1990s only the residents of municipalities were entitled to organise the former, then this right was extended to the citizens of counties and regions<sup>4</sup>. However it seems that it is not the legal possibility to organise referenda that was and is crucial, but the effective use of this institution.

Local referendum is defined in the Act of 15 September 2000 on Local Referenda as:

*'a poll in which the residents of given unit of local government express their will regarding, the manner of deciding matters concerning their community and remaining within the scope of tasks and jurisdiction of the authorities of that unit, or regarding the dismissal of the legislative body, and in the case of the municipality also regarding mayor dismissal. A referendum consists in giving a positive or negative response to a question or questions on an official ballot, or in making a choice between the proposed options' (ibid.)*

The referenda can be divided into two major groups: mandatory and facultative ones. Moreover, the polls can be organized in the following issues: to recall an organ of local

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4 The first Act of Municipal Referendum was passed on 1st October 1991. In 2000 by the Act of 15 September 2000 on Local Referendum the regulations were changed and the possibility to organize referenda at county and regional levels was introduced. See. Dz.U. [Journal of Laws] 2000 No. 88 item 985, the Act of 15 September 2000 on Local Referendum.

government (councils, mayors at municipal level) before the end of its tenure; to self-tax of inhabitants for public purposes (only at municipal level); to decide about other matters of importance to the local unit.

However, since 1990 local government has been struggling with the following problem – although referenda have been organised, the attendance of people participating in them did not allow for recognition the results as valid and binding.

Under the first Act of Municipal Referendum from 1991 either the municipal council or the inhabitants could petition for a referendum, various entities were included in the latter group e.g. citizens, the structure of the political party or the organization operating in the municipality. The municipal council could put to a vote the issue of self-taxation or some other issues crucial for the municipality and the inhabitants, as indicators of a referendum, could petition for a referendum on various matter, including the dismissal of the municipal council<sup>5</sup> (on the details see further Sidor 2011). The petition to organize the referendum had to be signed by at least 10% of those entitled to vote and the result of the voting was valid if at least 30% of citizens entitled to vote took part in it.

The first term of local government (1990-1994) was dominated by the referenda concerning the dismissal of the municipal council. The most frequent reason to start the procedure of the recall was the conflict between community and local authorities; the arguments of authorities' arrogance, hypocrisy and ineffectiveness in problem solving were arisen by citizens (Słobodzian 2011:254). Nevertheless, among all 48 initiatives that were taken only 3 appeared to be successful. The average turnout for all referenda was 14.4%.

That first, four years of practice indicated that the institution of referendum needed some clarification and amendments. On the foundation of the Act of 29 September 1995 on Local Self-Government and the amended Act of 11 October on Municipal Referendum the regulation was introduced to the effect that a referendum on the dismissal of the council before the expiry of its term of office could only be held at the request of the inhabitants. The council was thus deprived of this right. What is more, the possibility was limited to calling a referendum at any time during the council's term of office. Therefore, a vote on the dismissal of the municipal council cannot be held until twelve months after the day of the elections or after the day of the previous referendum on the council dismissal (Sidor 2011; Słobodzian 2011:254-255).

During the second term of local government (1994-1998) 104 referenda were conducted. Nevertheless, again only 9 polls were valid.

In 1998 the second step of decentralization reform took place what resulted in creation of counties and regions. In consequence the new law concerning the referenda was passed. On the basis of the Act of 15 September 2000 on Local Referenda the possibility of using the institution was broadened on county and regional levels (for the details see

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5 Dz. U. [Journal of Laws] 1991, No. 110, item 437, the Act of Municipal Referendum was passed on 1st October 1991.

Słobodzian 2011:255). However, among 196 referenda that were held between 1998 and 2002 only 25 were valid. Only one referendum was organized at the county tier, none at the regional level (Sidor 2011).

During the fourth term (2002-2006) 89 referenda were organized at municipal level and 3 at county level. However, again only 11 of all 92 polls were valid. The most of the initiatives (69) concerned the recall of municipal bodies (Zakrzewski 2011: 83-103). Moreover, in 2005 the law was amended again and the regulation was introduced that in the event of referenda concerning dismissing a body of a local government unit elected in direct elections, a poll is valid if not less than 3/5 of the number of persons participating in the elections of the body being dismissed take part in it. A referendum on self-taxation of municipal residents for the public purposes is valid when self-taxation is supported by at least 2/3 of valid votes. In the result of these alterations the referenda concerning the recall of local bodies started to be more efficient. During the last term (2006-2010) 81 referenda were organized and among them 14 polls were valid.

Available in Poland since the 1990s local referenda have undergone significant legal, political and social transformation (Sidor 2011). However, an unambiguous assessment of its practice constitutes a challenge. On the one hand, some authors indicate that Polish society is more and more mature and that the number of valid polls is growing (Sidor 2011; Piasecki 2011). On the other hand, during five terms of local government (1990-2010) referenda held to recall organs of local government dominated as are accounted for about 85% of all initiatives. The referenda regarding other important for local communities' issues are quite rarely organized and have very low turnout. The famous example was the ballot organized on the controversial Augustów ringroad. Though the referendum campaign was huge, with visible involvement of central authorities, political and environmental activists, local government and finally media, in the end the poll was invalid due to low turnout. Moreover, it is estimated that since 1990 only around 30 polls were organized on self-taxation.

In addition, the practice applied so far indicates that in a lot of cases referenda are not the way to solve issues crucial for local communities, but an institution by means of which local political elites compete with each other. On this basis in terms of effectiveness and efficiency, this tool of democracy should be assessed rather negatively.

### *CITIZENS' INITIATIVES & CONSULTATIONS*

Apart from referenda, local communities can also make use of the citizens' initiatives and consultations (Piasecki 2011:135). However, this form of participatory democracy, successfully functioning in Western Europe, is clearly underestimated in Poland both by local authorities and local communities. This refers equally to normative basis and the practice of applying them in public life.

The local government legislation does not provide for citizens' initiatives, however some

cities decided to introduce this possibility for inhabitants by by-law (for instance in Wrocław a petition signed by three thousands people is required). Initiative proposals submitted in this way usually refer to local or social issues. Nevertheless, inhabitants seldom use this right and their initiatives proposals do not always receive the council's approval (Piasecki 2011:135).

The consultations were added to Act on Local Self-Government in the amendment of 1996. Despite the fact the institution has constitutional foundations, the procedure only in some cases is mandatory and therefore is not used permanently. Some local authorities decided to regulate this issue by introducing a relevant provision in their by-laws. Consultations very rarely took the form of a popular vote, though again it some cases local authorities that e.g. were considering a change of the name of their town conducted public consultations before taking any action (Piasecki2011:135; Kijowski 2010:15; Olejniczak-Szawłowska 1997).

### *OTHER FORMS OF CIVIC INVOLVEMENT*

Finally, to have a full picture of the participation at local level in Poland other possibilities of civic involvement should be mentioned. First, since the 1990s Poles have had a possibility to involve themselves in the work of NGOs (foundations, associations and other organisations that operate at local level); (for further details see Kijowski 2010:11-21).

Second, especially during last years some initiatives concerning the participative democracy were taken. On the basis of the Act of 20 February 2010 on Village Head Fund (fundusz sołecki) the more financial freedom was given to the municipalities' auxiliary units (villages)<sup>6</sup>; (for auxiliary units in rural municipalities see further Abramowicz 2011:17-37). The village head fund is a sum of money separated from the local budget and ensured for activities that improve inhabitants' life conditions. The exact destination of the money is defined by inhabitants themselves. Decision about spending of the money takes place in auxiliary units, that are usually formed by one or two villages. Inhabitants of a unit, gathered on public meeting, called residents'/village assembly (zebranie mieszkańców/zebranie wiejskie). They present proposals, discuss and vote what to spend the money on. The assembly is the key element of the fund and is an element of direct democracy. Decisions of local inhabitants taken during village assembly are 100% binding. The role of the local authorities is limited to inclusion of people proposals into the municipality's budget<sup>7</sup>.

Moreover, some municipalities inspired by the experiences of Brazil and some Western European democracies e.g. Spain, Germany, Portugal, France, Great Britain, Italy, decided also to introduce participatory budgeting. The solution was already implemented

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6 See Dz. U. [Journal of Laws] 2009, No. 52 , item 420 , the Act of 20 February 2010 on Village Head Fund.

7 For more details see: [http://funduszesoleckie.pl/41,456,how\\_it\\_works.html](http://funduszesoleckie.pl/41,456,how_it_works.html) (access 09/04/11)

in auxiliary units of Sopot, Łódź and Lublin. Some cities went further and started to experiment with deliberative democracy (e.g. citizens' juries in Poznań).

However, it is important to assess the 'efficiency' of the described methods. Regarding to civic involvement as Social Diagnosis indicates, after twenty years of independent governance the idea of acting together is rather diminishing. According to a research carried out in 2011, only 14.8% of respondents were members of 'some organisations, associations, parties, committees, councils, religious groups, unions or circles' (Sulek 2011:278). The reasons of this situation are varied. As Jerzy Regulski indicates twenty five years is a long period in peoples' life, though it is rather a short time as regards system's transformation (Regulski 2006:15)<sup>8</sup>. In addition, despite the relatively successful decentralization reform that was carried out, it seems that the part of the energy Polish society had at the beginning of the 1990s, was wasted (Kulesza 2007:5). As the surveys indicate after more than two decades, Poland still has not fulfilled the conditions for civil society. Instead of growing the percentage of people who think they cannot trust others is diminishing. European Social Survey (ESS) from 2008 revealed that Poland had one of the last places in Europe as regards the feeling of general reliance to other people and institutions (Czapiński 2011:285). Therefore, the social capital is still very weak.

Concerning the 'new tools' of participation democracy that have been already introduced also some issues are worth mentioning. The first examples of village head fund and participatory budgeting indicate that society has rather little knowledge about new solutions and it is not very eager to be involved (Leszczyński 2011). In Łódź, in first meeting concerning the funds divisions only 20 people participated (*ibid.*). Moreover, the practice shows that not only inhabitants are reluctant to reforms, but also part of local authorities. A number of councillors and mayors are afraid that the new solutions are going to reduce their power and position and therefore are not eager to support it.

## CONCLUSIONS

The decentralization process that was started in Poland in 1990 revolutionised local government's system. Michał Kulesza indicates that:

*'the reform was implemented not because of a miracle but because an opportunity to do it appeared and the politicians and reformers seized it. Indeed the reformers were lucky. For a brief moment the curtain went up and the reformers found themselves in the right place at the right moment to play the reform on stage. Shortly afterwards the political curtain went down and today no reform of the system of government on such a scale would be possible.'* (Kulesza 2002:205).

The decentralization opened the possibilities to built new mechanisms of participation at both national and local levels that were supposed to result in formation of civil society.

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8 The author refers to the democratic changes that were started in the 1980s.

However, it seems that after more than twenty years of transformation not all changes were successfully implemented.

Firstly, at present Polish society has different and varied possibilities to participate, based on representative, participative and deliberative solutions. However, since 1990 the turnout in local elections never exceed 50% and the most of the referenda were invalid due to low polls. Therefore it is difficult to expect that further participatory reforms regarding the popular concept of local governance will be successful if basic institutions of social participation fail. Consequently, Polish government should rather consider why the society is disappointed with representative democracy than applying further methods of civic involvement by force.

Secondly, concerning the public apathy it seems it is not simply a result of citizens' disapproval towards local authorities but rather a lack of the social capital and the belief that an individual vote does not make a difference. What is more, the frequent changes in electoral law and voting procedures, as well as the partisanship of local authorities do not help to attract society to polling stations.

Thirdly, in Poland the lack of the debate on the quality of civic participation is visible. Still many identify 'more participation with more democracy'. There is also no discussion over the tensions between representative and deliberative democracy that may occur. However, first clashes have been already seen. Till recently under the auspices of the President's Chancellery the government act concerning the public participation was being prepared. The proposed solutions included: an abolition of approval quorum required for the referendum to be valid, introduction of monocratic and directly elected executive at county level, more formalised procedure of local consultations and introduction of public hearing. The inhabitants were also supposed to have formal right to submit the resolutions (obywatelska inicjatywa uchwałodawcza). Nevertheless, the proposed changes caused strong objections of local authorities and the whole idea was rejected. At the same time it is not however clear if the society is also interested in using these new 'tools' of public involvement.

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# EUROPEAN ACTORS AND SUBNATIONAL DEMOCRACIES: STIMULI FOR REFORM IN ROMANIA

Diana – Camelia Iancu<sup>1</sup>

## INTRODUCTION

For the 19-th century, saying *fin de siècle* was, to some extent, equivalent to thinking of cultural decadence, social alienation and (or) the process of elites dissolution. One hundred years later though, the same concept connected itself to one of the most debated, still not yet entirely clear, definition of globalization and its obvious (to some) consequences: "There will be no *there* anymore. We will all be *here*" (Waters, 1997:126). Difference in unity, liberal pan-democratization, global political culture - these are the basis of a world that, as early as 1900, was seen (as many are still seeing it) as a pure utopia - a society recognizing similar values and principles, a world where cooperation and humanism are omnipresent. Such a world tried the new Europe to be or, in Prodi's words, "such world *needs* Europe to be" (Prodi, 2001:25).

For the purpose of this paper yet, not globalization *per se*, is going to be considered as the driving force of change, but rather the Europeanization process. Contrary to what the historians contributing to the *Times Atlas of World History* (Burraclough, 1978 in Waters, 1997:65) have argued for - mainly that "by the middle of the 20-th century the European dominance had ended, and that the world had entered the age of global civilization", I will defend those that argue in favor of the growing influence supra-state organizations (e.g. European Union and Council of Europe)<sup>2</sup> have on sovereign entities, *lato sensu*, and on Central and Eastern Europe (CEE) subnational democracies, *stricto sensu*. As such, Europeanization refers to strategic documents of the European Union and Council of Europe, focused on subnational democracies European Union and their impact on CEE democratic legal systems. In this regard, the first assumption to be made is that the membership in the Council of Europe and the accession to the European Union facilitated the transformation of the CEE's subnational democracies so as to accommodate European principles of local self-government<sup>3</sup>.

My argument goes that at least as far as the subnational democracies were concerned, the domestic impact of the European regulations followed the rhetorical mode of the logic of

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2 See for further references: Bardi, Rhodes and Senior Nello, 2002:227 et seq.

3 Frank Schimmelfennig, for instance, in Linden (2002:5 et seq.), argues on the same issue, taking into account the possibility that the non-member status of the Central and East European countries may inhibit the domestic impact of European norms.

consequentiality<sup>4</sup>: the CEE democracies "talked the talk" of the European institutions and created their required formal institutions, while experiencing a rather difficult time with letting aside the old ways of behaving and assume the real costs of adaptation (Ungureanu and Iancu, 2010; Ungureanu, 2012). In validating this hypothesis, I channel my analysis on Romania and how did it manage to accommodate the European Charter of Local Self-Government (a strategic document of the Council of Europe) and the principles of the European Administrative Space (formulated by the European Commission) so to prepare its subnational authorities for the EU accession. The time frame of the analysis will be 1991-2001, a decade rich in administrative transformations and European stimuli.

## EUROPEAN STIMULI AND SUBNATIONAL DEMOCRACIES

It has been pointed out previously that the main actors that I will focus on during this analysis are European Union and the Council of Europe, as the international organizations mostly "responsible" for the Europeanization trend in a non EU-member state Romania.

### *THE EU ACQUIS FOR SUBNATIONAL DEMOCRACIES*

As it is widely known, the enlargement strategy adopted by the European Union since its creation (Treaty of Rome, 1957) has been an exclusive one - that is, EU communicated its constitutive norms to outsider entities, stating the conditions to be met by them, before being entitled to join<sup>5</sup>.

Set out at the Copenhagen European Council (1993), the "Copenhagen criteria" for instance, are a very good example of what the European Union expected from its CEE candidates: in short, they were supposed to prove to be viable democracies, supported by market economies that hold "the capacity to cope with competitive pressure and market forces". In addition, they should have negotiated and finally harmonized their own domestic legislation with the whole body of EU rules, principles and judicial decisions (the "*acquis*"). Already hard enough to deal with, all these three conditions seemed to be left to interpretation, for there was more than one opinion that argued that EU accession

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4 According to the logic of consequentiality, actors follow norms out of extrinsic motivation. After a rigorous analysis of costs and benefits, they will choose the course of action that will maximize their individual utility. A totally different situation occurs within the logic of appropriateness, where actors follow norms for intrinsic reasons. They will as such choose to behave in a certain way, because it is deemed to do so. See for details, Schimmelfennig in op.cit. pp. 12-15.

5 It is once again a classification made by the international relations scholars; they oppose to this exclusive strategy, that is said to be typical for EU and NATO, the inclusive one, usually common for OSCE (Organization for Security and Cooperation in Europe). For further comments, see Schimmelfennig in op.cit. pp. 8 et seq.

provisions were ambiguous and lacked consistency<sup>6</sup>.

To solely discuss the "obligation of membership" issue for instance, it goes without saying that all the approximately 80.000 pages of European legal texts that previously represented the *acquis* were no longer sufficient to include the new directives, declarations and jurisprudence the growing Union was developing. Hence, the entire "alignment to the same (EU) standards" process became rather expensive (in terms of time and money spending) to both the EU - the regulatory state to be<sup>7</sup>, its institutions seem mature enough to properly prepare for and cope with future inconveniences "enlargement made". To support these statements, one may mention the broader definition of the *acquis* presently defined as: "all the real and potential rights and obligations of the EU system and its institutional framework" (Gialdino, 1995).

What about the issue of how the European administration should look like? What principles it should defend and on what grounds it should base itself<sup>8</sup>? As stated in a SIGMA report: "The Treaty of Rome contains no provision of general application to public administration. No General Directive has been adopted [...]. In other words [...] there are no Community rules regarding public management. [Hence] Public administration is the responsibility of national governments" (SIGMA, 1998: 120).

It was then, the "European administrative space" came into use. EU was not entitled to set conditions for future members in terms of public administration, but it did provide certain alternative models for serving its "unity through diversity" mission. And here, "a common administrative space... a set of administrative principles, rules and regulations that are uniformly enforced in a given territory covered by a national constitution" (SIGMA, 1999:15) became necessary. Although never produced as such, several principles were then proclaimed: 1. reliability and predictability (legal certainty); 2. openness and transparency; 3. accountability; and 4. efficiency and effectiveness.

Of course, much remained to be done in terms of modeling the significant quality differences that coexisted among European states; yet a starting point in creating common administrative regulations for all Europeans, did exist. I am not referring here once again to the common values and the "what to be done" questions, but to the only (at the very least) codification of European principles with regard to democratic power-sharing formula between central authorities and decentralized local or regional ones (Levrat,

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6 See Grabbe, 1999; Gialdino, 1995 and Smith, 1997.

7 Héritier (1996) quoted by Grabber (2002:253) suggests that due to the regulatory models EU tries to impose, a basic assumption for further analysis would be that the Union is heading towards a regulatory state: "The Union is an aid donor imposing conditions on relations with third countries that are intended to benefit by supporting post communist transformation of economies and societies. Yet, on the other hand, it is guiding these countries towards membership, which requires creating incentives and judging progress in taking on specific EU models".

8 Article 41 of the EU Charter of Fundamental Rights addresses this very issue, stating in its four paragraphs what may be regarded as truly European values of good administration. In the same note, the Resolution of the European Parliament approving the Code of Good Administrative Behavior (September 2001) offers an interesting example of what is or should be European in the national public administration practices.

1996:115) - The European Charter of Local Self-government.

### *COUNCIL OF EUROPE AND SUBNATIONAL DEMOCRACIES*

A seventeen years work result<sup>9</sup>, the Charter of Local Self-Government was the Council of Europe's first tool for creating true common European standards with regard to subnational democracies. To pinpoint to the Romanian case, ratifying the European Charter was considered to be the only possible solution for reforming the subnational level of government as to bring it as close as possible to the EU accession standards. Actually, from the beginning of its preparation to join the EU for instance, Romania acknowledged the need for "a structural and functional reform of the public administration" in order to increase the flexibility, the efficiency and the coherence of the administrative activities, to diminish the bureaucracy, to eliminate the malfunctions and superposition of attributions and to increase the degree of compatibility with the administrations of the EU members"<sup>10</sup>. And, at least in regard to the latter "need", the European Charter of the Council of Europe fulfilled completely its tasks, as all the EU Members had ratified it.

It becomes then rather obvious why a country such Romania, on the way to align its norms to the European values of freedom and local democracy would choose to promote the need of reforming and consolidating its public administration by ratifying the European Charter of Local Self-government. As it will be revealed later on, prior to 1997 (the date of Romania's ratification of the Charter), the domestic subnational authorities had yet a long way ahead till achieving the status of local active governments. One year after the ratification, a new Local Public Finance Law was issued (that enshrined the fiscal autonomy principle) and three years later a new Local Government Act was adopted.

### **EUROPEAN PRINCIPLES FOR LOCAL DEMOCRACIES**

From the late sixties till the early eighties, most European countries rearranged the distribution of competencies between various levels of government, increasing the competencies reserved to the lower levels of government and sometimes introducing a new intermediate level of government. Roughly speaking, the decentralization wave of the seventies (Balducci, 1996) moved towards the periphery more and more competencies (mainly in the service area) and tried to increase the financial autonomy of local governments by reducing, for instance, the central governments' control powers

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9 As early as 1968, Conference of Local Authorities asked the Committee of Ministers to adopt a "Declaration of Principles on local autonomy" (Resolution 64/1968).

10 Statement of the Romanian Ministry of Foreign Affairs (1997); source: [www.mie.ro/integrare.html](http://www.mie.ro/integrare.html) (last access on the Ministry archives: 06.06.2012).

over the periphery. The former local administrations became as such local governments and the guardian states changed their ways of handling the *res publica*, accepting the active partnership with the civil society (Manor, 1999).

In this context, the local autonomy issue cannot be seen separately from the decentralization concept, since the greater the decentralization is, the more autonomous the local communities are (Millon - Delsol, 1992; Thoenig, 1993; Delcamp, 1993; Lane, 2000; Lijphart, 2000; Lazaroiu, Payne and Denoeux, 2001; Ionita and Spofford, 2002; Oliver, 2002; Würtenberger, 2002; Ortega, Nieto and Martin, 2002). Still, what can one understand from the - perhaps not so clear - concept of decentralization?

According to Bahl (1998) or Azfar et al. (2000), decentralization comprises many different aspects, including allowing local government representatives to be selected through local elections (*devolution*), transferring authority and responsibility for service delivery to local governments (*deconcentration*) and shifting authority to raise adequate revenues and to make expenditure decisions to the local level (*fiscal federalism*). Moreover, the literature has identified three main forms of decentralization based upon the location of decision making authority: deconcentration occurs when lower levels of government (e.g. regional or municipal) execute functions on behalf of the central government without having decision making authority. The lower levels of government essentially function as “branch offices” of the central government. Delegation is the process in which the central government transfers decision making over certain functions to relatively autonomous local governments, which have limited autonomy and are ultimately responsible to the central government. Devolution involves the complete transfer of decision making over finance and management of public services to quasi-autonomous local government units. Devolution usually transfers responsibilities for services to municipalities where residents elect their own mayors and council members, revenues are raised locally and local governments have independent authority to make investments.

For Romania, decentralization has involved aspects of each of the above-mentioned types of institutional change. The main target of my research is thus to show the changes brought to the Romanian local government system by the Europeanization process, focusing on fiscal decentralization, as an important way for achieving complete and coherent local autonomy.

Further more, I will assume that local autonomy is closely connected to the subsidiarity principle, as regulated by Article 4.3 of the European Charter of Local Self-government, and therefore, I will argue that application of the right of local authorities to regulate and manage a substantial share of public affairs under their own responsibility and in the interests of the local population is conditioned by the existing level of administrative and fiscal decentralization.

Hence, the assumption to be made is that the greater the administrative decentralization, the more responsibilities local governments have. It goes then that the greater the fiscal

decentralization level is, the powerful (in terms of functions and resources) local governments are, and therefore, the more promoted the local autonomy (and subsidiarity, for that matter) is. In addition, if the local authorities are presumed as autonomous, then the existing supervisory mechanisms are dialogue based mainly<sup>11</sup>.

In order to test the above hypothesis, and eventually assess how far did the Europeanization of administrative system went in Romania before joining the EU, three and three moments analyzed:

- T<sub>1</sub> - 1996 (The Romanian Local Government Act<sup>12</sup> - Law (L) 69/1991<sup>13</sup> has been substantially modified).
- T<sub>2</sub> - 1998 (The European Charter on Local self-government has been ratified by the Romanian Parliament and a new Local Public Finance Law - L 189/1998<sup>14</sup> has been issued).
- T<sub>3</sub> - 2003 (the moment of the analysis, 2 years after the new - modern and "more" European - Romanian Local Government Act - L 215/2001<sup>15</sup> has been adopted).

As it will be pointed out later on, 2001 was the year that witnessed the "reinvention" of the Romanian subnational democracy, since, at least on paper, subsidiarity was enshrined as a legal principle, and fiscal decentralization was further promoted. Considering the same issue, it may be assumed that, both L 189/1998 and L 215/2001 are direct consequences of Romania's ratification of the European Charter of Local Self-government<sup>16</sup> and of its need for Europeanization. Still, both of these assumptions would be mere speculations, so, they will not be used during my analysis.

In regard with the indicators to be used for measuring the decentralization process in the Romanian administrative system and the occurrence of any subsidiarity - related practices, it should be noted that I will base my argument on a comparative analysis of the own local revenues *versus* central - transferred local revenues ratio (Lijphart, 2000) and national *versus* sub national responsibilities of administrative authorities.

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11 Meaning, their final task is not to enforce the central government's will, but rather to encourage local initiatives.

12 Orig. (Ro): Legea administratiei locale - a mot-á-mot translation would use instead of "government", the term "administration". I have already discussed my opinion about the difference that I see between the two mentioned words. For the sake of coherence, though, I will translate the Romanian Law's title, as suggested in the body text of this paper.

13 First published in the Romanian Official Gazette, No. 238/ 28 November 1991 and republished on the grounds of Article 111, Law 24/1996 (The Romanian Official Gazette, No. 76/ 13 April 1996).

14 The Romanian Official Gazette, No. 404 (22 October 1998).

15 The Romanian Official Gazette, No. 204 (23 April 2001).

16 This was achieved by L199 /1997, (The Romanian Official Gazette, No. 331/ 26 November 1997). The stated comment may be valid if one takes into consideration Article 12 (of the Charter): "Each Party undertakes to consider itself bound by at least twenty paragraphs of Part 1 of the Charter, at least ten of which shall be selected from among the following paragraphs: Article 2, Article 3.1 and 3.2, Article 4.1, 4.2 and 4.4, Article 5, Article 7.1, Article 8.2, Article 9.1, 9.2 and 9.3, Article 10.1, Article 11".



Bearing all this in mind, my final argument will be that in Romania, at the time of EU negotiation began, in spite the formally enacted Charter principles, fiscal decentralization was still little promoted, and as such, local autonomy was rather limited. Although the Romanian local governments did have new functions in terms of financial and legal matters, they still received lots of subsidies and transfers from the central authorities in areas such as education, health, public roads and sanitation.

As a direct consequence of this, the autonomy enacted in the new Romanian Local Government Act was still formal and subsidiarity was not yet visible.

## **“BEFORE AND AFTER”: A CASE OF EUROPEANIZATION IN ROMANIA<sup>17</sup>**

### *LOCAL ALLOCATION OF RESOURCES AND RESPONSIBILITIES IN 1996*

Talking of fiscal decentralization in the 1996 Romanian normative framework would be quite inopportune. A further look at the budget responsibilities of the local authorities is, nonetheless, necessary.

To quote article 20.e of L 69/1991, the local councils were to approve: 1. the local budget, its formation, administration and execution; 2. credit transfers and the utilization mode of the budgetary reserve; 3. loans and the closing account of the financial year<sup>18</sup>. They were also entitled to “establish local rates and taxes as well as special taxes for a limited period of time”<sup>19</sup>.

Roughly speaking, it would seem that the previous judgment – the one about being rather impossible to encounter fiscal decentralization in T<sub>1</sub> Romania – is not correct; after all, local authorities could levy taxes, elaborate the budget or make loans, hence, they were quite autonomous in regard with their financial responsibilities. However, using the own local revenues/central - transferred local revenues ratio (Lijphart, 2000), it becomes obvious why it isn’t always advisable to exclusively “read” the norms before drawing any conclusions (table 1).

In short, table 1 shows that the level of state budget transfers in local budgets for the years of reference (mainly 1991-1997), is considerably high. That means that subnational democracies had little spending powers and relied on intergovernmental transfers (representing more than 75 percent of subnational revenues). Additionally, according to

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17 An important source of inspiration for this part of analysis was the article by C. Romanik and F. Conway, “Grant Transfers and Financial Supervision in Romania: a Focus on Major Reforms Introduced by the Law on Local Public Finance”, available online at:

Francis Conway <http://unpan1.un.org/intradoc/groups/public/documents/nispacee/unpan004617.pdf> (last access: 06.06.2012).

18 In Romanian legislation, the financial year starts on the 1-st of January, and ends on the 31-st of December.

19 Article 20.f, L 69/1991

Law 24/1994<sup>20</sup>, subnational authorities could collect taxes like: corporation tax<sup>21</sup>, tax on private agricultural land, income tax from tradesmen, family companies etc., yet central authorities were the only ones entitled to set the ceilings for the majority of the latter.

Table 1<sup>22</sup>. Local Government revenue/expenditure structure

| Million current lei                    | 1991   | 1992   | 1993   | 1994    | 1995    | 1996    | 1997     |
|--|--------|--------|--------|---------|---------|---------|----------|
| <i>Total revenues</i>                  | 58627  | 199667 | 712549 | 1767150 | 3336458 | 4998504 | 10468498 |
| Own revenues                           | 17216  | 31640  | 152538 | 1430655 | 2402911 | 3821115 | 8434792  |
| General transfers                      | 0      | 0      | 231770 | 668109  | 1203024 | 1972609 | 4644559  |
| Dedicated transfers                    | 41411  | 168000 | 328240 | 762546  | 1199887 | 1848506 | 3790234  |
| Loans                                  | 0      | 28     | 0      | 1496    | 10088   | 46894   | 49397    |
| <b>Ratios by major sources</b>         |        |        |        |         |         |         |          |
| Own revenues                           | 29.40% | 15.80% | 21.40% | 19.00%  | 27.70%  | 22.60%  | 19.00%   |
| Revenues from the state budget (total) | 70.60% | 84.10% | 78.60% | 81.00%  | 72.00%  | 76.40%  | 80.60%   |
| Loans                                  | 0.00%  | 0.00%  | 0.00%  | 0.10%   | 0.30%   | 0.90%   | 0.50%    |
| <b>Other ratios (percent)</b>          |        |        |        |         |         |         |          |
| Local taxes                            | 27.40% | 14.40% | 13.00% | 13.50%  | 22.00%  | 17.50%  | 14.50%   |
| Dedicated transfers                    | 70.60% | 84.10% | 46.10% | 43.20%  | 36.00%  | 37.00%  | 36.20%   |

Another indicator for the low degree of fiscal decentralization was the algorithm for the allocation of responsibilities between central government and the periphery. Prior to 1996, the Romanian central government was entirely responsible for education and health. Instead, the main responsibilities of local authorities were those concerning water supply, local transportation and district heating, as well as some other various minor activities in social assistance, municipal service, culture and arts, public investment and maintenance.

20 L 27/1994 on local taxation was first published in The Romanian Official Gazette No. 127/24 May 1994; it was then several times amended, and finally republished in The Romanian Official Gazette No. 375/24 December 1997.

21 This tax was to be raised from independent public corporations subordinate to communes, towns or counties.

22 Sources: official web site of World Bank ([www.worldbank.org](http://www.worldbank.org)), IMF ([www.fmi.ro](http://www.fmi.ro)) and Romanian Ministry of Finance ([www.mfinante.ro](http://www.mfinante.ro))

Table 2<sup>23</sup>: Expenditure responsibilities between the central and sub national tiers of government (1993-1994)

|                           |                | <b>Shared responsibilities</b> | <b>Sub national governments</b> | <b>Central governments</b> |
|---------------------------|----------------|--------------------------------|---------------------------------|----------------------------|
| <b>Education</b>          | <b>Primary</b> | -                              | -                               | √                          |
|                           | <b>Higher</b>  | -                              | -                               | √                          |
| <b>Housing</b>            |                | -                              | √                               | -                          |
| <b>Water and sewerage</b> |                | -                              | √                               | -                          |
| <b>Health</b>             |                | √                              | -                               | -                          |
| <b>Social services</b>    |                | √                              | -                               | -                          |
| <b>Roads</b>              |                | √                              | -                               | -                          |
| <b>Police</b>             |                | -                              | -                               | √                          |
| <b>Public utilities</b>   |                | -                              | √                               | -                          |
| <b>Public amenities</b>   |                | -                              | √                               | -                          |
| <b>Public enterprises</b> |                | √                              | -                               | -                          |

In terms of distribution of local government expenditures, Farcas (1994) gives the following figures (relevant for the same period of time: 1993-1994) that are in direct correlation with the data provided by the table above: municipal services and dwellings - 58.8%; transport and communication - 26.3%; administration bodies - 8.8%; culture - 4.2%; social assistance - 0.8% and others - 1.1%.

In 1996 though, local governments were priory mandated to act within the following areas: local economic development, local urban development, land administration and development, cemetery administration, protection of environment, housing, water supply, sewerage, local public roads and local transportation. At the county level, services to be provided were: maintenance of the county roads, public transport between localities within the county and administration of education and health institutions of county interest. In 1996 and 1997, only, the total expenditures of local governments looked as in the table below:

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23 Adapted from Bird, Ebel and Wallich (1995:20).

Table 3<sup>24</sup>: Total expenditures at local and regional level

| <b>Public services</b>             | <b>1996 (%)</b> | <b>1997 (%)</b> |
|------------------------------------|-----------------|-----------------|
| <b>Local administration</b>        | 6.9             | 7.9             |
| <b>Education</b>                   | 11.9            | 10.0            |
| <b>Health</b>                      | 12.4            | 12.8            |
| <b>Culture and sports</b>          | 3.2             | 4.7             |
| <b>Social assistance</b>           | 6.3             | 4.6             |
| <b>Housing</b>                     | 37.6            | 39.0            |
| <b>Transport and communication</b> | 19.9            | 19.6            |
| <b>Reserves</b>                    | -               | -               |
| <b>Other activities</b>            | 1.5             | 1.2             |
| <b>Total expenditures</b>          | 100             | 100             |

The figures presented above, have yet little relevance for the level of local autonomy, giving the fact that all the "local" money spent for providing the stated public services was actually more central than local. In fact, the so far analysis on local allocation of resources and responsibilities between different tiers of government proves the very essence of the principle enshrined in Article 1.2 of L 69/1991 (republished): "Local autonomy shall be [only] administrative".

#### *LOCAL ALLOCATION OF RESOURCES AND RESPONSIBILITIES IN 1998*

In October 1998, The Romanian Parliament adopted a new Law on Local Public Finance (L 189/1998) which brought a significant restructuring of the administrative system, especially in regard to fiscal decentralization. Thus, the principle of financial responsibility of local authorities became a legal matter and the local authorities were endowed with new responsibilities in areas such as the establishment of expenditure priorities; the approval of investments; long-term budgeting; access to credit from the internal or external capital markets, and assessing and collecting revenues from local taxes and fees. Also, the local budgets were "enlarged" with different shared amounts from state revenues, transfers for co-funding and special funds for special services and activities. In brief, what L 189/1998 changed may be clearly viewed in the following table (table 4).

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24 Adapted from Human Development Sector Unit (2002).

Table 4<sup>25</sup> - Indicators for local autonomy and the new responsibilities of local authorities (study case, L 189/1998)

| Indicators (local autonomy)  | Responsibilities (local authorities)  |
|--|---|
| 9. new sources of income (local taxes and fees, wage tax, transfers from the state budget)<br>(Article 8.1 and 8.2, L 189/1998)  | → to collect local taxes and fees<br>→to settle local taxes<br>→ to finance previous state subsidized activities, including the social assistance and services of local interest  |
| 10. the right to pursue borrowing, without previous notice of the Government<br>(Article 48.6, L 189/1998)   | → on medium and long term, for local communities to share the burden of the borrowed amounts<br>→ the borrowing process requires the votes of the county assembly<br>→ to reimburse of the borrowed amounts from own resources  |
| 11. the right to sell or lease public goods belonging to the local governments' private domain<br>(Article 9, L 189/1998)  | →to comprehensive evaluate of the private domain and its public goods   |
| 12. the right to decide on local development issues<br>(Article 16, L 189/1998)  | → to elaborate the long term local development strategy<br>→ to prioritize the public investments that stimulate the increase of local economic development or of the revenues to be made "own revenues"<br>→ to take the initiative in discussing the local development strategy |
| 13. the right to lease or delegate local public services to private agents<br>(Article 9, L 189/1998)  | → to monitor and control the outcomes of the new public services provider   |
| 14. the right to make necessary changes in the local expenditures scheme (with the exception of the amounts to be used as "personnel funds")<br>(Article 44, L 189/1998)   | → to efficiently manage the local expenditures<br>→ to identify the local needs in spending public money  |
| 15. the right to extend the number of public services that fall under the budgeting of local authorities (as for instance, the child protection services or the cultural and religious activities)<br>(Article 18, L 189/1998) | → to balance the revenues and expenditures ratio<br>→ to manage the local resources, according to the principles of public finance theory   |

“Reading” the new provisions, it becomes rather obvious that this time, on paper, fiscal decentralization does occur. Still, a rather interesting question to ask at this particular time, would be: what was the context in which this radical change shaped itself? With high relevance for this paper, there is just one possible answer to give, and that is the one that draws the attention to the Romanian Declaration of Ratification of the European

25 A similar analysis may be encountered in CSPD (1998).

Charter of Local Self-government. It appears then that the new and improved financial responsibilities became essential to a fair, just and “local democracy”- type government, the moment Romania joined the *European standards* in local public administration. However, the formal changes that the Charter brought to the Romanian administrative system had major consequences on the local own revenues/central - transferred local revenues ratio. In this regard, tables 5 and 6 give more details:

Table 5. Local Government revenue/expenditure structure  
(sources: World Bank, MOF and IMF)

| Million current lei                    | 1996    | 1997     | 1998     | 1999     | 2000                 |
|--|---------|----------|----------|----------|----------------------|
| Total revenues                         | 4998504 | 10468498 | 13454174 | 22243670 | 33393515             |
| Own revenues                           | 3821115 | 8434792  | 3328885  | 15512215 | 24063098             |
| General transfers                      | 1972609 | 4644559  | 4997959  | 2522821  | 3323181              |
| Dedicated transfers                    | 1848506 | 3790234  | 5054462  | 3845955  | 6007236              |
| Loans                                  | 46894   | 49397    | 72868    | 362649   | <i>Not available</i> |
| <b>Ratios by major sources</b>         |         |          |          |          |                      |
| Own revenues                           | 22.60%  | 19.00%   | 24.70%   | 69.70%   | 72.10%               |
| Revenues from the state budget (total) | 76.40%  | 80.60%   | 74.70%   | 28.60%   | 27.90%               |
| Loans                                  | 0.90%   | 0.50%    | 0.50%    | 1.60%    | <i>Not available</i> |
| <b>Other ratios (percent)</b>          |         |          |          |          |                      |
| Local taxes                            | 17.50%  | 14.50%   | 18.40%   | 26.30%   | 25.80%               |
| Dedicated transfers                    | 37.00%  | 36.20%   | 37.60%   | 17.30%   | 18.00%               |

Table 6: Macroeconomic fiscal indicators

| Macroeconomic fiscal indicators (source: IMF) |        |        |        |        |        |
|---|--------|--------|--------|--------|--------|
|   | 1996   | 1997   | 1998   | 1999   | 2000   |
| <b>Billion lei</b>                            |        |        |        |        |        |
| GDP   | 108391 | 252926 | 368261 | 521736 | 796534 |
| Total public expenditures                     | 36810  | 85639  | 131123 | 193567 | 283566 |
| Local public expenditures                     | 4955   | 10370  | 13382  | 21599  | 33217  |
| Local public revenues                         | 5000   | 10469  | 13454  | 22246  | 33394  |
| Transfers                                     | 3821   | 8436   | 10052  | 4308   | 4308   |
| Own local revenues                            | 1130   | 1984   | 3328   | 17935  | 17935  |
| <b>% of GDP</b>                               |        |        |        |        |        |
| Total public expenditures                     | 34     | 33.9   | 35.6   | 37.1   | 35.6   |
| Local public expenditures                     | 4.6    | 4.1    | 3.6    | 4.1    | 4.2    |
| Local public revenues                         | 4.6    | 4.1    | 3.7    | 4.3    | 4.2    |
| <i>Transfers to local authorities</i>         | 3.5    | 3.3    | 2.7    | 0.8    | 0.5    |
| <i>Own local revenues</i>                     | 1      | 0.8    | 0.9    | 3.4    | 2.3    |
| <b>% of Public Expenditures</b>               |        |        |        |        |        |
| Local public expenditures                     | 13.5   | 12.1   | 10.2   | 11.2   | 11.7   |
| Local public revenues                         | 13.6   | 12.2   | 10.3   | 11.5   | 11.8   |
| <i>Transfers to local authorities</i>         | 10.4   | 9.9    | 7.7    | 2.2    | 1.5    |
| <i>Own local revenues</i>                     | 3.1    | 2.3    | 2.5    | 9.3    | 6.3    |
| <b>1996 = 100</b>                             |        |        |        |        |        |

|                                       |     |    |     |     |     |
|---------------------------------------|-----|----|-----|-----|-----|
| GDP                                   | 100 | 93 | 95  | 87  | 132 |
| Total public expenditures             | 100 | 93 | 100 | 95  | 139 |
| Local public expenditures             | 100 | 84 | 76  | 78  | 121 |
| Local public revenues                 | 100 | 84 | 75  | 80  | 120 |
| <i>Transfers to local authorities</i> | 100 | 88 | 74  | 20  | 20  |
| <i>Own local revenues</i>             | 100 | 70 | 82  | 286 | 286 |

As it can be easily compared, a first impact the L 189/1998 had on local budgeting in terms of revenues /expenditures structure, was to increase the amounts to be placed under the “own revenues” label, while decreasing the share of state transfers. Apart from that, the increase in local government fiscal autonomy has taken place in a context of macroeconomic decline, and local government revenues declined steadily between 1996 and 1998, both in absolute numbers as well as a share of GDP (Table 7). Central government transfers to local governments' budget decreased in 1998 relative to 1996 and 1997. However, revenues from local taxes and fees increased in real terms in 1998 relative to 1997. This reflects the initial impact of the amendments to the Law on Local Taxation adopted in 1997 and 1998 that adjusted rates to inflation. Local government expenditures declined both in real terms and relative to the overall economy from 1996 to 1998.

This trend was reversed in 1999 when local government expenditure began to grow as a percent of GDP. This up and down trend is an important factor to keep in mind when looking at the finances of any local government in Romania. While some are better off than others are, all of them have been operating in a difficult environment characterized by positive and negative year-to-year changes in overall expenditures largely outside their control. Fiscal transfers (including subsidies) have followed a negative trend over the five-year period. They were equivalent to 3.5 percent of GDP in 1996 and were less than one percent in 2000. Fiscal transfers, as a share of national government expenditures also declined during the same period.

However, this trend is deceptive, as there were important changes in the local government finance legislation between 1998 and 1999 that reduced the overall local dependence on fiscal transfers. Starting in 1999, local governments received a percent share of the revenues from the personal income tax (originally the wage tax). These funds are paid directly into local government accounts by the tax offices at the moment when they are collected. They do not pass through the State budget and thus, technically, they are not transfers. Additionally, revenues from local taxes and fees increased. Together, these constitute a growing importance of the local fiscal base as a key factor in shaping local finances<sup>26</sup>. To view how local governments have chosen to spend their money in 1998 and 1999, see the table below:

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26 Here it can be once again argued over the existence of a direct correlation between the increasing local financial autonomy and the Romanian ratification of the European Charter of Local Self-government (with its relevant to this situation, Article 12).

Table 7: Total expenditures at local and regional level  
(source, adapted: Human Development Sector Unit, 2002)

| <b>Public services</b>      | <b>1998 (%)</b> | <b>1999 (%)</b> |
|-----------------------------|-----------------|-----------------|
| Local administration        | 13.4            | 7.9             |
| Education                   | 9               | 10              |
| Health                      | 0.5             | 12.8            |
| Culture and sports          | 4.9             | 4.3             |
| Social assistance           | 9.3             | 7.4             |
| Housing                     | 41.3            | 38.4            |
| Transport and communication | 20.3            | 12.6            |
| Reserves                    | -               | 0.6             |
| Other activities            | 1.2             | 11.5            |
| Total expenditures          | 100             | 100             |

To summarize, while the L 189/1998 has a general favorable influence over the fiscal decentralization process, it does have one problem – it doesn't manage to correct the inconveniences L 69/1991 have put into practice. To be more specific, L 69/1991 lists the “tasks” of the local governments. However, these tasks are not functional competencies, but authorities to act. For example, local governments can lease public services or assets. They can establish local companies. They appoint and dismiss managers of their local companies and public institutions. They prepare and adopt the local budget. The functional responsibilities (services provided by the local self-governments) are in fact determined each year through an Annex to the Annual Budget Law. This annual determination and modification of local expenditure responsibilities reflects the lack of an overall consensus or “vision” of the role of local government in Romania.

#### *LOCAL ALLOCATION OF RESOURCES AND RESPONSIBILITIES IN 2001*

A closer look to the reforming act of the local public administration in 2001 (Ionita, 2001; Giurgiu, 2002; Alexandru, 2002: 94 - 98) contributes to identifying all the three dimensions of the decentralization process already mentioned above - namely, the administrative, fiscal and political decentralization. In fact, L 215/2001 may be called an European law, and the Table below clarifies this thoroughly, by producing a comparison between the first chapters of the Romanian law and the European Charter of Local Self-Government.



Table 8: European Charter of Local Self-government *versus* L 215/2001

| European Charter of Local Self-government  | L 215/2001   |
|--|--|
| <p>Art. 3.1 Local self-government denotes the right and the ability of local authorities, within the limits of the law, to regulate and manage a substantial share of public affairs under their own responsibility and in the interests of the local population.</p> <p>Art. 3.2 This right shall be exercised by councils or assemblies composed of members freely elected by secret ballot on the basis of direct, equal, universal suffrage, and which may possess executive organs responsible to them. This provision shall in no way affect recourse to assemblies of citizens, referendums or any other form of direct participation where it is permitted by statute.</p> <p>Art. 4.2 Local authorities shall, within the limits of the law, have full discretion to exercise their initiative with regard to any matter which is not excluded from their competence nor assigned to any other authority Art. Art. 4.3 Public responsibilities shall generally be exercised, in preference, by those authorities which are closest to the citizen. Allocation of responsibility to another authority should weigh up the extent and nature of the task and requirements of efficiency and economy.</p> <p>Art. 6.1 Local authorities shall be able to determine their own internal administrative structures in order to adapt them to local needs and ensure effective management.</p> <p>Art. 9.1 Local authorities shall be entitled, within national economic policy, to adequate financial resources of their own, of which they may dispose freely within the framework of their powers.</p> <p>Art. 9.2 Local authorities' financial resources shall be commensurate with the responsibilities provided for by the constitution and the law.</p> | <p>Art. 3.1 The local autonomy represents the right and the effective capacity of the local public administration authorities to solve and to administer in the name and interest of the local communities they represent, the public problems, according to the law.</p> <p>Art. 3.2 The communities rights are exert by the local council, by the mayor and by the county council which are local public administration authorities elected through universal, equal, direct, secret and free express vote.</p> <p>Art. 3.3 The provisions of the paragraph 2 can not touch the citizens right to be consulted through a local referendum or through any other direct methods in the community public problems of a special interest, according to the law.</p> <p>Art. 5.2 The local autonomy principles give to the local public administration authorities the right to have within the framework of the law, the initiative in all the local domains except those purposely given by the law in the other public authorities' competence.</p> <p>Art. 7.1 The competencies and the prerogatives stipulated by law are prior exert by those local public administration authorities that are closer to the citizen.</p> <p>Art. 7.2 The local public administration authorities' competencies and the prerogatives other than the ones stipulated in paragraph 1 are establish taking into consideration the extent and the nature of their responsibility as well as the efficiency and efficacy needs.</p> <p>Art. 8 The central public administration authorities have to consult the local public administration authorities' associations before adopting any decision that directly concern the activity of those associations.</p> <p>Art. 9 As part of the national economic policy, the communes, cities and county are in title to possess their own resources that are administrates by the local public administration authorities, according to the law. The local public administration authorities' financial resources must be proportional with their competencies and responsibilities stipulated by law.</p> |

As may be read in the table above, there are practically few sentences that do not match in the case of the two cited normative acts. Formally then, there will be nothing more

reasonable to say than that L 215/2001 is definitely European by text. Did L 215/2001 further promote fiscal decentralization? Unfortunately, it did not: many functions were delegated *via* L 215/2001 from the centre to the periphery, without any State mandate for the latter. On the other hand, in regard to the transparency and ratio in the local expenditures, the main subjects of sub national debate were education and social welfare. The increase of amount of local revenues and expenditures, did not yet all the time indicate a high level of financial autonomy, especially in a system (as the Romanian one), where the fiscal powers of the national government have not been entirely coordinated with the delegated local responsibilities of the "closest to citizens" authorities. As such, though between 1998 and 2001, the decentralization, *lato sensu* has been substantial, it may still be considered as an incomplete process, the local financial autonomy being rather restricted than promoted (Lazaroiu, Payne and Denoex, 2001: 21, 35 - 36, 41 - 42). Going further, by limiting the exclusive financial local control, the even principle of subsidiarity is under threat. This is because in light of Article 7.1 and 7.2 of L 215/2001, the state intervention at the basilar levels appears to be legitimate in only two situations: a) when the nature and the extent of the responsibility belonging to the local authorities requires it; b) or when efficiency and efficacy reasons demands it. Setting the Town Hall employees' number or the maximum limit for protocol expenditures may yet be hardly regarded as legitimate in the just presented sense. It is then the decisional powers that seem to be less visible in the Romanian subnational democracies; and the even legal provisions that enshrined the subsidiarity principle the ones that now restrict its application.

## CONCLUSION

Getting Europeanized was priority number one for those countries interested in re-becoming part of the Europe and of the European Union. And Romania made no difference in this, since it was with great joy that all the relevant domestic political actors received, in 1999, the green light for accession to the EU structures. Soon, massive transformations followed. What impact did they have on the Romanian subnational democracy? Have they helped it into getting the decision making process closer to those governed, to the citizens?

To address these questions, two basic assumptions were made. First, that Romania's EU "non-member" status facilitated the transformation of its domestic norms and policies, in accordance to the regulations that the EU *acquis* contains. And second, that getting Europeanized was not only about formally including the European standards into the domestic legal framework, but also about achieving their successful practical implementation.

Yet, since the European values of public administration are still rather hard to point event at this particular time in the EU *acquis*, answering the questions about Europeanization of

the Romanian local administrative structures needed a point of reference. And the standards the European Charter of Local Self-government provides were fully taken into account. Moreover, it was the principle of subsidiarity, enshrined in Article 4.3 of the Charter, the provision that became the appropriate instrument in testing the consequences the adjusting to the "European way" hold on Romania's subnational democracy. One variable was used in assessing the "closeness to citizens" dimension of the sub national decision making processes, namely: fiscal decentralization (with allocation of resources and responsibilities between the different legal levels of government as main indicators) between 1991 and 2001. The subsequent hypothesis was: the greater the fiscal decentralization level is, the powerful (in terms of functions and resources) local governments are, and therefore, the more promoted the local autonomy (and subsidiarity, for that matter) is.

To summarize the findings, it has been noted that prior to 1997 (the date of Romania's ratification of the European Charter of Local Self-government), the domestic local governments were actually mainly administrative decentralized. The local budgets were central coordinated, and no power in assigning the local revenues or expenditures was granted to the "closest to citizens" authorities. In addition, a closer look at the own local revenues/ central transfers ratio proves that prior to 1998, the year when a new law on local public finance was issued (L 189/1998), there was no financial autonomy for the sub national authorities. With regard to the allocation of responsibilities, L 69/1991 recognizes the mandate of local governments to act within the areas of: local economic development, local urban development, land administration and development, cemetery administration, protection of environment, housing, water supply, sewerage, local public roads and local transportation. The county level, on the other hand, was to provide the following services: maintenance of the county roads, public transport between localities within the county and administration of education and health institutions of county interest.

In 1998, though, one year after Romania decided to ratify the European Charter of Local Self-government, a new Local Public Finance Law was issued. For the first time in Romania, norms, mechanisms and procedures that clearly limited the constitution and using of the local communities' financial resources from the state budget were established. As such, the level of state transfers in the local budgets' revenues considerably diminished (from over 75% prior to 1998, to less than 30% after L 189/1998 came into force) and the local government expenditure began to grow as a percent of GDP (since 1999). Still, while the L 189/1998 has a general favorable influence over the fiscal decentralization process, it does have (at least) one problem – it doesn't manage to correct the inconveniences put into practice by L 69/1991, namely to establish a "task" list for local governments, that are not authorities to act, but functional competencies. Still, on the overall, by means of L 189/1998, the Romanian local authorities became more accountable to citizens and thus, closer to them than under any other previous

regulations. Subsidiarity was yet to be legally enshrined in Article 7.3 of the new "European" Law on local public administration, L 215/2001.

In the 2001 Regular Report, the European Commission pointed out that: "Romania has continued to make progress with the adoption of the *acquis*. However [...] the overall capacity of the public administration to implement the *acquis* remains limited and represents a major constraint on Romania's accession preparations. While certain parts of the administration are able to function effectively there are many important sectors where the weakness of the administration is a serious cause for concern". Thus, the aim of the reforming process of public administration that followed intended it to make the latter capable of fulfilling its mandate and thus of contributing to the economic and social development in the region. As a consequence, L 215/2001 was entirely inspired by the European Charter's provisions. So, not only subsidiarity became binding, but also, the financial and, to some extent, the political decentralization. In terms of local mandated functions, the sub national authorities became responsible for delivering social welfare and educational services (two items highly expensive, in any public system), without yet being able to adjust the ceilings of the tariffs or to fully manage the local money involved in the process. Moreover, there are still some inconveniences that need to be addressed as soon as possible (e.g. local protocol expenditures are limited by central provisions), if the Europeanization of local administration is more than a formal change in a transition country, on its way to the European Union.

To conclude, a decade ago, Romania substantially altered its subnational authorities; still, basically, fiscal decentralization was less promoted than argued (the State still interfered at local level by setting the standards, and making regulations), and as such, local autonomy was rather limited. The Romanian subnational democracies did have new functions regarding financial and legal aspects, but they still received lots of subsidies and transfers from the central authorities in areas such as education, health, public roads and sanitation. As a direct consequence of that, the autonomy enacted in the 2001 Romanian Local Government Act was still formal, and therefore, it needed to get further internalized. A complete Europeanization of the Romanian local government system has then not yet been achieved. As suggested by this paper, a comparative analysis between other CEE countries or the Balkans may provide further data on formal and substantial impact of EU regulations / European values on national and subnational patterns of democracy.

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