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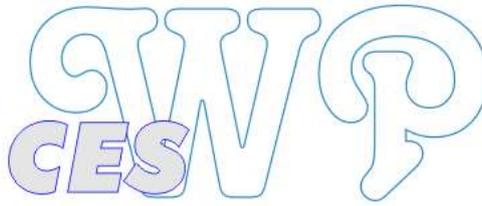
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Volume VIII, Issue 1, 2016

## Table of contents

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TOURISM AND TERRORISM: A WORLDWIDE PERSPECTIVE	1
<i>Cristina Elena ALBU</i>	
<hr/>	
ECONOMIC FREEDOM - A VECTOR OF TRANSITION FROM THE INFORMAL TO THE FORMAL ECONOMY	20
<i>Corneliu-Sorin BAICU and Luminita-Claudia CORBU</i>	
<hr/>	
AN ANALYSIS OF THE "BIO" / "ECO" PRODUCTS MARKET, REFERRING TO THE EU AND ROMANIA	33
<i>Ionel BOSTAN</i>	
<hr/>	
O.S.C.E. 1975-2015. 40 YEARS OF PEACEFUL CONFLICT RESOLUTION	45
<i>Daniel BURLACU</i>	
<hr/>	
FROM A PARLIAMENTARY ASSEMBLY TO A EUROPEAN PARLIAMENT: AN UNFINISHED PROCESS	57
<i>Ioana Antoaneta DODI</i>	
<hr/>	
ROMANIA AND THE EURASIAN UNION. PLANS, PREDICTIONS AND PERSPECTIVES	74
<i>Mircea-Cristian GHENGHEA</i>	
<hr/>	
THE TPP AND TTIP TRADE AGREEMENTS: THE INTERNATIONAL NEGOTIATION PROCESS	81
<i>Ioana GUTU</i>	
<hr/>	
EU POLICIES REGARDING THE DEVELOPMENT OF TRUST-LIKE DEVICES - RECENT CHALLENGES, ACHIEVEMENTS, PROSPECTS AND TERMINOLOGICAL INSIGHTS	93
<i>Irina GVELESIANI</i>	
<hr/>	
NEW GEOPOLITICAL REALITIES AND UKRAINE: IN SEARCH OF NEW INTERNATIONAL MODELS AND COMBINATIONS	103

*Vladlen MAKOUKH*

---

ROMANIA, THE EUROPEAN UNION AND RUSSIA 110

*Ion MUSCHEI*

---

THE DEVELOPMENT OF LEGAL RESPONSIBILITY FOR A SOCIALLY RESPONSIBLE BEHAVIOR FOR BUSINESS OPERATORS IN ROMANIA, MEMBER STATE OF EUROPEAN UNION 120

*Laura MURESAN (POTINCU)*

---

THE BUSINESS ENVIRONMENT IN CEE COUNTRIES: CURRENT CHALLENGES AND PERSPECTIVES 128

*Valentina Diana RUSU and Angela ROMAN*

---

VENTURE CAPITAL FINANCING IN EMERGING ECONOMIES 148

*Valentina Diana RUSU and Carmen (SANDU) TODERASCU*

---

THE CURRENT STATE AND PROSPECTS OF ECONOMIC DEVELOPMENT IN THE EU'S EaP COUNTRIES 163

*Ilkhom SHARIPOV and Sergey LISNYAK*

---

THE IDENTIFICATION OF INFLATION RATE DETERMINANTS IN THE USA USING THE STOCHASTIC SEARCH VARIABLE SELECTION 171

*Mihaela SIMIONESCU*

---

COORDINATES AND REPRESENTATIONS OF ARCHITECTURE FOR A REGIONAL CROSS-BORDER DEVELOPMENT STRATEGY 182

*Marcela SLUSARCIUC*

---

THE EUROPEAN UNION LOOKING FOR THE FUTURE. NEW FORMS OF ACCOUNTABILITY AND GOVERNANCE 197

*Emiliana Oana TATARCAN*

---

THE CONSOLIDATION OF EU GOVERNANCE: THE EUROPEAN SEMESTER AND THE EVALUATION OF EUROPEAN INTEGRATION DEEPENING 206

*Nicolae TODERAS and Ana-Maria STAVARU*

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## TOURISM AND TERRORISM: A WORLDWIDE PERSPECTIVE

Cristina Elena ALBU\*

*“The attacks in Jordan, just like those before it in Indonesia, Egypt, Spain and the United States, demonstrate that terrorism does not discriminate by race, ethnicity or region. Instead, terrorists indiscriminately target those seeking to live a peaceful, loving and free life.”*

Allyson Schwartz

**Abstract:** *We live in a society marked by major changes in the tourism field. Tourist destinations make all possible efforts to best promote their tourist offer and attract as different tourist categories as there might be. However, these tourist destinations are sometimes associated with terrorist attacks that can turn a famous tourist area into a highly avoided one. Terrorism may be permanently detrimental to a tourist destination on both social and economic levels. The purpose of this paper is to highlight the impact that terrorist attacks have on tourism around the globe. The research method used for the achievement of this article is documentary research. Through the proportions and forms that it has taken, terrorism has become one of the more and more active and threatening calamities that affect the international community. For some organizations, terrorism has become a means of solving their political, cultural and religious problems, taking tourism as a niche through which they can carry out their targets.*

**Keywords:** tourism; terrorism; global terrorism index; tourists' behavior; destination image

**JEL Classification:** L83; Z32

### Introduction

Tourism expresses freedom of travelling and can contribute to getting acquainted to different cultures. At the opposite end, terrorist movements are propelled by religious and ethnic factors that arise when a certain segment of the population condemns the Occidental lifestyle on which most of the tourist destinations are based (Korstanje *et al.*, 2012, p. 10).

One may notice the international activity of terrorist organizations from different states that want to enthrall new territories through their terrorist actions. Terrorism is not a phenomenon characteristic to the contemporary age only. It has been practiced through all ages, affecting most peoples and manifesting itself through reprobable actions with most disastrous consequences for human relations (Sofroni, 2010, pp. 6-7).

For the international community it is intolerable that terrorist acts – so many a time resulting in human lives termination and taking place mostly outside a conflict area – should affect the interests

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of one or more states, or even disrupt the bases of communication and normal relations between nations, nationalities and peoples, and the international order essential to everyone. The increasing number of terrorist acts around the world has brought along the need for developing an international system to fight this phenomenon through coordination of the efforts of different states at the highest level.

Tourist destinations make no exception from being strongly affected by terrorist acts. According to Sofroni (2010), this is the reason why “such events may lead to a fall in tourists’ number in a given touristic destination or even to the complete avoidance of that destination for a very long period of time, until tourists’ confidence might be restored”.

### **1. Terrorism: notion, consequences, actions**

The term “terrorism” derives from the term of Latin origin “terror” meaning “physical violence, fear, dread deliberately generated by public violent acts, the premeditated use of certain means capable of bringing about collective peril” (Servier, 2002, p. 42).

As the former president of the USA, John F. Kennedy, said in 1962, “terrorism is just another type of war - new in intensity, old as origin – a war of guerillas, of rebels and assassins; a war waged by ambuscade and not by fighting, by infiltration, not by aggression, where victory is obtained by wearing down the enemy and not by engaging it” (Enciclopedie Citatepedia, 2015).

Terrorism comprises the violent acts committed by one or more individuals against randomly chosen victims with the scope of maintaining a power, a will of domination by fear and dread that quickly become contagious for the entire population. Therefore, terrorism is an “offensive system used by an individual or by a large or smaller group to impose their will on an entire people or even on an entire civilization, to exercise an influence over history”. If we consider this perspective, “the terrorist, whoever might embody him/her – an individual or an entire nation – turns into the supreme vigilante, holder of an absolute justice, in the name of some principles that are often only known to or acknowledged by himself” (Servier, 2002, p. 31).

According to Servier (2002), the terrorist wave intensified after 1968, when violence appeared as an irrational manifestation of student movements in France, then in the other Western countries as well. Its part within the political conflicts has grown in significance especially after World War II, in relation to the national liberation movements (Sofroni, 2010, p. 44).

Terrorism began to build momentum in the years 1970-1971. The strategy of these groups was formulated according to the following slogan: “intimidate your adversary and propagate the cause

that you are fighting for". Many of the most active terrorist organizations are divided into two main groups:

- anarchist terrorist movements and leftist movements that promote social changes and the change of political regime through revolutionary action (Italian Red Brigade, the Japanese Red Army, the German Red Army);
- national liberation separatist movements and national minorities movements (Spanish Basque Organization, the Irish Republican Army, Muslim movements from Arab countries, the Kurds in Turkey).

These groups' actions are designed to trigger the following consequences (Sofroni, 2010, p. 42):

- to demonstrate the governments' incapacity to defend their own citizens and diplomatic missions accredited in the respective country;
- to force governments into taking supplementary security actions, including the withdrawal of public freedoms, fact that would lead to negative reactions on the part of the population;
- to determine the target-state's citizens to put pressure on their own government to cease the actions that attract the terrorist attacks.

Terrorism implies "organization, planning, funding and equipment as well as individuals trained for carrying out the concrete fight actions". There are situations in which terrorist groups are under the command of intelligence services of different states for various well-founded reasons (Servier, 2002, p. 43). One of these reasons is the influencing of certain political decisions to the end of determining a government or a political group in power to conform to terrorist interests. Terrorism is used as a form of conventional war, as a weapon directed towards an enemy that cannot be attacked otherwise.

From the point of view of the used tactics, there can be identified two main types of actions (Sofroni, 2010, p. 43):

- those by means of which terrorists take precautions to save their life after the attack – for example, hostage-taking;
- suicidal missions or kamikaze, which present two great dangers: defense against them is extremely difficult; the terrible human and material losses produce real emotional shocks amid the population.

In the first stage, terrorism involves four types of attempts (Servier, 2002, p. 63):

- kidnapping of personalities for obtaining a ransom and often for detained terrorists exchange;
- plane-high jacking, usually followed by liberation demands of certain detained terrorists;

- robbing of banks and armament warehouses to sustain the armed groups both financially and logistically;
- destruction of certain tourist buildings/objectives that have great significance for the respective state.

Terrorists' extremist orientation originates in their conviction that they will never be able to attain their goals on a legal way, so they search for different forms of manipulation, of changing peoples' behavior through fear, unsafely and social division.

## **2. Terrorism and tourist destination image**

Tourism contributes to the development of tourist destinations. The main advantages of tourism consist of creating jobs, attracting foreign currency to a certain area, developing other sectors closely related to tourism and developing the infrastructure without which any tourist destination could not be known, through limited access of tourists (Alsarayreh *et al.*, 2010, pp.145-160).

### ***2.1. Conceptual boundaries on the image of a tourist destination***

The tourist destination may be a country, a city, an area that attracts tourists through the particularities it owns. Be it a resort or a country, some places have a higher probability to develop as tourist destinations if certain factors are present, while their absence may constitute barriers of various degrees. Tourism researchers have underlined the importance of the image of a tourist destination as a crucial factor in the promotion of an area, influencing its prospects of being chosen, its perceived quality, the satisfaction it may offer, the loyalty it may engender, as well as its recommendation within the circle of friends/acquaintances (Alvarez *et al.*, 2008, p. 38).

The image is an essential component within the process of choosing a holiday destination, making the difference between tourist destinations. At the same time, it influences the tourist's decisional process. The destination image is defined as the global perception or the whole set of impressions of an individual regarding a certain place. People create for themselves images and representations about places from the information they get. In the past, this information was transmitted by literature and written papers but, nowadays, the media plays the essential part in transmitting the images and representations (Hall, 2002, p. 458).

As previously mentioned, the image of a tourist destination may contribute to making the decision of purchasing a touristic product. Thus, if the respective destination has a certain reputation

or its standards meet the tourist's level of expectation, then the tourist will tend to choose that which offers safety and certainty. Of course, there is also the situation in which the tourist wants to try a new destination, even if he/she doesn't have detailed information about it.

The image of a country was defined by Nagashima in 1970 as a special image, a stereotype the consumers have in mind in relation to a certain country; this "picture" may be shaped by historical, economic and traditional variables. It is also in this case that the image of a country can ease the process of making a decision to purchase a touristic product or service in that country (Rezvani *et al.*, 2012, p. 205). The image is often created through stereotypes, by classifying nations and people by categories. Although stereotypes can be superficial, they may trigger certain international attitudes or orientations (Hakala *et al.*, 2012, p. 14). Stereotypes may distort one's perceptions about a destination. This happens especially when events take place that leave an unpleasant mark on the tourists during their vacation. Feeling resentful, the respective tourist will foully "advertise" the destination, fact that may change the perception of his/her friends and relatives on the analyzed destination, determining them to give up visiting that particular place (Albu, 2013, p. 8).

Each tourist has his/her own personality, fact that leads to the making of various decisions. In this respect, Corniglon and Turnois (2011) consider the image of a destination as an influencing factor not only on the actual situation of the destination, but also on the tourist's behavior, in general.

Global and local events such as terrorism, epidemics and political turmoil's are illustrated in the media and affect representations and perceptions related to a certain place. Disasters' reflection by the media can generate bad publicity for tourist destinations, reducing their general reputation as to safety, attractively and comfort (Sönmez *et al.*, 1999, p. 13). Beginning with the September 11<sup>th</sup> 2001 events, the numerous terrorist attacks, epidemics and natural disasters, these ones' risks, crises and impact have started to gain considerably more importance within tourist research. Terrorist attacks represent a specific form of tourist crises, as destinations are usually hit unexpectedly. The symbolic images of panic and destruction become deeply rooted in the potential tourists' minds and the decrease in demand may strongly affect tourist industries (Aschauer, 2010, p. 4).

An important aspect in tourist industry is tourist intention to return to a specific area/region/city/country. That is why we should take into account the fact that a tourist destination image may positively influence tourist's behavioral intentions, especially their desire to return to that particular area (Lertputtarak, 2012, p. 111). Roth and Romeo (1992) consider that the image of a country is represented by the consumers' general perception on that country, based on the strong and weak points by which the respective country has made itself known. Tourist image is considered to be an important aspect of a country's general image. Every destination has an image, but some

destinations have more powerful images than others (Sönmez *et al.*, 2002, p. 185). We may quote in this sense the image of Paris (considered the city of romance) and the image of the Danube Delta (renowned nature reserve in Europe). In the first case, the city of Paris is a worldwide well-known destination, with a powerful impact on tourist perception. In the second case, the Danube Delta is known rather on a European level, being chosen as destination only by those tourists that might be keen on the flora and fauna of the area.

## ***2.2. Components of a tourist destination image***

Some authors consider that the structure of the image consists of a single component: the cognitive one. Schneider and Sönmez (1999) define the cognitive component as “assessment of known attributes of the product or as perception of product from an intellectual perspective”. The emotional dimension is the second component of the tourist image structure and consists of the impressions that a tourist has about a particular object or place, while on the other hand, there might also be a third series of opinions envisioning the structure of a tourist destination as formed by three components. Gartner (1993) clarifies that the three components of a tourist destination are: the emotional component, the cognitive component and the conative component.

In his opinion, the conative image component is analogue to behavior, since it represents the action component leading to the making of a decision after both internal and external information has been processed.

Echner and Ritchie (1993) have proposed a single tri-dimensional model that divides the image into two components, based on attributes and holistic. Each component presents items that might have functional or psychological features and reflect common or unique characteristics of the destination.

In Echner’s and Ritchie’s opinion, the image is based on specific attributes (e.g. good restaurants, high prices, night clubs) and mental/holistic attributes (e.g. a group of friends having fun in night clubs along the beach).

At the same time, the image might also refer to measurable characteristics (beaches, parks) or to psychological characteristics (the reputation of the destination). The third classification emphasizes the unique objectives of the destination (e.g. the Giza Pyramids in Egypt, The Eiffel Tower in France) or the common ones (e.g. natural environment, mountains, beaches).

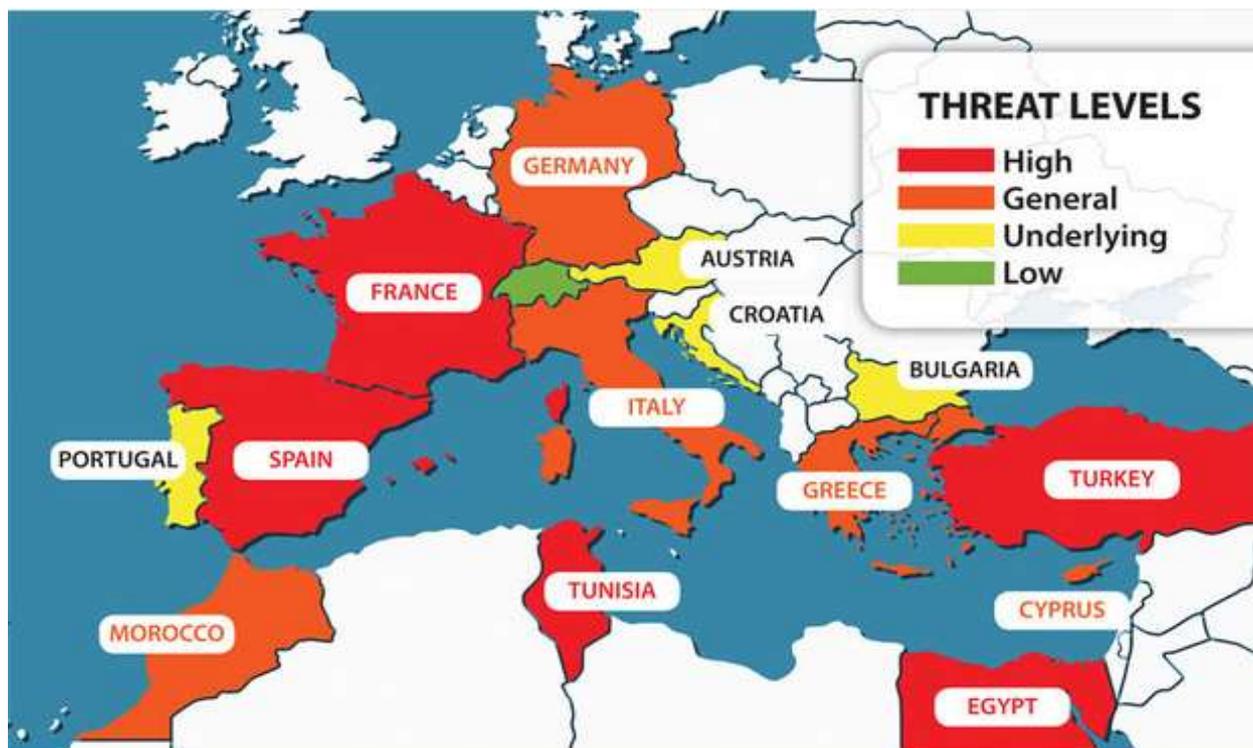
### 2.3. Terrorism impact on the image of a tourist destination

The development and worldwide reputation of some tourist destinations may also have a negative impact: that of becoming a target for terrorist attacks. These terrorist attacks are usually engendered by misunderstandings regarding political aspects between countries, racism or religious discrimination, but also by other reasons related to government and governmental decisions that affect more than one state.

Some terrorist attacks have permanently changed the way in which tourist activity is taking place within the affected areas/countries. It has been noticed the need for higher security measures within the tourist areas, especially in those countries whose economy depends on the tourist industry, such as Spain, France, Greece, Italy, Egypt, Tunisia (especially the Mediterranean Basin countries because they are among the most important countries receiving tourists).

The map below shows the terrorist threat levels for certain countries in Europe and from the entire Mediterranean Basin.

**Figure 1 – Countries targeted by terrorist threats**



Source: Thema News (2015)

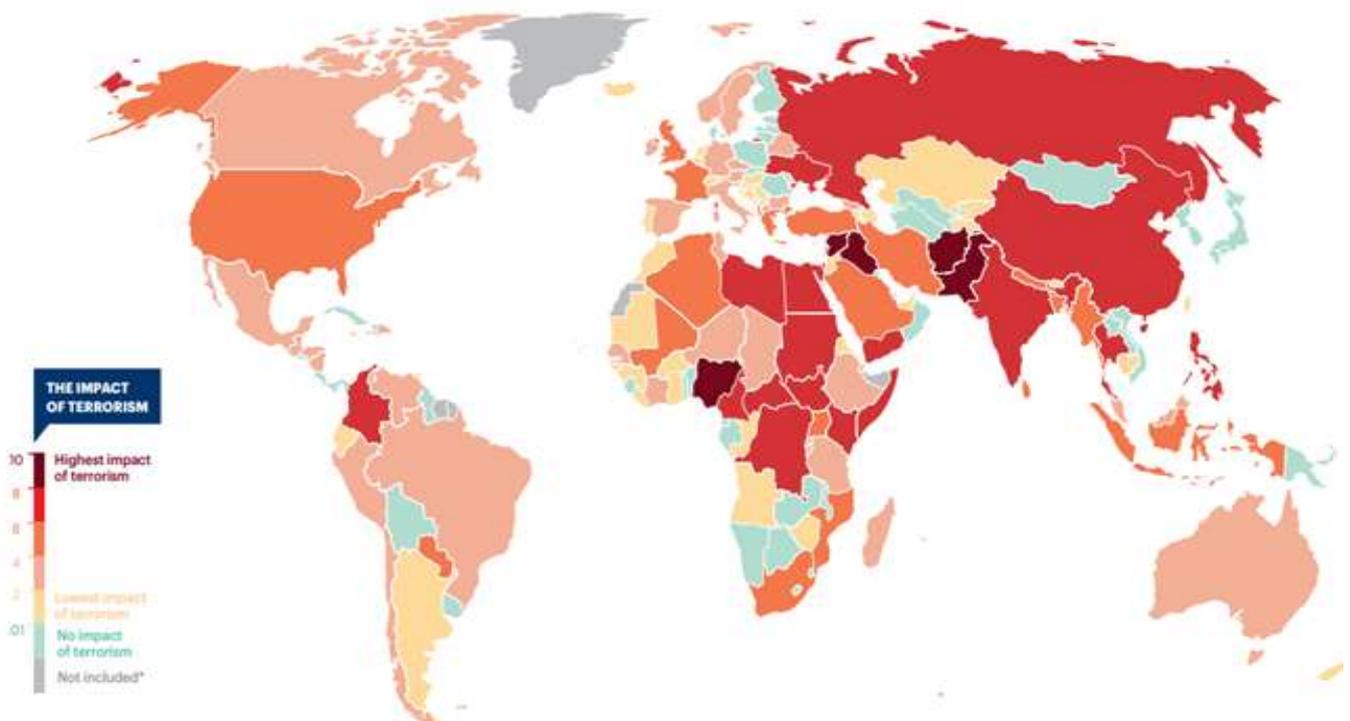
Analyzing the above map we can notice high levels of terrorist threats in countries such as Spain, France, Turkey, Tunisia and Egypt. General threat levels are present in countries such as Germany, Italy, Greece, Cyprus and Morocco. Underlying threat levels are to be encountered in Portugal, Austria, Croatia and Bulgaria, while terrorist threat levels in countries such as Switzerland are low.

One can notice that all these mentioned countries play a fundamental part in tourist industry, being renowned for their resorts, special natural environment, as well as for various unique tourist landmarks. On the other hand, the economic wellbeing of some countries such as Germany may attract terrorist attacks with the scope of reducing population's trust in the government of the country and creating panic among the less developed states.

According to the studies done by the Institute for Economy and Peace (2015), terrorist events have increased by 80% in 2014, the highest ever recorded level according to the Global Terrorism Index. Unfortunately, data that show what was exactly the increase relative to the tourism developed areas are not available.

These violent acts killed 32.658 people in 2014, compared to 18.111 in 2013, according to the Global Terrorism Index. The map below highlights the countries where this index has different values, according to the impact of terrorism on that particular area.

**Figure 2 – Worldwide Terrorism Impact**



Source: Institute for Economics & Peace – Global Terrorism Index (2015)

According to the Global Terrorism Index, among the countries scoring a strong impact of terrorism is: Iraq, Afghanistan, Nigeria, Pakistan and Syria (in these countries, the Global Terrorism Index reach level between 8 and 10 on the terrorism impact scale). They are followed by India, Libya, Thailand, Philippines and Egypt (with a 6-8 index), while a medium level of terrorism is scored by countries such as Turkey, the UK, Greece, the USA and France, with a 4-6 index.

The Global Terrorism Index scores values between 2 and 4 for countries such as Tunisia, Germany, Italy, Cyprus, Spain, Bulgaria and Canada. A low level of this index (with values between 0 and 1) is scored by countries such as Belgium, Jordan, Morocco, Switzerland, UAE, Portugal and Croatia.

At the same time, there are also countries where this index is or tends to be 0, meaning that there have been no terrorist events within these areas, or that their impact was insignificant. This is the case of countries such as Romania and Moldova.

On a geographical basis, the table below synthesizes a part of the values that the Global Terrorism Index has scored worldwide.

**Table 1 – Global Terrorism Index in 2015**

Rank	Country	Score	Rank	Country	Score	Rank	Country	Score
1	Iraq	10	27	Turkey	5.737	72	Canada	2.297
2	Afghanistan	9.233	28	UK	5.613	82	Belgium	1.977
3	Nigeria	9.213	29	Greece	4.976	85	Jordan	1.751
4	Pakistan	9.065	35	USA	4.613	92	Morocco	1.446
5	Syria	8.108	36	France	4.533	95	Switzerland	1.349
6	India	7.747	47	Tunisia	3.697	101	UAE	1.045
9	Libya	7.29	53	Germany	3.442	110	Portugal	0.267
10	Thailand	7.279	54	Italy	3.364	116	Croatia	0.115
11	Philippines	7.27	61	Cyprus	3.08	121	Moldova	0.038
13	Egypt	6.813	65	Spain	2.622	149	Romania	0

Source: Personal adaptation after Institute for Economics & Peace (2015)

As a result of the values scored by the Global Terrorism Index we can notice a worldwide ranking of countries. We can see that a number of countries noted for their tourist activities are to be found in the above table, with different values of the index. Among them there are: India, Thailand, Egypt, Turkey, Greece, France, Tunisia, Italy, Spain, Jordan and Morocco, countries that might have

economic problems in the absence of tourism industry. Countries like Syria, India, Egypt and Tunisia have come to be chosen very carefully by tourists, their number dropping considerably or totally (the case of Syria), precisely because of the terrorist attacks that have started to take place frequently in these areas.

The increase of terrorist attacks can be attributed to the Islamic State group (ISIS) and Boko Haram, a Nigerian jihadist group that allied itself with ISIS in March 2015. This alliance was practically responsible for 51% of the deaths resulted from the terrorist events of 2014.

Terrorist groups are usually financed by certain sponsoring states. According to Johnson *et al.* (2010), besides the Taliban regime in Afghanistan, “a total of seven countries were listed as sponsors of terrorist groups in 2000: Cuba, Iran, Iraq, Libya, North Korea, Syria, and Sudan”. These countries provided financial and logistical support to terrorist organizations. However, in order to avoid detection, terrorists are continuously looking for new ways to gain more support (Johnson *et al.*, 2010, p. 110).

Johnson *et al.* (2010) also consider that “some states support terrorism indirectly, through investing in certain particular sectors of activity or through different political arrangements”.

Terrorist attacks cause repercussions of various intensities on the economy, as well as on the psychological level of a tourist destination. The tourism industry contributes to the rapid development of a country's economy, creating millions of jobs worldwide (Stojanovic, 2012, p. 1260). There are some external factors that can affect the success of the tourism industry (Prideaux, 2005, p. 780). However, indirect repercussions may fall on several sectors and across several countries (Brück, 2007, p. 5). We can talk here about travel agencies from different countries working together to mutually promote their services or to meet the needs of several categories of customers from different continents. A terrorist attack could create economic problems for both travel agents, even if one of them is not located in the attacked area. Thus, both agencies would suffer from the falling in demand for the tourist destinations they had been promoting, especially if their work had been focused mainly on those destinations.

Both tourism and terrorism involve crossing borders and citizens from different countries. The reasons why terrorists attack tourist areas are the desire to affect the economy of that area, to attract international attention and to advertise themselves (Kamrava 2011, p. 341). The kidnapping of tourists of certain nationalities is, in fact, a sign of protest made manifest by terrorists against the support of certain governments/countries, and aim to destroy public confidence in the respective government (Bremer, 2000, p. 4). Of course, the indirect goal is to get financial resources in exchange for releasing the prisoners or other advantages such as the release of captured terrorists.

At the same time, the government of certain Muslim countries that refuse to support terrorism can cause an avalanche of terrorist attacks as retaliation against the disobedience to the requirements of terrorist extremists. This is the case of Egypt, whose new president (since June, 2014) is Abdel Fattah El-Sisi. He was commander of the Egyptian Armed Forces, Minister of Defense, and contributed significantly to the removal of the former president Mohamed Morsi, a supporter of several terrorist groups.

The social and economic problems triggered by terrorist attacks are related to unemployment, lack of shelter (as a consequence of destroying one's home), tension, and criminality. Tourism generates revenue for both the developing states and for those already economically developed, so any issue affecting this industry can turn into a big problem (Kalia, 2009, p. 1).

Some terrorist activities are focused on issues that are directly associated with the tourism industry: hotels, restaurants, airlines, tourist attractions, famous tourist resorts. Therefore, security in these locations must be a priority for all tourist destinations that want to preserve their tourists and maintain the safety in the area.

#### ***2.4. Selective chronology of terrorist events***

Further on we will display a selective chronology of terrorist acts of the last half century. Some of these events, taking place before 2009, have been made available to the general public by the Romanian Intelligence Service (2015). Emphasis was laid especially on those events that occurred in areas popular for their tourist activity (Toma, 2013, pp. 409-412):

- 1970: three planes with more than 400 passengers aboard are hijacked by the Popular Front for the Liberation of Palestine. Two are taken to Jordan, where hostages are released and the planes blasted, while the third plane was blown in the air, in Egypt. Another team tried unsuccessfully to hijack a plane from the London airport, one of the kidnappers being caught.
- 1971: the Jordanian prime minister is killed by Palestinian terrorists from the Black September group at a hotel in Cairo, Egypt. A month later, in London, the Jordanian ambassador to Britain is the target of an attack by a Black September team.
- 1972: eight Palestinian terrorists from the Black September group kill two Jewish athletes and take nine hostages in the Olympic village in Munich (FRG). In the releasing attempt all the hostages are killed, together with five terrorists and a police officer.

- 1979: Two hundred Islamic terrorists take hostages hundreds of pilgrims in the Grand Mosque of Mecca (Saudi Arabia). French and Saudi security forces take control of the most important place of worship in the Islamic world, after an intense fight in which 250 people were killed and another 600 injured.
- 1981: Egyptian President Anwar Sadat is shot dead by a group of rebels during a military parade in Cairo. Seven other officials were killed and 28 wounded. The assassins were later executed.
- 1984: Indian Prime Minister Indira Gandhi is assassinated by her own bodyguard, Sikhs, in New Delhi, India. Nearly 3,000 people died in incidents which followed the assassination.
- 2001: Two planes, domestic flights of US airlines, are flown into the twin towers of the World Trade Center in New York, while another plane is crashed over one side of the Pentagon building. The attack, the worst in the US history and world terrorism, made thousands of victims, and though it has not been claimed, the information obtained revealed the involvement of Al-Qaeda, led by the Saudi billionaire Osama bin Laden. The US launched a retaliatory military operation in Afghanistan following bin Laden's support by the Taliban regime in Kabul.
- 2002: remote-controlled bombings and car bombs took place in a bar in Bali, Indonesia. The attack ended with 202 dead and 209 wounded.
- 2003: bombings took place in Casablanca, Morocco, against Hebrew and Spanish targets. The attack was claimed by Jihad Salafia, a branch of Islamic Combatant Moroccan Grouping (Al-Qaeda related) and resulted in 33 deaths.
- 2003: bomb attacks in Istanbul, Turkey: several synagogues and a British bank were attacked, resulting in 57 dead and 700 wounded.
- 2004: the Moroccan Islamic Combatant Group attacked several trains in Madrid with conventional explosives and the effect was 191 dead and 1,800 wounded.
- 2005: bombing in London, that consisted of three explosions in the subway and a bus attack (56 dead and 700 wounded). The attacks were claimed by some local groups related to Al-Qaeda.
- 2005: terrorist attack on a bus in the tourist resort of Kusadasi, Turkey (5 people killed and 14 wounded).
- 2005: bombing in the tourist resort Sharm-el-Sheikh, Egypt (at least 65 dead and 200 wounded).

- 2005: suicidal bombing attacks in three restaurants in Bali, Indonesia (22 dead and 100 wounded).
- 2005: bombing attacks on several hotels in Jordan (62 dead and over 100 wounded).
- 2006: suicidal bombing attacks in the tourist resort Dahab, Egypt (23 dead and 83 wounded).
- 2012: an Islamist extremist opened fire in a Hebrew school in Toulouse, France, killing three children and one adult. But the total number of victims attributed to him rises to seven, including three soldiers.
- 2014: armed militants from the Muslim terrorist group Boko Haram (“Western education is forbidden” in a rough translation) attacked two neighboring settlements, Gamboru and Ngala, located in the Borno state, Nigeria. A total of 336 peaceful villagers were mercilessly killed and the settlements were destroyed and burned. The few survivors managed to escape by fleeing into the neighboring country, Cameroon. On the same night, the Boko Haram group kidnapped 11 Christian girls (aged 12-15 years) from the Chibok School, and they forced them to become Muslim wives for their militants.
- 2015: in January, France underwent a series of multiple terrorist attacks (one of them is that of Charlie Hebdo) which ended tragically, with 17 dead and 22 wounded.
- 2015: ISIS terrorists detonate a bomb in a train station in Ankara, Turkey. This is believed to be the biggest terrorist attack in Turkey's history. A number of 102 people were killed and more than 200 - wounded.
- 2015: in November, France had a series of separate incidents which held Paris under terror. Bombs on Stade de France, suicide bombings at some terraces and a hostage situation at an auditorium during a concert, lead to a terrifying balance - about 150 dead and 200 wounded.
- 2015: in March, at Aswan, Egypt, an area highly frequented by tourists, a bomb attack caused the death of two civilians and got another five seriously injured.
- 2015: in June, the General Attorney of Egypt, Hisham Barakat, was killed in a car bomb assassination in Cairo. The incident took place in a context in which former President Mohamed Morsi, spokesman of the Muslim Brotherhood, was sentenced to death and during a wave of capital convictions or life sentences among Islamist militants from Egypt.

- 2015: in June, there was a terrorist attack in Egypt at the temple of Karnak, near Luxor, a highly populated tourist area. The Egyptian police killed two suspected Islamist militants near the ancient temple and a suicide bomber detonated the explosive he had on himself near the famous tourist spot, fortunately with no victims among the population.
- 2015: in June, in Tunisia, men disguised as tourists opened fire at two hotels located in the El Kantaoui resort. Some of the tourists staying at these hotels were from aboard a couple of cruise ships which had made stopovers in Tunisia. At least 37 people were killed and another 20 injured. The terrorist attack was claimed by the Islamic State organization.
- 2015: in October, a Russian plane transporting tourists from Sharm-el-Sheikh to Sankt-Petersburg was shot down in the Sinai Peninsula, Northern Egypt, resulting in 224 dead. The attack was claimed by the Fundamentalist Group Sinai Province, a subsidiary of the Islamic State terrorist network.

Terrorist attacks are quite common in countries such as Iraq, Afghanistan, Pakistan or Sri Lanka, and most of them remain unclaimed by any terrorist groups. These areas are often avoided by tourists because of the high risk of suicidal or bomb attacks and armed robbery.

As outlined above, the terrorists have focused in recent years on some states known as tourist destinations visited by tourists from around the world: Spain, Turkey, Egypt, Tunisia, and France. These attacks are aimed at killing foreigners from different states in order to create tension between countries, generate panic among the population, and consequently make that the respective destination become avoided by tourists. This entire complex tends to economically destabilize the area and destroy the collaboration between some countries.

### **3. Terrorism and tourists' behavior**

Some activities and sectors are more vulnerable to terrorist attacks than others. This vulnerability can be given by the services' characteristics, particularly their intangibility and inability of storage to be sold later - specific features for the tourism industry. At the same time, terrorist attacks can cause changes in the tourists' need to visit a certain tourist destination (Bruck *et al.*, 2004, p. 4).

Swarbrooke and Horner (2007) consider that the tourists' behavior is derived from the consumers' behavior, fact which underlines the factors that determine the tourists to purchase certain

tourist products over others. Equally important are the factors determining those tourists to travel to a certain destination.

One of these factors refers to the perception the tourist has of a tourist destination, this perception being practically the image he/she has formed about that destination (Seba, 2011, p. 23). For example, Paris is perceived as a romantic city, while Ibiza is famous for its numerous entertainment opportunities. These perceptions are formed in our minds sometimes involuntarily, following our exposure to a range of information provided by the Internet, television, media, or friends who have already visited the respective locations.

Consumers' behavior is influenced by a number of internal and external factors. Internal factors aim directly the tourist's perception or experience about a certain tourist destination, and among external factors we have the economic conditions, that can affect the behavior of tourists who want to visit a particular destination (Musadiq, 2002, p. 103). In other words, financial resources play an important role in knowing a tourist destination, facilitating or limiting the access to certain tourist areas coveted by tourists.

The form of government represents another external factor, a country being able to facilitate or limit tourists' access. We may note here the case in which one wants to attract a certain category of tourists who can afford to spend a lot of money in a certain country. This is, for example, the policy of Qatar - an Arab emirate in Southwest Asia - which targets especially very rich tourists, the living standard being very high in this area. It is also impossible to entry this country without having a prior visa and this visa can only be issued through embassies and not at the usual border crossing points. These formalities sometimes make the tourists turn to other destinations, where their access is easier.

A previous visit to a tourist destination helps the tourist form a perception about that particular destination (Jack, 2006, p. 37). Thus, the tourist will decide more easily whether to visit that destination again or choose another. At the same time, the tourist can have a good perception of a tourist destination, and nevertheless might like to visit another destination he/she has never been to before. Conversely, their perception can influence a lot of people to choose or not the already visited tourist destination.

An equally important aspect is the level of satisfaction regarding the whole experience had by a tourist in a tourist destination (Maxwell, 2005, p. 49). Tourists' confidence in receiving quality services, the comfort, the culture of the area, the locals' hospitality, an enhanced security and no terrorist events, along with the professional employees of the tourist accommodation structures play a major part in the tourists' decision to return to a tourist destination. It is also worth mentioning that tourists may behave differently in different countries. For example, in a tourist destination like Egypt,

tourists will have to adapt to the local culture, to dress decently and behave accordingly. Instead, in a country like Italy, tourists can feel comfortable and free from local prejudice, regardless of what they might choose to wear.

### **Conclusions**

Tourism isn't just a means by which terrorists can convey their messages. Tourism can also encourage the development of certain political, economic, cultural or religious resentments in relation to some renowned destinations. Terrorist attacks within tourist destinations are meant to elicit international attention and their impact is all the greater as they create more victims in areas previously known for tourists' safety and lack of terrorist events.

The economic costs of terrorism are extremely high. Terrorism has influence on the economic bases of states such as Egypt, Israel, Turkey or Cyprus, countries that have high tourism income and which are practically taken out of this industry in the periods of affliction. As the society develops, the terrorism becomes more complex, more elaborate, crueller, remaining an integrant part of organized crime since ancient times, with an unfortunate prediction of persisting further into the future. Consequently, states must join and work permanently to exclude the possibility of terrorist attacks, whether they occur in tourist destinations or common areas.

Most often, terrorist actions do not hit the state military force, but the civil society. The purpose of terrorist activity is the emotional involvement of the population; this makes the psychological pressure on the state to be much stronger than in the case of a usual military conflict. The main aim of such actions is to spread fear. The higher the fear is, the greater the pressure on the state. The impact is all the greater as the area survives thanks to its income gained exclusively from the tourism industry.

The emotional reaction of the population to the consequences of terrorist attacks is natural. The fear that the next time one might be a victim is as real as possible. Tourists avoid the tourist areas where terrorist events have occurred, their confidence in the respective destination being very hard to recover. International terrorist attacks have led to the strengthening of security and military sectors in many of the affected states, as well as to the review of crossing interstate borders policy and the strict passengers' control, even if their purpose of travel is tourism.

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*“Terrorism is a biological consequence of the multinationals, just as a day of fever is the reasonable price of an effective vaccine ... The conflict is between great powers, not between demons*

and heroes. Unhappily, therefore, is the nation that finds the heroes underfoot, especially if they still think in religious terms and involve the population in their bloody ascent to an uninhabited paradise.”

Umberto Eco

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## ECONOMIC FREEDOM - A VECTOR OF TRANSITION FROM THE INFORMAL TO THE FORMAL ECONOMY

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**Abstract:** *This study aims to show that concerted action by the state and civil society can lead to an effective output of informality sphere by official or legal sphere. Such an action is represented by the vector concept named economic freedom. The resultant vector - economic freedom - is obtained by conjugating and composing of noneconomic factors (ownership freedom, freedom from corruption etc.) or cvasieconomic (fiscal freedom, labor freedom, investment freedom, etc.) and it is a prerequisite to a series of actions which are aimed at progressing progress and a healthy economy. If we cannot eradicate the phenomenon of informality, at least we can create a transition from the informal to the formal more efficiently and with positive effects in social and economic policy. The exit from the sphere of informality involves transitions strategies and not a simple translation from one sector to another.*

**Keywords:** informal economics; formal economics; economic freedom; transition strategies

**JEL Classification:** O17; P48; H11

### Introduction

Regardless of the dualistic, structuralist or legalistic visions, the interaction between the formal economy and the informal economy is a challenge for the academic world, governments and national and international institutions. Most often, the transition strategies from the informal to the formal economy either have a descriptive or theoretical character or they are prisoners of institutional bureaucracy. The vulnerability of these strategies is their inability to find a multidimensional method to quantify the translational actions between the two types of economy. The concept of economic freedom (as defined by the Heritage Foundation and by the Wall Street Journal), expressed by 10 qualitative and quantitative factors synthesized in the form of indices, represents in our opinion the instrument through which effective transition strategies can be developed. Given the complexity of the formal-informal relationship and the composite character of the concept of economic freedom, this work falls into the category of conceptual research. In the framework of the methodology used, the deductive aspects are harmoniously combined with the inductive aspects. The conceptual aggregation of the research topic is based on several factors: the informal economy, the formal

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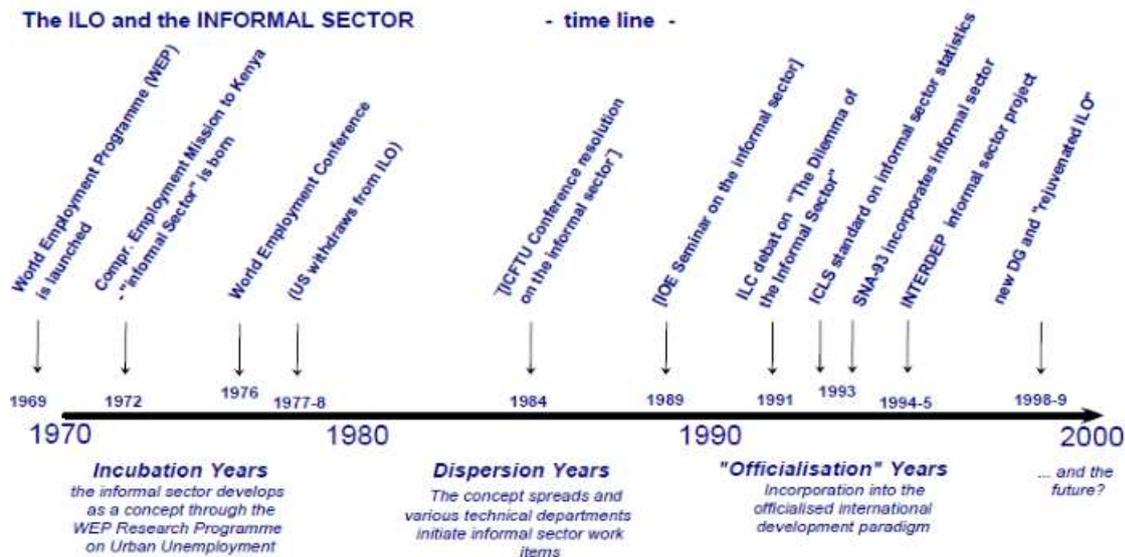
economy, economic freedom - seen globally or in terms of its components, the strategies and the transition actions from the informal to the formal dimension. The first part of the paper intends to define the concept of economic informality and the presentation of transition strategies. The second part of the study is aimed at outlining a model of formal-informal interaction which has as its epicenter the idea of economic freedom that acts as a transition vector from the underground to the official sector.

### **1. Economic informality. The evolution of the concept. Definition**

The concept of informal sector has been launched by the ILO (International Labour Office) five decades ago. Over time, this concept and the social problems that revolved around it have generated heated debates that had as spearhead ILO almost all the time, more than any other international institution.

Economic informalism, or more specifically, the informal sector extracts its sap from the thinking related to the development trends specific to the 50's and 60's; it developed conceptually through 1970; it evolved by being gradually absorbed in the development paradigm of the 1980s and 1990s and the beginning of the 21<sup>st</sup> century. Though the informal sector is still centered on the social justice mandate established by the ILO, the preponderance of the economic side and the complexity of the phenomenon require in our opinion a translation of the analysis of the phenomenon mainly into the fiscal and socio-economic dimensions.

Paul E. Bangasser (2000) proposes an analysis of the concept of informal sector through the "official record" of the ILO, meaning by this the evolution over the time of the concept during conferences, seminars as well as in the papers and documents issued under the aegis of ILO (annex 1). The institutional history of the concept is organized in three phases, correspondent to the three decades presented through timeframe (figure 1).

**Figure 1 -The ILO and the Informal Sector**

Source: Bangasser, 2000, p, 2

Although the term "informal sector" first appeared in 1972, its roots are to be found in the economic development efforts of the 1950s and 1960s, considered years of trust and optimism. The involvement of the UN through its various agencies such as OIM, UNIDO, UNESCO, FAO or OMS has proved to be necessary, especially in terms of achieving a development framework for third world countries. The technical expertise of the OIM targeted the workforce and the workforce planning. As part of the OIM, The Department of Human Resources and Workforce Planning found that some of the aspects regarding the main aspects identified and the workforce recording presented serious shortcomings in the sense that the development plans and some statistical data did not match.

In the first decades of the post-war period, investments and raising labor productivity created numerous jobs. However, less "modern" jobs (in trend with the technological development) were created than what people wanted. Many of the employees found jobs working outside the official or planned "work" frame. Activities of this type were called "informal occupation", in other words an economic activity outside the official framework. Informal activities took place under various forms: "moonlighting" performed by underpaid clerks, home activities or activities in agriculture.

The phenomenon of urban migration caused in the urban environment a gulf between the "planned employment of labour force" and daily reality. Although a larger number of people were economically active, they were not included in the plans and records of the national and international institutions. The national and international authorities for development and cooperation have reacted quite confusingly as regards to the "fugitives" of the National Development Plans, sometimes manifesting an open hostility, other times showing a benign indifference without being officially encouraged or assisted in doing so. The premise of the workforce analysis was that the problem was

a temporary one and that the development process that was amplified, respectively the “new modern sector” would gradually absorb this escaped workforce. Unfortunately, the “temporary problem” worsened and the gap in relation to the “modern” jobs increased to the extent that it could not be ignored. ILO’s reaction to this paradox consisted in putting in place The World Employment Programme -WEP. The first global mission in the field of employment occupation was held in Africa, the Kenya Mission, in 1972. During this mission the concept of informal sector was implemented.

The 70’s are considered the years of incubation. Although the concept was not embraced enthusiastically by the ILO, some changes were made to meet the challenges posed by the new concept. During the 70’s, a series of events hall-marked the informal sector in the context of the ILO. Among them one can mention the Tripartite World Conference on Employment - Income Distribution and Social Progress and the International Division of Labour (World Employment Conference, June 1976). For the first time, the WEP (1976) brought together the ministries of planning and finance with the ministries of labour at the same table to resolve the problems related to employment.

The 1980s- were the years of dispersion. The activities related to the informal system began to be addressed in other various major programs. The department of labor employment OIM through PIACT (The international programme for the improvement of working conditions and environment, known by its French acronym) included elements regarding the informal work sectors. Also in the 80s, the trend of speculation of the positive vision, idyllic, penciled in during the 70’s over the informal sector takes shape. The concept of “informal sector” has become synonymous with the poorest of the poor, with those who remained behind progress. The perspective on the subjects involved in the informal sector was focused more on “helping the victims” than on analyzing the causes. The vision with pauper accents of the informal sector had as a result the decrease in the expression of the strengths of this sector and made a vision over the informal sector as a viable approach, as originally presented, as an alternative to the formal economy.

The 90’s are recognized as the years of “institutionalization”, by incorporating the concept into the international official paradigm. A series of high profile events regarding the informal sector have marked this decade. Worth noting are two events that had a major impact on the importance of economic informality, namely: the inclusion of the informal sector on the agenda at the 15<sup>th</sup> International Conference of Labour Statisticians (ICLS) and the revision of SNA (System of National Accounts) under the overall leadership of the Statistical Commission of UN, with full technical and financial participation by Eurostat, IMF, World Bank, OECD and various UN specialized agencies.

The year 2002, a representative year for the first decade of the 2000, was a reference year for the ILO for addressing informality. Global recognition and magnitude of the phenomenon marked a

significant movement in the area of conceptual informality by switching from restricted terminology of "informal sector" in the new concept of "informal economy".

In some countries the term "informal economy" refers to the private sector and in other countries, the term is considered synonymous with "underground", "shadow" economy or "gray" (ILC 2002). The ILO unilateral vision over the informal economy is carried on the employment issue. According to the Angelescu *et al.* (2001, p.183) informal economy defies "the totality of undeclared economic activities of institutions in charge of setting taxes and social contributions, which escape from national accounting and statistical records." It can be said that informal economic activities (undeclared) are a starting point for defining informality in the economy. In this respect Neef *et al.* (2007, p.15) conducted an informal classification of activities (table 1) using various criteria analysis tools (illegal-legal, production-transfer, market economy-domestic economy).

**Table 1 - Types of informal activities**

		Market economy		Domestic economy	
		Illegal		Legal	
Production	1a/activities outside the law	Underground economy		Households	
		2a/tax evasion	3a/undeclared work	4a/production of goods and services in the household	
Transfer	1b/corruption	2b/shifts in nature between companies		4b1/ own consumption	4b2/ inter-household transfer

Source: Neef *et al.* 2007, p.15

## 2. Transition strategies

The informal economy was an analysis pretext for researchers, governments and various institutions. The etiology and the morphology related to the study of the informal economy revealed the extent and complexity of this economic phenomenon. Malignant influences at social and economic levels have put on the table the issue of "conversion" of the informal economy (even if not in all, at least in part) by identifying actions and strategies to ensure the transition from the informal area to the formal area.

Chen (2007) analyses the formal-informal relationship by reconsidering the connections between the informal economy and the formal economy through the formal regulatory environment. The author suggests that more "fair" links between the informal economy and the formal economy should be promoted through appropriate policy and regulatory framework. Studies of this kind perceive transition tacitly through the actions of "formalization" of the informal economy. With this understanding, the set of measures and regulations is possible whereby the "actors" of informal

economy can obtain should be promoted licenses, open accounts and pay taxes and customs more easily.

ILO was among the first institutions that saw the need for a coherent way of transition from the informal economy to the formal economy by putting this issue urgently on its agenda (ILO, 2014). The political discussions, debates and analyses have generated a diagnostic framework based on seven main approaches to formalization (figure 2). The diagnostic analysis underlines the importance of vertical integration and advocates for consistency in the entire range of refutable policies of informality, while the horizontal dimension focuses on intensifying the actions in each domain of action policies. The policy areas targeted are: strategies for economic growth and generating employment jobs (quality); regulatory environment including strengthening the international labor standards and fundamental rights, organization and representation and social dialogue; promoting equality gender, race, ethnicity, age, disability; measures - entrepreneurship, skills, finance, management, market access extension of social protection - building a platform of social protection and a system of social security; local development strategies (rural, urban).

**Figure 2 - Transition to Formality – Integrated Strategy**



Source: ILO, 2014, p.13

According to the opinion of Enste (2015) the shift from the informal sphere to the formal sphere can be approached by a two-pillar strategy: 1. Reducing attractiveness, the option called exit options (output from the underground economy); 2. Consolidation voice option (voting and participation). In this model constitutional elements should be consolidated and the instrument-forms of direct

democracy, such as referenda and legislative initiative should be introduced to give citizens more opportunities to participate in the process of decision-making and designing the tax system. Through this strategy a reduction of the attractiveness of the informal economy will be obtained (by diminishing the perception regarding the institution of restrictions as far as the personal liberty is concerned, stimulating fiscal morality, civic consciousness) and a shift towards the official economy.

**Table 2 - A two-pillar strategy for reducing the attractiveness of the existing option (shadow economy) and strengthening the voice option**

<b>Exit option</b>	<b>Voice option</b>
Reducing financial incentives to escape into the shadow economy	Strengthening popular participation in government
Improve and simplify the tax system to strengthen acceptance	Build trust and invest in social capital (for example, through support of corporate social responsibility)
Reform social security systems by strengthening the equivalence principle (more social tax contributions equals higher payments)	Reduce centralization
Boost efficiency in administration and combat corruption	Support more direct democratic elements in some areas
Focus on higher growth and welfare in the official sector to reduce pressure on government budgets	Encourage popular participation to increase commitment and loyalty and reduce free riding
Protect property rights and increase investment in infrastructure	Avoid attacking the symptoms through stricter controls, which encourages hiding participation in the shadow economy rather than reducing it

Source: Enste, 2015, p.9

### **3. Economic freedom vector of transition from the informal to the formal sector**

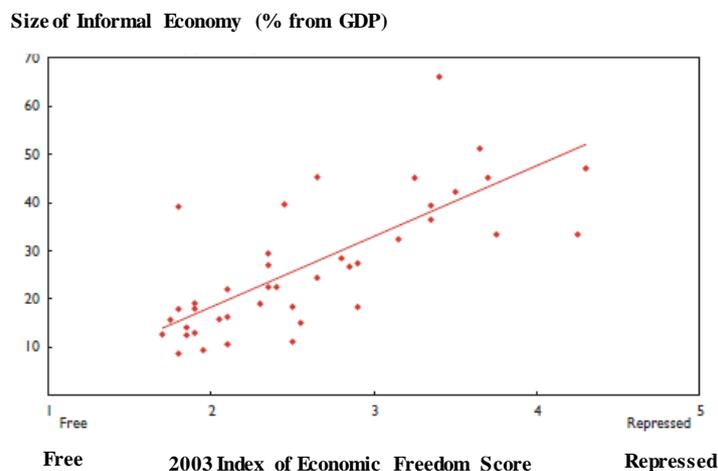
The transition theories developed by researchers or institutions will not prove effective in the absence of a genuine economic freedom. The concept of economic freedom seen in unity or through its components (property rights, freedom of business, financial freedom etc) is in our opinion a serious premise for realizing an effective transfer from the informal area to the formal one. The purpose of this initiative is to achieve a healthy economic and social development.

The Heritage Foundation and the Wall Street Journal have created in 1995 the economic freedom index (annual index) and a ranking based on it to measure the degree of economic freedom of the countries of the world. Economic freedom is defined as the fundamental right of every man to control (elevate) his work and his propriety. In a society free from the economic point of view,

individuals are free to work, produce, consume and invest in any way they want; governments allow labor, capital and goods to move freely; state institutions refrain from coercion or do not exert coercion beyond the extent necessary to protect and maintain liberty itself. Measuring economic freedom is based on 10 qualitative and quantitative factors, grouped into 4 broad categories or pillars of economic freedom: Rule of Law (property rights, freedom from corruption); Limited Government (fiscal freedom, government spending); Regulatory Efficiency (business freedom, labor freedom, monetary freedom); Open Markets (trade freedom, investment freedom, financial freedom)–(The Heritage Foundation, 2015).

Assuming that there is a statistically identifiable relationship between economic freedom and economic development Britton, Ford and Gay (2004) showed that there is a relationship between the economic development and the underground economy. In other words, the more economic freedom there is, the higher the GDP per capita; the higher the GDP per capita is, the lower the participation in the informal economy. The underground economy in Isaac Maniu’s opinion (2004, p. 236) is related to the construction of the economic freedom index that reflects restrictions, taxes and imperfections on the market. Ana Isabel Eiras (2003) considers that the index of economic freedom represents an excellent guide to identify the relationship between informal economic activity and economic freedom. Surveys show a positive correlation between the two factors, the informal economy and the economic freedom index. Figure 3 illustrates the relationship between the economic freedom and the size of the informal economy as a percentage of the GDP in 21 OECD countries and 22 economies in transition. In other words, the more the economic freedom decreases, the higher the share of the informal economy in the GDP.

**Figure 3- Economic Freedom and the Size of the Informal economy**



Source: Eiras, 2003, p. 2

Financial freedom is also expressed by assuring a reasonable access to lending. To have a better standard of living and (implicitly) to escape from poverty, people should have access to credit. In developed countries, for example, without credit, you cannot have a house, a car or a TV, a holiday or more that ensures comfort and convenience in daily life. The loan makes it possible (in the most varied ways) for a middle-class person to make improving the living standard a habit. Proof of income implies a formal job (official) and the property is established through a title. The existence of the informal economy is closely linked to the monetary sphere, in particular by the pronounced inclination towards liquidities (the lack of credit or the possibility of opening an account) that is manifested by those who work as payers or are being paid in this area (Craiu, 2004, p. 90). The motivation of this behaviour is obvious, cash transactions are less visible than banking operations. In a study commissioned by Visa it was pointed out that the underground economy is fuelled by several factors to include the predominance of cash and lack of transparency of transactions (ATKearne *et al.*, 2013).

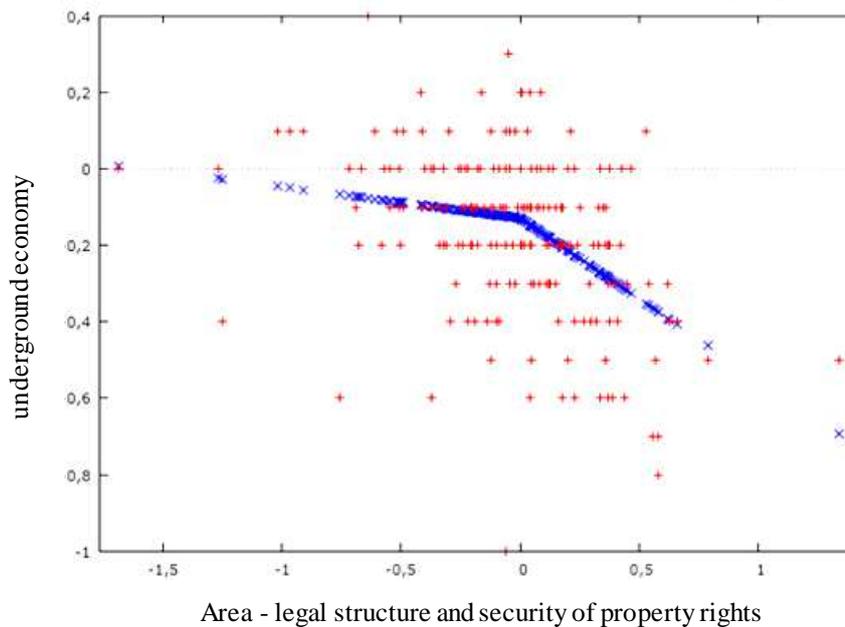
*The institution* of credit, as an output option from informal economy, highlights the fact that people in informal employment are doomed to a standard of living significantly lower than formally employed people (official) and that have access to credit.

We cannot speak of full economic freedom in the absence of full enjoyment of the property rights. Property rights are vital for providing information and signs about the opportunities of buyers and sellers, identifying the proper offers and realizing in safe and accurate conditions the ownership transfer. The relationship between the economic effects of secure property rights and a legal system that works was well explained by Feulner (2002, p. 5). People seen as “economic” actors act primarily in their own interest and tend to carry on with work and investments only if they have a reasonable likelihood of enjoying the fruits of their efforts. In the event that property rights are less secure for example, because of high crime rates or high taxation, people tend to work less and invest less. In other words, the security of private property rights promotes development and facilitates the monetized formal economy. In the situation in which private property rights are weakened, people would have more energy and act with greater dedication in order to avoid formal markets and the integration in the underground economy.

Freytag *et al.* (2013) have shown that economic freedom can be regarded as a global indicator or through two sub-components (1) legal structure and security of property rights and (2) the freedom of international trade that can influence the size and evolution of the underground economy. The greater the economic freedom is, the smaller the size and development of an underground economy. The changes of the freedom index constitute a bench-mark of the involvement or non-involvement in

the underground economy, by the fact that people are more easily willing to leave the underground economy than step into the informal sector. Studies have shown that sub-indices “structure and security of property rights” have by far the greatest impact on the scale and development of the economy. The better the legal system is and the higher the security of the property rights is the smaller the underground economy (comprising the underground economy has as effect an exit from the informality sphere followed by an input in the formal area).

**Figure 4 –The relationship between the changes in the underground economy and changes of economic freedom (area - legal structure and security of property rights)**



Source: Freytag *et al.*, 2013, p. 11

For example (figure 4), when the rate of change of "legal structure and security of property rights" increases with a unit, there is a decrease of 0.19 percentage points in changing the underground economy. In the situation in which the changing rate of the indicator "legal structure and security of property rights" is negative and decreases with a supplementary unit, there will be an increase of 0.014 percentage points in the rate of change of the underground economy.

### Conclusions

Informality creates a culture of contempt for the law, encourages corruption and bribery in the public sector, thus affecting the necessary and beneficial economic freedom. Strengthening the health and legality of an official economy is achieved by implementing through the researchers agenda, government and institutions, the transition from informal to formal. The purpose of this study lies in

the need to achieve integrated transition strategies that can be more easily assessed and measured. The mere reference to the GDP, employment or tax fraud is not sufficient. In our opinion, any transition is doomed to failure if it doesn't consider true economic freedom. Economic, quasieconomic and noneconomic factors that are found in the structure of economic freedom represent reference or action modalities in order to achieve an effective transition to a performant economy. Whether it is the ILO or the national governments, economic freedom should constitute a barometer of official-non official or legal-illegal rapport. In practical terms, based on accurate and well-substantiated scientific criteria can be prerequisites for an assessment of the transition from informal to formal.

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### **Annex 1**

1969 - World Employment Programme (WEP);

1984 – ICFTU (International Confederation of Free Trade Unions) – Conference resolution on the informal sector;

1989 - IOE (International Organisation of Employers) - Seminar on the informal sector;

1991- The dilemma of the informal sector, Report of the Director General, International Labour Conference (ILC), 78th Session;

1993 - International Conference of Labour Statisticians (ICLS) – standard on informal sector statistics;

1993-System of National Accounts (SNA) – incorporates informal sector;

1994 - 1995 Interdepartmental Project on the Informal Sector – INTERDEP - informal sector statistics.

## AN ANALYSIS OF THE "BIO" / "ECO" PRODUCTS MARKET, REFERRING TO THE EU AND ROMANIA

Ionel BOSTAN\*

**Abstract:** *The EU and Canada represent the largest market in the world for the sale of ecological products attracting exports from many third countries and recording a total sale of 95% of the worldwide total market. The European market for ecological products – also known as “bio” / “eco” – in absolute figures – is somewhere around 20 billiards euro/year, and in the case of Romania, the market for those products varies around 200 million euro/year. According to European legislation, there are harmonized provisions and procedures for the import of ecological products which can be implemented in two ways: either by complying with the EU legislation on ecologic products, or based on the equivalence between the existent standards and control systems. In many European countries, the operators on such a market obey the rules established by Legislation for ecologic productions strictly. In Romania, a sanctioning system against those economic operators who fraudulently use product labels suggesting they are organic products has just recently been considered. Taking into consideration all these aspects, the present paper relies on the most recent bibliographic and statistical references in this field.*

**Keywords:** environment; ecological production; organic food; biological agriculture; exports; internal market; regulations on “bio”/“eco” products

**JEL Classification:** K2; Q1; Q5

### Introductory considerations

Ecological farming is intended to produce healthier food and food more appropriate to the human metabolism, this type of farming being highly correlated to the preservation and the development of the environment, referring to that system of agriculture similar to “organic farming” or “biological farming”, that used by other EU member states (MARD, 2013).

It is more and more acknowledged nowadays that this type of agriculture plays a key role in sustainable development, in increasing the economic activities with important value added and increasing the interest in rural areas.

Referring to the ecological production, we point out that it represents in fact a global system of administering agricultural exploitations and food production having as objective sustainable farming, obtaining high quality products and using processes that are not harmful to the environment, human health, plants, animals or animal well-being (ECA, 2012).

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The characteristics and the benefits of “bio” products could be presented as follows (BIOSENS, 2012):

- Absence of chemical substances (pesticides, synthetic substances etc.) which, after being used for a long period of time, are harmful to humans and to the environment;
- Nutritional quality: “bio” products contain up to 40 % more antioxidants, more essential minerals and higher amount of nutrients than regular food products;
- Ecological products are characterized by a high content of amino acids, vitamins and oil elements;
- Contribute to saving the environment – biological agriculture is a production process that respects biodiversity and the natural balance;
- Biological cosmetic products are highly nourishing; they consist of important active ingredients for the body with long term effects;
- Not being contaminated with pesticides or mycotoxins, organically certified products can prevent early ageing, chronic diseases and can increase work capacity.

Ecological products (“bio”/“eco”) – considered “premium” products – are obtained by respecting a precise set of rules, like the rotation of cultures, use of genetically modified organisms is forbidden and very strict limits to the use of synthetic chemical pesticides and chemical fertilizers, animal antibiotics, food additives etc. in the processing of agricultural products (Table 1).

**Table 1 - “Bio” / “Eco” product in relation with both natural and chemical product**

<b>”Bio”/”eco” product</b>	<b>Natural product</b>	<b>Chemical product</b>
<ul style="list-style-type: none"> <li>• cultivated in non-polluted areas</li> <li>• the species and the varieties used are characterized by high resistance to environmental conditions</li> <li>• naturally fertilized soil</li> <li>• feed is prepared with raw materials allowed by the standards of ecological farming</li> <li>• products are not genetically modified</li> <li>• No synthetic chemical additives are used</li> </ul>	<ul style="list-style-type: none"> <li>• Are obtained in agriculture without the use of chemical substances</li> </ul>	<ul style="list-style-type: none"> <li>• Are also obtained in agriculture but assume the use of chemical substances</li> </ul>

Source: SSAJ, 2012

“Bio” products have shorter validity terms than regular products as they don’t include synthesis food additives – conservatives, colorants, taste and thickening agents (BIOSENS, 2012).

In the conditions presented here, these products are generally more expensive than conventional products.

### **1. Agriculture and ecological production in the European area**

The issues repave represented the main subject of various specialty papers – directly (Kilcher *et al.*, 2011; Lampkin, 1999; Mitchell *et al.*, 1997; Fitiu, 2007; Costin, 2008) or indirectly (Stefan *et al.*, 2013; Toncea *et al.*, 2013), that were received with interest by those interested in this important field.

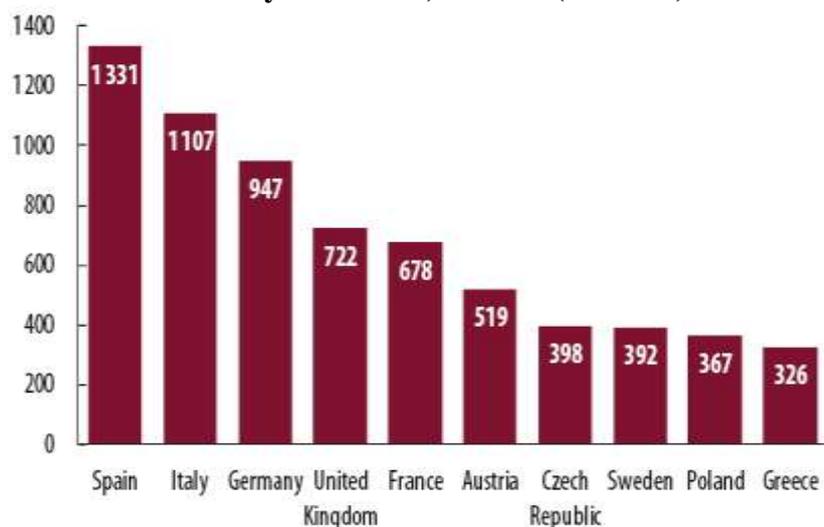
From a legislative point of view, given the importance of the subject (Simiz et al, 2013), the catering sector is subjected to EU regulations on hygiene and food product labelling (EC, 2007; COM, 2008a; COM, 2008b), which state that the labels referring to the production process cannot be used so to mislead the buyers (EP, 2000). As a matter of fact, the objectives, principles and norms applicable to ecological productions are included in the EU and national legislations in this field. These rules, apart from defining the production method in the plant, animal and aquaculture production sectors, regulate the multiple aspects related to the system of ecological farming: the processing, labelling, commerce, import, inspection and certification (MARD, 2013).

According to a report of the European Commission for the European Parliament and the Council on the application of EC Regulation no. 834/2007 (COM, 2012), seven member states have introduced national norms, while other ten member states use private standards. These rules focus on certifying ingredients, types of foods, menus or operations carried out in the catering sector in general.

Considering the total surface of land used in ecological farming, almost 8.6 million hectares are used for this in the EU (4.7% - EU 27/2009); the number of companies involved being of almost 200 000 (1.4% - EU 27/2009).

Figure 1 presents the situation of the EU member states with the largest surfaces used in organic farming.

**Figure 1 - The 10 EU Member States with the most organic agricultural land (in conversion and fully converted) in 2009 (1 000 ha)**



Source: ECA, 2012; Willer, 2009

The largest organic surfaces are cultivated in Spain, Italy and Germany which own 40% of the cultivated land in organic farming in EU, estimated at almost 9 million hectares. If Austria, Sweden or Estonia cultivate between 13 and 20 % of their land organically, Romania, Bulgaria and Ireland have the lowest percentage among the member states (below 2%) (Capital, 2012). The European market for organic products is estimated at 20 billiards Euro/year (Willer, 2009), which represents a market share of 1.5% of the food market in general (FiBL, 2008).

The average amount of organic food consumed in the eastern part of Europe is 3-5 %. In Germany the consumption level is 5% and in England and Austria, 3%. The average in Western Europe is 3 – 5%, in Hungary it has reached 2% while in Romania it is just above 1%.

What should be known is that almost 15% of the organic products consumed in Europe are imported from third countries (ECA, 2012), they are mainly products rarely or not at all cultivated in the EU (coffee, bananas, cotton etc.).

## **2. Analysis of the evolution and the trends of organic farming in Romania**

Among the strategic management actions for assimilating and putting into practice the principles of sustainable development in Romania we find the one related to ensuring food security and safety by capitalizing the competitive advantages of the country in developing agricultural production, including organic products (MECC, 2013). At the same time, this action considers the correlation of those measures related to quantitative and qualitative increase of agricultural

production for ensuring food for people and animals with the request of increasing the production of biofuels, without leaving aside the requirements on maintaining and increasing soil fertility, biodiversity and environmental protection.

An important measure included in the National Rural Development Program (NRDP) which refers to recreating and protecting biodiversity on agricultural lands (MARD, 2014), focuses on providing the necessary protection to natural resources by encouraging organic farming of almost 80 000 ha of agricultural land.

On a whole, organic farming is a dynamic sector in Romania and in the last few years it has recorded an increasing trend (Table 2).

**Table 2 - The evolution of organic farming in Romania, 2006 – 2012**

<b>Indicator</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>
• number of operators registered in organic farming	3 409	3834	4191	3228	3155	9703	15544
• surface cultivated in organic farming - arable land (ha)	45605	65112	86454	110014.4	148033.5	147581.55	174644
• permanently surface cultivated – pastures and hayfields (ha)	51200	57600	46006.5	39232.8	31579.11	78197.51	105836
• orchards and vineyards (ha)	294	954	1518	1869.4	3093.04	4166,62	7781
• collection from spontaneous flora (ha)	38700	58728	81279	88883.4	77294.35	338051	1082138

Source: MARD, 2013

This is due to the fact that Romania, through MARD (Ministry of Agriculture and Rural Development) provides specific financial support for the conversion period (EC, 2009; GR, 2010) making additional annual payments for exploitation.

The conversion period varies for the plant, animal and apiculture production (GR, 2000; AE - Zi de zi, 2007) as follows: 2 years for annual cultures, 3 years for perennial cultures and plantations, 2 years for lawns and feed cultures, 12 months for beef cattle, 6 months for small ruminants and pigs, 6 months for animals, 10 weeks for poultry bought at the age of 3 days, 6 weeks for egg laying birds, 1 year for bees if the family was bought from conventional bee gardens.

The organic farming package has been included in the National Sustainable Development Programme (MARD, 2014); at the same time, the organic beekeeping sector is supported along with conventional apiculture, through the National Apiarian Programme (GR, 2013).

Another measure that focuses on promoting products is represented by the financial support provided by the European Commission consisting in financing 50 % of the value of the promotion programs proposed by professional and inter-professional organisations within the sector which participate with at least 20% of the real cost of the actions, 30% of the value being covered from the state budget.

The significant potential in obtaining organic products (food) refers to all the development regions of Romania (Figure 2).

**Figure 2 - Production of organic products distributed on counties**



Source: MECBE, 2011

For promoting Romanian organic products, both on the European and the international markets, the state supports 50% of the costs the economic agents have with participating at fairs and international exhibitions (MECBE, 2010).

If we consider the latest studies (Cauea, 2013), Romania is placed in the first 15 exporters of organic raw materials, with more than 300 000 hectares of organically certified agricultural land. Moreover, in 2011 it was placed in the first place worldwide according to the increasing the number of farmers certified in the organic system.

The market for “bio” products (Table 3) varies somewhere around 150 million euro/year and has increased continuously, being on a continuous increase, the best sold products being fruits and vegetables, followed by bee honey, dairy products, eggs etc.

**Table 3 - Products specific to the Romanian “bio” market**

“Bio” food products	“Bio” non-food products
<ul style="list-style-type: none"> <li>• <i>vegetables, fruits</i></li> <li>• <i>honey and bee products</i></li> <li>• <i>teas</i></li> <li>• <i>dairy products and cheese varieties</i></li> <li>• <i>wine, juice</i></li> <li>• <i>bread, flour and bakery products</i></li> <li>• <i>oils</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>cosmetics</i> (make-up and beauty products, intimate care products)</li> <li>• <i>organic textiles</i> (organic clothes, linens)</li> <li>• <i>household appliances</i> (mills for grinding cereals, germination pots, fresh juice for germinated cereals, soya milk appliances, appliances for drying fruits and vegetables etc.)</li> <li>• <i>children care</i> (organic creams and lotions, organic dippers, napkins for intimate hygiene)</li> </ul>

<ul style="list-style-type: none"> <li>• <i>soya products</i></li> <li>• <i>baby food</i></li> <li>• <i>nutritional supplements etc.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>household</i> (detergent, laundry balm and whitener: have less chemical substances; cleaning solutions)</li> <li>• <i>relaxation products</i> (bathroom products, massage and aromatherapy products)</li> <li>• <i>organic rubber</i> etc.</li> </ul>
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Source: BIOSENS, 2012

The tendency for the next period is that the “bio” products commercialized in Romania will be sold in proportion of 60% in organic shops, 30% in supermarkets and 10% in other types of shops.

The value of the exported “bio” products is of almost 250 million euro/year (more than 90% represent raw materials, the highest amount exported in the recent past being registered as cereals, berries and wine) and the main export markets are the states from Western Europe such as Germany, Austria, France and Denmark but also USA to where cereals and corn are delivered (Business – 24, 2013).

In the future, the values presented might grow especially if measures like the ones below are put into practice (PCPPAD, 2013):

- Drawing up a national action plan for organic farming, simultaneous with the adoption of an institutional framework capable of inspiring consumer confidence in “bio” products;
- Analysing and improving MARD competences in inspecting and certifying the Romanian “bio” products;
- Organizing and systematically controlling the entire chain of “bio” products and eliminating the possibility of falsifying the “bio” certificates in Romania;
- Obtaining the maximum financial support offered by the EU for the Romanian “bio” farmers, having an appropriate economic basise;
- Drawing up a coherent subvention system for “bio” products and “bio” processing in particular for obtaining value added products;
- Applying lower VAT values to the basic organic products.

At the same time, it is also necessary to stimulate the “bio” processing sector by providing support through PNDR from 75% to 90% of the value of the investments coordinated by the Payment Agency for Rural Development and Fisheries.

### **3. Adjusting the institutional framework necessary for establishing contraventions and applying sanctions as regard to the status of “bio” / “eco” products**

The measures and the sanctions necessary for respecting the provisions of CE Regulation no. 834/2007 concerning both organic production and the labelling process of organic products have been established relatively recently in Romania. They were adopted through a Government Decision in 2013 (GR, 2013).

In fact, the previously mentioned legal document creates the legal framework necessary for establishing contraventions and applying sanctions in the field of organic farming; based on it, the staff responsible for technical inspections in the field of organic farming from the management bodies in agriculture has the possibility to apply contraventions in more situations.

Thus, for the fraudulent use of the terms “ecologic”, “biologic” and “organic” or their abbreviations “eco” or “bio”, as commercial marks or usage practices during the production, processing, packaging, transportation, storing and product distribution, including on the product’s label, advertising materials and commercial documents, which can mislead the consumer and which are not obtained according to the rules of organic production, the applicable fines range from 20,000 to 30,000 lei. The measure to withdraw the operator from the commercialization of the products in question can be added.

The violation of the rules regarding producing, processing, packaging, transportation, storing, distribution and import of organic products from third countries can lead to sanctions between 10 000 and 20 000 lei. The fine is higher (25 000 lei – 35 000 lei), in case the operator’s documents are missing, including those related to the production evidence, transactions and the stocks of all ecologic products through which the product can be tracked during all the phases.

In case certain commercials do not allow the access of the inspector designated by MARD within the unit, or if they refuse to present the documents and the control registers, the law maker established the application of a fine ranging between 20 000 and 30 000 lei.

In spite of all the interest for legalizing coercive measures, the phenomenon cannot be completely controlled if we consider the small number of people in charge with making such controls within a county (up to 5 people). Nonetheless, in our opinion, once things have started to be on the right course, the situation can be improved.

## Conclusions

For the time being the request for “bio” / “eco” products is higher every time, as the consumers are more and more interested in them. In Romania (2007 – 2012) the land surface cultivated organically and the number of operators involved have increased several times, as has the number of animals bred using ecological methods, especially sheep and goats, dairy cows, laying hens and bee families.

Nonetheless when referring to capitalizing on organic products, they are mostly commercialized as unprocessed (raw material). Or, the interest is to distribute processed products with high added value at large scales.

Hence, the priorities in the field in question focus on selling organic products with high value added, identifying new export markets and the development of an effective processing and distribution system.

In our opinion, for the development of the sector we refer to, fiscal measures should also be used. Here, we consider VAT reduction for the “bio” sector, which would be equivalent to the development of the organic processing sector in Romania and, quite probably, will lead to a new explosion of the industry after the one in 2012 when EU subventions were introduced.

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## O.S.C.E. 1975-2015. 40 YEARS OF PEACEFUL CONFLICT RESOLUTION

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**Abstract:** *The European Union, in light of developments in the field of crisis-management concepts, is still in the phase of institutional building and foundation of its own concepts and doctrines. This does not mean that the EU has taken important steps towards the creation of a doctrine based on a crystallized concept of crisis management. It should be noted at this point that since 2004 the EU has defined a comprehensive approach to crisis management. However, although conceptually placed one step ahead of NATO's comprehensive approach, operational in concept, its actual implementation has proved to be a slow and difficult process for the EU because the EU does not have a military component of its own, being much more focused on the civilian crisis management component as part of its comprehensive approach and on the idea of cooperative security, where the EU has managed to become a major player in the area of strategic interest on the global scene.*

**Keywords:** O.S.C.E.; crisis management

The security environment is in a constant dynamic, accelerated by the globalization processes, thus causing a dynamic in the conceptualization of crisis management by the various security organizations involved.

One can notice how the world we live in has changed the balance of power from the end of the second world conflagration to a tense bipolar balance until 1989, passing through relatively short periods of unipolarity and then multipolar balance, and nowadays we are witnessing a new kind of balance of power of an interpolar type.

The latter, interpolarism, is a consequence of globalization and of the existence of several power poles, which include actors that do not belong to only one power pole but are part of and act in several centers of power, either regional or global. A significant example is our country, Romania, which is part of the European Union, NATO, UN and also an OSCE participating State.

In this particular context, the crises occurring in the international environment present a high degree of complexity, which leads to solutions with an appropriate response, with a high degree of complexity and requiring a constant adjustment of the concept of crisis management.

Covering a generous geographical area, from Vancouver to Vladivostok, we can say that the OSCE is an extensive regional security organization, contributing to the consolidation of peace, democracy and stability in the world.

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OSCE proved to be a useful forum for high level political dialogue, comprising a wide range of security issues, and at the same time acting as a regional instrument for early warning, conflict prevention, crisis management and post-conflict rehabilitation, aimed firstly, at cooperation, the determining factor in building trust between states.

Through the institutions that make up its structure, the units of experts and the network of field missions, the OSCE has proved that it has abilities to act in various fields with an impact on common security: conventional weapons control, measures for increasing trust and security; combating transnational threats; economic activities in the field of environment; promotion of human rights and fundamental freedoms and democratization.

The organization has its roots in the early '70s, the Helsinki Final Act being adopted in 1975, which led to the creation of the Conference on Security and Co-operation in Europe (CSCE), which, throughout the Cold War, provided support for multilateral dialogue and negotiation between the East and the West.

In the context of the fall of the Berlin Wall, the Charter of Paris of 1990 reflected the desire of the participating States for a new "era of democracy, peace and unity" and sealed the end of the Cold War.

After the adoption of the Charter of Paris, the CSCE gained some permanent institutions: the Secretariat and Conflict Prevention Centre; the Office for Democratic Institutions and Human Rights, as well as operational capabilities. Since 1992, the Security Cooperation Forum, the Economic and Environmental Forum and the High Commissioner on National Minorities have also been created.

However, it has to be noted that until the signing the Helsinki Final Act in 1975, the history of the Conference on Security and Co-operation in Europe (CSCE) spanned over two decades of debate, more or less intense or frequent, between Moscow and Washington.

The first step or initiative in this debate belonged to the Soviet Foreign Ministry at the time, Vyacheslav Molotov, and ended unsuccessfully in 1954. Moscow's wish was to organize a European conference, without the participation of the United States, in order to legitimize a new distribution of forces on the European continent, and with the express requirement to dismantle the newly established NATO.

The plan of the conference initiated by Moscow reached a deadlock until 1969, a year after the intervention of the Warsaw Treaty Organization in Czechoslovakia, when, eager to get a formal agreement on the geopolitical situation in Europe, the Soviet Union renewed its proposal, giving up, this time, on the issues it defended earlier on, namely the rejection of the participation of the United States and on the abolition of NATO.

Moscow's come back, in 1969, to the idea to renew the proposal to organize the conference made Henry Kissinger, Secretary of State and National Security Adviser of the US to state: "Once the European Security Conference did not have as purpose to replace the Atlantic Alliance and confirmed the United States as a European power, the Soviet policy was found on the defensive.

The purpose of stabilizing the relationships between the two blocks (...) signified that, at least with regard to Europe, Moscow will now be on the defensive, trying to preserve what it obtained."(Kissinger, 2000, p. 635-637).

In good American tradition, this analysis performed by Henry Kissinger is partisan, exaggerating the threat of the Soviet Union with the sole purpose to counteract as efficient as possible, by using similar means to those he blamed Kremlin for using. By doing so, the former Secretary of State made a pertinent analysis of the position of the USSR in the mid 70's in order to increase the insecurity of Moscow and, at the same time, global security.

The Conference on Security and Co-operation in Europe (CSCE) comprised three major pillars: „security, economic cooperation and humanitarian cooperation” (Dobrynin, 1995, p. 345).

Anatoly Dobrynin (1995), ex-Soviet Ambassador in Washington, recalls that Moscow was only concerned with maintaining stability and with the enhancement of economic relations, denying or minimizing the importance of human rights. The West did not give up, thus forcing in the end Brezhnev and his acolytes to sign the final document.

Both Washington and Moscow made concessions, but both sides considered that, overall, the result will be favorable on the medium term as well as on the long term (Vincent, 1995, p. 55). Moscow's calculations have, however, proved to be inaccurate. This is because on signing the final version in the Political Bureau of the CPSU (Communist Party of the Soviet Union) major reservations were expressed, the final version being negotiated word by word by experts and politicians from the two camps, but eventually Leonid Brezhnev weight in favor of signing the document.

The caution shown by the General Secretary of the CPSU was due to the fear of the positive publicity that the document could have won at home, "when the Soviet public would have learned of the final agreement on the postwar borders, for which he sacrificed so much", as well as its receival in the West:

"In terms of humanitarian issues, they could have been mentioned only vaguely home, without much publicity. He thought that this will not bring much trouble within our country, but he was wrong. The situation of the Soviet dissidents has not changed overnight, but they were undoubtedly encouraged by this historic document. Even its publication in Pravda gave it the weight of a formal

document. Gradually, it became a manifesto of the dissident and liberal movement, an evolution totally beyond the imagination of Soviet leadership (underlined in orig.)." (Dobrynin, 1995, p. 346).

It turned out that the acceptance of the West or "bourgeois" variant of human rights brought major ideological and political issues for Moscow, both in the USSR as well as in the entire communist camp.

In Washington, it was also not easy for the Secretary of State Henry Kissinger to convince the ultra-conservatives within the Congress of the usefulness of the conference. They considered that the United States had made the biggest ideological concessions by legitimizing the existence of the socialist camp (Dobrynin, 1995, p. 347-348).

While accepting the European borders as agreed upon after 1945, the West introduced, under the pressure and the categorical insistence of the FRG, the possibility of peaceful territorial reunification. If the separation between the two Germanies had been deemed "inviolable", the path was opened then, at least in theory, for a non-violent reunification of Germany (Kissinger, 2000, p. 639), and this indeed happened much faster than anyone could have foreseen at that time.

What one can notice in this brief introduction to the topic, addressed within the CSCE, is that what constituted the "apple of discord" between East and West, the significance given to human rights, will be a philosophy that will take over American foreign policy in the second half of the 70's. By reading article seven, chapter three of the Conference document one can clearly understand the Western, liberal meaning of the phrase: "The participating States will respect the human rights and the fundamental freedoms, including freedom of thought, conscience, religion or belief, for all without distinction as to race, sex, language or religion" (Oxford University Press, 1991, p. 160-162).

The adoption, even superficial, of the liberal principles of human rights, from an ideological point of view, proved to be the result of an unacceptable commodity in the context of what should have been the fight against the "bourgeois" reality, entailing a weakening of the "revolutionary vigilance" that resulted in the slow and inevitable "bourgeois character" of the communist principles.

The new humanitarian rules and criteria advanced by the West played precisely this role, to deeply and lastingly delegitimize the principles of communism, as well as the other initiatives: the "«Helsinki monitoring groups » have increased in several countries of the east block, of which the most famous was Charter 77 in Czechoslovakia. They interpreted the Helsinki Final Act as the consecration of human rights in international law - a vision that we fully support". (Kissinger, 2000, p. 648).

It should be reminded that, especially during the Carter presidency (1977-1980), human rights, in addition to a moral concept underlying the US militant democratic vision of their global role

represented an excellent instrument of political pressure against regimes from Eastern Europe. Ambassador Dobrynin recalls that President Carter “really believed that it is morally justified to defend human rights”, but at the same time, “saw the issue as a weapon of propaganda convenient (yea, really!!) in order to manifest public discontent at the expense of agreements on other major issues from the Soviet-American relations” (Dobrynin,1995, p. 389), such as economic cooperation or negotiations for disarmament and nuclear nonproliferation.

According to Carter's adviser in matters of national security, Zbigniew Brzezinski, the Ford administration had exploited insufficiently at an international level the idea of human rights, which, he thought, could be a useful ideological counterweight for the presumptive expansionist tendencies of global communism (Zbigniew Brzezinski, 1983, p. 124).

Bucharest made itself noticed in the context of the preparations for the conference in Helsinki in 1975, on several points: stressing the need to treat states equally at an international level, to renounce to force in resolving disputes between the state, to recognize the inviolability of existing borders and, a very important point for Ceausescu, the "noninterference in domestic affairs" (González-Aldea, 1975, p. 32). Secretary of State Henry Kissinger was made aware, on this occasion, of the wishes expressed by Romania, Poland and even Hungary to obtain increased spaces for maneuver relative to the center from Moscow (Kissinger, 2000, p.645).

Romania made itself noticed, though, also by not accepting, on a virulent tone, the "Western" variant of human rights, which led to hinder, from a procedural standpoint, the conference, but especially to continue discussing the principles issued within it in the coming years.

The re-initiative of the conference, taken by Moscow in the late 60's, led the Romanian communists to follow with great interest the preparations for the CSCE.

Nicolae Ceausescu, who wanted to benefit from a greater influence in favor of Romania at European and even global level, propagated the favorite subjects of discussion, such as terminating the war and the "threat of force", boosting the "international proletariat", in particular the working class from the "capitalist countries" in the struggle to achieve his social and political rights, from which he was systematically robbed by the governments subservient to "imperialism", supporting the youth and women at an international level (of course, only to the extent in which they possessed or developed a proper "socialist conscience"), the growing role of the "small and medium countries" in the world and the moral need for the decision-making "equalization" of all states in international affairs, the renunciation at the politic of the "blocs" and the concomitant dissolution of NATO and the Warsaw Treaty Organization, a necessary measure in order to eliminate "foreign military bases" and " to withdraw all troops from the territories of other States, within the limit of their national

borders" and, not least, on strictly European issues, "acknowledgement of the existence of two German States ", the GDR and the FRG," and the development of normal relations with the two, in order for them to participate in solving all European issues (emphasis. in orig.)"(Ceausescu, 1970, p. 39-56).

In the preparatory phase of the conference, the representative of Romania, Valentin Lipatti, protested in 1972 against the holding by Great Britain, France, the Soviet Union and the United States of three seats each, while other countries had to be content with only two. "Romanian diplomacy has paid off, so the next day all delegations benefited from two seats." (González-Aldea, 1975, p. 19).

During the conference Romania did not have a clear position, it was neither on the West nor on the "socialist camp's" side and did not make any effort to integrate into the camp of the Third World; it adopted, except on the human rights issues, where it proved to be more virulent than the Soviet Union itself, a specific tone, trying to get as many advantages, irrespective of which side they came from. Spain, Yugoslavia and the Vatican did the same, for more or less obvious reasons (González-Aldea, 1975 p. 27).

We may conclude that during the conference Romania wanted to become a highly visible presence, personifying the romantic notion of Ceausescu, of the little "Prince Charming" caught in a heroic battle with the "dragons of the modern world". (Ceausescu, 1970, p. 325-326), but failed, to the dismay of the Secretary General of RCP (Romanian Communist Party), to overcome the condition of a small state, with little relevance in the dichotomous logic of the Cold War. "« He had a fertile and perfidious participation»", "the Spanish diplomat Jorge Fuentes appreciates, "often inappropriate, sometimes defeated, but always full of imagination" (González-Aldea, op. cit., 1975, p. 28).

With such a position on display within the conference, Romania 'made upset' even the Soviet Union, to some extent, by insisting constantly on the respect for the national sovereignty and the non-interference in the internal affairs, because the major purpose of Moscow in the Conference on Security and Co-operation in Europe consisted in legitimizing its influence over Eastern Europe (King, 1972, p. 1-25).

The issue of continuing to develop the ideas of the conference was raised even after signing the Final Act with the clear aim of implementing and developing the principles that have been brought to the forefront of the discussions. Romania and Yugoslavia got themselves noticed as the two socialist countries hoping to broaden their power of decision in relation to Moscow.

Had the international environment not been tense, then it would have allowed Romania to focus on its foreign policy interests without irritating Moscow too much (King, 1972, p. 3-4).

The fear of the socialist countries was that the West will use the conference as a means of enhancing the injunctions for complying with the humanitarian principles, issue on which a formal agreement was reached for the first time.

On the other hand, the Western countries were concerned about the possibility of transforming the conference into a dissemination tool of the communist propaganda towards the West. The fears that came true in the end were those of the socialist states.

At the next meeting of the Conference on Security and Co-operation in Europe, which was held in Belgrade between 1997 and 1978, Romania was represented by its ambassador, Valentin Lipatti, who said that this meeting ended 'with unsatisfactory results' (Lipatti, 1985, p. 137) because the consensus reached at Helsinki had disappeared: the East was insisting on the political and economic issues, the West wasn't hesitating to hit the most vulnerable point, the (non-) compliance with the humanitarian commitments. The differences amplified, and, in the absence of an agreed conclusion, the mechanical repetition of the statements made in the Final Act was used (González-Aldea, 1975, p. 62-65).

At the conference in Belgrade, the focus was on some ideological, humanitarian issues, correlatively neglecting the economic or social problems. Another downside of the reunion lay in the fact that it was purely advisory, 'not having the ability to take decisions' that are compelling for the participants (Lipatti, 1985, p. 139). The socialist states, including Romania, had been disturbed by the fact that the Western countries were criticizing them for the lack of implementing the respect for human rights, which led to 'polemics and ideological confrontations'; Valentin Lipatti criticized somewhat paradoxically the 'advisory' nature of the reunion, its inability to establish binding decisions for the participating states.

The inter-ideological polemics amplified at the conference in Madrid, and the political tensions reached their peak. The intervention of the USSR in Afghanistan in conjunction with the Western pressures on the subject of the need of respecting the human rights have greatly contributed to the decline of the relaxation of the global tensions.

The fact that Mihail Gorbaciov reached the position of leader of the Soviet Union made the situation change fundamentally at the conference in Vienna, conference which was conducted in the second part of the 80s. Mihail Gorbaciov proved more receptivity to the humanitarian problems, thus easing the opening of the gates for the EAST-WEST dialogue and bringing a major contribution in ending the Cold War (González-Aldea, 1975, p. 20).

In 1981, Dumitru Tinu condemned vehemently the humanitarian obligations incumbent on Romania, in the context of the Conference on Security and Co-operation in Europe, arguing that the

number of dissenters is a small percentage compared to the total population, them being only ‘victims of the propaganda of incitement to emigration carried out by the reactionary circles, hostile to the extension, to serve the monopolies interested in increasing the millions of uprooted wonderers, cheap manpower, reliable source for over-profit. These are the true ... «humanitarian» purposes of the campaign demagogically initiated after the Conference from Helsinki and which aimed the transformation of the European reunions into a kind of «international courts» designed to judge the policy of various states, their domestic laws’ (Tinu, 1981, p. 159).

Even if it seems paradoxical considering the international position that it had, Romania wanted to dictate the rules of the game, and not accept or accept only selectively the rules established by the other participants in the Conference on Security and Co-operation in Europe.

Romania insisted on the disarmament issue (although it did not have an impressive arsenal), on the pacification and ‘democratization’ of the international relationships (which were equivalent to the equalization of the power of decision on all states externally and the adoption of decisions only by consensus – a measure that apparently was courting the ‘bourgeois’ morality, being however unable to put into practice in the detriment of the bombastic enthusiasm of the Romanian diplomacy; Nicolae Ceausescu would have thus made his contribution in creating the conditions for the settlement of the most tricky international disagreements, becoming a global leader) and, finally, on the articulation of an European framework for security through economic and political cooperation, and not necessarily through cultural and social cooperation. In fact, Romulus Neagu said that the basic principles of the Conference on Security and Co-operation in Europe would not represent anything else than the confirmation of the innovative thinking of Ceausescu at international level... (Neagu, 1976, p. 261).

The reformation of the former Conference on Security and Co-operation in Europe, the establishment of the Organization for Security and Co-operation in Europe and the affirmation in the geopolitical and strategic background of the modern world, alongside other international organizations and bodies focused on missions of peace enforcement / keeping did not lead only to the animation of the security ‘scene’, but it capped in to an equal extent the perseverance of the participating states’ leaders to counter by all means, mechanisms and instruments the disasters that undermines the worldwide peace and stability, bringing a serious and irreparable prejudice to the human rights, the principles of the international law and the social order.

If we want to compare this to the approach of the Council of Europe on the protection of the human rights, we will find that the latter has a legal touch, where according to which the EU places a great emphasis on supranational institutions and mechanisms, the Organization for Security and Co-operation in Europe, (richer in the number of the participating states and with implications which

exceed the Europe's borders such as North America, Mediterranean, Far East of the Russian Federation), has as objectives the relationships between security and economic cooperation, plus the democratic liberties, gradually advancing an original mechanism of the human rights dimension. The missions rely on the concept of comprehensive, common and indivisible security. It promoted the civil objectives of the human rights, democratic institutions, free media, performance of free and fair elections and good governance alongside the traditional political and military issues of the security.

In this profoundly multifaceted context, the crises that appear in the international environment present a greater degree of complexity, which leads to finding some highly complex and appropriate answer solutions and which require a constant adjustment of the conception on the crisis management.

The same is also valid for NATO. From a conceptual point of view, we can see that the two organizations have tried to adapt their concepts and doctrines on crisis management, especially in the last 26 years.

Then, what is the difference between the two international organisms?

The foundation of NATO is based on the concept of Alliance, where the signatories of the Treaty have common geopolitical goals, common interests that can be harmonized through permanent consultations (relatively small number of members, their positions in relation to various security subjects are known, the decision-making mechanisms are flexible, there is only one political-military decisional organism at strategic level, etc.)

The success of the Organization for Security and Co-operation in Europe during the Cold War is based directly on its vocation to be a forum for dialogue between the two parties whose positions seemed irreconcilable

If we want to weight up (but still keeping the proportions) the differences, we can conclude that there are still two topical issues that the Organization for Security and Co-operation in Europe will have to address soon:

- o The status of the Organization for Security and Co-operation in Europe does not yet have the status of an organization with international legal personality, its affiliated members still have the status of participating states and not that of member states.

The status of an international organization with legal personality should determine clarity and a greater consistency arising from the development of an own concept of the Organization for Security and Co-operation in Europe, followed by an institutional or action development which gives efficiency and effectiveness to the organization.

- o A second problem is the relatively large number of participating states, 57 compared to 35 states participating in signing the Final Act from Helsinki. This determined the USA and the European

West states to reduce their interests towards the Organization for Security and Co-operation in Europe, due to the fact that the decisions within the Organization for Security and Co-operation in Europe are taken by consensus, this being quite difficult having membersstates that are still in the dawn of democracy, or others that are still under the influence, at least economically if not politically, of Moscow. Because access to the Organization for Security and Co-operation in Europe is not made based on some political ‘performances’, or an *acquis communautaire*, as in the case of the EU, or based on some demanding criteria in terms of implementation of some reforms, this determines the fact that some states with questionable democracies still have access. This is one of the founding principles of the Organization for Security and Co-operation in Europe.

As regards the European Union, in the light of the evolution of the management concepts of the crisis, we can say that it is still under institutional and foundation construction of some of its own concepts and doctrines.

This does not mean that the EU has not taken important steps towards the creation of an own doctrine based on a crystallized conception for crisis management. It should be noted at this point the fact that since 2004, the EU has defined the concept of comprehensive approach on the crisis management.

However, we see that even if conceptually it placed itself one step ahead NATO on the comprehensive approach, the operationalization of the concept, its implementation has proved to be a slow and difficult process for the EU due to the fact that it does not have an own military component, being much more focused on the civil component for crisis management, as part of the comprehensive approach, as well as on the security emphasis on cooperation, where the EU has managed to become a major player in its strategic interest area.

It is noteworthy that the adaptability, flexibility and the capacity of transforming, learning from past mistakes, are elements in favour of the organization that embraces these principles. The only international organization whose concerns of continuous transformation are raised at the level of strategy is NATO. Moreover, it is also the one only that, from a structural and organizational point of view, indicates this by the existence of a Strategic Command for Transformation, as an important element in the dynamics of this organization.

On the other hand, the complementarity between NATO and UE on the military capabilities of NATO and the civil ones of the UE in the field of crisis management fully justifies the strategic partnership between the two institutions. However, the European Union aims to develop its own military capabilities hoping to become a major global player.

The economic and financial crisis in the last 6-7 years has determined a more judicious

allocation of funding for defence expenses, determining, on one hand, NATO to start the Smart Defence program and, on the other hand, the EU to start the pooling sharing program. Both start from the same needs to finance in a smarter way the defence and the security.

With the Strategy from Maastricht, the allies of the Organization for Security and Co-operation in Europe have revealed that the poor governance and the omission of states to ensure the functional framework and the appropriate democratic institutions to promote stability can create threats.

Over time, the Organization for Security and Co-operation in Europe 'refined' its own mechanisms for enforcing and keeping security, its actions being among the most diverse, extending from the political sphere, focused on the promotion of the principles of a good governance and the rules of democracy, in the military and the security one, until the respect of the journalistic freedoms, the rights of minority and the principle of non-discrimination.

To these one may add the environment and education protection, which highlights the versatile capabilities of this international organization to contribute to the enforcement and the maintenance of security.

The involvement of the Organization for Security and Co-operation in Europe in the conflict in Ukraine shows us that the concept of 'comprehensive security' is more topical than ever in the vision of the member nations, nations for which the conflict does not represent a show to which they assist as mere spectators, but a palpable and unquestionable reality to which they must adapt permanently.

Taking as a case study the conflict in Ukraine, in the defusing of which the Organization for Security and Co-operation in Europe got involved substantially and unconditionally, and starting from the assumption that diplomatic problem-solving might be the key to success, led to the conduct of several meetings and negotiations both at presidential and ministerial level, with the participation of some diplomats experienced in defusing the conflicts, the result of the mediation consisting in signing the *Protocol from Minsk on 5<sup>th</sup> September 2014*, followed by an implementation memorandum agreed by the representatives of the Trilateral Contact Group on Ukraine (consisting of Russia, Ukraine and the Organization for Security and Co-operation in Europe) and by the leaders of the self-proclaimed states Donetsk and Lugansk, in order to cease the violence in the Ukrainian region Donbass.

Finally, we can conclude that the Organization for Security and Co-operation in Europe is not indifferent, but it upholds the respect of the rights and the values it defends, starting from the assumption that security cannot exist without judicial order, in the same way that the right cannot apply efficiently except in conditions of full security.

These are principles that the world leaders should respect and implement, with the understanding that peace is the only way towards the progress and the stability of the humanity.

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## FROM A PARLIAMENTARY ASSEMBLY TO A EUROPEAN PARLIAMENT: AN UNFINISHED PROCESS

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**Abstract:** *The Parliamentary Assembly of the European Communities was the precursory body of the European Parliament, but it lacked the legitimacy the latter would gain starting with 1979, the year when the first European elections were held. The two entities differ in many ways, such as the internal organization, the competences and the connections with other European institutions, but the fundamental difference is the one that also determined the rest of the previously mentioned aspects, specifically the way their members were appointed. Although this aspect may seem solved, it will not be so until the suffrage for the European Parliament will not only be direct, universal and secret, but also accessible, assuring all interested stakeholders the same fair conditions for participation, thus eliminating all formal and informal obstacles for independent or party candidates.*

**Keywords:** political parties; elections; democratic deficit; discourse construction; ideology

### Introduction

The European Union is a complex structure that is legally an international organization, but that has developed institutions, policies and practices that resemble those of a state. Nevertheless, this two sided feature leads to what academic literature calls *the democratic deficit*, given the fact that its institutions are composed of European officials that are not politically invested by the European citizens. This problem has been subject to the academic debates, but also to political negotiations in the moments of amending the Treaties of the EU. Thus, in this section, I shall present these aspects in order to formulate the main question that will be answered throughout the following two sections of this chapter: Does ideology matter for the reduction of the democratic deficit of the EP and implicitly, of the EU?

### 1. The democratic deficit of the European Parliament and of the European Union

While “the earliest charges of a democratic deficit in the EU centred on the weak role of the EP and national parliaments” (Caporaso, 2005, p. 62), given that “when the demos cannot employ its

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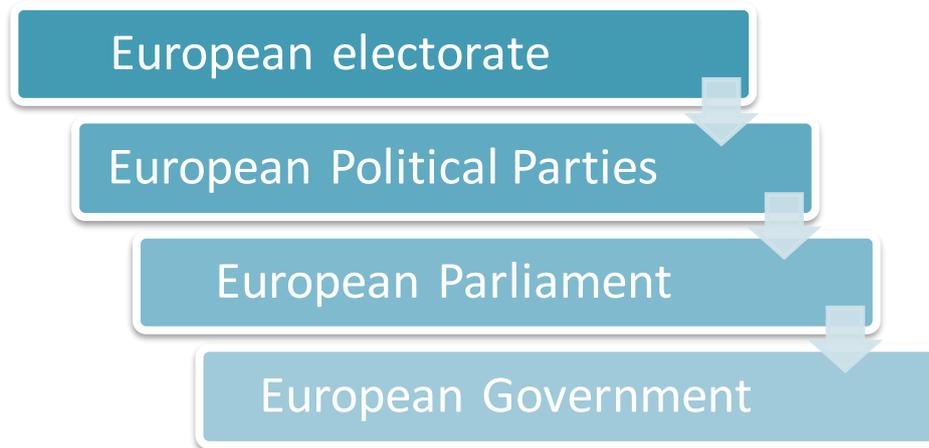
national parliaments to exercise control over the transnational political process it can be said that there exists a loss of national democratic autonomy” (Chrysochoou, 1998, p. 114), the democratic deficit is defined as “a net loss of democracy that comes from transferring powers from state to Union institutions without also democratising the second to the standards of the first” (Lord, 2004, p. 6). The counter response of the European Union was to create the idea of legitimizing its institutions by placing them under the control of the European Parliament, which was seen as a democratic institution due to the fact that its members were chosen by vote. Nonetheless, “sceptics point to the absence of European-wide political parties and general voter apathy in the elections of the European Parliament (...) repeated failures in extending the political identity to a higher level” (Bowman, 2006, p. 197), which are the main elements that the electoral process combines.

A cause for the EU’s democratic deficit is identified within “disparity in power” between the EP and the Commission (Burns, 2002, p. 62), but this aspect seems to have found an improvement in the institutional changes brought by the Lisbon Treaty. The increase of the influence that the European Parliament has on the European Commission was also a result of the pressures applied by the MEPs that reinforced the motivation that led to this pledge by reminding the investment vote they receive from the citizens. As evidence to that is the fact that in the plenary, the EP resolution that emphasised the fact that “as many members as possible of the next European Commission should be chosen among newly-elected MEPs so as to give voters more say”, was adopted with “316 votes in favour, 90 against and 20 abstentions” (EP, 2014). This direction resembles the path that is foreseen for reducing the EU’s democratic deficit, namely transforming the EU “into a more accountable (parliamentary) regime” (Gerven, 2005, p. 349).

Moreover, since “democracy is no longer about the mobilization of citizens towards consensus on the common good, but about aggregating individual preferences in what is now a pluralistic, morally diverse civic universe. In democracies, such aggregation of interests principally takes place through voting in competitive elections (Dahl, 1972), with political parties being the central actors in the process” (Tsakatika, 2007, p. 871), the importance of the consolidation of the ideological representation carried out by MEPs is even higher, especially since “democratic deficit concerns tend to be motivated by abstract principles of democratic representation” (Sajó, 2004, p. 434).

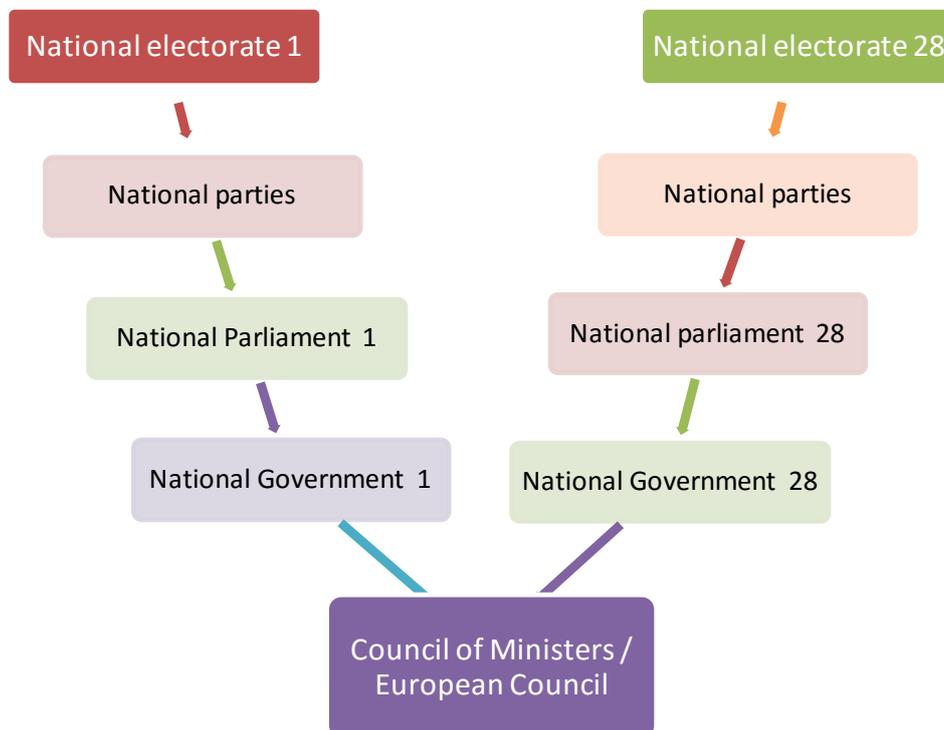
Thomassen and Schmitt (2007, p. 17) separate the two types of political representation for the European Union according to the two types of political entity the EU would aspire to become:

**Figure 1 – The federal model of European political representation**



Source: Thomassen and Schmitt (2007, p. 18)

**Figure 2 – The intergovernmental model of European political representation**

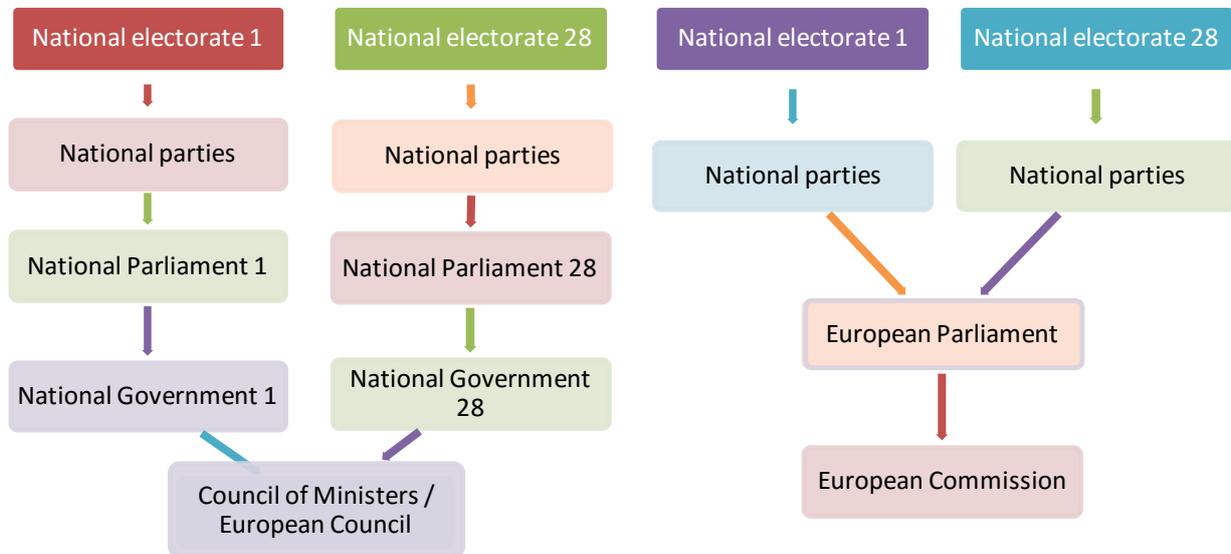


Source: Thomassen and Schmitt (2007, p. 18)

Nevertheless, judging by these models, the EU does not currently fit entirely into only one of these categories, given that it is a polity whose citizens are represented both through the Council of Ministers and the European Parliament. This aspect is not problematic, as much as the fact that the political actors involved in the electoral process, which act according to intergovernmental norms within a federal setting, combine the two models in a distorting way.

Thus, the federal model of European political representation is actually incomplete because some of its electoral components still belong to the intergovernmental model. So, the EU's current model of political representation has the following configuration:

**Figure 3 – The intergovernmental model of European political representation**



Source: Own elaboration by adapting the two previous models provided by Jacques Thomassen and Herman Schmitt (2007, p. 18) to the post Lisbon Treaty framework

The colours chosen for the figures are also meant to highlight the differences between the electoral and institutional dispersion of all 28 national electorates, political parties, Parliaments and Governments, as opposed to the institutional coordination brought by the Europeanization of electoral practices, that would be reflected in a European electorate, European political parties, a politicised European Parliament and European Commission, under political control of the legislative. So, the 3<sup>rd</sup> figure, corresponding to the current state of the art concerning political representation in the EU, resembles more to the 1<sup>st</sup> one in terms of electoral dispersion, but reflects the progress made concerning the institutional Europeanization advanced through the EP's increased political control over the Commission. This outlines a clear case of functional spill over effect that requires the need for further Europeanization in the early phases of the electoral process, given the Europeanization of its top phase, the proposal of a President of the EC by the European political group that has won the majority of seats in the EP.

These four institutions have their particular representation functions at different levels and in different policy areas, like for example in the Foreign Affairs domain, but the European Parliament stands out as the only directly elected institution and the one that benefits from the direct investment

of the European citizens whom it should represent. Thus, this electoral process should comprise Europeanized practices, especially since its result is a presumed politicised institution that would rather compare to the legislative model in a federal type polity.

## **2. Process of empowerment of the European Parliament: causes and effects**

The previous section revealed that the debate regarding the democratic deficit of the European Union is built around its remoteness with respect to its citizens, their low influence over the European institutions and their lack of accountability. The solution foreseen by the Member States and the European institutions has been the empowerment of the European Parliament given that “as the political culture of the EU evolved and concern about its lack of democratic accountability deepened, the role of the Parliament and the manner in which its members were chosen came under greater scrutiny, and the logic of direct elections became more compelling” (LeDuc, 2007, p. 140).

Also, another effect was that the EP’s legitimacy would also pass to those institutions or policies that would in this way fall under its control, monitoring or approval. In the following pages I will analyse the competences that the EP has received over the years and the implications that these transfers have had in the development of the EP as a representative institution.

The Treaty of Rome that entered into force in 1958 was the starting point of the empowerment process of the European Parliament, given that it introduced the “consultation procedure” (Hix, 2002, p. 261), making it possible for this institution to have a say on European topics, although at this stage, it could have been ignored (Hix, 2002, p. 261). This gives nothing else than evidence of the political weakness that the EP had in the European system, as a consequence of its initial format and of its representativity, which was low and so, did not demand a higher involvement in the interinstitutional relations. The Single European Act that entered into force in 1987 brought significant increases in the power of the EP although 7 years had passed since the first organization of direct elections for it and provided that the “Parliament’s powers were enhanced by including the requirement of Parliament assent when concluding an association agreement. Besides, the act institutes the cooperation procedure, which reinforces the position of the European Parliament in interinstitutional dialogue and gives it the possibility of two readings of the proposed legislation. However, the scope of application of this procedure remained limited to cases in which the Council acts by qualified majority, with the exception of environmental matters” (EUR-Lex a). Thus, the Single European Act empowered the EP regarding both external issues, such as the relations of the European Union with third countries and internal issues, notably initiating the relationship with the Council in matters of decision-making.

The Maastricht Treaty that entered into force in 1993 focused on the construction of the political dimension of the European Union that was then created. In this sense, it comprised progresses for the European Parliament, such as (EUR-Lex b): a) providing for more areas to be subject to the cooperation procedure and the assent procedure, b) the creation of the codecision procedure, c) involving the EP in the validation of the Commission, d) recognising the “role played by the European political parties in European integration” and of the fact that they “contribute to forming a European awareness and to expressing the political will of the Europeans”. Thus, the Maastricht Treaty provided especially the EP with more powers in the European institutional system.

The Amsterdam Treaty that entered into force in 1999 continued the direction of empowerment of the EP through elements such as (EUR-Lex c): a) the large extension of the codecision procedure through the fact that it became “the general rule both for matters where qualified-majority voting applies and for the new areas brought into the Treaty for the first time”, except for the Common Agricultural Policy and for “certain questions where the Council decides by unanimous vote”, b) the elimination of the Council’s third reading within codecision, putting the EP “on an equal footing with the Council, which will have to seek a compromise if it wishes the proposal to be adopted”, c) the restriction of the number of MEPs to 700 in the perspective of the enlargement towards Central and Eastern Europe, d) the fact that the EP could “draw up proposals for elections by direct universal suffrage, in accordance with a uniform procedure in all Member States or in accordance with principles common to all Member States”, e) the freedom to “lay down regulations governing the performance of its Members' duties (...) with the approval of the Council, and acting by unanimity after consulting the Commission”. Thus, the Amsterdam Treaty provided the EP with powers in the European institutional system, but especially in the internal plan, opening the way for an independent design concerning its internal configuration and the electoral process it is based on. However, the EP did not take advantage of these opportunities, given that it did not reform its electoral process in the direction of its Europeanization.

The Nice Treaty entered into force in 2003 and introduced few modifications regarding the European Parliament in terms of (EUR-Lex d): a) the status of European political parties, b) the extension of the areas where codecision was applied, c) provisions concerning the adaptation of the EP to the countries that were going to accede to the EU in the following years. Thus, its enhanced dimension was the political and ideological one.

The Lisbon Treaty that entered into force in 2009 is, after the Maastricht Treaty, the one that brought major institutional changes for the European Parliament. It is the successor of the Treaty establishing a Constitution for Europe that would have established a clearer trajectory for a federal

model that would have put an end to the controversies concerning the type of polity the EU aims to become and implicitly, the shaping that its components must have, including the European Parliament as a representative body. The Lisbon Treaty has a prominent political character due to the fact that it sets as an aim to “strengthen European democracy, particularly in order to improve the legitimacy of decisions and to bring the EU and its citizens closer together” (EUR-Lex e) and to the fact that it has increased the EP’s role in the European political system, regarding (EUR-Lex f): a) the recognition of the political dimension of European citizenship, b) stimulating the European Commission as for it to invite “national and European political parties to inform the electorate of their affiliation links and to publish, before the elections, the name of the candidate for President of the Commission they are supporting”, c) “the strengthening of legislative power” through the transformation of the codecision in the ordinary legislative procedure, d) “a greater role at international level: the Parliament shall approve international agreements in the fields covered by the ordinary legislative procedure”, e) “the strengthening of budgetary power: the Parliament is henceforth placed on an equal footing with the Council in the procedure for adopting the EU’s annual budget”.

Thus, the Lisbon Treaty provides the legal framework for the deepening of the politicization of the European Parliament and the extension of its political control over vital policy areas such as the European budget or over other institutions, like the Commission, which joined the EP in its endeavour to enhance the visibility of the ideological dimension of the European elections, promoting the electoral battle between the parties’ candidates for the position of President of the Commission.

Although the empowerment process has been a continuous one, it has not been constant in each treaty’s case. However, Aldecoa (2011, p. 25) highlights that the dynamic characteristic of the European integration process is due to the treaties’ modifications, that had two directions: on one hand, to “deepen the European project through its opening towards more and more areas” and on the other, to “democratize the decision making system through conferring an increasing power of decision and control to the European Parliament that is elected by direct universal suffrage”. So, the way that the EP was formed was used in order to justify the attribution of competences towards it or the call for the necessity of such a procedure.

### **3. The process of democratization of the European Parliament**

The empowerment process analysed in the previous section conditioned the European Parliament to live up to its status of being representative institution, a status due to which it had received its functions in the first place. This challenge of democratization compelled the EP to

reinforce its bonds with the European citizens, by improving the organization of the European elections and by developing its political system. These two elements are analysed in the parts that follow.

### ***3.1. Electoral reforms of the European Parliament***

During the functioning of the Parliamentary Assembly, its members were not selected through a procedure that involved the interaction with European citizens, so the starting point of this Europeanization process had quite a strong intergovernmental dimension, given that the Assembly's composition depended entirely on the Member States. This perspective changed in 1976, with the approval of the Act that announced the introduction of direct elections three years later, with the aim of transforming the EP into an institution that will be "the custodian of fundamental liberties. It will also exercise control, not only over the Community budget (...), but also over the Community executive, thereby preventing the Community from drifting into technocracy. That is what democracy means" (EP, 1977 a, p. 5), fact that was anticipated even in "the goal of European integration in the form of political union planned for 1980 will require, speedy measures to extend the peoples' participation in the construction of Europe" (EP, 1977b, p. 30). Thus, the political dimension was foreseen since then through the explicit intention of placing the European Commission under parliamentary control that would reflect ideological perspectives as opposed to technocratic approaches.

Nevertheless, although the suffrage was universal, direct and secret, the Member States and the national political parties still had a very important role because of the fact that the elections were organized at national level. The step had been made towards an institution that would be seen as representative based on European elections, but the European electoral setting was missing. Yet this was subject to Article 7 of the Act on direct, universal suffrage, which stated that "the Assembly shall draw up a proposal for a uniform electoral procedure. Pending the entry into force of a uniform electoral procedure and subject to the other provisions of this Act, the electoral procedure shall be governed in each Member State by its national provisions" (EP, 1977a, p. 14-15), fact that was enforced by the EP's requirement in its *Resolution on the adoption of a draft convention introducing elections to the European Parliament by direct universal suffrage*, namely that it "instructs its Political Affairs Committee immediately to carry out the necessary preliminary work for the introduction of a European electoral system" (EP, 1977c, p. 29). Therefore, the national organization of the European elections was supposed to be a temporary measure until the Parliament itself would

reach a consensus upon a uniform electoral design. Nonetheless, the obstacles for further progress on the matter were presented by Schelto Patijn, Rapporteur of the Political Affairs Committee, given that “it has not yet proved possible to convince the responsible politicians of the need to take this step which is so fundamental to integration” (EP, 1977b, p. 30). This had been also clearly stated by H. Lautenschlager, draftsman of the opinion of the Legal Affairs Committee, in the debates in the European Parliament on the 14<sup>th</sup> January 1975 sitting: “One of the greatest problems over the years has been the uniform electoral system. It is understandable that each Member State felt its own system was best and tried to have it accepted by the others. To escape from this impasse, it was essential to study whether the term ‘uniform’ necessarily referred to an entire system” (EP, 1977d, p. 71), outlining the fact that the main influence on delaying the decision for the configuration of the European electoral system belonged to the countries.

Thus, it was considered that the national electoral systems could be borrowed since they gave democratic result on national level, provided the “all the electoral laws in the Member States satisfy the five minimum requirements for democratic elections: they are free -as are all citizens-, they are equal-we do not have an electoral system based on classes-, they are secret, they are direct- no electoral college is involved- and they are universal” (EP, 1977d, p. 71). However, the asymmetries they created at the moment when all results were aggregated in order to form a representative institution were not taken into consideration.

So, the elections became European in theory, but national practices prevented them from being European in terms of content given the unfolding of the electoral campaigns and in terms of results, given the effects determined by characteristics of the electoral systems used in the 28 countries.

The Political Affairs Committee estimated that the election to be held after 1980 could already be held “in accordance with this uniform procedure (...) taking account of political developments in the Member States” (EP, 1977 b, p. 40). Yet, what followed was a period of 36 years in which the reforms were small and targeted at particular aspects such as the **harmonization of the general category of voting model**, namely recommending through the Council’s Decision 772 of 2002 that the elections for the European Parliament were organised using proportional representation models, either the list system or the Single Transferable Vote system (Council Decision 2002, p. 1), but without revising the whole set of factors that influence the elections’ result. For example, the **threshold limit** was established at a maximum of 5% (Council Decision 2002, p. 1), but that did not cancel the effects produced by the differential use of thresholds in the range between no thresholds at all and having others up to 5%.

Another reformed electoral element regards the fact that „the office of representative in the Assembly shall be compatible with membership of the Parliament of a Member State” (EP, 1977a, p. 14) that has been eliminated given that „from the European Parliament elections in 2004, the office of member of the European Parliament shall be incompatible with that of member of a national parliament” (Council Decision, 2002, p. 2). The **withdrawal of the possibility of being both a MEP and a member of a national parliament** is significant for the Europeanization process because holding both a supranational and a national mandate from the citizens meant that the two could have merged in the practice, making harder the distinction of European issues and areas of interest for national citizens and thus, complicating their shift of loyalties towards the supranational level and preventing them to perceive themselves and act as integrating parts of a European electorate.

The harmonization of the category of ballot was the most visible progress for the European Parliament, given that it drove even the United Kingdom, a country with many opt-outs along the history of EU integration until present, to change its scrutiny to a proportional representation one of closed lists in Great Britain and Single Transferable Vote in Northern Ireland (European Parliamentary Elections Act 1999). Although it organised a referendum for consulting the electors on the possibility of changing the First-Past-The-Post type of ballot with an Alternative Vote one (Parliamentary Voting System and Constituencies Act 2011), the results were against it with 67.90% of English rejecting the proposal (United Kingdom Electoral Commission, 2011). Therefore, the United Kingdom preserved its plurality voting system for national elections, while ceding to the adoption of a proportional representation voting system for European elections.

As Duff conceived the need for electoral reform even since the modifications brought up by the Amsterdam Treaty, “the Treaty requirement of a uniform electoral procedure (Article 138 3) was intended to make the elections a fully European event in which citizens would vote on European issues” (Duff, 1997, p. 60). Nevertheless, given the stagnation periods in this respect, in order for this to become a reality, there is the need for an unblocking factor which can be represented by the supranational political groups that can determine the Europeanization of the electoral campaign that would mean a Europeanization of the electoral process’ content, leading to the consolidation of the European political actors recognised as such, who will put pressure for creating a common electoral law that would not favour only some of them anymore.

### ***3.2. Development of European political actors for the EP***

The European public sphere has not made significant progress regarding its formal institutionalization until after the Maastricht Treaty that encouraged the national and supranational actors to construct the political infrastructure of the European Union.

A cause for the slow evolution of this coagulation can be that “the timing and content of politicization would have been controlled by the Eurocrats and their interest group allies. Blocked in their aspirations by the resistance of national politicians to supranationality, they would appeal directly to the publics benefiting from expanded trade, lower transaction costs, cheaper consumer prices, greater personal mobility, regional subsidies, etc., and mobilize them to clamour for an even greater transfer of sovereignty or funds to the emerging centre” (Schmitter, 1998, p. 140). This waiting from part of the supranational political groups must be replaced with a proactive attitude in order to achieve considerable advances.

#### *3.2.1. The formalization of European political parties and families*

In the debate about Europeanization, why is it important to strengthen the EP groups, even if there is a European political party? The groups can focus on European matters and European citizens’ interests, while the parties obviously would also have to respond to their national institutional restraints and interests that exceed the European Union space, as European transnational parties are composed also by states that are not members of the EU.

So, what should bond the parties in the European public sphere are the European issues of interest, not mere bureaucratic organizations in supranational structures that function in fact still at national level and only join supranational reunions and eventually subscribe to general principles assumed by the supranational political group or party. That would be the characteristic for the political parties at European level (PPELs) that would differentiate them from other types of international organizations of political parties.

Nevertheless, “the adoption of a common European statute for all PPELs, based on EU law and defining a common legal, organizational and financial status is a fundamental precondition for the creation of a European polis and a common political space” (Bardi *et al.*, 2014, p. 28), given that this formalization would mean the recognition that these entities have an independent existence, that does not double the one of the national parties they comprise. Due to the fact

that “where parties have a long-standing organisational tradition, their primary interest is to maintain their structural articulation, by adapting their form and functioning to external changes” (Bardi et al. 2014, p. 75), a supranational statute for the European parties would determine an ongoing process of politicization of their own activity in order to fold according to changing inputs from the citizens. Moreover, they could use this opportunity for demanding more competences for the EP, which would lead to their further Europeanization, given that “as the EP’s role is growing, the political parties tend to be more active in the process of unification” (Sidjanski, 2010, p. 228).

Moreover, the Giannakou Report, adopted by the Committee on Constitutional Affairs in the European Parliament, underlines that „the Treaty of Lisbon provides for this role of the political parties and their foundations with a view to creating a European polis, a political space at EU level, and a European democracy; (...) the European political parties, as they stand, are not in a position to play this role to the full because they are merely umbrella organisations for national parties and not directly in touch with the electorate in the Member States” (Giannakou, 2011, p. 6), while at the same time „stresses the important challenges in terms of organisational capacity that the European political parties will have to face in the light of the reforms that may be made to the European electoral system - creation of an additional constituency, establishment of transnational lists” (Giannakou, 2011, p. 7), highlighting the need for a formalization that would make the parties valid competitors for the citizens’ interests and that would also prepare them for dealing with new financial conditions applicable to European parties, given that the report provided that „the Commission should propose the creation of a new title in the Financial Regulation devoted solely and tailored specifically to the funding of European parties and foundations” (Giannakou, 2011, p. 8). Thus, the debates in the European Parliament emphasize the formal requirements that would be needed in order to consolidate the European parties as truly political actors, not only international supra-party organizations.

Furthermore, Amie Kreppel argues that the increase of the EP’s role in the decision-making process determined the enforcement of the supranational party system because it made it accountable, given that before the Single European Act “the EP was constrained to giving its opinion without an effective avenue of independent influence over legislative outcomes” (Kreppel, 2004, p. 36). This is a valid point of view, especially since it follows the line of the previously formulated relation between the empowerment of the EP and its democratization.

Therefore, formalizing the European political parties would mean giving them a political stake in developing their own political programme that would differentiate them among the other actors in

the European public space in the fight for the citizens' attention and votes. As long as European parties are not formalised accordingly in order to gain its own institutional powers, they will depend on the national parties to gain seats in the European Parliament. In an analogy with the European Parliament, it was only after its formalization as a directly elected institution that the Member States agreed to increasingly transfer competences towards it and even more, it was only then that the EP itself enhanced its attempts to gain more power.

### *3.2.2. Adding content to the forms: Europeanization of loyalties in the EP plenary*

The transfer of loyalties is not a feature only for the European electors, but also for the political parties that compete in the electoral process, so it is important to also assess their point of interest in terms of loyalties, especially since a study on the reactions to the empowerment of the European Parliament showed that “at the party level (...) there is evidence that partisan ideologies affect parties' perceptions of the European Parliament” (Winzen *et al.*, 2015, p. 86).

Moreover, Ladrech finds that “the stimulus for changing party rules regarding the activity of its politicians would be the demands placed upon MEPs by the desire of the EP groups to increase voting discipline” (Ladrech 2012, p. 578), but how big are the differences among political parties from the same country in this sense? In order to answer this question, based on the data of the ongoing European Parliament's term provided by VoteWatch Europe (updated to 2015), I will analyse the obedience of the parties of the EP towards the political group on two axes: a) the parties that register the minimum rates of compliance and b) the variation of rates of compliance of all political parties from each Member State with their correspondent political group.

So, the minimums of the compliance rates rank between (VoteWatch Europe 2015) 27,94% in Latvia, 30,94% in Greece, 34,33% in Lithuania, 38,80% in Italy, 57,46% in Slovakia, while Belgian and French ones reach 68,99% and 64,20%. Czech Republic, Poland, Netherlands and Sweden they go as low as between 75% and 79%. Estonia, Ireland, Croatia and Denmark have a minimum loyalty threshold between 81% and 83%, while Portugal reaches 85,21% and Germany, Luxemburg, Finland, Slovenia, Spain and United Kingdom go up to values between 86% and 89%. Parties in Austria, Bulgaria, Cyprus, Hungary, Malta and Romania are above 94%. Thus, the states where parties register the lowest rates of compliance are minimum are Latvia and Greece and the ones where the lowest rates of compliance are maximum are Austria, Bulgaria, Cyprus, Hungary, Malta and Romania.

Therefore, a hierarchy cannot be established between the central level of the parties and their loyalty to the political group they are affiliated to, given that the parties from all Member States have

different loyalty rates and the lowest value for each of the 28 Member States also varies with an average of 70%, as previously observed.

## Conclusions

The European Parliament's evolution since the organization of the first direct elections in 1979 has been of a significant importance, given its electoral reforms regarding the elimination of the compatibility between the position of the MEP and the MP, the establishment of a maximum threshold or the harmonization of the wide category of electoral systems used in the European elections. These changes were necessary in order for the EP to be able to demand and gain, by means of treaty amendments, more competences in the European institutional system. Once the EP got those competences, it had to further modify its attributes as to reduce its democratic deficit.

Nevertheless, vital aspects of the organization of these elections are nationally configured, such as the number and design of the constituencies or the financial and signature guarantees required. Therefore, the democratic deficit of the European Parliament can be reduced through the Europeanization of its elections and through the consolidation of the European political parties and families.

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## ROMANIA AND THE EURASIAN UNION. PLANS, PREDICTIONS AND PERSPECTIVES

Mircea-Cristian GHENGHEA\*

**Abstract:** *Following the events in Ukraine, Romania might represent one of the key points for the Eurasian perspectives that have circulated in the last years in Moscow. Through our text we intend to present and to highlight the main ideas and plans of Eurasian inspiration regarding Romania, as well as the interesting predictions made, in certain moments, by some representative characters for the Eurasian paradigm, like Aleksandr Dugin, for instance, who is its main ideologist and promoter. At the same time, one must not neglect the signals of discontent from Moscow about the need of dissipating the so-called sanitary cordon of the Western powers, in which the Baltic States, Poland, and Romania are included – another aspect bearing a particular importance for understanding certain gestures, attitudes and statements related to the role and the place of the Eurasian Union.*

**Keywords:** Eurasian Union; Romania; Aleksandr Dugin

**JEL Classification:** F50; F53; F54

### Introduction

The date of January 1<sup>st</sup>, 2015 marked the beginning of the official existence of the supranational body entitled the Eurasian Union. Discretely announced, without the usual ceremonies and pomp which used to accompany this kind of things, the event was soon to be thrown into the background due to various tragic situations which occurred at the beginning of this year. Nevertheless, in spite of all sceptics and criticism (Boonstra, 2014), the Eurasian Union designed and initiated by Russia has become reality. Including the Russian Federation, Belarus and Kazakhstan, the supranational body is intended to be a powerful economic and political counterweight against the European Union and the United States of America. Given that the leaders in Moscow are planning to regain at least a part of the influence that Russia had during the Soviet times, the South-Eastern Europe seems to bear a particular importance, a fact which can also be noticed by considering the way in which the process of establishing the Eurasian Union was designed and promoted.

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## **1. Romania – the policy of certainty**

A general opinion shows that Ukraine represented a key-piece for the plan of the Eurasian Union. Therefore, its absence from this organism was perceived as a potential threat by the Russian Federation and constituted an important vulnerability for the Eurasian project.

While it is true that the European option of Ukraine irritated Russia, it is also true that the potential dismemberment of Ukraine was taken into consideration even since the end of the '90s, as one can see/read within the writings of Aleksandr Dugin, the main ideologist and promoter of the Eurasian plans. Under these circumstances, Romania gained a particular importance, both from the point of view of the European Union's plans (with a certain reference to the situation of the Eastern Partnership) and especially of the United States and NATO. Given that, during 2014, the situation in countries like Greece, Bulgaria, and Hungary was rather agitated and discomfoting, politically and economically wise, Romania represented a sort of oasis of tranquillity in a rough sea, a reliable partner for the European Union, the United States of America and NATO.

The regional stability was possible due to the bilateral and multilateral cooperation process between Romania and its traditional or newest allies. The internal justice mechanisms which began to unfold quite an impressive number of investigations and inquires, in order to fight the institutionalized corruption also contributed to the general improvement of Romania's image abroad and offered serious reasons to consider that Western economic and political interests might benefit from this. In spite of the contradictions and disputes between the representatives of certain Romanian political parties, a number of high-ranking officials and prominent administrative figures were brought to justice.

Mainly due to the conflict in Crimea and Eastern Ukraine the regional security background shifted in an almost radical way. The European Union, NATO, but especially the neighbouring member states of the conflict zone like Romania, Poland, Hungary, or Slovakia should be prepared for any turn of events. The Western presence increased over the last year in the Baltic States, several common military exercises took place there and also in Romania, Poland, and even Ukraine. Nevertheless, Romania's membership of the European Union and NATO has done much for the country's stability and security in South-Eastern Europe, a region which, historically speaking, is practically prone to turbulence.

## **2. Romania, Aleksandr Dugin, and the Eurasian plans**

When discussing the issue of the Eurasian Union and Romania one must not forget that Romania has been assigned the role of a true bridge between the East-Slavic area and certain states of South-Eastern Europe – Bulgaria, Greece, Serbia, and Hungary. The fact as such has already been mentioned by various promoters of the Eurasianist ideas. Situated in the South-Eastern part of the European continent, perhaps in the most exposed flank of the European Union, in connection with countries where there is a certain degree of sympathy for Russia, like Serbia or Bulgaria, Romania represents an area where Russia would definitely prefer to have a greater influence.

Another coordinate that can make us understand better the increasing attention towards our region is represented by the particular significance which Romania gained after the Crimean Peninsula became a part of the Russian Federation. As the United States Navy almost concluded the organization and the arrangements of the Deveselu base in order to install the already famous missile shield elements, Moscow was more than displeased and frustrated, a fact proved not only by an entire series of statements, but also by bringing troops, as well as hunting and bombardment aircrafts at various airbases in Crimea (Pircalabu, 2015).

Finally, another issue that may have greater relevance in the near or more distant future is that the Romanian state is quite an inconvenient geopolitical actor for Russia in the Black Sea; representing not only its national interests, but at the same time those of the European and North-Atlantic allies, Romania may also play a certain role when discussing the pipelines and the transit of natural gas between the two major geopolitical zones – Eurasian and Occidental.

These are but a few aspects that might explain the attention which the Russian Federation, on one hand, and the United States of America, NATO, and the European Union, on the other hand, pay to the situation in Romania. However, it has become obvious that Kremlin's media and image offensive in various European countries, including Romania, has increased in intensity in the last few years (Campeanu, 2015), perhaps a proper example being the recent opening of the Russian Centre of Science and Culture in Bucharest (15 May 2015).

In this context, we should not be surprised that the main ideological exponent of contemporary Eurasianism, namely Aleksandr Dugin, has made several statements and predictions regarding the future of Romania and its possible inclusion within the Eurasian sphere of influence. The invocation of certain cultural affinities and an ancient heritage, which constitutes a synthesis between Western and Oriental civilization coordinates, represents one of the favourite and quite often used arguments. Moreover, in the preface of the Romanian edition of his book *The Foundations of Geopolitics*,

Aleksandr Dugin shows that “in the Romanian-Russian cultures’ dialogue one should consider the Euroasianist doctrine, which is independent but, through the differences, diversity, and proportions it disposes and gives us a solid basis for approach, mutual understanding, and friendship” (Dugin, 2011, p. 13).

According to Dugin, Romania and other Central and East-European countries like Poland, Latvia, Estonia, and Lithuania are trapped within the so-called Atlanticist paradigm, which would actually enforce the position of the United States of America and Great Britain.

Aleksandr Dugin noticed correctly that states having the size and importance of Romania cannot have their own geopolitics – these states gain geopolitical importance by being included in a large alliance or political and military block. As a consequence, Romania is capable of manifesting itself only as a power with limited interests, of local and regional significance, its foreign policy being unavoidably subordinated to the strategic interests of the alliances and organizations of which she is a part of – the European Union and NATO.

In the last few years, Dugin predicted several times the inevitable decay of the European Union and the ascension of the Eurasian Union. When talking about Romania, he usually outlined its possible Eurasian integration and deplored the treatment of Romanians like second-hand European citizens, as he did during an interview in Moscow back in 2013:

Romania is on the periphery of the European Union, it is an uninvited guest, treated worse than the countries which are in difficulty like Spain, Italy, Greece, Portugal, and Ireland. In the European Union these countries are labelled pejoratively as the “PIIGS”, meaning “the group of pigs”. Does it mean, in this context, that Romania is a country of the tenth hand? There is a negative and unjust perception of Romanians in Europe. They are not welcomed as guests. They are not allowed in the Schengen space. An entire nation is judged on the basis of a few corruption cases. It is an unseemly situation for a country which possesses a great Orthodox culture, a culture which I consider to be a real pearl of the European culture of the 19<sup>th</sup>-20<sup>th</sup> centuries. In reality, the Romanian society is one of the European societies which are the most interesting, intellectual, closest to us (Mandrasescu, 2013).

Aleksandr Dugin warned against the possibility of using the Romanian nationalism by the Western powers, considering that “playing with the patriotic feelings of the Romanians, the operators

of the world geopolitics will try to achieve their specific goals” (Dugin, 2011, p. 17). Ironically, he is absolutely right here as he himself has fully proved it several times when talking about that.

Sometimes, the mentioning of Romania and the eventual integration within the Eurasian Union was accompanied by the indication of the possible unification of the Republic of Moldova and Romania: “by entering this union, Romania might unite with Moldova in which Transnistria would re-integrate”. One big happy family, as the Americans would say. Yet, despite the extraordinary generosity that he shows when discussing the possible unification of the two Romanian states, the members of the family would still be those already known and heavily promoted by the former Soviet propaganda and by the actual supporters of Moldovenism and Moldavian statehood, as even Aleksandr Dugin stated in Moscow, in 2013:

The paradigm of the unavoidable approach is determined by many factors. Russians, Romanians, Moldovans, Transnistrians – they are all Orthodox, they are bound by the same regional space that might also become a common economic space and a common Eurasian platform where everyone will find an honourable place (Mandrasescu, 2013).

At the beginning of 2015, following the official appearance of the Eurasian Union, Dugin made another statement in which he “outlined his extraordinary vision of merging Central and East European countries into one big conglomerate as well as offering a rare criticism of Putin” (Tóth, 2015), as Dugin seems to be fallen out of Russian president’s favour in the last year. This statement was made in an interview given to Alfahír, a Jobbik-affiliated online news outlet and might be regarded as a part of Dugin’s efforts to internationally promote “his Eurasian theory within radical right-wing circles” (Tóth, 2015). This “extraordinary” vision consists (nothing new, after all!) in creating a sort of supranational body in order “to reunite the former crown lands of Hungary in a kind of Eastern European super state”. Naturally, all the countries involved (Hungary, Romania, Serbia, Slovakia, Austria, and also a part of Ukraine – the Volinski oblast) would lose their national sovereignty and the Eurasian dependence would be implicit.

## **Conclusions**

One must be aware that all the Eurasianist ideas and arguments mentioned in our text represent only variations of the same issue: the attempt of Russia to regain the influence and the status it had

during the Soviet times. For achieving this, the leaders in Kremlin seem to be capable of almost anything, including a fratricidal war against Ukraine, a situation which was practically unconceivable by most Ukrainians and Russians alike.

At the moment, the Eurasian Union plan seems to be on hold, on account of the economic sanctions that Russia must bear. However, it is also true that the Eastern Partnership is in a very delicate and difficult position and the European expectations of Ukraine and Republic of Moldova have almost no chances of being fulfilled in the near future, as the Summit in Riga in May 2015 has already proved.

For Romania, the very idea of becoming a member of the Eurasian Union seems to be a science-fiction thing. As a member of the European Union and NATO, Romania suddenly gained a greater importance for both these organizations following the events in Ukraine. It also constitutes a very interesting target for the Russian Federation in its attempt of creating a regional propaganda network and counteracting the initiatives and actions of the Western powers. The simple fact that Romania is officially leading a NATO-backed project meant to improve Ukraine's cyber-defence (Popescu, 2015) says quite a lot about the role that the Romanian state has in terms of regional security.

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## THE TPP AND TTIP TRADE AGREEMENTS: THE INTERNATIONAL NEGOTIATION PROCESS

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**Abstract:** *Free trade is one of the ultimate purposes of the free trade agreements currently negotiated over the world. Two of these trials are represented by the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP). The common feature of these two trade deals is represented by the United States, a global actor that is making sure that it will be able to trade in best conditions on both of its geographical shores: on the Pacific and on The Atlantic. The negotiations are still ongoing, but results are expected on both sides. An important issue for the third parties, but not only, is represented by the secrecy of the negotiations undertaken and the lack of transparency shown by the negotiating Governments. If the agreements are concluded, a major global impact on trade and investments is expected, with significant positive implications for the TPP and TTIP negotiating states.*

**Keywords:** TTIP; TPP; EU; US; international negotiations

**JEL Classification:** F010

### Introduction

Trade agreements are a subject that can determine all the economic sectors to be susceptible to major changes, involving a numerous number of national governments, creating a domino positive effect in a globalized trade world. In support of this idea, nations across the Globe are trying to boost their own economies by taking part in two of the largest negotiation processes that have ever occurred with regard to economic development and investment protection.

Transatlantic Trade and Investment Partnership (TTIP) and Trans-Pacific Partnership (TPP) are two major trade pacts that are aimed at liberalizing trade, on one side between EU and US by covering the Atlantic geostrategic area, and on the other side among US and 11 other countries, by covering the Asia-Pacific area. The TTIP's negotiation process started in 2013, while talks with regards to the TPP started in 2010, both agreements aiming at increasing trade and investment, through lowering tariffs and other trade barriers among the participating states.

In general, the purpose of trade deals is to lower tariffs. But as history records, as trade expanded, it shifted from already low tariffs to non-tariff barriers, increasing the role of rules and regulations. These aspects may take a complete or incomplete form by helping or being an obstacle

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in the economies' development, but the general reason for their existence is to protect workers, consumers, the economy and the environment.

One of the characteristics of the negotiations of the two above-mentioned free trade agreements is the secrecy of the process. Both negotiation teams representing TTIP and TPP kept the process and the results away from the public while the process was on-going ; but, according to current events, the European Commission has started an intensive campaign of informing the public with regard to the latest topics related to the negotiation status of the TTIP, and the United States is due to the end the negotiations with regard to the TPP, alongside 11 other involved international entities and keeps the interested parties informed about the ratification process and the newly negotiated TPP textual basis, that according to the United States Trade Representative public releases, may take up to two years.

### **1. The evolution of the Trans-Pacific Partnership**

Trans Pacific Partnership (TPP) is a regional regulatory and investment agreement that was negotiated by 12 countries throughout Asia Pacific region, namely Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States and Vietnam. The proposed agreement had its baseline under the name of Trans-Pacific strategic Economic Partnership Agreement (TPSEP or P4) starting with the year of 2005 for four countries – New Zealand, Singapore, Brunei and Chile, as founding members. The original TPSEP agreement contained an accession clause, allowing the members to affirm their “commitment to encourage the accession to this Agreement by other economies” (New Zealand Ministry of Foreign Affairs & Trade, 2005).

In March 2008, the US joined the negotiations by expressing its intention to include the areas of financial services and investment in the negotiations, areas not mentioned by the initial TPSEP agreement. This international decision was closely followed by Australia, Peru and Vietnam, that joined the process the newly proposed agreement covered a larger geostrategic area, and was presented to the public under the name of Trans Pacific Partnership (TPP). The effective negotiations started in March 2010 and took into consideration the joining of a new member – Malaysia that joined the negotiations during the same year; as for Canada and Mexico, they were formally invited to join the TPP negotiations in 2012. Japan was the latest TPP participant to take part in the negotiations and brought the membership to twelve, and fully starting negotiations in July 2013. In early 2014, South Korea began to consult with the other TPP negotiating partners on the possibility of joining, but it

has never made a formal request. It was important that all the members of the TPP negotiators were also members of the Asia-Pacific Economic Cooperation (APEC), making the fusion process more difficult for the non-member countries.

### *1.1. Current negotiation status*

The agreement was negotiated within seven years, while 19 rounds of talks and numerous ministerial ad-hoc meetings were held between 2008 and 2015; according to a study of the Congressional Research Service, the most recent ministerial meeting occurred in Hawaii during March 24-31, 2015 (Ferguson *et al.*, 2015) where progress was made, resulting in the conclusion of the agreement six months later, in September 2015, by the chief negotiators of the 12 states, during the meeting in Atlanta, USA.

The Free Trade Agreement (FTA) had 30 chapters under negotiation, TPP partners envisioning the agreement to be “comprehensive and high-standard” (Kovshenin, 2015), by eliminating tariffs and non-tariff barriers to trade in goods, services and agriculture. Another issue of great importance for the trans-pacific negotiations agenda was to establish and to expand the existing rules in regard with intellectual property rights, foreign direct investment and other trade related issues. TPP negotiating partners strived to create a “21st century agreement” (Kovshenin, 2015) addressing important issues for all the economies in the context of a globalized economy.

### *1.2. How the negotiations worked*

The 12 countries representatives were ministers and negotiators representing each government participating in the TPP negotiations. During the official meetings, leaders attended, and ensured a transparent process of engaging stakeholders in the relevant countries, by valuing their input on many issues.

The discussions occurred both bilaterally and multilaterally, in order to address specific issues and provide guidance to the negotiators. There was a number of formal rounds of talks, that took place in different locations within the territories of the countries actively involved, and also a number of inter-sessional – ministerial and chief negotiators meetings, where proposals were exchanged, creative and pragmatic solutions to outstanding issues were identified and gaps closed.

The scope of this intense activity was to seek an agreement that balanced the members' range of expressed interests and achieve a comprehensive and transformative agreement with shared benefits (USTR, 2013).

The TPP is defined by five features, which can set standards for the future agreements. These chapters include areas like comprehensive market access, regional agreement, cross cutting trade issues, new trade issues (covering new issues that have emerged in the global trade) and a living agreement that includes an accord on the structure, institutions and processes that would enrich the future joint work in areas of common interest of future trade deals.

At the end of the negotiated period, in 2015, the representatives of the actively implicated Governments signed the text of the Agreement and the procedure was followed by making the result of seven years of negotiations available to the public. Each of the parties has to ratify the text, and this process estimated to take no longer than two years; this implies that in line with the internal legislation of each state involved, the legal text of the agreement will be examined by the members of the Parliament, the Governments and in some cases, voted by the public. If the text will be ratified by all the 12 states in the next two years, as stated by the official representatives at the end of negotiations, the legal Trans-Pacific Partnership text will come into force, the maximum effect of the results are not estimated to occur earlier than before the next 15 years (Horowitz, 2015).

### *1.3. Contents of the TPP*

The Trans-Pacific Partnership is designed to comprise 40 percent of the global economy and one third of global trade. The United States Trade Representative Office outlined 30 TPP chapters that include trade and trade-related issues, starting with trade in goods and continuing with customs and trade facilitation; sanitary and phytosanitary measures; technical barriers to trade; trade remedies; investment; services; electronic commerce; government procurement; intellectual property; labour; environment; "horizontal" chapters that will fully ensure the development of the TPP, competitiveness and inclusiveness; it continues with provisions in regard with dispute settlement, exceptions and institutional provisions (USTR, 2015).

The key features of the TPP seek to set new standards for global trade and incorporate issues that would increase the TPP countries' competitiveness in the global economy (USTR, 2015). These include competitive market access; its design seeks to eliminate tariffs and barriers to trade and investment, in order to create new opportunities in both areas – jobs and businesses- and immediate benefits for the consumers. Another key issue is represented by a fully regional agreement designed

to facilitate production and supply chains among TPP parties. Cross-cutting trade issues comply with regulatory coherence by promoting trade process and making it seamless and efficient; another cross cutting issue touches the sphere of competitiveness and business facilitation by promoting regional economic integration through the development of supply chains and regional production. Small and Medium Sized Enterprises would be encouraged to trade internationally; development is supported by a robust and comprehensive market liberalization, by strengthening TPP countries' institutions and effectively implement the agreement and fully realize its benefits.

The fourth key feature involves new trade challenges that promote a competitive business environment across the TPP region. One of the last attributes of the TPP is represented by its characteristic of being updated appropriately to the trade issues that may emerge in the future, as a result of its expansion to include new countries and the novelty of the trade issues that might occur.

The scope of the agreement is to undertake within a single body text all key trade and trade-related areas, by updating traditional approaches to issues covered by previous trade agreements (FTAs) the TPP includes, but also emerging trade issues and cross cutting issues. For this purpose, negotiating groups were formed, where representatives of the Ministries and specialists from different domains were involved. The legal text that emerged out of negotiation rounds covers all aspects of commercial relations among the TPP countries, with country-specific exceptions in annexes. An important issue that the TPP addresses is its coexistence with the existing international agreements among the countries involved (where WTO Agreement, bilateral and regional agreements are included) status which is being recognized within the Initial Provisions and General Definitions Chapter.

Leaders of the twelve TPP countries will continue alongside the negotiation teams to schedule the next steps that are complementary to the negotiated text of the agreement, by ratifying and implementing it within all the 12 states, and setting global standards to be achieved by the so called "third" parties to whom they keep commercial and investment connections with.

The TPP activity is ongoing through meetings among the Chief Negotiators, trade ministers and national structures responsible with the ratification of an international agreement. Both TPP leaders and ministers will meet on the sidelines of the negotiated text, making the conclusion of the agreements' ratification "a top priority" (Ferguson *et al.*, 2015).

## **2. Transatlantic Trade and Investment Partnership**

The comprehensive Transatlantic Trade and Investment Partnership (TTIP) is a free trade agreement currently being negotiated involving two of the largest economies worldwide, namely the European Union (EU) and the United States of America (USA). Its aim is to reduce the already low trade barriers to zero and protect and encourage investments on both sides of the Atlantic, by encouraging trade facilitation and job creation.

### *2.1. Evolution of TTIP*

Launched in 2013, its design involves increasing trade and investment between the two members, by reducing and where possible, eliminating trade barriers to transatlantic trade and investment flow. This aim is shared among the EU Member States and the US federal states, given the fact that after the end of the negotiations, the legal provisions will be implemented and used by all sides.

Early in 1990, The European Community (EC) composed of 12 countries and the US initiated a transatlantic dialogue by signing a *Transatlantic Declaration*. The initiative continued by creating in 1995 a pressure group of business people, namely the Transatlantic Business Dialogue (TABD) on both sides of the Atlantic, under the coordination of public authorities. Communication continued between Europe and North America by creating at first the Transatlantic Economic Partnership, and subsequently the Transatlantic Economic Council. The importance of these structures was given by the activity involved, where firms from both sides of the Atlantic organized advisory meetings for both the EU Commission and the US Government. The conclusions of this communication tandem resulted in 2011 in the creation of a high level group of experts whose recommendations in 2013 led to the launch of the negotiations for a comprehensive free trade agreement - TTIP.

### *2.2. Current negotiation status*

The TTIP negotiations are held in a format of week-long cycles, housed in locations on both sides of the Atlantic, mainly in Brussels and in Washington. Currently, eleven rounds of negotiations took place, the last one being held in October 2015, supposedly the twelfth round will be organized after January 2016. The design of the future trade agreement contains 24 chapters (EC - DG Trade,

2015) grouped into three parts, namely market access, regulatory cooperation and rules, suggesting principles and modes of cooperation that would be mutually respected by both parties.

### *2.3. How TTIP negotiations work*

TTIP is an agreement currently negotiated by the representatives of both EU and US. The European Commission is the European structure in charge of negotiating on behalf of the 28 Member States. The activities are led by the Directorate General (DG) Trade, the leadership belonging to a Chief Negotiator, supported by a team of experts and other parts of the Commission. On the behalf of European Commission, these actions are being completed with the support of nine other Directorates General (EC – DG Trade, 2013) together with the Secretariat General. These include: DG Internal Market, DG Agriculture and Rural Development, DG Enterprise and Industry, DG Taxation and Customs Union, DG Environment, DG Climate, DG Energy, DG Communications Networks, Content and Technology, and DG Competition (EC - DG Trade, 2015) covering a variety of negotiating areas.

The members of these European structures are negotiating on behalf of European Union, more precisely, representing all the 28 Member States governments. On behalf of the United States, the actions related to the TTIP negotiations are supported by The Office of the United States Trade Representative (USTR), in collaboration with stakeholders and representatives of the US Congress, as well as homologous of the negotiators and specialists that take part in the negotiation meetings.

In the cases when an agreement is reached, the 28 governments of the EU will have to approve or reject the agreement negotiated in the EU Council of Ministers; by this point, the European Parliament will be asked for its recommendation. The 28 EU Member States are governed by different judicial systems that impose a certain way of approving or ratifying the document. The United States will put forward the TTIP for ratification by both houses of the United States Congress: the Senate and the House of Representatives, which share a total number of 535 of voting members.

### *2.4. Contents of TTIP*

TTIP is designed to have 24 chapters, grouped into three parts (EC - DG Trade, 2015). The Market Access part includes Trade in Goods and Customs Duties, Services, Public Procurement and Rules of Origin. The second part, the regulatory Co-operation touches the areas of Regulatory Coherence, Technical Barriers to Trade (TBTs), Food Safety and Animal and Plant Health (SPS),

Information and Communication Technology (ICT), Pharmaceuticals. The third and last part of the desired TTIP agreement covers areas such as Sustainable Development, Customs and Trade Facilitation (CTF), Small and Medium Sized Enterprises, Investment Protection and Investor-State Dispute Settlement, Competition, enumerated non-exhaustively.

In 2015, the European Commission takes part in a transparency initiative, by making public the contents of the negotiations via proposals tabled on the second and third parts of the TTIP and the EU Position Papers. TTIP implies meetings with representatives of the civil society, and DG Trade's Civil Society Dialogue involves such meetings where trade policy issues are discussed. The topics discussed are of current interest, such as improving transparency and accountability of the TTIP negotiating process.

### 3. TPP and TTIP negotiating process

TPP is designed to have 30 chapters, and similarly to any FTA, each of the chapters consists of provisions covering different fields of interest. This is the reason for which the negotiating teams formed by representatives of all the 12 TPP member states worked as joint working groups, each team being formed of specialists covering a specific negotiation field.

The Ministries which were responsible for the development of the negotiations of the TPP according to each participating country are displayed as follows:

**Table 1 - TPP Negotiating Governments (by member state)**

Australia	Australian Government Department of Foreign Affairs and Trade
Brunei Darussalam	Ministry of Foreign Affairs and Trade Brunei Darussalam
Canada	Foreign Affairs, Trade and Development Canada
Chile	Ministry of Foreign Affairs of Chile
Japan	Ministry of Economy, Trade and Industry
Malaysia	Ministry of International Trade and Industry
Mexico	Secretariat of Foreign Affairs
New Zealand	New Zealand Ministry of Foreign Affairs and Trade
Peru	Ministry of Foreign Commerce and Tourism

Singapore	Ministry of Trade and Industry
United States	Office of the United States Trade Representative
Vietnam	Ministry of Industry and Trade

Source: own processing

Due to the fact that the TPP is designed as a multilateral agreement, its specificity consisted in the fact that, taking into consideration the need to speed up the negotiation process, countries also formed bilateral negotiation groups, where contradictory opinions were solved and proposals discussed. The conclusions of these bilateral actions were presented within the formal negotiation rounds, where the Leaders and other representatives took act of them and proceeded to the next issues on the working agenda.

The TTIP has 24 chapters, in the framework of which each field of interest is being analysed; the working groups are organized in the framework of this structure; this is why there are 24 joint EU-US working groups. Each working group deals a separate aspect of the agreement and organizes a week-long meeting, periodically, in varying locations ranging from Brussels to Washington and New York. The responsible structures negotiating on behalf of EC and USTR are displayed in Table no. 2.

**Table 2 - TTIP Negotiation Structures**

European Commission	Office of the United States Trade Representative
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Source: own processing

In the case of the TPP, official negotiation rounds vary, covering locations from all the 12 members of the treaty. Formal negotiation meetings, both in the cases of the TPP and the TTIP develop through a number of phases that are to be followed. At first, there is an exchange of position papers and at this point each party presents its aims and ambitions with regard to each aspect to be discussed. These are backed up by proposals of texts from each side, and where the case asks for, initial offers are made by the relevant sides. Negotiations continue, and new proposals are granted with acceptance or rejection, or partial agreements or partial denials; in the cases in which both sides are ready, a consolidated text is prepared. Provisionally, the text is considered to be agreed upon, the only remaining subjects of negotiation resting in the differences expressed in the text between brackets. The next step in reaching an agreement is provisionally closing each topic the agreement,

until a working consensus is reached. The importance of this process is given by the fact that unless each text containing a specified topic is not finalized, the agreement is not considered as being negotiated as a whole.

In October 2015, negotiations with regard to the TPP came to an end. The TPP is considered to be the most promising platform for ASIA-Pacific regional trade integration, designed to enhance trade and investment among the 12 TPP partner countries by promoting innovation, economic growth and development, and supporting the creation and retention of jobs. The TTIP is an ambitious, comprehensive and high-standard trade and investment agreement currently negotiated between the European Union and the United States, a companion of the TPP, a process where the EU negotiates on behalf of all the 28 Member States, designed to result in multilateral economic growth (EC - DG Trade, 2014).

### **Final remarks**

The teams negotiating for the TTIP are close to finalizing the landmark agreements, while the seven years of ongoing negotiations in the framework of the TPP have successfully come to an end. The ministers and negotiators have made significant progress in the last meetings; the teams have engaged actively bilaterally, addressing specific issues and provided guidance for the negotiators.

Concerning the TTIP, negotiating teams met for eleven formal rounds of talks, starting in 2013, as well as in numerous inter-sessional meetings, when proposals were exchanged and new solutions to outstanding issues were proposed. In the last seven years, the TPP negotiators met for more than 19 formal rounds of talks, starting in 2005. As countries adhered to the TPP negotiations, the number of representatives increased exponentially and the need for bilateral and multilateral negotiations became more prominent.

The two trade deals involve some of the most powerful economies of the world. Lowering trade barriers, and creating no-tariff geographical areas will conduct to an increase in international trade. If every TPP and TTIP country agrees with the provisions regarding international trade and their minimal regulations, the danger of misinterpreting the rules by corporations and third parties will increase. This is the reason why the secrecy surrounding the negotiations of the two trade deals is not considered as being a healthy behavior by the non-negotiating parties. Another high risk is that companies would have the opportunity to funnel their money through different countries, taking into consideration the strength of their legal position in relation to the government.

Closing these trade agreements will change the prospects and potential of trade across the Globe. The fact of negotiating the two agreements in parallel, covering together more than two thirds of the global economy and the most important part of the trade in goods and services, comes like a reciprocal backup for the involved economies. International trade rules and high standards are created, all complying with the international norms established by the WTO; these aspects encourage interpretation from the non-positive thinkers of the current economy, argument that is being supported by the US National Intelligence Council with the argument of Multi Component Global Power Index that maintains the idea that by 2030, no matter what the power index indicates, the present developing powers will overtake the developed states (Van Ham, 2013). This line of thinking has not been denied by the literature so far, thus encouraging the idea of the need for complementarity to sustain the survival of the two agreements – the TPP and the TTIP.

Not taking into consideration China represents a strong issue for both international agreements, as the potential of this growing economy is a concerning factor for the success of the implementation of the TTIP and the TPP. Given these facts, it can be concluded that politics should once more go beyond what is possible, and focus on the reality of what is possible, in our terms, getting a good outcome from the two agreements and saving the course of the actual global economy.

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## EU POLICIES REGARDING THE DEVELOPMENT OF TRUST-LIKE DEVICES - RECENT CHALLENGES, ACHIEVEMENTS, PROSPECTS AND TERMINOLOGICAL INSIGHTS

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**Abstract:** *“Trust” is a versatile instrument which is suitable for a great variety of purposes. Many scholars believe, that the original form of this institution appeared in common law, while in the 20<sup>th</sup> century the process of globalization stipulated the “internationalization” of the trust mechanism. The starting point of this process was the conclusion of the Hague Convention on the Law Applicable to Trusts and on their Recognition. Initially, the civil law jurisdictions were unable to adopt “trust” structure in which common-law power and equity power belonged to separate entities. Despite this fact, in the recent years, trust-like devices have been introduced in certain economic-juridical systems of Europe. Their rapid implementation raised the question of the establishment of innovative policies. This paper will discuss the latest achievements and existing challenges based on the example of the German juridical-economic system. The aim is to make useful proposals for the successful planning of the European entrusting processes.*

**Keywords:** globalization; trust; trust-like device

**JEL Classification:** K3

### Introduction

EU has not escaped the “overwhelming” process of globalization. It is vividly felt in almost all branches of the economic, social and juridical spheres. Rapid developments are predicted in all areas of human activities.

It’s a well-known fact, that the economy of a particular country as well as the law is not a static, but a dynamic phenomenon. It is a vivid result of a historical evolution which did not happen on its own, as if in a vacuum. Today’s globalizing processes stipulate the emergence of the institutions which facilitate intensive financial transactions, profitable investments and increased flows of money. The common law “trust” and its European “descendants” (German “*Treuhand*”, Italian “*Fondo patrimoniale*”, French “*Fiducie*”, etc.) can be regarded among these institutions. The English “trust” “is undoubtedly an extremely versatile instrument which is suitable for a great variety of purposes, even leading some commentators to qualify it as a “universal fix-it” (Koessler, 2012, p. 13). Many scholars believe, that the original form of this unique institution appeared in the common law of the Middle Ages. In 1872 the trust law was adopted in the State of Connecticut, while the first trust

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company was created in 1806 according to the recommendation of financier and politician A. Hamilton. During the 19<sup>th</sup> century, the given legal institution became popular in the American business sphere. It offered several economic and legal advantages, especially through mutual and pension funds, while at the end of the 20<sup>th</sup> century, the process of globalization stipulated the “internationalization” of the trust mechanism. The starting point of this process was the conclusion of the “Hague Convention on the Law Applicable to Trusts and on their Recognition” (1985) and its ratification by 12 countries. Initially, the civil law jurisdictions were unable to adopt the “trust” structure in which common-law power and equity power belonged to separate entities. Despite this fact, in the recent years, “trust-like devices” have been introduced in certain economic-juridical systems of Europe. Their rapid implementation raised the question of the establishment of innovative policies for the management of the functioning of these newly-emerged constructions. This paper will discuss the latest achievements and existing challenges on the example of German juridical-economic system. Moreover, it will make proposals, which will be useful for a successful planning of the European entrusting processes and terminological nomination of the concepts related to them.

## 1. German vis-à-vis English

It’s a well-known fact, that today’s Europe makes distinction between the civil and common legal traditions. In our paper these traditions are presented by England (common law) and Germany (civil law).

Many scholars believe that the greatest inconsistency between English and German jurisdictions is presented in the area of “Property law”. The German legal system comprises an absolute notion of ownership, which may be equalized with the Roman “*dominium*”. In the German reality, “the owner of a corporeal object is the person who is in principle entitled to “deal with the thing as he pleases and exclude others from any interference”. It belongs to him, and only him” (Häcker, 2009, p. 36). In contrast to the German law, the English juridical system embraces a non-absolute notion of ownership. “Firstly, English law adopts a system of relative titles as opposed to absolute entitlements. Secondly, the recognition that equitable interests are in some sense “proprietary” has led to the idea of ownership being “split” into bare legal title and an equitable (or beneficial) interest” (Häcker, 2009, p. 35-36). This division has historical roots. Moreover, it gave birth to the unique and remarkable common law institution named “*trust*”.

The “*trust*” can be described as an arrangement whereby property is managed by one person (*trustee*) for the benefit of another (*settler* or *beneficiary*). It has the following characteristics:

- a) “the assets constitute a separate fund and are not a part of the trustee’s own estate;
- b) title to the trust assets stands in the name of the trustee or in the name of another person on behalf of the trustee;
- c) the trustee has the power and the duty ... to manage, employ or dispose of the assets in accordance with the terms of the trust and the special duties imposed upon him by law”<sup>1</sup>.

It’s a well-known fact, that “German case law does not recognize the institution of the trust, as the trust is incompatible with the dogmatic foundations of German law and does not resemble the legal relationship of the *Treuhand*” (Sandor, 2014, p. 250). Moreover, “nowhere in German law can one find any single institution which by itself performs all those functions for which the common lawyer deploys the trust” (Kotz, 1999a, p. 85). However, the study of the contemporary German legal system reveals the existence of several “*trust-like devices*”, which work differently, but perform functions similar to the “*trust*”. B. Häcker directly indicates, that “in some situations a person holds rights for the benefit of another, via a device described by the umbrella term *Treuhand*... A *Treuhand* arises only in a limited number of particular instances (scattered throughout the BGB and developed outside the statutory framework), each subject to its own specific rules and principles” (Häcker, 2009, p. 39-40). Well-known German jurist Hein Kötz distinguishes three types of such institutions: “the *Testamentvollstreckung* and *Nacherbschaft*, which are used to control succession to property for several legatees (and typically for many years), the *Stiftung* which serves to collect and administer funds for charitable purposes, and the general *Treuhand* by which an estate is administered for the benefit of one or more persons” (Grundmann, 1998, p. 489). *Stiftung*, *Testamentvollstreckung* and *Nacherbschaft* are often regarded as *Quasitreuhands*, while *Treuhand* is a prime example of fiduciary arrangements of the German law.

### ***1.1. Treuhand***

The “*Treuhand*” is usually flexible and exempt from the state control. It considers the transference of ownership based on “*Vertrauen*” (trust) and “*Treue*” (loyalty). It can be established in three major ways: “through a full transfer of legal title (*fiduziarische Vollrechtstreuhand*), through a transfer of legal title with conditions precedent (*deutschrechtliche Treuhand*), and with a mandate granting dispositional rights (*Ermächtigungstreuhand*)” (Sandor, 2014, p. 253).

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<sup>1</sup>CONVENTION ON THE LAW APPLICABLE TO TRUSTS AND ON THEIR RECOGNITION, available at: [http://www.hcch.net/index\\_en.php?act=conventions.text&cid=59](http://www.hcch.net/index_en.php?act=conventions.text&cid=59)

Generally, the “**Treuhand**” “is created by a transfer of assets to the *Treuhänder* coupled with a contractual agreement made between him and the transferor under which he assumes, normally in consideration of a fee, a contractual duty to manage the assets in a particular way for the benefit of the beneficiaries” (Kotz, 1999a, p. 89). In other words, “**fiduziarische Treuhand**” is a fiduciary construction by which an individual transfers the full right *in rem* to the other individual. Therefore, the entrusting relations consider the following major elements:

- **Treugeber** (settlor/beneficiary) - an individual, which transfers the full right *in rem* to the other individual, who is obliged to deal with the assets in the manner specified by the contract;
- **Treuhänder** (trustee) – an individual, who is obliged to deal with the transferred assets in the manner specified by the contract.

“The Treuhand can exist without any written underpinning document. It can be concluded between any two persons capable of being party to a contract” (OECD, 2013, p. 39). Although in most cases the “**Treuhand**” represents a two-party relationship, it can include third party relationships. The “**Treuhand**” may take different forms: “hidden (verdeckte Treuhand) or disclosed to third parties (offene Treuhand)” (OECD, 2013, p. 39-40).

It is also worth mentioning, that although the **Treugeber** transfers his juridical ownership to the **Treuhänder**, he retains the economic ownership. Therefore, a trustee (**Treuhänder**) becomes a legal owner, whose duties are called fiduciary duties: “The *Treuhänder* acquires a full and unrestricted title to the Treuhand assets, whereas the beneficiaries’ interests are, at least in theory, merely the ordinary rights *in personam* of parties to a contract” (Kotz, 1999a, p. 93). The **Treuhänder** can transfer the legal title to a third person, while the **Treugeber** has only damages claims in those cases when the transferor violates the obligations. It means that the “**fiduziarische Treuhand**” does not fully protect the rights of the **Treugeber**. Therefore, the practical implementation of this construction seems quite risky.

However, the German legal system gives the **Treugeber** an opportunity to make a safer agreement (the so-called **Ermächtigungstreuhand** - trust by authorization), under which he (she) does not transfer the full right *in rem* to the **Treuhänder**, but simply authorizes him (her) to manage or dispose of the assets in a specific manner. When the trustee exceeds his authorization the disposal of the assets is not valid ... no real separation of property takes place and the protection of the settlor is of minor importance because he is still the legal owner with all of his power” (Rehahn *et al.*, 2012, p. 100-101).

### 1.1.1. *Stiftung*

*Stiftung* is usually identified with a “charitable trust”. It belongs to the group of juristic entities capable of owning property and of suing and being sued. If a person wants to dedicate assets to charitable purposes or to devote patrimony to specific aims, he/she “must declare such an intention in writing or by will (testamentary foundation), the *Stiftungsgeschäft* or endowment transaction” (Rehahn *et al.*, 2012, p. 102). The given transaction consists of two parties:

- a **founder (Stifter)**, which transfers a patrimony to a new legal entity and sets up rules of administration;
- a **foundation (Stiftung)** – a newly-created legal entity, which administers assets, but is supervised by the Bundesland.

The “*Stiftung*” can be created only with the permission of the “Bundesland”, or the federal state, where a newly-created legal entity will have its seat. It is worth mentioning that “apart from the creation of a new legal entity, the trustor can also transfer the property to an already existing person with the declaration that the transferee must separate these assets from his own property and has to administer them on a continuing basis as the trustor has set it up” (Westebbe, 1993). Such type of a transaction is nominated as “*Stiftungstreuhand*” or “*unselbständige Stiftung*”. The latter considers the transference of a smaller amount of property. The founder “transfers assets as a gift *inter vivos* or by will to another natural or juristic person – e.g. a university, a church, a museum, a charitable association - on the understanding that the transferee keeps the assets transferred separate from his own assets and that the gains made from the assets shall be used to further the charitable purpose prescribed by the founder” (Kotz, 1999b, p. 52). It is worth mentioning that in the case of “*Stiftungstreuhand*” or “*unselbständige Stiftung*” (*foundation trust* or *dependent foundation*), the trustee’s creditors are not able to take legal actions in respect to the separated assets. These actions can be impeded by a founder or by beneficiaries. This is a unique example of *Sondervermögen* (separated patrimony). The existence of *Sondervermögen* emphasizes the fact, that German law “accepts” the notion of “splitting-up” - owning of more than one patrimony by one person. Such separation of assets is determined by the concept of patrimony rather than that of property, because the German property law is not based on the distinction between legal property and equitable property. The major reason for splitting is that “the separated patrimony serves specific functions such as providing liable patrimony for specific creditors, a particular administration of that patrimony or the protection of certain persons. The creation of a *Sondervermögen* is only possible within the limits of statutory law” (Rehahn *et al.*, 2012, p. 95).

Therefore, an in-depth study of *Stiftung* reveals its similarity to a “charitable trust”. However, there are certain differences between these two institutions - the *Stiftung* (foundation) should be registered, “the representatives of foundations do not act in their own name, and the founder may not be exclusive manager (Vorstand) of the foundation. As an additional difference, the representatives are also liable to third parties” (Selbig, 2006, p. 167). The establishment of *Stiftung* is quite expensive. Therefore, a trustor can use a simpler and cheaper way. He/She may transfer “assets to another on the understanding that the assets shall constitute a separate fund, shall not form part of the transferee’s own estate and that the transferee shall have the power and the duty to manage the assets for the charitable purpose specified by the transferor” (H. Kotz, 1999a, p. 88). This type of relationship between parties can be analyzed as “*fiduziarische Treuhand*”, which has already been discussed.

#### 1.1.2. *Contractual Trust Arrangements (CTAs)*

German “*trust-like devices*” have gained the greatest importance in the sphere of the economy, especially, through company law. Since the 90s of the 20<sup>th</sup> century the so-called *Contractual Trust Arrangements* (CTAs) have been increasingly utilized by different types of German companies. These agreements enable each company “to improve its balance sheet ratios and creditworthiness in accordance with the International Financial Reporting Standards (IFRS), the United States Generally Accepted Accounting Principles (US-GAAP) and German accounting rules pursuant to the German Commercial Code by removing both the pension obligations towards its employees and the covering assets from the balance sheet” (Rehahn *et al.*, 2012, p. 103). *Contractual Trust Arrangements* are focused on the following:

- outsourcing obligations to a third person;
- ensuring the settlement of employees’ pension claims;
- protecting the covering assets against the access of the creditors in the event of the insolvency of sponsoring undertaking.

The lack of a coherent trust concept in German law leads to difficulties during the fulfillment of the last activity, because “in the event of the opening of insolvency proceedings regarding the assets of the sponsoring undertaking, the trust agreement shall expire which would normally establish a duty of the association to return the property to the insolvency administrator” (Rehahn *et al.*, 2012,

p. 104). The given problem is usually solved by the creation of a second trust. This is the case of the “*doppelseitige Treuhand*” (two-way trust).

In certain cases the members of personal companies or shareholders of public companies transfer their rights of shareholders to a third party/a third person, who performs the functions of a trustee. This trust solution “concerns a *Kommanditgesellschaft*, in which as a personally liable partner a limited liability company participates with dozens, sometimes hundreds, of individual investors as limited partners (*Kommanditisten*). Here, it would be impracticable to invite all those investors to general meeting of the company so that each could separately exercise his rights as partner” (H. Kotz, 1999b, p. 56). Therefore, the best management option in such cases is the transference of the limited partners’ interests to a single trustee, who is obliged to exercise them in the interest of investor-partners. This mode of management is called “*Gesellschaftsanteile*” (administrative trust of company shares).

### *1.1.3. Terminological Insights*

An in-depth study of the contemporary German economic-juridical “*trust-like devices*” and their English equivalents enables us to make some terminological insights. The major emphasis ought to be put on the term “*Treuhand*”, because it is used “as a collective term in German legal literature and legal practice, which summarizes many different legal relationships of property management” (Sandor, 2014, p. 254).

The carried out terminological study vividly reveals that “Routledge German Dictionary of Business, Commerce, and Finance” presents the following English equivalents of the German lexical units related to the “*Treuhand*”:

“*Treuhand* – Trust;

*Treuhänder* – Trustee, fiduciary;

*Treugeber* – settlor, transferor, trustor (AmE)” (Routledge German Dictionary of Business, Commerce, and Finance, 1997)

The same data is presented in H. Haschka and H. Schmatzer’s well-known work “Aspects of U.S. business and law (An English-language survey with German-language comments)”. This book directly indicates, that “the essential elements of a trust are:

- A trustor or settler (*Treugeber*).
- A beneficiary (*Begünstigter*).
- A trustee (*Treuhänder*).

- A fund or corpus (zweckgebundene Vermögensmasse) the title to which passes to the trustee” (Haschka *et al.*, 1990, p. 167).

Additionally, “Collins English-German Dictionary” presents the following German equivalents of the common law term “*trust*”:

- “(law, finance) Treuhand (schaft) *f*
- (= property) Treuhandeigentum *nt*
- (= charitable fund) Stiftung *f*<sup>2</sup>.

The existence of all the above mentioned equivalents makes the essence of „*Treuhand*” obscure and equalizes it with the Anglo-American “*trust*”. Some scholars have thoroughly discussed this question, for instance, Sh. A. Stark directly indicated, that the term „*Treuhand*” had a purely German origin: “the German word “*treu*” means true and implies faithful” (Stark Sh., 2009, p. 3). Despite this explanation “the word *Treuhand* is not a clear term in German, it cannot be exclusively described as a trust in English either. For this reason, it is best to continue using the German word *Treuhand* because it has no equivalent in English” (Stark Sh., 2009, p. 3). J. Rehahn and A. Grimm share Stark’s idea and state: “German law is neither able to produce exactly the same effects as a trust in common law nor has it one specific concept that works as a trust... the German law does not know a homogeneous concept of a trust...” (Rehahn *et al.*, 2012, p. 94). According to J. Rehahn and A. Grimm the term „*Treuhand*” must be translated as „*German trust*”. The scholars directly indicate, that this will help with the “eradication” of any ambiguities during the process of translation. The same English equivalent (*German trust*) of “*Treuhand*” is presented in the following passage of the book “Property law and economics”: “Concerning the unitary ownership characteristic, society has created different kinds of ownership, which can be seen as forms of divided ownership, as the Treuhand (*German trust*) and fiducie-gestion (*French trust*)” (Bouckaert, 2010, p. 28). We believe, that „*German trust*” is the best English translation of the term „*Treuhand*”. Moreover, it is recommended to translate the “*Treugeber*” as the “German trustor/settlor” and to nominate the “*Treuhänder*” as the “German trustee”.

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<sup>2</sup>Collins English-German Dictionary, available at: <http://www.collinsdictionary.com/dictionary/english-german/trust>

## Conclusions

Therefore, the juridical-economic study of the contemporary German reality vividly reveals that it has no single institution which performs all the functions performed by the common law “*trust*”. Even the “*Treuhand*” - a prime example of fiduciary arrangements - is irreconcilable with the “*trust*”, namely, in the third party relationships. Some scholars directly indicate that German law cannot cope with the doctrine of the “real subrogation”. This means that in those cases, when the “*Treuhänder*” buys assets with the money supplied by the *Treugeber* “or with the proceeds of sales of the original property, or obtains property it exchanges for the original property, it is not clear whether the beneficiaries will be awarded a proprietary right in the substitute property and on this basis take priority over the *Treuhänder*’s private creditors” (Kotz, 1999a, p. 95).

All the above mentioned directly indicates to the following prominent fact: the German court has no general competence in exercising the supervisory and administrative functions needed to make the “*Treuhand*” as effective as the “*trust*” in the issues of the management of property. Therefore, the rules of the German law regulating the “*fiduziarische Treuhand*” need clarification and improvement via defining the questions of third party relationships and “real subrogation”. Moreover, significant changes must be made in the terminological sphere in order to reflect the difference between the common law “*trust*” and German “*Treuhand*”. We believe that „*German trust*” is the best English translation of the term „*Treuhand*”. Moreover, we recommend to translate “*Treugeber*” as the “German trustor/settlor” and to nominate the “*Treuhänder*” as the “German trustee”.

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## NEW GEOPOLITICAL REALITIES AND UKRAINE: IN SEARCH OF NEW INTERNATIONAL MODELS AND COMBINATIONS

Vladlen MAKOUKH\*

**Abstract:** *The new geopolitical realities pose difficult challenges for Ukraine in reviving old, as well as in searching new international models, combinations and configurations. Thus, when considering regional models such as the incentives GUAM, «V4», or BSEC, Ukraine should take into consideration, both their ups and downs. Within this context, the current paper proposes to assess the risks of Ukraine's participation in various forms of blocs and alliances.*

**Keywords:** «Baltic-Black Sea-Caspian Union»; GUAM; «V4»; BSEC; Ukraine

### Introduction

The new geopolitical conditions, which are being formed in the Black Sea region, represent the major stimulus that pushes the Ukrainian Foreign Ministry to assess the feasibility of reviving old and finding fundamentally new regional alliances involving Ukraine.

This paper investigates the question of efficiency regarding Ukraine's participation in regional blocs and organizations that already exist, such as BSEC and GUAM, or within newly established «V4» group, as well as whether to assess the prospects of joining international association, which will probably be established in the near future ("Baltic-Black Sea-Caspian Union").

The issue of Ukraine's participation in various regional organizations, blocs and alliances was debated in the significant number of works of Ukrainian and foreign scientists, among which are the studies of political scientists of Odessa National University - Irina Maksimenko, Sergei Glebov, Lyudmila Rossokha, Hanna Shelest, Marina Vorotnyuk, as well as Nadiia Bureiko, and Oksana Dobrzhanska, affiliated to Yuriy Fedkovych Chernivtsi National University. Nevertheless, at global level, the interest in this topic among foreign scientists decreases every year. Despite this decrease, there are still researchers interested in this topic, such as the well-known Georgian research scientist and diplomat Zurab Marshaniya, the Turkish scientists Halil and Bugrahan Nuri Erdemir, or the Romanian scientists Lavinia Lupu and Alexandru Voicu.

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## **1. Regional blocks and alliances: assessment of feasibility of Ukraine's participation**

### ***1.1. Ukraine's participation in already established regional organizations***

GUAM (est. in 1997) represents a regional group conceived as an alternative to EurAsEC and to other integration blocks in the CIS. It includes Georgia, Azerbaijan, Ukraine and Moldova. Under the Charter (GUAM, 2015), the main purposes of GUAM are: promoting democratic values and the rule of law, ensuring of human rights and sustainable development; strengthening of international and regional security and stability; deepening of European integration for creation of common security space, and expansion of economic and humanitarian cooperation; development of socio-economic, transport, energy, scientific-technical and humanitarian capacity; intensification of political interaction and practical cooperation in the areas of mutual interest.

GUAM member states cooperate in the framework of international organizations, including the UN and the OSCE. In 2003, GUAM was granted observer status within the UN General Assembly. According to the GUAM-US framework program for facilitation of trade and transportation, ensuring border and customs control, combating terrorism, organized crime and drug trafficking, the members of GUAM with the assistance of the US, the SECI Centre, together with experts from Bulgaria, Romania and Hungary had implemented a number of joint projects. In particular, it was established the GUAM Virtual Center for combating terrorism, organized crime, drug trafficking and other dangerous crimes. Currently, the center works on realization of project for facilitation of trade and transport. On the 16<sup>th</sup> and 17<sup>th</sup> of September 2015, the GUAM Secretariat in Kyiv hosted the 35<sup>th</sup> meeting of the GUAM Council of National Coordinators. The Council considered the question of promoting the draft resolution «Protracted conflicts in the GUAM area and their implications for international peace, security and development» in the General Assembly of UNO.

The main standing challenge for GUAM is Russia's position in relation to the organization, which has been relatively negative from the beginning. The Kremlin sees GUAM as the organization that damages Russia's interests in the post-Soviet territory.

It is likely that an integrated approach will allow Ukraine to use GUAM as a platform to implement ideas and initiatives that could contribute to regional security and stability in the Black Sea. This can be achieved not only through the efforts of member states, but also by involving a wide range of international partners.

Cooperation within the **Black Sea Economic Cooperation** organization is an important priority for Ukraine. Except for Ukraine, the other members of the organization are: Azerbaijan, Albania, Bulgaria, Armenia, Greece, Georgia, Moldova, Russia, Romania, Serbia and Turkey (Black Sea,

2014). The primary task of the BSEC is to develop economic cooperation in the Black Sea region, including: the promotion of various joint integration projects, starting with the regional "free trade zone" to smaller, such as the transport corridor (so-called "ring around the Black Sea"), and various energy projects: transportation of oil and electricity.

Besides, the BSEC is extremely important for the EU as a possible tool for promoting European interests in the Black Sea region. After the EU accession of Romania and Bulgaria, as well as in the context of the existing internal debates among European countries regarding Turkey's integration in the EU, the actuality of the «Black Sea direction» strengthening in the regional policy of EU became apparent (Cooperation, 2015). In this regard, there could be outlined the decisions on both issues – the seriousness of EU's intentions to interact with the Black Sea regional organizations, as well as the reality of prospects for "Great Black Sea" countries integration to the EU (most of which are still outside the European Union - Georgia, Ukraine, Moldova, Azerbaijan and Armenia).

Taking into account the "special attitude" of Russian attitude towards the European integration course of these countries, the long-term strategy of President Putin includes the political and economic division of Europe ("West") with the aim to create opportunities to interact with each particular state, using the Russian military-political and economic potential. It is also clear that the occupation of parts of its neighbors' territories as a tool for blocking the process of these states' integration in the western political and security space and it becomes the main instrument of the regional dimension of Russia's policy.

Thus, at present, strengthening its positions within the Black Sea region should become one of the highest priorities for the EU, because after the Crimea annexation, the military-political potential and Russian ambitions in the Black Sea have increased significantly. It should be noted that both Turkey and Ukraine give particular importance to BSEC as an organization, and this fact increases their weight in negotiations about possible accession to the EU (Maksimenko, 2012). The presence of European states within BSEC is very important as it seriously contributes to shaping possible opposition to Russia's counteractions regarding a number of foreign policy issues, thus becoming a solution in which Ukraine is interested in. Moreover, a noteworthy aspect is that within the BSEC framework, Russia continues to show interest in participating in various projects concerning specific issues, such as: the common energy market, transport infrastructure, cross-border cooperation etc. With this in mind, one cannot rule out Russian lobbying of energy projects which for various reasons is not profitable for Ukraine. However, direct involvement of Russia in the Syrian conflict on the side of the forces of the President Bashar al-Assad regime and the differences in the positions of Turkey and Russia on "the future of Syria" may affect the dynamics of Turkish-Russian relations.

BLACKSEAFOR is a military component of the naval operative interactions in the Black Sea region. However, unlike EUROMARFOR or "Visegrad Battle Group", the BLACKSEAFOR now has more challenges than opportunities. For more than ten years of existence, BLACKSEAFOR has become less of a naval "unit", but rather a "club", where the military member countries may decide without mediators specific issues of military and military-technical cooperation in the context of security in the Black Sea region (Poltorakov, 2011).

### *1.2. Ukraine's participation in new regional associations*

"Visegrad Four" (also called "Visegrad Group" or «V4») – is an association of four Central European countries: Poland, Slovakia, Hungary and the Czech Republic. It was established during the Summit of Heads of State and Government of Czechoslovakia, Hungary and Poland in Visegrad castle, in Hungary, on February 15<sup>th</sup>, 1991. From the beginning, the Presidents of the three countries established the so-called "Visegrad three" («V3»), which after the dissolution of Czechoslovakia turned into "Visegrad four" («V4»). The initial aim of «V4» was to promote the integration of member countries into NATO and the EU.

The idea to create a group to support Ukrainian reforms was initiated in the course of negotiations of «V4» countries with western partners in Bratislava in 2014. Then, it was decided to organize a joint visit of the Polish, Hungarian, Slovakian and Czech Foreign Ministers to Ukraine (Doroga, 2015). In addition, «V4» countries announced a plan to create a special fund to support Ukraine. While the assets of the Fund have not been made public, it was announced that the Fund is ready to provide Ukrainian students with 410 scholarships to study in Europe (Korba, 2014).

During the official meeting in Kiev with the Foreign Ministers of Poland, Hungary, Slovakia and the Czech Republic, the Ukrainian President Petro Poroshenko announced Ukraine's intention to join the "Visegrad Four", and subsequently to convert the group into "Visegrad five". Some European countries "quartet" supported this idea. Thus, the Foreign Minister of Poland Grzegorz Schetina said that Poland is interested in the integration of Ukraine into the European Union and, accordingly, its joining the "Visegrad Four". Similarly, Slovakia expressed its interest in creating a more effective union based on «V4», provided that the main priority of such a union would be lobbying the common interests of the region of Central and Eastern Europe (CEE) on the EU forums. It is possible that with this purpose, some amendments would be introduced regarding the membership of the association and in the organizational framework of «V4». Overall, the Ukrainian party counts on the support of all organization's members on the issue of Ukraine's entry into the «V4» and its transformation to «V5».

Thus, it is essential to deepen cooperation between Ukraine and the "Visegrad Group", in particular, for borrowing the European experience and further development of cross-border cooperation in the process of enlargement of the European Union (using certain benefits from the creation of free economic zones, development of joint cross-border projects and cross-border infrastructure, improvement of cross-border control, etc.). It is also important to consult on other issues of mutual interest. Particular attention should be paid to issues related to the promotion of political and economic interests of Ukraine in international organizations and receiving effective assistance from the countries of the Visegrad Group in the form of additional financial resources (to support and stabilise the Ukrainian economy).

The initiative "**Baltic-Black-Caspian Sea Union**" (Voloshin, 2013) was announced by the former Presidents of Ukraine and Georgia, respectively Victor Yushenko and Mihail Saakashvili in 2005. It is believed that the Union should encompass countries-initiators (Ukraine and Georgia), countries of the Baltic region (Lithuania in the first place), Caucasus (Azerbaijan) and Central Asia (Kazakhstan, Uzbekistan). The geopolitical aim of the union, above all, was to create a political and economic counterweight to the Belarus - Russia - Kazakhstan bloc, which, at that time began to be strengthened, as well as to the Shanghai Cooperation Organization. An important role in distancing potential member countries from Russia's Union was played by Poland. In addition, there was a count of pro-American orientation among the potential member countries 'elites.

However, for that period the creation of the alliance was complicated by the presence of a number of factors. First, by the heterogeneous attitude of the planned Union population towards the new association. Second, by the fluctuations within Azerbaijan, Kazakhstan and Uzbekistan leadership on the entry into the Union (it should also take into account the fact that Kazakhstan and Uzbekistan had already been members of the Shanghai Cooperation Organization).

After a long "downtime" and in the context of the crisis in the recent years (including the conflict in the eastern part of Ukraine), in 2015, the President of Poland Andrzej Duda addressed the idea of a reanimation of the Baltic-Black Sea-Caspian project. He suggested setting up a union in an updated format (Latvia, Lithuania, Poland, Ukraine, Slovakia with the possible accession of Moldova and Turkey).

In such ideas, Warsaw can hope on Washington's assistance, as far as the US devotes great attention to the idea of Baltic-Black Sea-Caspian Union. The New Community may be useful to Americans as a lever of pressure on the old "pillars" of EU - France, Germany and the UK. However, the Baltic-Black Sea arc, which should be the place of accomplishing Andrzej Duda's geopolitical plans, is not very viable. Thus, relations between Poland and Lithuania have some historical nuances.

Adding to this the fact that many Central European countries have strong pro-Russian lobby. All potential candidate countries have their own national interests that may compete with each other (Leusenko, 2015).

In addition, for an effective functioning, the Union badly needs Turkey, which plays the role of a "cork" in the Caspian bottle. Thus, the pipeline in Central Asia can go only through Turkish territory, as far as Azerbaijan sandwiched between the territories of two countries which often display unfriendly attitude towards the American geopolitical experiments - Iran and Russia.

Moving forward with the plans for creating the Baltic-Black Sea arc (in any format), one can expect reactions from the Russian Foreign Ministry (Karaichentsev, 2004). Therefore, the tactics of Russia consist of creating and maintain the existing "frozen" conflicts, especially in the region between the Baltic, Black and Caspian Seas, which will allow Russia not only to slow down the integration process of regional states in NATO and the EU, but also to emphasize the internal contradictions within the European Union, thus trying to split its unity on the issue of sanctions against Russia.

### **Conclusions**

Based on the above, we can conclude that, in general, Ukraine's participation in the work of such organizations and blocs such as the "Visegrad Four", BSEC, or GUAM, will boost its international prestige and strengthen regional security and stability in the Black Sea region.

However, it should be noted that the main obstacle to Ukraine's joining the European integration space is a lack of consensus between Western, Central and Eastern Europe both on the issue of its membership in some international and regional organizations, as well as on the interaction between Ukraine and Russia, especially in the context of managing "hot" regional issues and "frozen" conflicts.

Overall, in the future, one cannot exclude the possibility of establishing new regional blocs, unions and organizations, which could incorporate Ukraine. It is likely that the participation in such unions contributes to restoring peace and enhancing stability, both in Ukraine and in the "frozen conflicts" areas located on the territory of other post-Soviet countries.

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## ROMANIA, THE EUROPEAN UNION AND RUSSIA

Ion MUSCHEI\*

**Abstract:** *Throughout history, international relationships have always witnessed the forming of alliances, bilateral agreements, mutual treaties, conventions, partnerships or founding organizations. All these agreements have lasted as long as all the actors involved have shared a common interest, but during conflictual periods they have been reduced to simple sheets of paper. Certainly, the very same states have, again and again, been both ‘friends’ and ‘enemies’ because in international relations “nations have no permanent friends or allies, they only have permanent interests.”<sup>1</sup> Thus, in a world of growing interdependence and continuous change, globalization will not turn this world into a flat one, nor will it bring history to an end. On the contrary, it will generate new threats and will make differences more obvious and more striking. Moreover, the events that have taken place during the last few years clearly point this out. Starting with the 2013 Summit in Vilnius, the European Neighbourhood Policy and the Eastern Partnership, in particular, have brought about major direct changes in Eastern Europe and indirect ones in Bruxelles, culminating in territorial changes in the immediate proximity of Romania. Taking into account both its significant geopolitical and geostrategic location and its membership to the European Union, Romania finds itself, as always, at a crossroads. In this context, the present paper aims at determining the role the European Union plays in Romania’s relationship with Russia.*

**Keywords:** European Union; Eastern Partnership; European Neighbourhood Policy; globalization

**JEL Classification:** F51; R58; F68

### Introduction

The relationship between Romania and Russia is defined by uniqueness, a feature that can be inferred from the way in which relations have fluctuated in time. One could say that they have been closer to abnormal rather than normal. A plain analysis of the geopolitical and geostrategic features shows that the two countries should have a peaceful relationship based on friendship and collaboration, especially since both of them have access to the shores of the Black Sea. History, however, proves the contrary, clearly showing that this relationship has always been antipodal. Romania and Russia have never had stable relations, either in the long or in the short term, and, whereas they were able to be good friends at times, they have been enemies most of the times. To prove this, I will only mention two examples that support my point of view.

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<sup>1</sup> The statement belongs to Henry John Temple, 3<sup>rd</sup> Viscount Palmerston, also known as Lord Palmerston, former British Prime Minister, 1855-1858 and 1859-1865, who claimed that his country had “no eternal friends and allies, only perpetual interests.”



The two countries worked in cooperation with one another for the first time between 1877-1878 during the Russo-Turkish War, which also led to Romania obtaining its independence from the Ottoman Empire, after centuries of Ottoman domination. This relationship was based on an alliance formed between the Russian Empire and the Romanian United Principalities and agreed upon through a treaty signed on the 4<sup>th</sup> of April 1877, in Bucharest. According to the treaty, the Romanian Principalities allowed Russian troops to cross their territories while the Russian Empire guaranteed to defend and maintain Romania's territorial integrity. At that time, Romania was a small state with high nationalistic ambitions, one which could not break from under the Ottoman domination on its own. To the victory won by the Russian Empire, Romania contributed with 125,000 soldiers, 12,300 horses and 190 cannons, an arsenal which could be considered quite significant for that period. At the end of the war, Russia not only acknowledged Romania's independence, but also signed over the Dobrogea region (in the south-east), the Danube Delta, including Constanta Harbor, and the Snake Island.

There followed a 4-decade period of neutral nature in the Russo-Romanian relations, except for the First World War, when Romania joined forces with the Entente, thus being an ally of the Russian Empire as well, until the latter withdrew in 1917 due to the outbreak of the Russian Revolution. A remarkable aspect of these relations during the interwar years was the special rapport between probably the greatest diplomats that the two states had, both of them former foreign ministers. One was Nicolae Titulescu, the Romanian diplomat who used to be the president of the League of Nations and the other one was Maxim Litvinov, the most influential Russian diplomat, who had a crucial contribution to the Soviet Union getting out of the post-revolutionary isolation.

Once the two foreign ministers, Ribbentrop and Molotov, signed the Non-aggression pact on the 23<sup>rd</sup> of August 1939, the relationship between Romania and the Soviet Union came to a deadlock. Starting that moment, the relations between the two states became detrimental for Romania, which became a subjugated state, while Russia turned into an aggressor state. Taking advantage of this treaty, the latter made territorial claims and presented Romania with an ultimatum to return Basarabia and the northern part of Bucovina, territories which, as a matter of fact, had always belonged to Romania. At first, Romania invited the Russian government to amiable consultations on all the issues, aimed at reaching a mutual agreement. However, this reply was interpreted without any spirit of friendship or intention of cooperation. Furthermore, it produced such discontent that V. Molotov transmitted a new ultimatum to the Romanian government demanding it to evacuate Basarabia and Northern Bucovina within no more than 4 days. Therefore, "the Romanian government, in order to avoid any severe consequences that resorting to force and aggression in this part of Europe might lead

to sees itself compelled to accept the evacuation terms stipulated in the Soviet response” (Scurtu, 2012, p. 11). The year 1940 may be actually considered the darkest in the history of modern Romania since, in addition to giving up Basarabia and Northern Bucovina, Romania also had to give up the Quadrilateral to Bulgaria and the Northeastern part of Transylvania to Hungary.

After the end of the Second World War, Romania became part of the sphere of influence of USSR. In Bucharest, a communist regime was forcefully set up and it was faithful to the politics of the Soviet Union. As a consequence, during post-war years, the Russo-Romanian relations were defined by the subordination of the Romanian communist regime to USSR. Therefore, one cannot truly speak of bilateral or friendly relations between Romanians and Russians in that period, even though the leaders of the two states frequently visited each other. Moreover, according to the Treaty of Versailles, Romania was considered a defeated state so it had to pay Russia material damage amounting to 300,000,000 USD, which was a sum far from insignificant and quite high for those times.

Afterwards, the situation changes dramatically due to two events that occurred in both states. On the one hand, there was the Romanian Revolution in 1989 which demolished the communist regime and, on the other, the fall, in 1991, of the “Evil Empire”, as Ronald Reagan called the USSR, in 1983. These two major events led to crucial changes within the two countries and therefore in their relations to one another, as well. Romania chose to move its politics towards the West, aiming at becoming part of the European Union and to integrate in the political-military structure of NATO. Whereas the Russian Federation, the rightful successor of the USSR, confronted with a large series of severe internal problems, it has oriented its politics towards economic rehabilitation and development.

Nowadays, the Russo-Romanian relations have reached a new stage with the signing of the basic Political Treaty in 2003, concerning the relations of friendship and cooperation between Romania and the Russian Federation, as well as several other collaboration agreements, shortly followed by the establishment and enforcement of the dialogue at high ranks – head of states, government, foreign affairs ministers and parliament leaders. The novelty is brought by the role that Romania was given after the events that took place in these two countries, especially in the last ten years. At present, the Russo-Romanian relationship is more complex, vaster and more ambiguous at the same time. Romania became a member of NATO in 2004 and a full member of the European Union in 2007. Meanwhile, Russia’s evolution was and still is defined by the Kremlin leader that is Vladimir Putin.

Taking all these into consideration, the Russo-Romanian relations have entered a new dimension and it is, therefore, intriguing to monitor and analyse whether Romania's membership to the European Union and NATO has any influence on these relations and to what extent, in particular. Is Romania, as member state of the European Union, an object or a subject in the Russo-Romanian relations? What can Romania do? What can the European Union do?

### **1. Relationship between Romania, as a EU member state, and Russia.**

When Romania became a full member of the European Union on the 1st of January 2007, it adhered to the largest economic market in the world and to an international organization with a *sui generis* structure. This organization has, at present, 28 member states and its frontiers are so large that they were inconceivable to the founders at the time of its creation. Consequently, the European Union became Russia's neighbour in 2004, through the integration of the Baltic States, and in 2007 it established its eastern frontier in the immediate proximity of Russia's sphere of influence, when Romania and Bulgaria adhered to the Union. Moreover, Romania's adhering allowed the European Union direct access to the Black Sea. The integration process was a strong desideratum for the Romanians and it was considered a great success for post-revolutionary Romania. Every Romanian citizen was enthusiastic about it and had a positive perspective. However, despite all these, the Romanian state was not able to exploit to the maximum the advantages that membership to this organization brings its members, so, during the eight years since adhering to the European Community, Romanians have started to doubt its efficiency and reason. It is very difficult to say what the situation would be today if Romania had not become a member of NATO or the European Union, but it is certain that with the integration in EU, the country gave up part of its sovereignty and aligned with the politics in Bruxelles. This means that in some fields, the European Union is the one that sets up the limits and conditions under which its members can use their competences. For example, according to the Treaty of Lisbon which came into force in 2009, EU has exclusive competence concerning a potential international agreement, if closing such an agreement is regulated by a law of EU; that is, only EU can legislate and adopt legally binding acts and the member states can only do this, if they are empowered by the EU. Therefore, Romania has no chance at directly negotiating with the Russian Federation and it is forbidden to close any bilateral agreement with Russia, if European principles and values are not taking into account. Thus, the Russo-Romanian relations must now be filtered through EU, which is not at all appreciated by Russians.

In a debate governed by the Chantam House Rule which took place in Bucharest at the Titulescu European Foundation, -which I, personally attended-, the Russian ambassador in Bucharest, Oleg Malginov, declared that Romania has only to lose from avoiding direct negotiations with the Russian Federation and therefore, Russia sees itself forced to discuss Romania's interests and problems with the EU. Thus, the ambassador cannot understand how Germany or France knows better what is good and what is not good for Romania. In this respect, it can be inferred that Romania plays mostly the role of an object, not that of a subject in its relations with Russia and that these relations are directly influenced by the Russo-European relations.

During the last decade, the Russo-European relations became one of the most analysed and media-covered subjects related to the international relations area of interest, and the reasons for this are easy to understand since Russia and EU are the most important actors on the European continent. Only one thing should help consolidate a strong strategic partnership for the two actors, that is, the commercial relations created around Russia's energy resources. Unfortunately, this is not the case and all unsuccessful attempts, together with the lack of a strong stable relationship between the two, have several causes. As far as the Russo-European relations are concerned, one can notice a few unpardonable mistakes made on both parts and which were generated by each party's ego.

In international relations, an essential factor during negotiations is the status of each participant, which can vary from superpower to continental power, regional power, or - in the worst case - area of influence, as the saying goes: "when you are not invited to the negotiation table you risk being on the menu". At present, the EU is undoubtedly an international power, especially an economic one, and this is a status that it asserts in its foreign affairs and particularly in relation to Russia. What can create problems in this context is the fact the EU still considers Russia to be a regional power, which it would not have been wrong 5 or 10 years ago. However, due to the reforms initiated by the president Vladimir Putin, Russia has been making remarkable economic progress and has been developing its military-industrial complex, which according to international relations theory can be seen as a main power component, especially of a *hard-power* type of actor. Therefore, to judge an opponent based only on an economic perspective could be misleading, thus an error. This is a problem for the EU since the European political elite does not see Russia as a global power, therefore its approach of the foreign politics in the east will not be well-balanced.

In this context, one should also take into consideration the typology of the nationalistic Russian state, especially after Vladimir Putin's calling the collapse of the Soviet Union "a major geopolitical disaster of the century." The European Politics of Proximity and the Eastern Partnership, in particular, can be given as the best example in this matter, since it was not very successful. Moreover, its most

recent revision does not even mention Russia's involvement in the eastern extremity. This is an aspect that will certainly upset Kremlin to a large extent.

Aware of its geographic location, the existing threats and the current situation in the area, Romania was one of the countries which insistently requested a revision of the politics of proximity in Eastern Europe. The new politics has relied on Romania's Proposal for the Updating of the European Politics of Proximity. Romania has launched a new concept - Security Trusts, which represents permanent political dialogue platforms aimed at approaching all types of security challenges, as well as considering the objectives of each participant. This proposal also highlights and focuses on the idea of involving "our neighbours" in the process of building and maintaining a *trust* environment between EU and its neighbours (Romania's Proposal for the Updating of the European Politics of Proximity, p. 2). Thus, Romania has once again clearly stated the need for having a more careful relationship with Russia, since all 6 member states of the Eastern Partnership, except for Armenia, border Russia. However, this issue has been once again elegantly avoided when EU revised and drafted the official act of the European Politics of Proximity.

The year 2014 brought territorial changes in the immediate proximity of Romania, just a few hundred kilometres away: against the background of the protests in Ukraine, the Russian Federation incorporated Crimea, following a referendum organized in this strategic peninsula. Both the EU and the USA considered this type of action a clear violation of international norms and laws and sanctioned Russia by imposing economic penalty measures against it. These measures were applied in several stages and whether they have met their purpose or not is a matter that deserves a more elaborated analysis in a separate article. What is important to analyse, and has been a premiere for EU, is the way in which all member states were supposed to agree with these economic sanctions in the spirit of the Treaty on the Functioning of the European Union, based on the principle of solidarity. In order to prove the strength of its foreign policy, UE had to speak with one voice and to present a single common opinion of all 28 member states, which is quite difficult to achieve since some European economies are very much interconnected with the Russian economy. For those states whose economies are weakly connected to the Russian one it was quite easy to adopt these sanctions, but for others, whose economies rely significantly on their connections to Russia or whose geostrategic and geopolitical location imposed a *modus vivendi* with Russia, applying these measures was rather difficult. Some of the founding countries of the EU and engines of the European economy, such as Germany, found themselves in this situation. But Romania did as well, since it is located at the eastern border of EU, it is a member state of NATO and has access to the Black Sea. This context was a challenge for the strength and resilience of the EU structure and also a call for ability and diplomacy

from the states that were linked to the Russian economy in one way or another. While Germany, as a member state of EU, inspite of having agreed to the imposition of the economic sanctions, continued to work with Russia and even initiate new projects, conflicting as they were. Romania failed to maximize its strategic interests and to avoid deteriorating the Russo-Romanian relations, not to mention trying to improve them. Romania chose to rally round the EU politics and strictly observe the economic sanctions imposed on Russia. From this point of view, these relations have only to suffer, but the situation is justified by the future actions of both parties. Romania is aware that its relationship with Russia is an uneven one. The country has always been surrounded by stronger and more hostile actors and this is probably one of the reasons why it sees in EU and NATO an ally that it can count on in conflictual situations, one that it can take into consideration in its relations to other countries. However, treating Russia in the same manner one treats Bulgaria is from the very beginning a case of misconception.

One issue in the Russo-Romanian relations that is interesting to determine is the role played by the press and other mass media. The matter is highly sensitive and can have a significant impact. Romanians are unaware of many important things about Russia and their opinions of this country still rely on memories of the past. Under these conditions it is extremely simple to misinform or to create the optimal background for propaganda and those involved in the pro-Russian or pro-Western propaganda know this very well. Although Romania is also aware of this, it does not act accordingly.

A recent study made by the Romanian Institute for Evaluation and Strategy (October, 26<sup>th</sup>-27<sup>th</sup>, 2015), entitled "The Perception of the Russian Federation in Romania," emphasizes the dichotomy in Romanian's perception of Russia. When asked to evaluate the current diplomatic relations between Romania and Russia, 43% of the interviewed considered them good to very good, while 45 % of the participants said they were bad to very bad and the rest said they were neither good nor bad (IRES, 2015). Moreover, 93 % of the participants see in Russia a military power, and more than half the interviewed consider Russia a real threat to Romania's security and that of EU and the entire world, in the current geopolitical context. While the USA and Germany are considered Romania's best friends and allies by 24%, and respectively 20% of the respondents Russians are also perceived as aggressive people, mean, fiery, cruel, determined, cold, heavy drinkers, partying, fighters, invading, expansionist, communist or uncivilized by 10-12% of the interviewed.

This study is relevant and important because it shows that, in Romania, Russia is hardly known, and consequently is highly misunderstood. Romanians' opinions of it rely on historical past events, on what other people say or on the western media. The influence of the pro-Russian propaganda in Romania has been frequently debated. There is, indeed, pro-Russian propaganda in Romania. Yet

Russia, like any other country, has the right to develop its own media networks, to buy media networks, to set up institutions, to create financing funds, cultural organizations, within the legal framework. Romania is still very much against Russia for the pro-Russian media actions to reach their target. The few pro-Russian sites and areas are highly marginal. Russians do not need much propaganda in Romania. The state, its institutions and especially the press are relatively weak, as latest events show that a single spark can overthrow the government. Romania's problem is not the pro-Russian propaganda, but the fragility of the Romanian institutions, the inability to ponder political, strategic and tactical issues and the lack of a good- quality press. (Ernu, 2015)

At present, Romania is short of a group of excellent experts on the relationship with Russia and this is felt and has the corresponding effects. In order to be able to negotiate with Russia, Romania needs experts who know thoroughly the Russian culture and values. A country which is smaller than its neighbours is forced to have better diplomats than an "empire" does (Malita, 2014, p. 28), because the logic of the great is based on conquests and expansion. Therefore, in order to have good relations with the Russians, Romania needs a body of professional experts, like the USA, Poland or China have. In Romania, as far as the relationship with Russia is concerned, the security services, the army and the foreign affairs departments rely solely on translations from the international press and on hiring Russian translators from the Republic of Moldavia. They do not employ people with an extensive knowledge of the area, people who know to put the information in the context, to analyse and to present the situation (Gosu, 2015).

Regarding these relations, the Romanian state's position relies on negligence and lack of seriousness. Firstly, there is no Russian TV channel, newspaper or any centre for Russian studies. Secondly, the Romanian mass media rely mainly on the mainstream Anglo-Saxon press, which in turn is predominantly anti-Russian, hence the same orientation as in Romania. Romania does not have any professional institutions or experts specialized in the relations with Russia, there are only a few doubtful reports and overnight "reinvented" experts who wrap in a "civilized" manner old stereotypes and clichés while being paid from Romanian or European funds. (Ernu, 2015) So, the anti-Russian opinion and the derangement generalized by the Romanian press make any form of judgement and rational analysis of the situation practically impossible, which should be a matter of great concern. It is not enough to be a member state of NATO or of the European Community and always use this status as justification, it is not enough to comply with the politics set up in Bruxelles; Romania needs to take serious actions in order to build a stable and secure relationship with its neighbours.

## Conclusions

In conclusion, it is highly evident that Romania, as a member state of EU, plays the role of an object and not that of a subject in its bilateral relations with Russia, which are strongly influenced by its membership to the EU. Romania, as a country which shares access to the Black Sea and has high interests in the Republic of Moldova, same as Russia, but also lies at the borders of EU, needs to establish a *modus vivendi* with the Russian Federation, despite being under pressure sometimes if EU considers a different course of action.

Romania should take into consideration the fact that Russia has an advantage over the European Community. According to the norms of international law, Russia is a state, while EU is an organization. Consequently, this allows Russia to enjoy a more secure stability, especially now that the European structure is dealing with the biggest problems it has ever had from its creation. When speaking of geopolitics and the Russo-Romanian relations, it is necessary to understand that the solutions to all the challenges that Romania faces, do not lie in Bruxelles, Washington, Berlin, Moscow or London, just as Romania's problems are not caused by Moscow or Bruxelles. Let us not forget that, in the same context, it is advisable to look at the map and realize which is closer, Washington or Moscow. We do not choose our neighbours and that is why we need to be ready to discuss, negotiate and even argue, if that is the case; the fundamental question still remains: is Romania able to do this?

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## THE DEVELOPMENT OF LEGAL RESPONSIBILITY FOR A SOCIALLY RESPONSIBLE BEHAVIOR FOR BUSINESS OPERATORS IN ROMANIA, MEMBER STATE OF EUROPEAN UNION

Laura MURESAN (POTINCU)\*

**Abstract:** *Legal responsibility represents an important component of social responsibility, together with ethical responsibility, ecological responsibility, economical responsibility and philanthropic responsibility. The integration of social responsibility into the activity of business operators in the Member states of European Union is pursued at European Union level. The article analyses the opinion of the Brasov city citizens, in the framework of a marketing research performed in 2015, as regards the possibility that legal instruments should influence a socially responsible behavior for public or private business operators. The aspects analysed for business operators in Romania can represent a model for other European Union states as well.*

**Keywords:** social responsibility; public institutions; economic operators; quantitative marketing research; legal responsibility

**JEL Classification:** M31; L32

### Introduction

Several traders instinctively know that “to do the right thing” – serve the clients, take care of the staff’s morale, be careful with the providers, be good neighbours, and protect the environment – means commercial sense. The socially responsible activity regards the provision of the economic success of a entity – private economic operator or public institution – by including social and ecological aspects into its activity. (European Commission, General Department for Enterprises, 2009, pp. 2-3)

In this context, a manager of a socially responsible entity – private economic operator or public institution – has several categories of ethical obligations. These obligations are divided into four directions, given four groups interested in the respective activity, i.e.:

- towards the shareholders, these obligations regard a correct management, loyalty, information, transparency, confidentiality;
- towards the employees, these obligations regard an equitable remuneration, professional development, respect for the personal life, respect for the petition right;

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- towards the clients, these obligations regard high-quality products/services, guarantee of the use safety, information;
- towards the community, these obligations regard the environmental protection, the contribution to solving social issues, observance of the cultural diversity. (Tigu, 2005 pp. 23-27)

### **1. Social responsibility and its component responsibilities**

At present, the social responsibility of an entity – private economic operator or public institution – must be regarded from a complex perspective. We consider (Potincu, 2012, pp. 85-106; Potincu, 2015b, pp. 106-107) that the social responsibility is what the community expects from an entity – private economic operator or public institution – ecologically, economically, legally, ethically and philanthropically. In our opinion, the social responsibility includes all these types of responsibilities: ecological responsibility, economic responsibility, legal responsibility and philanthropic responsibility.

The ecological responsibility is a reflection of the sustainable development considered by the specialty literature (Crane, 2008 pp. 92-93, 307) to be a basic value of the social responsibility. In this context, we can state that the ecological responsibility lays at the basis of the social responsibility.

The ecological responsibility of an entity – private economic operator or public institution – implies the integration of the environmental protection requirements into their activity. It is stated that the activity conducted by the entity – private economic operator or public institution – are not separate, but they are a component of the entire ecosystem. (Frederick, 2006, pp. 144-146, 150-152) The dynamics of the ecosystem complexity requires the entity to seek durable strategies.

One of the most important responsibilities of a business is considered being an economic operator which is operational on the market. The fate of several categories of persons, first of all its employees, depends on its availability on the market. For this reason, the economic responsibility acquires a major significance, and it must correctly be assumed by each economic operator or public institution.

The juridical responsibility implies the compliance with the normative documents in force. In the case of the failure to assume the juridical responsibility, the juridical liability steps in. *Juridical responsibility* is defined as a classical instrument of fulfilling the provisions of juridical norms. (Dutu, 2007, pp. 238-243)

Compliance with the law, in general, is a primordial attribute of a socially responsible attitude promoted by an entity – private economic operator or public institution. In this context, social responsibility implies, first of all, the compliance with the legislation integrated by law, because the application and responsibility in this field is confronted with the most difficulties.

The ethical responsibilities force the entity – private economic operator or public institution – to do what is just, correct and equitable, even if they are not obliged to do so by the normative documents in force at a certain time. (Muresan, 2007, p. 36)

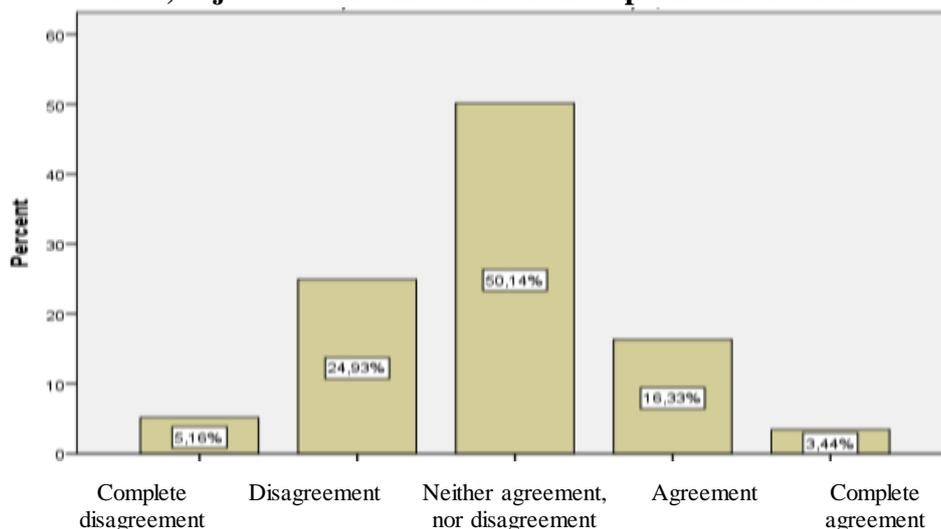
It can be stated that the philanthropic responsibility of an entity – private economic operator or public institution – is a requirement to be manifested within the community in which the company performs its activity. The philanthropic responsibility cannot be imposed.

## **2. The legislation regulating the activity of the public institutions, a premise for a socially responsible behaviour**

In 2015 a quantitative marketing research was conducted (Potincu, 2015c) – within the postdoctoral research entitled “*Use of marketing instruments in order to identify methods for implementing and developing socially responsible management in public institutions*” – regarding the promotion of the social responsibility by the Romanian public institutions. The quantitative research having the theme “*Opinions of citizens in Brasov city on social responsibility in the activity of public institutions*” took into consideration people over 18 years old, of both genders, dwelling in Brasov. The final size of the pattern was 393 people, to which an aleatory error of  $\pm 4,94\%$  corresponds.

We shall further analyse the opinion of the Brasov citizens who have been questioned regarding the manner in which the legislation regulating the activity of the public institutions clearly sets the values, objectives and missions of those public institutions.

**Figure 1 – The legislation regulating the activity of the public institutions clearly sets the values, objectives and missions of those public institutions**



Source: Potincu C. R. (2015) *“Use of marketing instruments in order to identify methods for implementing and developing socially responsible management in public institutions”*, Postdoctoral Research, Transilvania University of Brasov, Department of Management and Economic Informatics.

The role of this question on "The legislation regulating the activity of the public institutions clearly sets the values, objectives and missions of those public institutions" was to see whether this legislation could be the basis on which a socially responsible attitude would be developed. We took into consideration the fact that the entire activity of the public institutions is subject to a strict legislation, due to the social nature of the public institutions. Thus, a socially responsible attitude must at least be allowed, if not even expressly provided by the legislation regulating the activity of the public sector in Romania.

In this context, 30% of the questioned citizens were of the opinion that the legislation regulating the activity of the public institutions still had important additions to make in order to reach the level where the values, objectives and missions of those public institutions are set, and then reach the level of developing a socially responsible behaviour.

Only 19.77% of the Brasov citizens considered that the legislation regulating the activity of the public institutions was at the level clearly setting the values, objectives and missions of those public institutions, creating the premises for implementing a socially responsible behaviour.

The social nature of the activity performed by the public institutions is an aspect which eliminates their implication in the philanthropic responsibility field – constituent responsibility of little importance, in our opinion, of the social responsibility – however imposing an increased

transparency of the activity performed by the public institutions – a very important feature of the social responsibility.

In our opinion, the philanthropic aspects can be developed, but can just as well not exist; what must be complied with is the rest of the constituent responsibilities of the social responsibility: the juridical responsibility, the ethical responsibility, the economic responsibility and the ecological responsibility.

As for the need of transparency integrated into a socially responsible behaviour, this is provided in the normative documents regarding social responsibility, adopted at European Union level.

The Resolution of the European Union Council regarding social responsibility 2003/C 39/02 (of 6 February 2003) – normative document adopted at the European Union level – stipulates the promotion strategies of social responsibility. It is considered necessary for these strategies to be based on the need for credibility and transparency of the socially responsible practices of the private business operators and public institutions.

It is also intended that the Member States of the European Union continue to promote the dialogue with the stakeholders and the civil dialogue, promote the transparency of the practices and social responsibility instruments used by the business operators and promote the exchange of information and experience regarding the social responsibility policies.

Directive 2013/34/EU mentions transparency by mandatorily enforcing an economic instrument: the social responsibility activities report. Directive 2013/34/EU of the European Parliament and Council adds to the compulsoriness of reporting the financial results also the compulsoriness of reporting the non-financial results.

Directive 2013/34/EU – normative document adopted at European Union level – in its draft, stipulated that "the opportunity of improving the transparency of the social and environmental information provided by the companies in all sectors, in order to provide equitable competition conditions, has been acknowledged by the Commission [...] and reiterated in the communication <A new strategy of EU (2011-2014) for the social responsibility of enterprises>".

According to the proposal for Directive 2013/34/EU, "the non-financial transparency is one of the main elements of any CSR strategy".

The draft directive of the European Parliament and of the Council had the following main objectives:

1) Increasing the transparency of certain companies and increasing the relevance, consistency and comparability of the non-financial information – of social responsibility – currently disclosed by consolidating and clarifying the existing requirements.

2) Increasing the diversity of the companies board of administration by means of an increased transparency in order to facilitate an effective supervision of management and a solid governance of the company.

In its final form, adopted at European Union level, Directive 2013/34/EU of the European Parliament and of the Council pursues the same ideas.

### **Conclusions and proposals**

The aspects highlighted by analysing the question “The legislation regulating the activity of the public institutions clearly sets the values, objectives and missions of those public institutions” can open further subsequent analysis directions.

Firstly, this analysis aims at developing a socially responsible behaviour in the case of the public institutions in Romania, an European Union Member State. In this respect, the legislation regulating the activity of the public institutions will have to be amended in order to reach the desired level by clearly setting the values, objectives and missions of those public institutions. Then, other additions to this legislation will be required in order to allow or expressly set the development of a socially responsible behaviour by the public institutions in Romania.

Taking into account the fact that the size of this research has been established according to a simple random probabilistic method, considering a level of admitted error of  $\pm 5\%$ , and a trust level of 95%, the results of the surveys can be considered representative for the entire adult population of Brasov municipality, and also these could apply to other Romanian municipalities with a similar population size. (Potincu, 2008; Potincu, 2009)

Thus, secondly, based on analysing the opinion of the Brasov citizens regarding the question “The legislation regulating the activity of the public institutions clearly sets the values, objectives and missions of those public institutions”, we can state that the legislation regulating the activity of the public institutions in other European Union Member States has two levels to reach:

- the first level that must be reached is for it to clearly set the values, objectives and missions of those public institutions,
- the second level that must be reached is allow or expressly set the implementation and/or development of the social responsibility in the case of those public institutions.

Thirdly, the development of a socially responsible management in the case of the public institutions in Romania, or in other European Union Member States, shall have a positive effect on the relation to the private business operators.

At the same time, a socially responsible management in the case of the public institutions can be an example regarding the adoption of a socially responsible behaviour for the private business operators in Romania, an European Union Member State, or in other European Union Member States.

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## THE BUSINESS ENVIRONMENT IN CEE COUNTRIES: CURRENT CHALLENGES AND PERSPECTIVES

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**Abstract:** *The Central and Eastern European countries have experienced significant imbalances starting with 2008 that have affected their business environment profoundly. Thus, the firms operating in the region have faced, and continue to face, difficulties and major challenges. Through this paper we aim at analyzing the key indicators that characterize the business environment of a country, and by analyzing their values through time, we want to compare the situation from ten countries from CEE. We analyzed the indicators for a period of eight years, between 2007 and 2014. This period presents interest because it comprises the period of the recent financial crisis. By using indicators characterizing the business environment we analyze the ease of doing business, but also the ease of getting credit, domestic credit to private sector and reforms adopted in order to improve the access to credit by the CEE countries. We also analyze the time needed to start a business and the regulations regarding start-ups, which may encourage or discourage the new firms to enter the market. The results obtained show that the CEE countries are starting to recover from the current financial crisis, but are still lagging behind the developed countries of the European Union. However, the business environment has registered a series of improvements in the majority of the analyzed countries in the last two years, improving especially the areas of starting a business, getting a credit and paying taxes.*

**Keywords:** business environment; CEE countries; doing business; legal rights index; getting credit; financial crisis; reforms

**JEL Classification:** G32; O16

### Introduction

The economies in Central and Eastern Europe (CEE) have faced serious pressure in recent years, due to the recent financial crisis. The quality of the business environment is a defining element for the development and good functioning of the economy. Furthermore, the changes that occur on the financial market in the economy of a country play an important role in how firms operate on the markets of that country. The CEE countries have experienced significant imbalances starting with 2008 that have affected the business environment in the area. Thus, the firms operating in the region have faced, and continue to face, major challenges. The main problems reported by the firms as coming from the business environment are excessive bureaucracy and sector-specific taxation.

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Despite low corporate taxes, taxation systems remain in need of reform. There is also a problem with the existing arbitrary legislation (for example the sector-specific taxes).

Moreover, the business environment from CEE developing countries is increasingly dynamic, and the firms must adapt. In order to do that, they have to know really well all the characteristics of the business environment of the country they operate in. Having highlighted the problems above, the purpose of this paper is to analyze the main indicators that characterize the business environment from ten CEE countries (Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovenia and Slovakia) starting with 2007 and until now, in order to see which business environment has been more affected by the recent financial crisis, and which has recovered more quickly. The data used in the analysis in our paper is provided especially by the World DataBank, a data base provided by the World Bank which offers data about the development in countries around the world, Doing Business Reports and Enterprise Survey analysis.

Our paper is structured as follows: the first section presents a review of the specialized literature in the field, analyzing which indicators are better to be used in order to assess the business environment from the CEE countries. In the second section we focus on a comparative analysis between the business environment from ten CEE countries (Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovenia and Slovak Republic), by investigating a series of indicators, that measure the quality of the business environment. We also highlight a series of reforms adopted by the CEE countries for improving the business environment, especially after the recent financial crisis. The paper ends with concluding remarks.

## **2. Literature review**

In the last years a concerted effort has been registered to measure the quality of the environment for business and investment, and assess its implications for economic growth. Choo (1998) considers that analyzing the business environment is a key factor for the good activity of the firm, because the ability of the firm to adapt to its outside environment depends, in a large proportion, on knowing and interpreting the external changes that are taking place. The changes in the business environment of a country can be beneficial for the firms but, on the other hand, can affect them negatively. So, it is very important that a correlation exists between the internal strategy of the firms and the business environment, Lynch *et al.* (2012) show that if a firm becomes too internally focused it is in danger of missing opportunities that arise from changes within the external business environment. Also, in their study Olsen *et al.* (1994) show the fact that, because the managers of the firms do not know the

relationship which exists between the business environment and the firm's performance, they do not devote much time to scan their business environment. But the wish of managers to know the factors that influence the wealth and stability of their firms has aroused, in the present, their interest for assessing the business environment, fact that can be sometimes hard, due to the complexity of the business environment that decision-makers have to face (Nicolau, 2005).

The most used examples for measuring the quality of the business environment are the Doing Business Reports of the World Bank, which calculate an index. This index refers to the ease of doing business and it is composed of information on the ease of starting a business, dealing with construction permits, paying taxes, getting credit, registering property, protecting investors, trading across borders, enforcing contracts and resolving insolvency problems (Doing Business, 2015). Some authors have shown that these sub-indexes of the ease of doing business index have an important impact on the firm's activity, for example Ciccone and Papaioannou (2007) showed that longer periods to register a new business have a significant negative impact on new business entry on the market. Similarly, analyzing a database of European firms, Klapper *et al.* (2006) found that more rationalized business entry regulations contribute to more rapid creation of new firms, and these mentioned effects are most pronounced in the industries that have, naturally, a high rate of entry. They also found that the regulations of the business environment forced the new firms willing to enter on the market to be larger.

Bah and Fang (2015) show that various dimensions of the business environment affect the output and productivity of countries, they also obtained empirical findings that a poor business environment is quite damaging to a country's development, causing a misallocation of the resources. So, we observe that a healthy business environment is important for a country's development.

In an empirical analysis, Djankov (2009) demonstrates that the indicators used by the World Bank to represent the business environment of the countries, comply with the theoretical basis of foreign investment. But, on the other hand, the empirical analysis realized by Pinheiro-Alves and Zambujal-Oliveira (2012) on the ease of doing business index used by the World Bank to describe the business environment in a country, show its limited consistency and descriptive power of the business environment, and recommend that investors, researchers and policy-makers should be very careful when using it as a source of information to prevent decision making which is less than optimal.

Xu (2011) analyzed the effects of business environment on a country's development and found that these effects are heterogeneous and depend crucially on industry, initial conditions, and complementary institutions. Labor flexibility, low entry and exit barriers, and protection from the

government, as elements of the business environment, matter a great deal for most economies. Also, other elements, such as infrastructure and access to finance depend on the size of the market. The role of the government played in the business environment it is highlighted also by Yunus *et al.* (2014). They consider that, in order a country to have a conducive business environment that will assist business to flourish, it is necessary an effective and efficient functioning of local government to service their needs.

Gillanders and Whelan (2014) showed that business-friendly economic policies are the key determinant factor of the level of income per capita, also they show that a country's doing business rank is a key explanatory variable for a country's economic growth. Also, using the data from the World Bank Doing Business reports, Jayasuriya (2011) observed that for the average country an improvement on the ranking generates greater foreign direct investment inflows, but in the developing countries the improvement of ranking has, on average, an insignificant influence on foreign direct investment inflows. Moreover, his analysis shows that, on average, greater foreign direct investment inflows are not necessarily attracted by those countries that undertake large scale reforms compared to other countries. Other papers (Djankov *et al.*, 2006) proved that the quality of the business environment impacts economic growth, using measures of business regulations in 135 countries for ten years they obtained the results that an improvement in the business environment is associated with an increase in annual growth of 2.3 percentage points.

Moreover, regulatory and procedural reforms have improved the quality of the business environment as measured by these indexes. For example, since 2008, all the countries from CEE have applied reforms for improving the business environment, the biggest number of reforms being applied in the Czech Republic, Poland, Romania, Latvia and Lithuania (over 20 reforms) (Doing Business Reforms, 2015).

Prajogo (2015) examines the role of business environments on the effectiveness of different types of innovation strategies in obtaining business performance. His results show that dynamic environments strengthen the effect of product innovation on business performance, and, on the other hand, competitive environments weaken the effect of product innovation on business performance, but strengthen the effect of process innovation on business performance. The quality of the business environment has an important impact also on the Small and medium sized enterprises from that country, so the study realized by Rocha (2012) shows that low entry costs, easy access to finance, and good levels of business sophistication and innovation predict a larger SME sector. A productive and competitive SME sector is usually associated with sophisticated and innovative business

environments. In general, a competitive business environment may result in larger SMEs sectors in terms of number of firms and contribution to employment.

Gani and Clemens (2013) are modelling the effect of the indicators of the domestic business environment on services trade in a sample of low, middle and high-income OECD countries. Their results show that the time required to enforce a contract and the time required to register a property are strongly negatively correlated with the growth in services exports and imports. Also, internet diffusion, the strength of legal rights and the income growth are strongly correlated positively with the growth in services of imports and exports. So, their empirical findings has led to the conclusion that the domestic business environment does matter strongly for trade in services and it is very important for policy makers to continue improving their overall domestic business environment as it plays a crucial role in facilitating trade in services.

Until now, studies especially analyzing the business environment from only one emerging CEE country have been realized, but there are no studies that compare the business environment from the CEE countries, this problem being a starting point for our research. For example, Radukić and Stanković (2015) are trying to assess the local business environment in Serbia on the basis of twelve criteria and using different statistical methods. Their results show that the main problem for creating a friendly business environment in this country is the process of FDI attraction at the local level, and the main criteria that should be a priority for local authorities in order to improve the business environment are: a strategic approach to local economic development, an efficient system for issuing building permits, creditworthiness and financial stability and fostering public-private partnerships. On the other hand, Hamplová and Provazníková (2014) are analyzing the business environment in the Czech Republic compared to the European Union economies in general, and observe that Czech economy ranks relatively poorly. They show that the causes of this ranking are related to a weak and unstable legislative support of business as well as the current state of cultural dimensions. However another problem that disrupts the business environment in this country is represented by lengthy and complex administrative procedures of some agendas. Their paper shows that the government of the Czech Republic is working on the reduction of the administrative burden when establishing a company, improving tax collection and doing business in general.

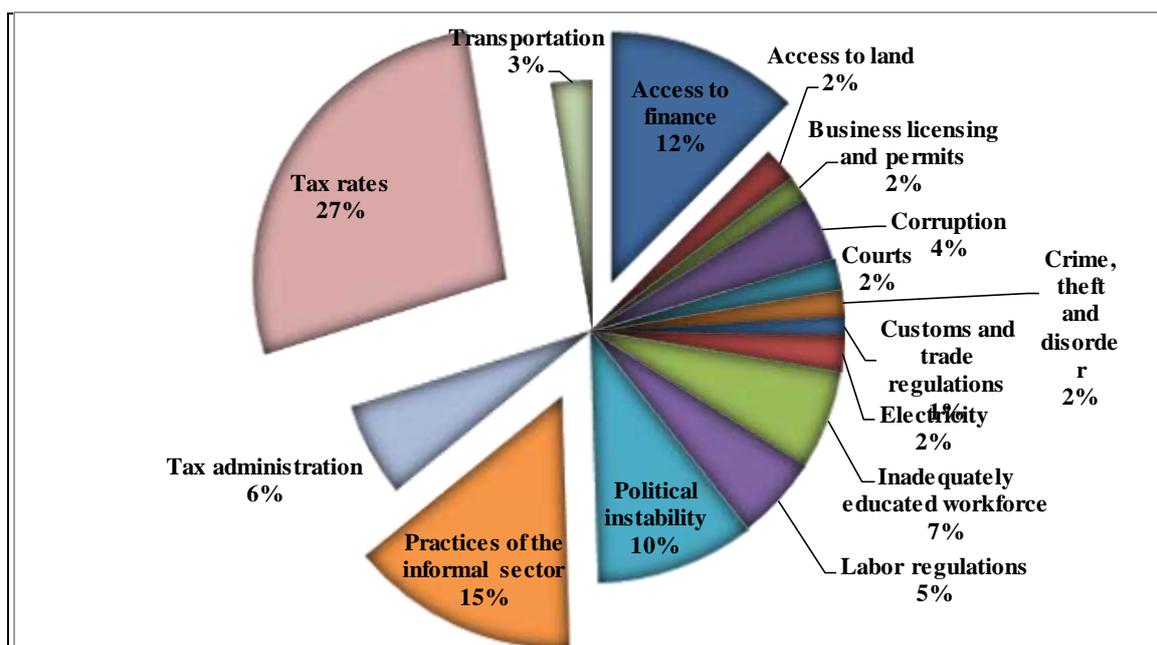
Also, the Slovak government has set a priority to improve the business environment, to create optimal conditions for doing business in Slovakia and to return to the original leading position in the assessment of international institutions. This statement came as a response for the deteriorating position of the Slovak Republic in international indexes, and aimed at improving the quality of the

business environment in Slovakia. The position of the Slovak business environment is getting worse and needs help to improve (Bánciová and Raisová, 2012).

### 3. COMPARATIVE ANALYSIS BETWEEN THE BUSINESS ENVIRONMENTS IN CEE COUNTRIES

Creating a business environment which is friendly with the existing enterprises and the potential entrepreneurs is one of the main objectives of the European Union. The situation for the CEE countries is different, because these countries have emerging economies, are formerly communist states and have to catch up with the developed economies. But, although they have a common situation, if we analyze them more closely, the CEE countries reveal that they are not homogenous; they present a diverse range of business risks and opportunities (The Economist, 2015). So, for the authorities that are willing to improve the regulatory environment for business, it is important to realize a comparison with the regulatory environment from other countries.

**Figure 1 – Top 10 business environment constraints for CEE countries, 2013**



Source: data processed by the authors after [www.enterprisesurvey.org](http://www.enterprisesurvey.org)

The economic growth in CEE countries is driven by SMEs, if the authorities from these countries make efforts to improve the access to finance of these firms, then they can reduce the dependence on foreign investment and lending. The region has a good potential, was one of the fastest

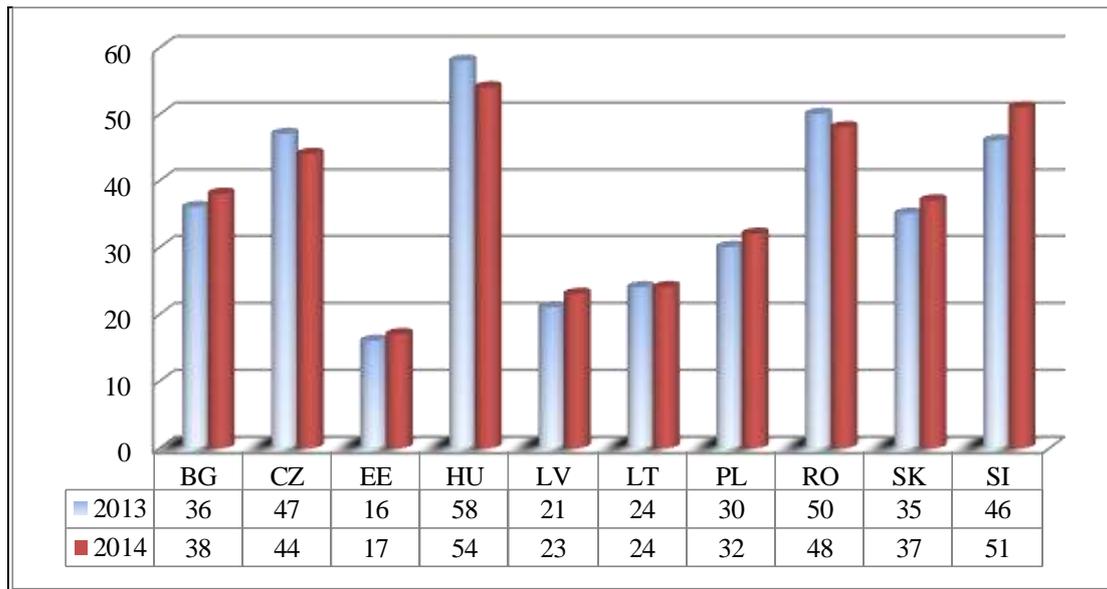
growing region in the world before 2008 (Labaye *et al.* 2013), its economic growth has, and will continue to exceed that of the euro area, but major risks persist across the region, such as widespread red tape and sector-specific taxation (The Economist, 2015).

In order to make a comparison between the business environments from CEE countries we analyzed a series of indicators from the World Bank data bases. First, we took into account the business environment constraints declared by the entrepreneurs in CEE countries. Thus, after being presented with a list of 15 business environment obstacles, business owners and top managers in the firms from CEE were asked to choose the biggest obstacle to their business. The results for the region were obtained by calculating the average of the responses for each of the ten CEE countries, and are presented in figure 1.

From figure 1 we observe that the top 5 business environment constraints in CEE are: tax rates (27% of the firms mentioned this as a problem), practices of the informal sector (15%), access to finance (12%), political instability (10%) and inadequately educated workforce (7%). Other problems mentioned are tax administration, labour regulations, corruption and transportation.

In comparing the business environments from the CEE countries considered, in the following paragraphs, we have considered a series of indicators that characterize the availability of the business environment for the enterprises. The first indicator is *the ease of doing business*; this indicator analyses the 189 economies around the world, and ranks them, the economy sitting in first place is considered to be the best. If a country has a high ranking (represented by a low numerical rank) it means that the regulatory environment from this country is more conducive to business operation, to starting and operating a local firm (Doing Business, 2015).

From figure 2 we observe that the best ranked countries in CEE on the ease of doing business are Estonia (being ranked the 17<sup>th</sup> in 2014), Latvia (ranked the 23<sup>rd</sup>) and Lithuania (ranked the 24<sup>th</sup>). The worst ranked are Hungary and Slovenia. However, Hungary has registered the biggest improvement in the ease of doing business in 2014 compared to 2013, moving up four places in the ranking. On the other hand, Slovenia has dropped five places in the ranking. Other countries that have improved their positions are the Czech Republic and Romania. Lithuania is the only country which maintained its position (the 24<sup>th</sup> place). However, the overall level of the ten CEE countries according to the ease of doing business is relatively good, being maintained in the last two years almost the same, without major imbalances. The regional average of the European Union on the ease of doing business is 40 (Doing Business, 2013); we observe that six of the CEE analyzed countries are situated above the EU average in 2014.

**Figure 2 – The ranking of CEE countries according to the ease of doing business indicator**

Source: data processed by the authors after Doing Business, 2014 and 2015

Another important indicator measured by the World Bank for assessing the business environment from world countries is the *legal rights index*. This indicator measures the degree to which collateral and bankruptcy laws, from each CEE country, protect the rights of borrowers and lenders and thus facilitate lending. The index can take values between 0 and 12; in the countries with the higher scores these laws are better designed to expand access to credit, and in the countries with lower scores they can, on the contrary, restrict the access to credit (World DataBank).

**Table 1 – The value of legal rights index in CEE countries, between 2007 and 2014**

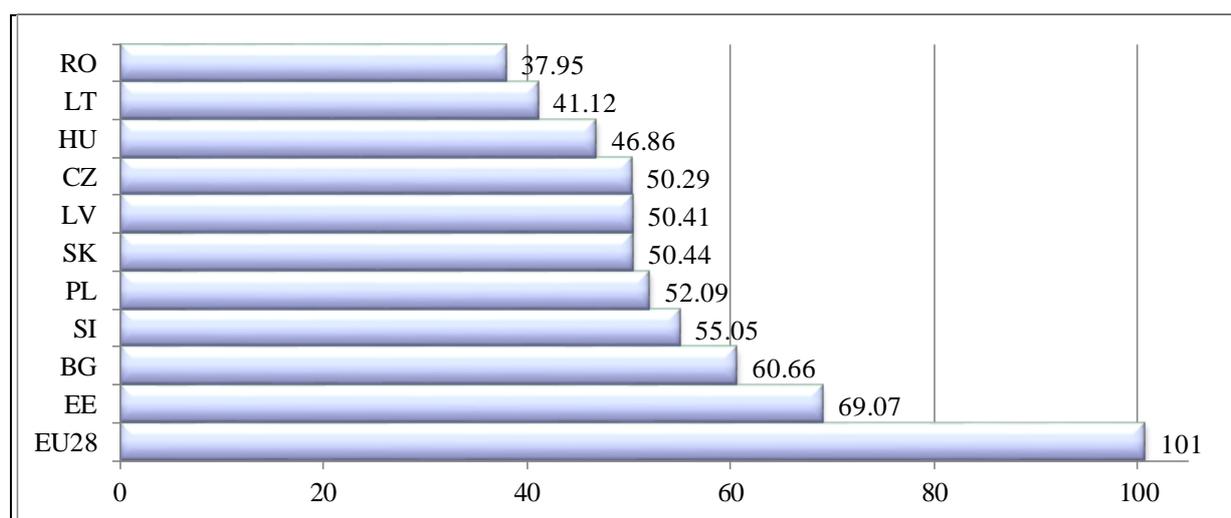
Tara	2007	2008	2009	2010	2011	2012	2013	2014
Bulgaria	9	9	9	9	9	9	9	9
Czech Republic	7	6	6	6	6	6	5	7
Estonia	6	6	6	7	7	7	7	7
Hungary	7	7	7	7	7	7	6	10
Latvia	10	10	10	10	10	10	9	9
Lithuania	5	5	5	5	5	5	6	6
Poland	8	8	9	9	9	9	7	7
Romania	9	9	9	9	9	9	10	10
Slovakia	8	8	8	8	8	8	7	7
Slovenia	5	4	4	4	4	4	3	3

Source: data processed by the authors after World DataBank

From table 1 we observe that the value of the legal rights index is high for eight out of ten countries. The best values of this index are registered in Hungary, Romania, Latvia and Bulgaria, fact that shows that in these countries the collateral and bankruptcy laws are designed to expand access to credit. Hungary registered the biggest improvement of this index in 2014, rising from 6 to 10. Romania also registered an increase of just one point, while Bulgaria maintained the value unchanged for the last eight years. Latvia, although maintained the value of the index high, in 2013 registered a decrease of one point. Lithuania and Slovenia are the worst ranked; although Lithuania has the value of index of only 6 it still registered as an improvement compared to 2012, but Slovenia has the value of legal rights index of only 3, worsening with one point in 2013. Other countries that registered a decrease in the value of the index are Slovakia and Poland. The overall situation of the CEE countries in the legal rights index is good (with an average of the index of 7.4 in 2014) compared to the European Union (with an average legal rights index of 5.75, in 2014) (World DataBank). The countries that really have to improve the laws on collateral and bankruptcy, in order to facilitate access to credit, are Slovenia and Lithuania, the others being situated around the EU average or above.

*Domestic credit to the private sector* is another important indicator in assessing the business environment.

**Figure 3 – The value of Domestic credit to private sector index (% of GDP), 2014**



Source: data processed by the authors after World DataBank

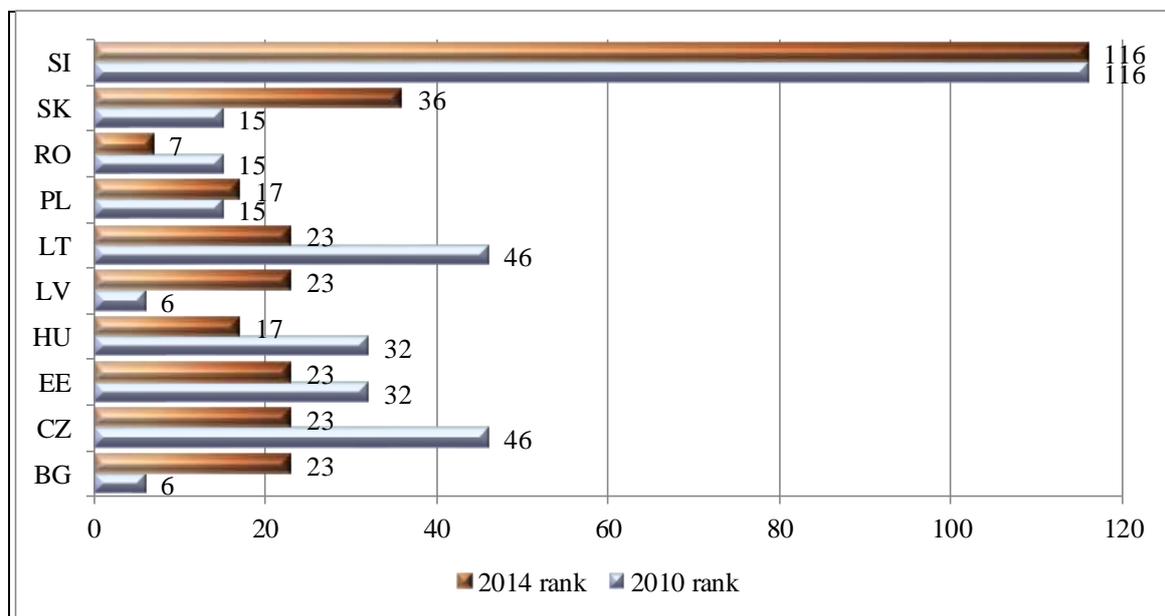
This indicator takes into account the financial resources, such as loans and non-equity securities, which are provided to the private sector by financial institutions (banks, other financial corporations), and it is measured as a percentage of GDP. If this indicator is higher, then the financial resources or financing to the private sector is higher and there is a greater opportunity and space for

the private sector to develop and grow. If the private sector is better and has a bigger role in national economy, then generally the health and the development of the economy of a country is better.

The emerging and developing economies from CEE have registered the sharpest drop in credit growth among all the European Union. These countries have benefited from a substantial inflow of foreign funds and cross-border lending before the crisis, but when the financial crisis struck, credit growth dropped dramatically and has not recovered yet. From figure 3 we observe that all the CEE countries considered have the value of domestic credit to private sector (as % of GDP) below the EU 28 average. Financing to private sector is very low in Romania, Lithuania and Hungary (with values of the indicator below 50%). Estonia and Bulgaria are the countries with greater opportunities for the private sector to develop and grow. All CEE countries still have to work to improve this indicator.

Related to this indicator, in order to analyze the business environment from CEE countries we also consider the ranking of countries on *the ease of getting credit* realized by the Doing Business Reports of the World Bank (see figure 4).

**Figure 4 – The ranking of CEE countries on the ease of getting credit**



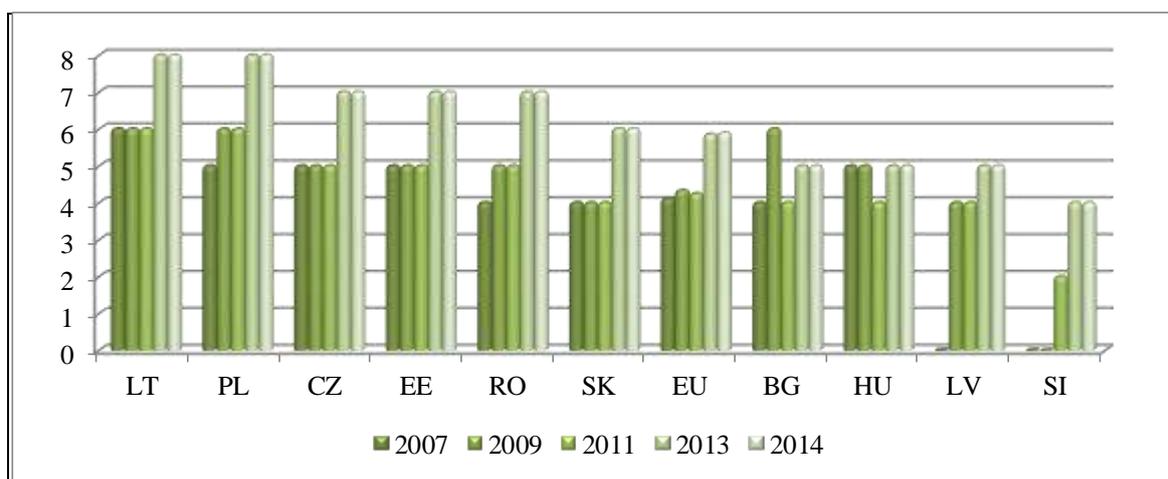
Source: data processed by the authors after Doing Business 2011 and 2015

Best ranked in 2014, on the ease of getting credit is Romania (ranked the 7<sup>th</sup> and with a score of 85), followed by Poland and Hungary (ranked 17<sup>th</sup> with a score of 75). Worst ranked is Slovenia, in the 116<sup>th</sup> place; this country did not register any improvement since 2010. The countries that have worsened their ranking since 2010 are Bulgaria, Latvia, Poland and Slovak Republic. The biggest

improvement was registered by the Czech Republic and Lithuania that improved 23 places in the ranking.

*The depth of the credit information index* is another indicator used to assess the business environment, when it has higher values it can facilitate lending decisions. It can take values between 0, which is the lower value, up to 8, representing the highest value, indicating that more credit information is available, from either a public registry or a private one. These index measures rules affect the scope, accessibility, and quality of credit information available through public or private credit registries. The values of this index are presented in figure 5. As we can observe, this index has the biggest values in Lithuania and Poland, followed by the Czech Republic, Estonia and Romania, these being also the countries that have registered the biggest improvement since 2007. Lithuania and Poland have reached the highest value of the index in 2013 and 2014, fact that facilitates lending decisions of the firm from these countries. The countries with values of the index below the EU average are Bulgaria, Hungary, Latvia and Slovenia.

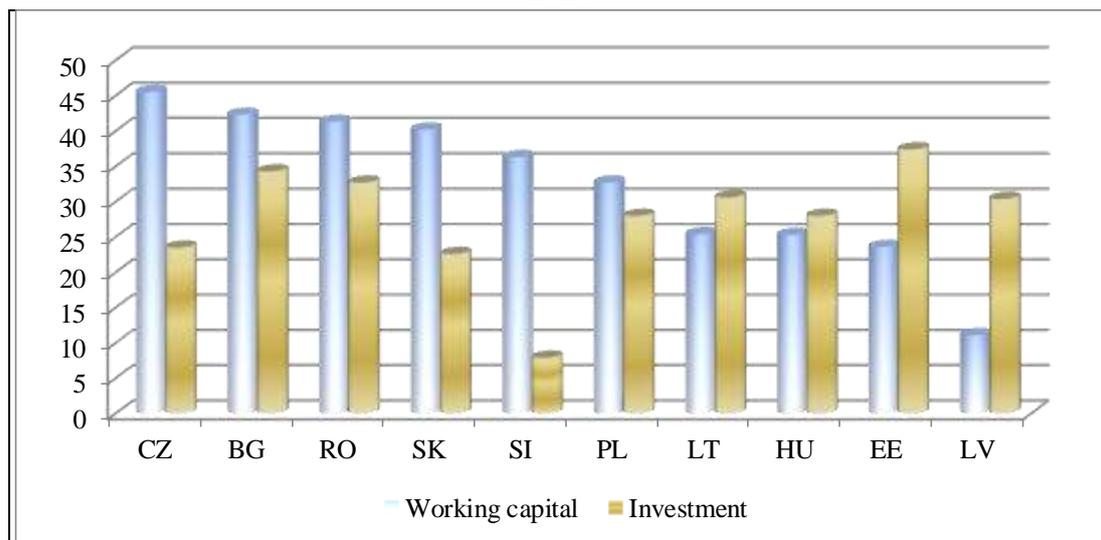
**Figure 5 – The evolution of depth of credit information index**



Source: data processed by the authors after World DataBank

Getting credit is important for the CEE firms because they use in a large proportion bank products to finance their activity or their investments, as can be seen in figure 6. When the firms use bank products to finance their working capital then their dependence on banks is rising. The percentage of firms that used banks to finance their working capital is higher than 30% in Czech Republic, Bulgaria, Romania, Slovak Republic, Slovenia and Poland. Estonia is the country where just a small percentage (10%) of firms use banks to finance working capital.

**Figure 6 - Firms using bank to finance their working capital and investment (% of firms), 2013**



Source: data processed by the authors after WorldDataBank and Enterprise Survey

On the other hand, when analyzing the percentage of firms using bank product to finance their investment we observe that the situation is different, Estonia is the country that uses in the higher proportion bank products to finance investment, followed by Bulgaria, Romania, Lithuania and Latvia. The country which uses bank products to finance investment in the smaller proportion (almost 8% of the firms) is Slovenia.

To help revive the flow of foreign direct investment into CEE economies, in order to reach the levels existing before the financial crisis and to encourage the expansion of the business environment but also the creation of new business, the governments from the CEE countries can improve their business environment in many ways. But the most important ways of improvement are simplifying the administrative and regulatory processes, strengthening the legal protections for investors and improving the access to finance for the firms in the region. As we can observe from the analysis above, bank loans are the main source of financing used by the enterprises from CEE countries, thus, the access to credit is an important issue for the enterprises from these countries in doing their business. In order to improve the access to credit, the authorities from these countries adopted a series of reforms, as seen in table 2, some of them were useful in improving access to credit but some of them were not, making it more difficult to do business.

**Table 2 – Reforms adopted by the economies in the CEE countries to get credit easier**

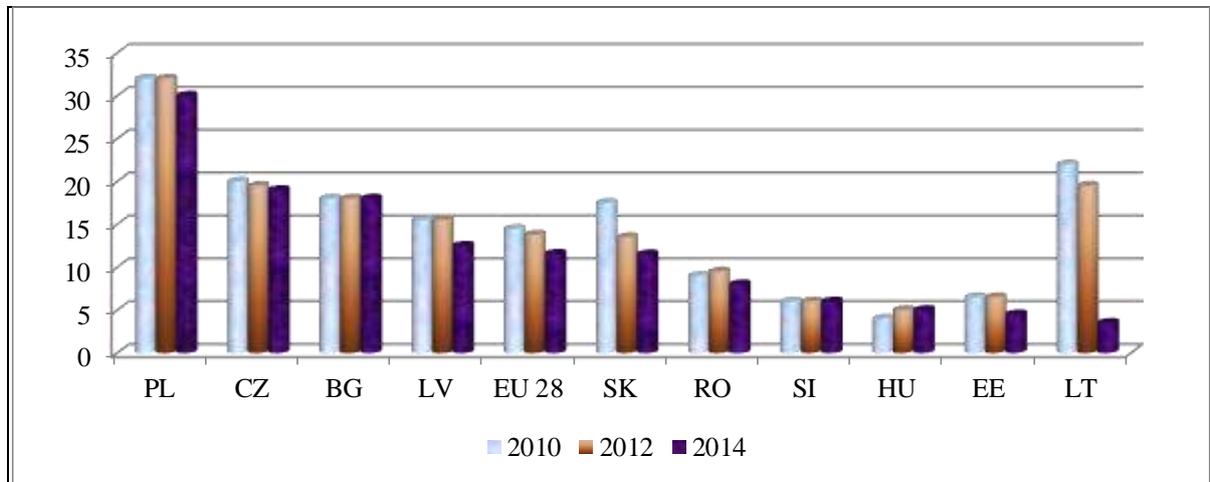
Country	Year	Reform
Romania	2008	Parties may agree to out-of court-enforcement of the security right when the security agreement is signed.
	2013	Romania strengthened its legal framework for secured transactions by allowing the automatic extension of security interests to the products, proceeds and replacement of collateral.
Slovenia	2008	As a result of Euro adoption, the public credit registry from this country has increased the minimum loan requirement from 0 to 500 Euros.
	2009	A new private bureau started its activity: SISBON. The access to finance became more difficult due to the decrease of secured creditors' rights during reorganization procedure.
Czech Republic	2009	This country made access to finance more difficult by decreasing secured creditors' rights during reorganization procedure.
Latvia	2010	Latvia's access to credit information was improved by the fact that the new public credit registry started sharing data on loans.
Poland	2010	Poland improved access to credit with an amendment to the 1996 Act on Registered Pledges and the Pledges Register to allow all legal persons including foreign entities to have capacity as a pledgee. Poland improved its credit information system by collecting and distributing information on firms.
Estonia	2011	Estonia improved access to credit by amending the Code of Enforcement Procedure and allowing out-of-court enforcement of collateral by secured creditors.
Lithuania	2011	Lithuania's private credit bureau now collects and distributes positive information on borrowers
Bulgaria	2012	Bulgaria made access to credit information more difficult by stopping the distribution of credit reports to financial institutions by the private credit bureau (Experian).
Hungary	2012	Hungary reduced the amount of credit information available from private credit bureaus by shortening the period for retaining data on defaults and late payments (if repaid) from 5 years to 1 year.
	2013	Hungary improved access to credit information by passing its first Credit Bureau Law mandating the creation of a positive database on individuals
Slovak Republic	2012	The Slovak Republic improved its credit information system by guaranteeing by law the right of borrowers to inspect their own data.

Source: processed by the authors after Doing Business Reforms, 2015.

*Time required to start a business* and *start-up procedures needed to start a business* are another two important indicators of a business environment of a country. Time required to start a business refers to the number of days needed to complete the legally imposed procedures for operating a business. The start-up procedures include the procedures needed to obtain the necessary licenses and permits but also those necessary to complete all the verification and inscriptions. These indicators influence the creation of new enterprises and the development of the business environment. In figure 7 we can see that the biggest problems concerning the time needed to start a business are observed in Poland, where although improvements were registered in 2013, a timeframe of 30 days is still needed in order to start a business. The following worst ranked are the Czech Republic, with 19 days needed

to start a business (and a small improvement of just one day), Bulgaria, with 18 days needed and Latvia, with 12,5 days (and an improvement of three days registered in 2013).

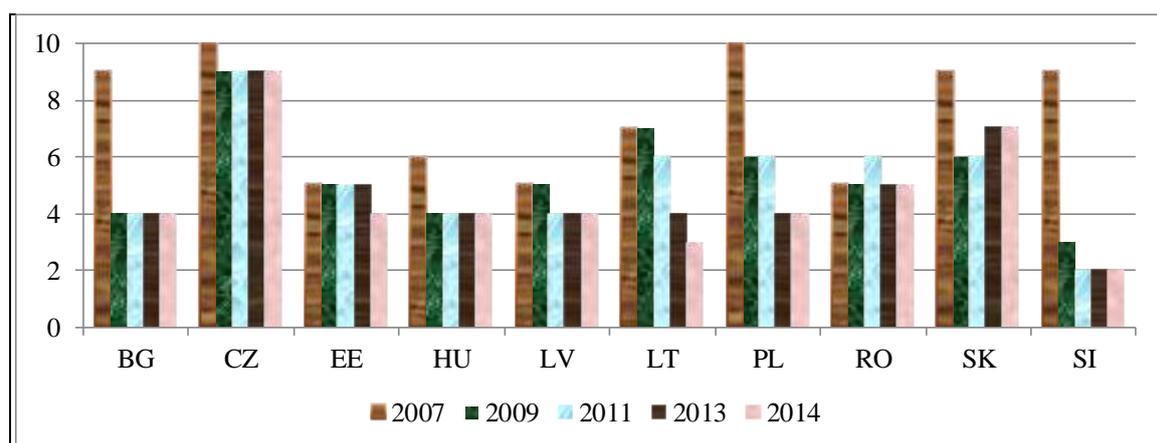
**Figure 7 - Time required starting a business in CEE countries**



Source: processed by the authors after World DataBank

The greatest improvement was registered in Lithuania, from 22 days needed in 2010, to 3.5 days in 2014. The countries that are best rated according to this indicator are Lithuania (3.5 days), Estonia (4.5 days), Hungary (5 days) and Slovenia (6 days), all being under the EU 28 average. Bulgaria and Slovenia have not registered any improvement regarding the number of days necessary to start a business in the last five years.

Figure 8 presents the start-up procedures needed to obtain licenses and to register a new firm. The best ranked in 2014 on this index are Slovenia and Lithuania, with the smallest number of procedures. The worst ranked in 2014 are the Czech Republic (with 9 procedures) and the Slovak Republic (with 7 procedures needed). The biggest improvement compared to 2007 was registered in Slovenia (a reduction with 7 procedures), Poland (a reduction of 6 procedures) and Bulgaria (with a reduction of 5 procedures). The other countries had a slightly descending trend in the number of procedures, with the exception of Romania and the Slovak Republic. In Romania the number of procedures needed to start a new business is the same as in 2007 (5 procedures), with an increase in 2011. The Slovak Republic was the only country that registered an increase in the number of procedures needed to start a business, in 2013.

**Figure 8 - Start-up procedures needed to start a business in CEE countries**

Source: processed by the authors after World DataBank

Another indicator used by the World Bank to assess the quality of the business environment is *the distance to the frontier score*, which shows on average how far an economy is at a certain point in time from the best performance achieved by any economy on each Doing Business indicator since 2005. It can take values between 0 and 100, with 100 representing the frontier. According to the ease of doing business country reports ([www.doingbusiness.org](http://www.doingbusiness.org)) Bulgaria decreased two places in the ranking of doing business in the last year. This country registered small improvements on trading across border and registering property. The only reforms adopted were in the field of starting a business. Regarding the distance to the frontier, the value of the indicator for 2015 is 71.80%, being improved with 0.08 percent points compared to last year. The Czech Republic improved 3 places in the ranking of the ease of doing business; best improvements were registered on getting credit, followed by registering property, with a small improvement. The reforms adopted by the Czech Republic were referred to starting a business, getting credit and enforcing contracts. Regarding the distance to the frontier, the value of the index is 70.95% (in 2015), and has improved compared to the previous year with 1.20 percent points. Estonia decreased one place in the ranking of doing business in the last year. It has registered improvements only in the field of starting a business. And, no new reforms were adopted. Regarding the distance to the frontier, the value of the index in 2015 was 78.84% (the biggest from the CEE analyzed countries) and it improved with 0.30 percent points compared to 2014. Hungary improved four places in the ranking regarding the ease of doing business; the biggest improvement was registered on getting a credit and it was followed by a small improvement as regards the paying of taxes. Reforms were adopted on getting credit and paying taxes. Less changes than those concerning doing business were made in the field of starting a business. Regarding the distance to frontier, the value of the index was of 68.79% in 2015 (the smallest value

from all the analyzed CEE countries), and it has improved with 1.97 percent points, compared to 2014. Latvia dropped two places in the ranking of doing business in the last year; the biggest improvements were registered in paying taxes and registering property. Reforms were adopted in the field of paying taxes. Less changes than those concerning doing business were made in the field of starting a business. Regarding the distance to the frontier, the value of the index was 76.73% in 2015, with an improvement of 0.14 percent points compared to the previous year. Lithuania did not register any changes in the ranking of doing business in the last year. The greatest improvements were registered in dealing with construction permits, starting a business, enforcing contracts and getting electricity. Reforms were adopted in dealing with construction permits, starting a business and enforcing contracts. Regarding the distance to the frontier, the value of the index was 76.31% and it improved with 0.45 percent points. Poland dropped two places in the ranking of doing business in the last year; the greatest improvements were registered in trading across borders and enforcing contracts. Reforms were adopted on getting electricity, registering property and trading across borders. Regarding the distance to frontier, the index indicated a value of 73.56%, an improvement with 0.20 percent points. Romania improved its doing business rank in the last year, the biggest improvements in doing business being registered in paying taxes, followed by trading across borders and enforcing contracts (with a smaller improvement). Reforms for improving the business environment were adopted in paying taxes. Regarding the distance to the frontier, the value of the index was 70.22% in 2015 and it improved with 1.74 percent points compared to 2014. The Slovak Republic dropped two places in the ranking of doing business in the last year, the biggest improvements being registered in starting a business and enforcing contracts. Reforms on making easier to do business were adopted in starting a business and getting credit (although these reforms were made, Slovakia dropped 6 places in the ranking of getting credit in 2015). Regarding the distance to the frontier, the index indicated small improvement of only 0.10 percent points, having the value 71.83% in 2015. Slovenia dropped 5 places in the ranking of doing business in the last year; the biggest improvements were registered in dealing with construction permits. Reforms were adopted in resolving insolvency. Regarding the distance to the frontier, the value of the index in 2015 is 69.87% and it has improved with only 0.03 percent points compared to the previous year.

We can observe the fact that all the economies have registered an increase of the distance to the frontier indicator, fact that is good, indicating that they are getting closer to the best performance achieved by any economy since 2005. The value of the distance to the frontier index have varied between 68.79% and 78.84%, values that show that the business environment from the CEE area is relatively well situated, and it continues to improve.

## Conclusions

The business environment from the CEE developing countries is increasingly dynamic, and the firms must adapt, in order to do that, they have to know really well all the characteristics of the business environment in which they operate in. To characterize the business environment from the CEE countries we have analyzed a series of indicators, such as: the ease of doing business, the legal rights index, the domestic credit to private sector, the ease of getting a credit and the depth of credit information. We have analyzed, also, the percent of firms using bank products to finance their working capital and investment, but also the reforms adopted in order to improve the access to credit for the firms. In order to measure the expansion possibilities of the business environment we took into consideration the time required to start a business and the number of start-up procedures needed to start a business.

The results of our study highlight the problems faced by the business environment in the countries considered in the analysis, and the need to intensify the concerns of policy makers for reforms in order to help stimulate the development of the business environment so as to contribute to national economic recovery and to the increase of their competitiveness.

Regarding the *ease of doing business*, our key findings show that the best ranked countries in the CEE according to the ease of doing business are Estonia, Latvia and Lithuania. The worst ranked are Hungary and Slovenia. However, the overall level of the ten CEE countries in the ease of doing business is relatively good, being maintained in the last two years almost at the same level, with six of the CEE analyzed countries situated above the EU average in 2014.

As regard to the legal *rights index*, we observe that its value is high for eight out of ten countries. The best values of this index are registered in Hungary, Romania, Latvia and Bulgaria. Lithuania and Slovenia are the worst ranked. The overall situation of the CEE countries as regard to the legal rights index is good (with an average of the index of 7.4 in 2014) as compared to that of the European Union (with an average legal rights index of 5.75, in 2014). The countries that really have to improve the laws on collateral and bankruptcy, in order to facilitate access to credit, are Slovenia and Lithuania.

*Domestic credit to private sector* and the *ease of getting credit* are two related indicators with major importance for the quality of the business environment. All the considered CEE countries have the value of domestic credit to private sector below the EU 28 average. Financing for the private sector is very low in Romania, Lithuania and Hungary. Estonia and Bulgaria are the countries with greater opportunities for the private sector to develop and grow. All CEE countries still have to work to improve this indicator. The ranking of countries on *the ease of getting credit* shows that the best

ranked in 2014 is Romania, followed by Poland and Hungary. Worst ranked is Slovenia. Although financing in the private sector is very low in Romania and Hungary, the firms from these countries can get credit easier than the ones from other countries.

*The depth of credit information* index is another indicator used to assess the business environment; we can observe that this index had the biggest values in Lithuania and Poland, followed by the Czech Republic, Estonia and Romania. Lithuania and Poland have reached the highest value of the index in 2013 and 2014, fact that facilitates lending decisions to be made by the firms from these countries. The countries with values of the index below the EU average are Bulgaria, Hungary, Latvia and Slovenia.

The biggest problems as regard to the time needed to start a business are observed in Poland, which needs 30 days in order to start a business. The following worst ranked are the Czech Republic, with 19 days, Bulgaria and Latvia. The countries that are best rated on this indicator are Lithuania, Estonia, Hungary and Slovenia, all being situated under the EU 28 average. Regarding the start-up procedures needed to obtain licenses and to register a new firm, the best ranked in 2014 are Slovenia and Lithuania. The worst ranked in 2014 are the Czech Republic and Slovak Republic.

*The distance to the frontier score* has registered an improvement for all the CEE countries in the last year, fact that shows us that the economies from this area are continuing to register improvements. For many of the analyzed indicators, there are countries that are situated above the EU average, fact that shows that the CEE countries are continuing the process of recovery from the recent financial crisis. In the future there are countries which will continue their development, and will outpace the overall EU growth (Poland and Bulgaria) (Doing Business, 2015). CEE countries offer exceptional capabilities and productivity and the markets from these countries will continue to grow in the next years. Also, according to their particularities, each country should continue to adopt reforms in order to improve the indicators of the quality of the business environment.

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## VENTURE CAPITAL FINANCING IN EMERGING ECONOMIES

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**Abstract:** *The problem of how financing through venture capital functions in environments that significantly differ from mature and developed markets, begins to be an important issue for researchers. In this article we aim to analyze the venture capital practice in the emerging markets. Obtaining venture capital is different from applying for a loan, because venture capitalists are usually very selective in deciding where to invest. We analyze the venture capital financing process, and what the conditions are for a firm to be able to benefit from this type of financing in the emerging economies of the Central and Eastern European countries. The results obtained have implications also for the entrepreneurs and entrepreneurial ventures that seek venture capital financing in emerging economies.*

**Keywords:** emerging markets; CEE; venture capital market

**JEL Classification:** G32; M13

### Introduction

Venture capital is a specialized form of financial intermediation which is centred on supporting innovative companies, by providing finance and also by providing monitoring and advice services. Venture capital firms are sophisticated investors, whose partners have extensive knowledge of the industry and often previous managerial experience. Their strong commitment to generate high returns in the medium term makes them active investors. As a new form of financing, venture capital has attracted the interest of researchers in the field of finance. The purpose of this paper is to analyze the use of venture capital financing in seven selected emerging countries from Central and Eastern Europe (Bulgaria, Estonia, Hungary, Latvia, Lithuania, Poland and Romania). Groh and Liechtenstein (2007) show that the CEE countries have a great unexploited potential and they are attractive for the venture capital investors, but they also highlight the strength and weakness of the region and offer solutions in order to increase this attractiveness.

Our paper is structured as follows: the first section is dedicated to an analysis of the literature in the field of venture capital, highlighting the impact of this strategy of financing on innovation,

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economic value creation, the entry of new enterprises on the market, employment, and company growth. Section two presents the key data regarding venture capital financing in seven selected Central and Eastern European countries and its evolution in the last years. Furthermore, in this last section we take into consideration the measures adopted by decision makers in CEE countries in order to improve the use of venture capital. The paper ends with the concluding remarks and future directions of the research.

## **1. Literature review**

Kortum and Lerner (2000) provide a systematic assessment of the fact that venture capital promotes innovation, examining the relationship between venture capital financing and patenting. By analyzing firms of US manufacturing industries, they found that venture capital financing was associated with sectors that have higher contemporaneous patent production. Having more patent applications increases the chances of the company obtaining venture capital financing (Engel and Keilbach, 2007). To support this idea, Mann and Sager (2007) showed that companies that had more patents obtained more venture capital investments. They also found that venture capital backed companies with more patents obtained higher valuations, especially in earlier rounds.

On the other hand, Hirukawa and Ueda (2008) found no significant relationship between the use of venture capital and an industry's total factor productivity (TFP) growth, although they did find a positive relationship between venture capital and labour productivity. Chemmanur *et al.* (2011) also examined the relationship between the use of venture capital and TFP growth, and they found that companies financed by venture capital already had higher TFP growth in the years prior to obtaining venture capital. Moreover, they observed that obtaining venture capital financing was associated with continued higher TFP growth.

Other authors highlighted the relationship between venture capital and innovation, for example Hellmann and Puri (2000) showed that the firms more likely to obtain venture capital financing were the ones using innovation strategies. Also, they showed that venture capital backed companies brought their products on the market faster. This effect was more significant for innovator companies, where time to reaching the market is likely to be of greater strategic importance. Puri and Zarutskie (2011) found that venture capital investors fund companies with no initial revenues but only if they demonstrate stronger growth potential.

Lindsey (2008) examined the relationship between venture capital financing and the formation of strategic alliances. The author showed that companies that have a common venture capital investor

are more likely to form strategic alliances. Moreover, such alliance formation is associated with better exit performance.

Apart from the analysis of how venture capital impacts innovation it is important to examine how venture capital impacts the new value creation, such as new entry on the markets, employment, and company growth. Samila and Sorenson (2011) using panel data examined the relationship between venture capital financing and the number of start-ups, employment and income. As a result, they found a positive relationship between venture capital financing and all these variables across a variety of model specifications. Also, they showed that increases in venture capital investments determined the increase of new business creation. Following the same line of thinking Popov and Roosenboom (2008) found that higher levels of venture capital investment were associated with more entry on the market, especially in industries with high investments in research and development. Also, they demonstrated the existence of a positive correlation between venture capital, new entry on the market and employments growth.

Other researches sustain these findings, for example Chemmanur *et al.* (2011) found a positive effect of venture capital on company productivity. Davila *et al.* (2003) and Engel and Keilbach (2007) also found a positive effect of venture capital on employment. So it can be observed that the specialized literature consistently finds a positive relationship between venture capital financing and other measures of economic value creation.

Puri and Zarutskie (2011) showed that venture capital backed companies grow faster at every stage of the investment cycle, both before and after the receipt of venture capital.

Winton and Yerramilli (2008) and Ueda (2004) compared venture capital financing with bank financing showing that venture capital investors have better ability to monitor the firm's activity, but on the other hand they demand higher returns. In contrast, banks are less skilled at monitoring, but demand lower returns from entrepreneurs because they themselves face lower funding cost by exposing themselves to liquidity shocks. Venture capital financing is optimal only if firms face highly risky and positively skewed project cash flows, with low probability of success, low liquidation value, and high returns if successful, and if they face highly volatile cash flows across two continuation strategies.

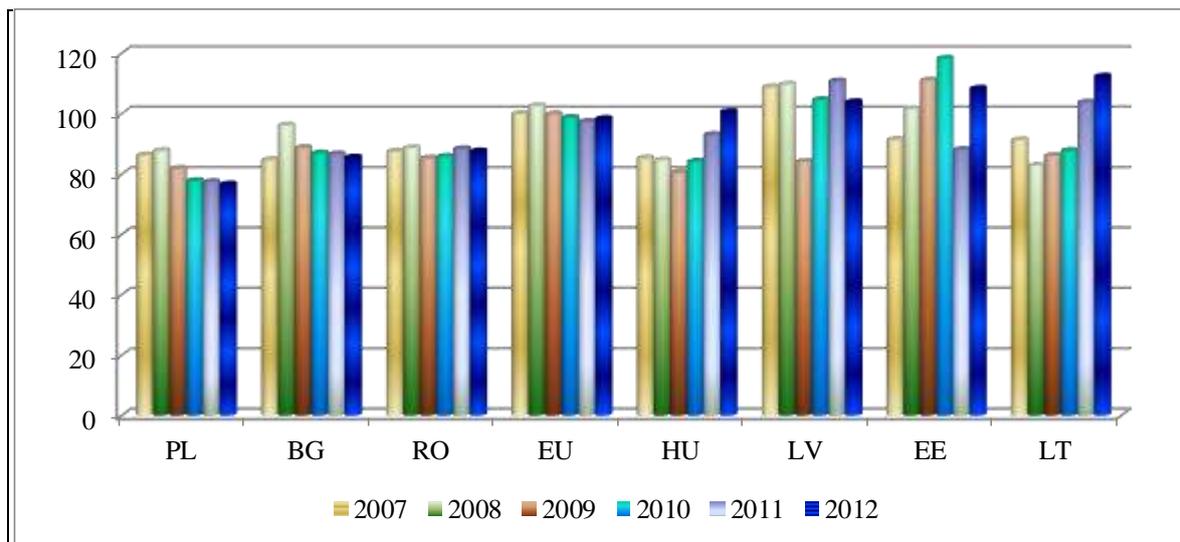
## 2. Venture capital in CEE countries: a comparison

In order to analyze the venture capital financing in the countries from Central and Eastern Europe we consider the SME Access to finance index (SMAF index) and especially the Sub-index on access to equity finance. This sub-index contains information regarding five indicators:

- Total venture capital investment calculated as a percentage of GDP (in thousands of euro);
- Number of SMEs that benefit from venture capital (reported to GDP);
- Total volumes invested by business angels as a percentage of GDP (in thousands of euro);
- Number of investments made by business angels as a percentage of GDP;
- Percent of firms feeling confident to access financing from equity investors or venture capital firms.

The equity finance sub-index is calculated using data from the European Venture Capital Association and the European Business Angel Network. Hungary, Latvia, Estonia and Lithuania are the strongest performing countries in the region with values of the index above 100, whereas Poland, Bulgaria and Romania have the least favourable equity finance environments. The value of the sub-index for European Union is 98, indicating a slight decline since 2007.

**Figure 1 - SMAF Sub-index on access to equity finance, by country, 2007-2012**



Source: processed data after European Commission, SMAF Index

From the seven countries examined only three have improved relative performance in the equity finance sub-index between 2007 and 2012 (Hungary, Estonia and Lithuania). The rest of the

analyzed CEE countries have registered a slightly decline of venture capital in the period 2007-2012 or have remained relatively stable.

Regarding the structure of the CEE private equity market, we have observed in our analysis that it was much more oriented towards venture in the CEE countries than in all of Europe when looking at the number of companies financed in 2014. So, 72% of the total number of companies received venture financing in CEE compared to only 58% across Europe. The CEE growth segment accounted for 15% of the total number of companies receiving private equity investment, compared to 23% in Europe overall. Finally, CEE buyouts accounted for 10% of all financed companies, compared to 17% in Europe as a whole.

**Table 1 - Type of investment in CEE, 2013-2014 (in thousands euro)**

	<i>2013</i>		<i>2014</i>	
	<i>Amount</i>	<i>No. of companies</i>	<i>Amount</i>	<i>No. of companies</i>
<i>STAGE FOCUS</i>				
<i>Seed</i>	4.154	37	8.314	45
<i>Start-up</i>	32.475	75	47.762	106
<i>Later-stage venture</i>	34.499	43	41.863	62
<b><i>Total venture</i></b>	<b>71.128</b>	<b>154</b>	<b>97.939</b>	<b>210</b>
Growth	259.305	49	232.385	45
Rescue/Turnaround	6.703	1	23.696	4
Replacement capital	24.669	6	22.107	2
Buyout	426.897	33	934.787	30
<b><i>TOTAL</i></b>	<b>788.702</b>	<b>242</b>	<b>1.310.914</b>	<b>290</b>

Source: processed by the authors after EVCA, 2015, p. 20

From table 1 we observe that growth investments in 2014 decreased by 10%. If we consider the amount invested, we observe a decrease from 259 million of euro (in 2013) to 232 million of euro in 2014. But, if we analyze the number of companies backed by venture capital, this fell 8% in 2014, and only 45 companies received growth financing compared to 49 companies in 2013. The average growth investment per company did not change significantly in 2014 compared to 2013, being maintained at around 5.2 and 5.3 millions of euro, respectively.

The buyout investments in the CEE region registered an increase of 120% in 2014 (from 427 million of euro in 2013 to 935 million of euro in 2014). But, although the investment amount increased significantly, the number of companies involved in buyout transactions registered a slight decline to 30 from 33. This means that the average equity investment per company increased significantly to 31 million of euro compared to 13 million of euro in 2013. But, we have to take into account that the two largest buyout transactions, in 2014 alone, accounted for over 500 million of

euro, so, if we exclude these two deals, the average for the remaining 28 buyout investments in 2014 was of 15 million of euro, similar to the average in 2013.

The CEE venture investment significantly increased in 2014, both in value and according to the number of companies financed. So, we observe that the value of investment rose by 38% to approximately 98 million of euro, increase supported by the fact that all venture sub-segments from the starting point through to later-stage capital investments increased in 2014. At the same time, the number of companies receiving venture financing grew strongly, setting yet another record of 210 companies financed across the region, surpassing the previous record of 154 companies in 2013. The number of companies backed also rose in all three venture sub-segments. However, the most notable rise in 2014 was among companies receiving start-up funding, with 106 companies financed – 31 more than in 2013.

**Table 2 - Type of investment by CEE country, 2013-2014 (in thousands euro)**

	2014						
	Bulgaria	Estonia	Hungary	Latvia	Lithuania	Poland	Romania
<i>STAGE FOCUS</i>							
Seed	1.178	400	1.496	0	1.570	1.820	0
Start-up	758	763	22.174	1.760	4.952	9.722	1.825
Later-stage venture	397	3.239	8.477	1.547	3.224	10.472	3.478
<b>Total venture</b>	<b>2.333</b>	<b>4.402</b>	<b>32.146</b>	<b>3.307</b>	<b>9.746</b>	<b>22.014</b>	<b>5.303</b>
Growth	0	15.500	27.412	25.700	24.561	65.410	22.426
Rescue/Turnaround	0	0	0	0	0	0	1.060
Replacement capital	0	20.000	0	0	0	2.107	0
Buyout	0	0	110.375	4.970	4.537	161.388	49.182
<b>TOTAL</b>	<b>2.333</b>	<b>39.902</b>	<b>169.933</b>	<b>33.977</b>	<b>38.845</b>	<b>250.920</b>	<b>77.971</b>

	2013						
	Bulgaria	Estonia	Hungary	Latvia	Lithuania	Poland	Romania
<i>STAGE FOCUS</i>							
Seed	0	0	0	0	1.329	1.559	0
Start-up	4.718	2.954	8.421	600	2.468	4.946	0
Later-stage venture	380	3.225	8.290	500	5.500	9.127	2.984
<b>Total venture</b>	<b>5.098</b>	<b>6.179</b>	<b>16.710</b>	<b>1.100</b>	<b>9.297</b>	<b>15.632</b>	<b>2.984</b>
Growth	6.000	20.875	36.194	2.200	7.157	150.412	10.075
Rescue/Turnaround	0	0	0	0	0	0	0
Replacement capital	0	0	0	0	0	8.214	9.455
Buyout	0	500	3.360	12.000	6.076	205.775	47.835
<b>TOTAL</b>	<b>11.098</b>	<b>27.554</b>	<b>56.265</b>	<b>15.300</b>	<b>22.530</b>	<b>380.033</b>	<b>70.349</b>

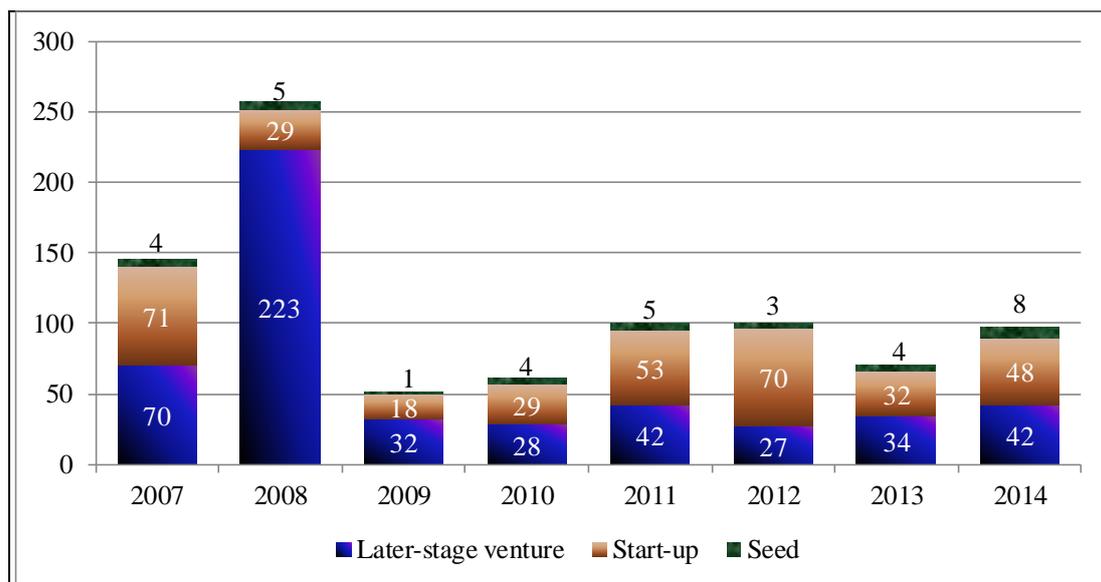
Source: processed by the authors after EVCA, 2015.

When analyzing the situation by country we observe that the increase in buyout activity in 2014 was sustained by a small number of sizeable buyout transactions in Hungary (see table 2). Also, although it registered a decrease of 22% in the buyout activity in 2014, Poland was still the largest buyout market from the analyzed CEE countries, reflecting its position as the biggest economy in the region.

Also, Poland remained the largest CEE market for growth investments and it alone accounted for 28% of growth capital investment in the entire region in 2014, though investments in value terms fell sharply by 57% to 65 million of euro. However, growth investments grew notably in other CEE countries in 2014, with Latvia, Lithuania and Romania, taking a significantly larger slice of the overall segment.

Hungary and Poland led the region in venture investment, accounting for a combined 55% of total CEE venture investment amount in 2014. Hungary's venture investment value grew most strongly with a 92% year-on-year increase from 17 million of euro to 32 million of euro in 2014. Venture investment in Poland grew by 41% from 16 million of euro to 22 million of euro and helped contribute to the marked rise in the region as a whole. Lithuania was the next largest CEE venture capital market in 2014, venture investment in this country being relatively stable when compared to 2013.

In figure 2 we observe that the increasing trend of venture capital investments in CEE was interrupted by the recent financial crisis, and the region was not able to reach the value obtained in 2008 in the last six years. Start-up investments registered an improvement in 2012, almost reaching the value from 2007.

**Figure 2 - CEE venture capital investments by stage, 2007- 2014 (in millions euro)**

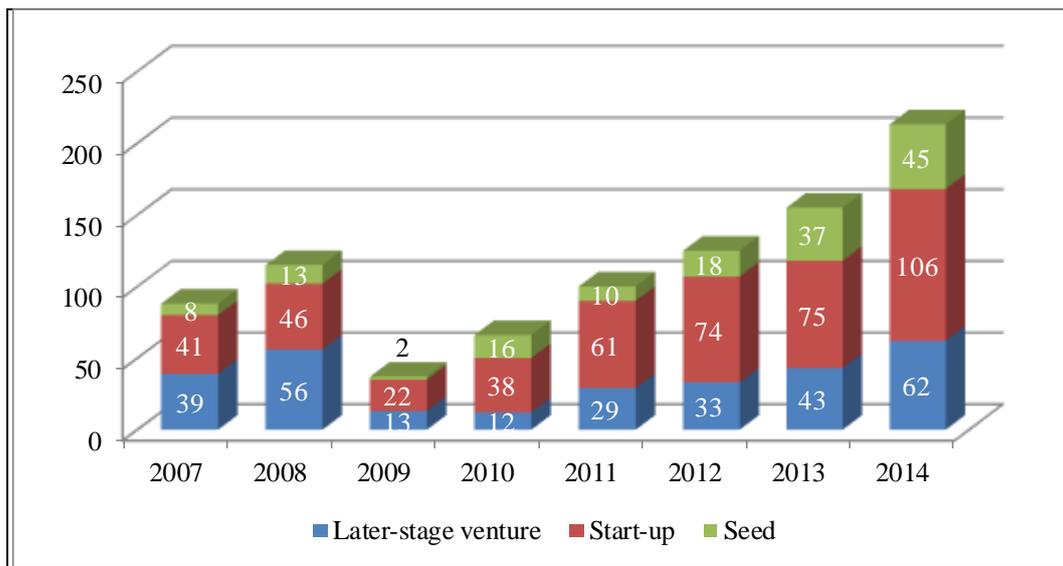
Source: processed by the authors after EVCA, 2015, p. 29

We also observe that the early-stage funding (combining seed and start-up) comprised the majority of CEE venture capital financing in 2014 with 57% of the year's total investment value. The structure of the venture capital investment market in the CEE region is similar to Europe overall, where early-stage investments comprised 55% of the total European venture market in 2014.

But when we analyze venture capital investments in CEE in the last years according to the number of companies the situation is different, we observe an important decline in 2009, and after that the effects of the recent crisis started being felt in CEE countries, but after that the trend showed an increase, in 2012 surpassing the overall number of companies from 2008. The biggest increase was registered for seed investment, from 2 companies in 2009 to 45 companies in 2014, start-up from 22 to 106 companies and later stage venture, from 12 to 62 companies (see figure 3).

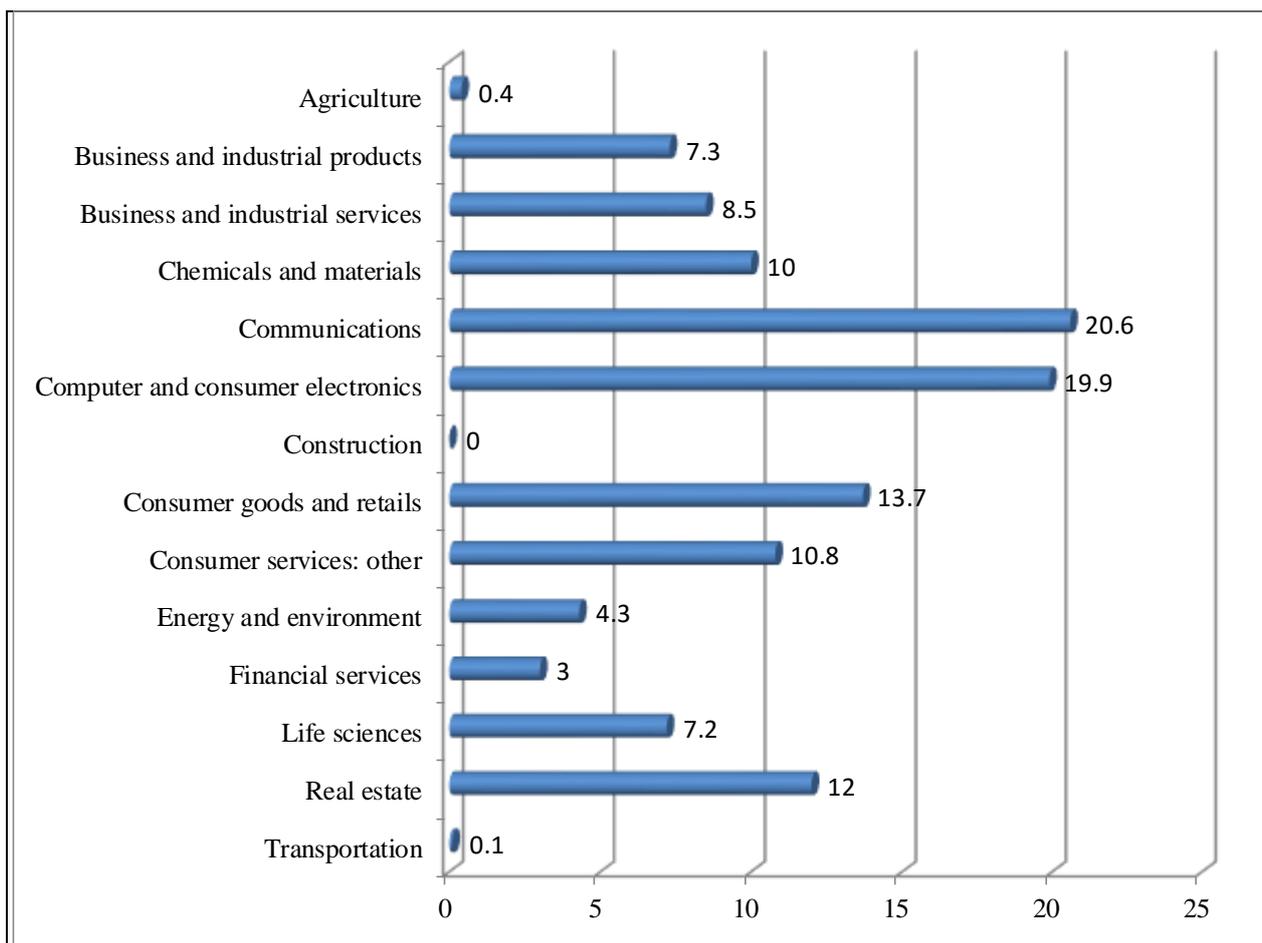
According to the number of companies, CEE also followed the European trend with 72% of all venture-backed companies financed by early-stage venture investments compared to 75% across Europe. When comparing in depth particular sub-segments of the venture capital market, it could be noticed that the CEE was also similar to Europe as a whole, with start-up financing being the most prominent. In CEE it accounted for 49% of total venture capital investment value in 2014 and 50% of venture companies financed, compared to 52% of investment value and 60% of companies in all of European venture.

**Figure 3 - CEE venture capital investments by stage, 2007 - 2014 (no. of companies)**



Source: processed by the authors after EVCA CEE Statistics 2014, p. 31

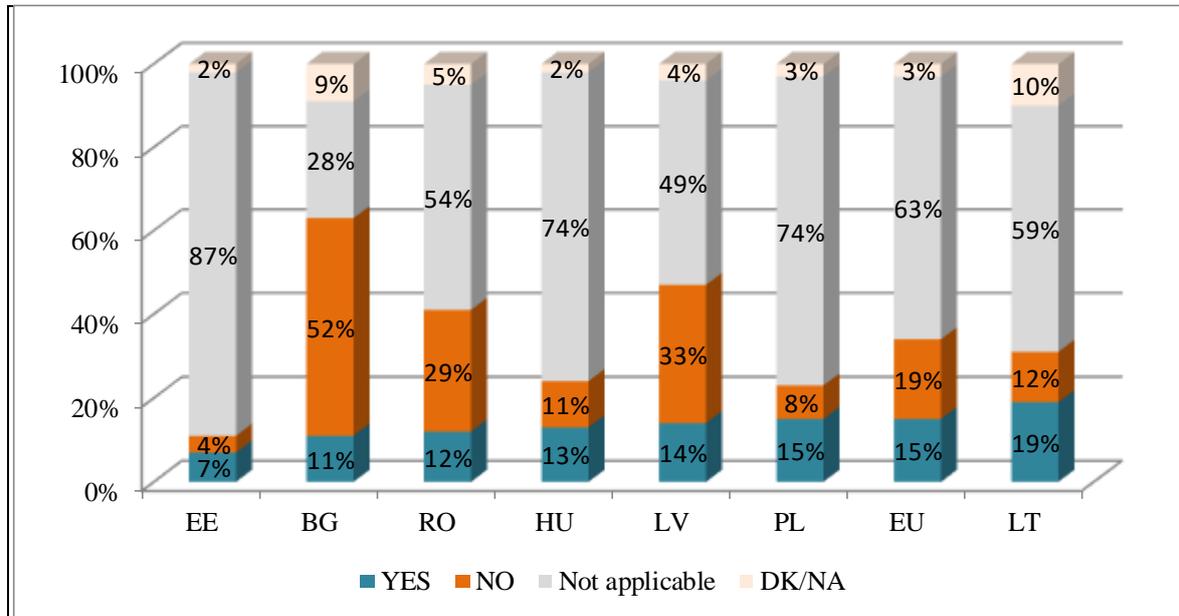
When analyzing the number of companies that received venture capital investment in CEE in 2014, Hungary took the lead with 66 companies financed comprising 31% of the total number of companies across the region. Poland came in second with 54 companies backed by venture capital (26% of the regional total) and Lithuania third with 39 companies (19% of the CEE total). Together, these three leading countries accounted for 76% of all CEE companies financed by venture capital in 2014.

**Figure 4 - Venture capital investment by sector, 2014 (amount in millions euro)**

Source: processed by the authors after EVCA, 2015, p. 32

The sectoral split of CEE venture capital investments in 2014 was similar to 2013. Communications, computer and consumer electronics, and consumer goods and retail were the three most invested sectors in CEE, representing 55% of the total value of venture investments in 2014, compared with 63% in 2013 (see figure 4). The same three sectors led the field according to the number of companies backed, representing 52% of the total in 2014 compared to 60% in 2013. Other sectors that showed notable increases of venture capital investment levels in 2014 compared to 2013 were business and industrial products and services, with a combined value of 16 million euro of venture investment in 2014 among 33 companies, as well as life sciences, with a notable 21 companies obtaining venture financing in 2014. Investments in the energy and environment sector, historically one of the largest venture investment sectors in CEE, remained at a relatively low level. It accounted for just over 4 million euro invested representing 4% of the CEE total. The sectors with the smallest values of venture investments were constructions, transportation, agriculture and financial services.

**Figure 5 - Managers' confidence in talking about financing with equity investors/venture capital firms**



Source: processed by the authors after SAFE 2013, p. 86

From figure 5 we observe that firms in Lithuania were the most confident in talking to equity investors and venture capital firms about finance, being above the EU average. The next most confident were Poland (15%) and Latvia (14%). Also, the managers from Bulgaria (52%), Latvia (33%) and Romania (29%) were notably less confident than others in talking to equity investors about obtaining finance. In Estonia (87%) and Poland (74%) almost a third of the managers said that this type of financing was not applicable. Also, in all other analyzed countries, except Bulgaria (28%), half of the managers said that this type of financing was not applicable. These results were obtained because a bigger part of the enterprises from the CEE used bank financing, and venture capital was used in a small proportion (as we have observed in the analysis above).

In the following table we put together an analysis the situation of venture capital financing on the market of each considered CEE countries and the reforms adopted in order to improve venture capital financing in that country.

**Table 3 - Venture capital financing in CEE countries and the reforms adopted**

<i>Country</i>	<i>Venture capital situation</i>
Bulgaria	<ul style="list-style-type: none"> <li>- venture capital investments have sustained the entrepreneurial activity especially for information and communications technology sectors</li> <li>- venture capital investments are still used in a very small proportion</li> <li>- the enterprises have only few alternative financing instruments on the market.</li> </ul>
Estonia	<ul style="list-style-type: none"> <li>- the Baltic Innovation Fund is encouraging cross-border investment</li> <li>- specialized funds are used in order to sustain private equity and high risk projects (including start-up firms)</li> <li>- some associations that contribute to the development of capital were established</li> <li>- market: the EstVCA - Estonian Private Equity and Venture Capital Association and the Cluster Finance Estonia.</li> </ul>
Hungary	<ul style="list-style-type: none"> <li>- venture capital financing has increased in the recent years</li> <li>- venture capital financing only comes from the JEREMIE scheme.</li> </ul>
Latvia	<ul style="list-style-type: none"> <li>- the Baltic innovation funds is working to improve the availability of equity financing</li> <li>- there are used three financial intermediaries and three new risk capital funds to sustain development of venture capital market.</li> <li>- a new pilot project for a business accelerator was established (European Commission, 2014).</li> </ul>
Lithuania	<ul style="list-style-type: none"> <li>- the venture capital financing has improved significantly in the last years (LTVCA)</li> <li>- the JEREMIE scheme is providing risk capital through a variety of instruments.</li> </ul>
Poland	<ul style="list-style-type: none"> <li>- equity finance is still underdeveloped (European Central Bank, 2014).</li> <li>- the Polish Growth Fund of Funds was established with the purpose of stimulating venture capital investments and mezzanine funds.</li> <li>- The National Capital Fund is another organism established for sustaining venture capital financing especially in the start-up phase for the innovative SMEs (European Commission, 2014).</li> </ul>
Romania	<ul style="list-style-type: none"> <li>- risk capital market is still underdeveloped, venture capital investment registering a constant decline since 2007</li> <li>- the investments in new enterprises are very low fact that affects the growth of innovative companies</li> <li>- in 2012, Romania was the fourth worst performer out of all EU Member States in terms of total venture capital investment (European Commission, 2014).</li> </ul>

Source: processed by the authors

## Conclusions

The analysis in this paper showed that venture capital financing is still underdeveloped in the emerging economies of Central and Eastern Europe. The sectors attracting investments from risk capital were the most innovative ones: communications, computer and consumer electronics and consumer goods and retail. We have also observed an improvement of venture capital financing in the region in 2014 compared to 2007, but the amounts of investments are still very small compared to the developed countries from European Union. The investors have observed the potential of the countries from CEE in using venture capital, but there are still some weaknesses of the region that have limited venture capital investments.

A big problem with using this type of financing is the confidence of the firm. Therefore, our analysis showed that managers from the CEE economies do not have the confidence to talk about the financing aspect with equity or venture capital investors. The countries in the region have adopted a series of reforms in order to improve venture capital financing, such as: the establishment of the Baltic Innovation Fund, the Estonian Private Equity and Venture Capital Association, the Polish Growth Fund of Funds. But these organisms are still at the beginning of their activity, and their establishment has not determined big improvements yet. We have to wait and see if in a couple of years they will achieve the purpose they were established for. We also have to be reminded of the lag that exists between CEE countries and the developed countries from Europe regarding the development of the venture capital market.

In other future research we propose to extend our analysis to all European Union countries, and maybe to observe which are the economic and financial factors that sustain the development of the venture capital market and to what extent they can be applied to the emerging markets from Central and Eastern Europe.

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## THE CURRENT STATE AND PROSPECTS OF ECONOMIC DEVELOPMENT IN THE EU'S EaP COUNTRIES

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**Abstract:** *Economic development is one of the main aims of economic policy in many countries around the world. By strengthening the process of economic development, we can bring the state on the path of sustainable growth and ensure stability and security in it. The paper analyzes the main indicators of socio-economic development in the EU's Eastern Partnership countries in the period 2000-2015. It also examines the current state of relations between the Eastern Partnership countries and the European Union. The main purpose of this paper is to determine the current state of affairs and prospects of economic development in the EU's Eastern Partnership Countries.*

**Keywords:** economic development; economic growth; Eastern Partnership

**JEL Classification:** O1; O4; O52; O57

### Introduction

Countries of Eastern Europe and the region as a whole have always been an area of interest to world powers which did still not lost its relevance nowadays. Thus, following the historic fifth round of enlargement, the EU started to rethink its external relations with bordering countries and launched the European Neighborhood Policy (ENP) as result, which spans 16 neighboring countries to the south and east of the EU. At the initiative of Poland and Sweden, the Eastern Partnership (EaP) was launched in May 2009 during the EU Prague summit as an offshoot of the ENP. The Eastern Partnership is a joint initiative of the EU and its Eastern European partners: Armenia, Azerbaijan, Belarus, Georgia, the Republic of Moldova and Ukraine. It supposed to bring Eastern European partners closer to the EU, supporting and encouraging reforms in the EaP countries for the benefit of their citizens. The main goal of the Eastern Partnership is to create the necessary conditions to accelerate political association and further economic integration between the European Union and interested partner countries (European Council, 2009). This program is a continuation of the European Neighborhood Policy (ENP) proclaimed in 2003. One of its main objectives is the formation of a "ring of friends" to the eastern and southern borders of the EU, i.e. the Post-Soviet republics sharing

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European values and models of economic and political system (Vlah, 2015). Taking into account that the EaP also implies economic integration of member countries with the EU, this paper examines the current state and prospects of economic development in the EU's Eastern Partnership countries.

### **1. The EaP and the Current Status of Members**

The development of the Eastern Partnership is based on four thematic platforms (European Council, 2009):

- Democracy, good governance and stability;
- Economic integration and convergence with EU sectoral policies;
- Energy security;
- Contacts between people.

The Partnership foresees stronger political engagement with the EU, namely:

- The prospect of a new generation of Association Agreements;
- Integration into the EU economy with deep free trade agreements;
- Easier travel to the EU through gradual visa liberalization, accompanied by measures to tackle illegal immigration;
- Enhanced energy security arrangements;
- Increased financial assistance;
- Deeper cooperation on environment and climate issues;
- Increased people-to-people contacts and greater involvement of civil society.

The Joint Declaration of the Eastern Partnership Summit in Warsaw, held in September 2011, emphasized the strategic importance of the Partnership as a way to deepen and strengthen relations between the EU and the partner countries, to speed up their political association, economic integration and approximation towards the EU and to support their modernization efforts (European Council, 2011). Later on, during the Third Eastern Partnership Summit held in Vilnius (European Council, 2013), the Association Agreements / Deep and Comprehensive Free Trade Areas with interested parties was scheduled to be concluded before autumn of 2014. In fact, Association Agreements / Deep and Comprehensive Free Trade Areas with Georgia, Republic of Moldova and Ukraine were concluded on June, the 27<sup>th</sup> of 2014.

For both Georgia and the Republic of Moldova, the provisional application of the DCFTA has already led to the successful development of trade with the EU in 2014. The provisional application

of the DCFTA for Ukraine was postponed until 1/1/2016. In the meantime, the EU unilaterally granted trade preferences to Ukraine (EEAS, 2015).

The Declaration of the Eastern Partnership Summit held in Riga in 2015 states that citizens of Ukraine and Georgia may be exempted from visa requirement only after the progress report (to be carried out by the end of 2015) on implementation of the 2nd phase of the Visa Liberalization Action Plans by Ukraine and Georgia respectively (European Council, 2015). A visa-free regime has already been in place since April 2014 for citizens of the Republic of Moldova holding biometric passports.

Regarding the other three countries, namely Armenia, Azerbaijan and Belarus, the Association Agreements / DCFTA were not concluded with the EU. Moreover, Belarus and Armenia have chosen a different integration project—the Eurasian Economic Union. Five post-Soviet countries are currently members of the Eurasian Economic Union: Russia, Kazakhstan, Belarus, Armenia and Kyrgyzstan. One of the consequences of the EU–Russia rivalry is that the “common neighborhood” now seems deeply divided between those countries that have joined the Eurasian Economic Union and those that have signed the Association Agreements and the Deep and Comprehensive Free Trade Agreements offered by the EU under the Eastern Partnership (Delcour, 2015).

## **2. Economic Development in the EU’s EaP Countries**

The countries of the EU’s Eastern Partnership cover a large territory of Eastern Europe and the Caucasus, with a total area of more than 1 million square kilometers and a total population of over 72 million people (as of January 1, 2015). The largest and most densely populated area belongs to Ukraine with 603.7 square kilometers area and a population of 42.8 million people. The second largest territory belongs to Belarus with an area of 207.6 square kilometers and population of 9.5 million people. Approximately the same number of population in Azerbaijan - 9.4 million people, and an area - 86.6 square kilometers. Armenia: area – 29.8 square kilometers and population - 3 million people. Moldova has almost the same area – 33.8 square kilometers and population 3.6 million people. Area of Georgia is 69.7 square kilometers and population 4.5 million people.

One of the main indicators of economic development of the country is the nominal GDP and GDP per capita. The following figure (figure 1) shows the dynamics of the nominal GDP of the EU’s EaP countries during the period from 2000 to 2015. The graph shows that according to the size of economy the largest one is Ukraine with a GDP of about 131 Bn. US\$. Comparable in economy size are Azerbaijan and Belarus with a GDP of about 76 Bn. US\$ each. The other three countries: Armenia, Georgia and Moldova are relatively smaller in size of the economies with a GDP between 8 and 16

bn. US\$. A moderate growth of GDP is observed in the three countries. More rapid GDP growth is observed in Azerbaijan and Belarus.

In Ukraine, there are periods of sharp economic downturn during the world economic crisis and the current conflict in Ukraine.

Figure 1 – GDP Growth Dynamics (Bn. US\$)



Source: World Bank database

**Figure 2 – GDP Per Capita Growth Dynamics (US\$)**



Source: World Bank database

When considering the GDP per capita dynamics (Figure 2), the picture becomes slightly different. In this case Azerbaijan and Belarus are better positioned, with a GDP per capita with more than 8 thousand US\$. The second group of countries with a GDP per capita of 3 to 4 thousand US\$ includes Ukraine, Georgia and Armenia. Moldova's GDP per capita as of January 1, 2015 was of 2.24 thousand US\$.

**Table 1 – General Government Expenditure (as of Jan 1, 2014)**

	Expenditure (mill. US\$)	Education Expenditure (% Bud.)	Health Expenditure (% Bud.)	Defense Expenditure (% Bud.)	Expenditure (% GDP)	Expenditure per Capita (US\$)
Armenia	2 643,3	8,87%	7,85%	17,91%	23,8%	889
Azerbaijan	27 946,7	7,3%	3,5%	12,31%	38%	2 949
Belarus	30 749,9	12,3%	13,45%	3,14%	42,07%	3 248
Georgia	4 632,2	6,71%	6,71%	8,81%	28,7%	1 032
Moldova	3 072,2	20,82%	13,41%	0,87%	38,48%	864
Ukraine	86 387,6	13,67%	12,17%	4,97%	48,11%	1 909

Source: World Bank database and data from countryeconomy.com

Further on, Table 1 shows the general government expenditures according to the main expenditure items, including social spending on education and healthcare. In this table, we can distinguish the relatively high level of total expenditure per capita in Azerbaijan and Belarus, which constitute 3-3.2 thousand US\$ per capita. In Ukraine the expenditure per capita reaches 1.9 thousand US\$. It is also necessary to note the high level of spending on education and health in Moldova, which make up to 20.8% and 13.4% of the national budget. Investment in people – is an investment in the growth of the country in the future. In defense expenditures we can highlight Azerbaijan (12.3% of budget) and Armenia (17.9% of budget).

**Table 2 – Foreign Trade (as of Jan 1, 2015)**

	<b>Exports (mill. US\$)</b>	<b>Exports (% GDP)</b>	<b>Imports (mill. US\$)</b>	<b>Imports (% GDP)</b>	<b>Trade Balance (% GDP)</b>
Armenia	1 519	13,05%	4 402	37,82%	-24,77%
Azerbaijan	29 400	39,67%	9 000	12,14%	27,53%
Belarus	36 288	47,68%	40 788	53,6%	-5,91%
Georgia	2 861	17,31	8 596	52,01%	-34,7%
Moldova	2 339,5	29,4%	5 317	66,81%	-37,41%
Ukraine	54 199	41,5%	54 330	41,6%	-0,1%

Source: World Bank database and data from [countryeconomy.com](http://countryeconomy.com)

Table 2 presents data on foreign trade of the EU's Eastern Partnership countries. The table shows that Ukraine and Belarus have the largest foreign trade turnover (108 bn. US\$ and 77 bn. US\$ respectively). Armenia, Georgia and Moldova have significant negative balances of trade (-24.8%, -34.7% and -37.4% of GDP respectively). On the contrary, Azerbaijan has a significant positive balance of trade (+27.5% of GDP). Ukraine (-0.1% of GDP) and Belarus (-5.9% of GDP) have the most balanced trade balance.

**Table 3 – Ratings and Indices**

	<b>Human Capital (2015)</b>	<b>Doing Business (2015)</b>	<b>Global Peace (2015)</b>	<b>Life expectancy (1 Jan 2014)</b>	<b>Fitch Rating (Nov 20, 2015)</b>
Armenia	43 place	45 place	91 place	74,54 years	B+
Azerbaijan	63 place	80 place	132 place	70,69 years	BBB-
Belarus	57 place	n/a	110 place	72,47 years	
Georgia	n/a	15 place	79 place	74,08 years	BB-
Moldova	71 place	63 place	70 place	68,81 years	B-
Ukraine	31 place	96 place	150 place	71,16 years	CCC

Source: World Bank database and data from [countryeconomy.com](http://countryeconomy.com)

Table 3 shows various indices and ratings that reflect the situation in these countries in terms of doing business, living, human capital and the overall security in the country. Thus, according to the Human Capital Index, of the 124 countries represented in the index, the highest index belongs to Ukraine (31 place) and Armenia (43 place). Despite the high share of expenditures of Moldova on education and health in the index Human capital and Life expectancy Moldova stands lower than other states. Regarding the Doing Business ratings, Georgia holds the 15th place. As for the sovereign credit ratings, the higher rating stands for Azerbaijan (BBB-) and Georgia (BB-). A lower rating is indicated for Ukraine (CCC), which implying a possible default risk. Also, according to the Global Peace index, Ukraine is among the least safe countries (150 place), which can be explained by the conflict taking place in this country. Although the share of expenditures of Armenia and Georgia on health is not so high, according to the Life expectancy index, citizens of these states are among the most long-lived people with a life expectancy of up to 74 years.

### **Conclusions**

Given the fact that the Association Agreement / DCFTA with three countries of the partnership were signed only last year, it is still early to draw concrete conclusions on the actual economic effects of these agreements on the economic development of the EU's Eastern Partnership countries. However, in the long term, this partnership maintains its relevance and significance for the EU and the EaP countries.

For Armenia, Azerbaijan and Belarus, the economic indicators show a relatively stable economic growth in these countries. With regard to Azerbaijan, taking into account the decline in energy (oil and gas) prices on international markets, a slowdown of the economy is expected.

Also, despite the fact that Armenia and Belarus became members of the Eurasian Economic Union in January 2015 and that Azerbaijan's refused to sign an Association Agreement with the EU, the continuation of constructive cooperation with these countries can be mutually beneficial and will contribute to the development of the economies of these countries. In Armenia, the development of an export component in Armenia may contribute to a more stable development of its economy. In Georgia and Moldova there is also a moderate steady growth. However, according to the results of 2014, there was a slight decline in GDP per capita in these countries. Export development in these countries may also contribute to a more stable economic development.

In Ukraine there has been some economic slowdown mainly related to the unstable situation in the country. Resolution of the conflict in Ukraine could contribute to the stabilization and growth of

its economy. EU preferences for Ukraine, unilaterally imposed under the agreement on free trade areas, have undoubtedly had a positive impact on the stabilization of the Ukrainian economy.

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## THE IDENTIFICATION OF INFLATION RATE DETERMINANTS IN THE USA USING THE STOCHASTIC SEARCH VARIABLE SELECTION

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**Abstract:** *Inflation rate determinants for the USA have been analyzed in this study starting with 2008, when the American economy was already in crisis. This research brings, as a novelty, the use of Bayesian Econometrics methods to identify the monthly inflation rate in the USA. The Stochastic Search Variable Selection (SSVS) has been applied for a subjective probability acceptance of 0.3. The results are validated also by economic theory. The monthly inflation rate was influenced during 2008-2015 by: the unemployment rate, the exchange rate, crude oil prices, the trade weighted U.S. Dollar Index and the M2 Money Stock. The study might be continued by considering other potential determinants of the inflation rate.*

**Keywords:** inflation rate; stochastic search; crisis; prices

**JEL Classification:** C52; E31

### Introduction

For policymakers, the determinants of the inflation rate are essential for targeting the inflation. The goods prices growths are followed with interest also by consumers. In literature there are many methods used to identify the factors of inflation, most of them coming from objective Econometrics. Different types of econometric models were proposed, but in this study a Bayesian algorithm based on the selection of the inflation determinants in a final Bayesian regression model is applied.

After presenting some determinants of the inflation rate in the USA from literature, a theoretical part will describe the methodological framework represented by *Stochastic Search Variable Selection* (SSVS). This Bayesian procedure has been applied for recorded data of the inflation rate starting with 2008. The monthly inflation in USA has been determined by: the unemployment rate, the exchange rate, the crude oil prices, the trade weighted U.S. Dollar Index and M2 Money Stock.

### 1. The Determinants of the USA inflation in literature

There are many studies that confirmed changes in the inflation process in the last decades. The inflation is more stable and much lower in the entire world. The sensitivity to resource utilization and

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to input costs increases declined. The main cause of these aspects is represented by the more effective monetary policy. On the other hand, another explanation is brought by authors like (Borio and Filardo, 2007, p. 5) who argued that prevailing inflation models tend to be too country-centric. This means that the inflation models do not consider too much the impact of global factors on the inflation evolution. Oil prices and imports are global factors that could be used as proxies for global economic slack.

The monetary policymakers have to understand the inflation determinants in order to obtain their target for inflation. The policymakers must change their concerns regarding domestic capacity utilization if the foreign capacity constraints have generated increases in domestic prices.

The monetary authorities are interested in having an inflation that is dependent on the real structure of the economy. For example, more competitive services and goods markets may diminish the incentive for monetary authority to choose unexpected inflation in order to keep the employment or production above the equilibrium level. The globalisation and the unexpected positive shocks in supply help central banks in imposing lower inflation rates. This measure is consistent with the opportunistic approach to disinflation (Aksoy *et al.*, 2003, p. 1880).

Mocero, Watanabe and Cournède (2011, p.5) identified the determinants of inflation for USA and other areas like Japan, United Kingdom and the euro zone. The authors analyzed the role of inflation persistence and expectations, imported inflation and resource utilisation. In the crisis period, the stability of inflation expectations included the actual inflation, the disinflationary pressure being moderated by resource utilisation and by the flattening of the Phillips curve. The relationship between the past values of the inflation rate and long-run inflation expectations has become weaker over time.

The traditional Phillips curve considers that, at least in the short term, low unemployment generates an ascending inflation. Tootell (2002, p. 579) built a Phillips curve for the USA by weighing the foreign output gap with trade. The author considered only the G7 trade partners and he found that there was no relationship between the USA inflation and the foreign measures of slack for the period 1984-1996.

For USA inflation, many studies considered resource utilization as a main determinant. This is in accordance with the New Keynesian theory. However, many researchers considered that resource utilisation is a determinant of the short-run inflation dynamics. The relationship between inflation and unemployment only for the short run is placed by (Mankiw, 2001, p. 29) in the hierarchy of the ten basic principles of Economics. For the long run the relationship between resource utilisation and inflation might not be stable. For example, Martínez-García and Wynne (2013, p. 3) found quite

fragile empirical evidence between slack or resource utilization and the USA inflation over the 1979-2010 period.

If the forecasting models of inflation rate include the international perspective, the predictions might improve compared to naive forecasts (Ciccarelli and Mojon, 2010, p. 525). Some papers considered the international co movement of inflation. Factor models were used by (Mumtaz and Surico, 2008, p. 6) and (Monacelli and Sala, 2007, p. 103) to decompose the national sectorial inflation into the following components: national component and world component.

The history of the USA's inflation might also be analyzed in the context of fiscal theory. In the context of short run debt, the fiscal theory links the level of prices with the present value of the next surpluses. The quantitative theory associates the prices with the income or transaction flow (Cochrane, 1999, p. 325). It is very difficult to measure the present value. The data actually shows wrong correlations. The 1970s were characterized by high inflation and low deficit, while the 1980s knew low inflation and a very high increase in government debt. In the depth recession with low inflation and rising debts, large deficits were also registered.

The increases in foreign goods prices have an indirect impact on USA inflation. The recent debates considered that foreign goods prices have a low influence on the actual inflation. The American producers cannot raise the prices even in conditions of cost pressures, because they do not want to decrease their market share.

In the USA the changes in exchange rates, including foreign producers' costs in dollars, have a low impact on foreign producers' prices in dollars. Since the 1980s the degree of pass-through has been intensively studied. Only a partial pass-through was explained in the mid-1980s. The companies that faced a downward-sloping demand curve passed through only a part of modification in dollar value of the output costs to the USA prices. If these foreign producers are insignificant on the USA market, they will take the given dollar prices with a small pass-through (Tootell, 2002, p. 582). The Boskin Commission identified an upward bias in the prices index with important consequences like: quality and substitution effects, outlet implications, new goods effects (Gordon, 2000, p. 23).

Recently, the relationship between USA inflation and output was modelled by (Conrad and Karanasos, 2015, p. 3). The authors used an augmented variant of the UECCC GARCH model, also taking into consideration the data uncertainty. The high inflation is against output growth in the nominal uncertainty framework. The increase in output generated increases in prices especially indirectly by reducing the real uncertainty.

The USA inflation dynamics was also analyzed by (Guegan and Charfeddine, 2014, p. 1009) using two types of models: long memory processes and structural changes models based on the

Markov Switching process. The changes in the means are correlated with the price oil shocks and the Vietnam War. The existence of breaks in the data series has generated spurious long memory behaviour.

## 2. The stochastic search variable selection

We start from the specification of a multiple regression model in order to solve the problem of identifying the variables with the largest impact on the dependent variable Y. In this model, X1, X2, ..., Xp are a number of p independent variables. Our scope is to select a subset of independent variables (X1\*, X2\*, ..., Xq\*) that are used to construct the best model. The model is represented below:

$$Y = X_1^* \beta_1^* + X_2^* \beta_2^* + \dots + X_q^* \beta_q^* \quad (1)$$

$\beta_1^*, \beta_2^*, \dots, \beta_q^*$  – coefficients

In this study, we chose a Bayesian approach for identifying the most suitable subsets of variables: the *Stochastic Search Variable Selection (SSVS)*. This procedure was proposed by George and McCulloch (1997) and it implies the calculation of a Bayesian hierarchical prior mixture. This mixture is used to compute a posterior probability. The best model will have the highest value for this posterior probability. It is not necessary to determine the probabilities for all  $2^p$  models. The estimation process is based on the Gibbs sampler algorithm in order to simulate the sample from posterior distribution. This estimation algorithm allows an efficient and rapid simulation. There are high chances to detect high probabilities.

Firstly, we represent a linear standard model that states the relationship between the endogenous variable and the potential predictors (X1, X2, ..., Xp):

$$f(Y / \beta, \sigma) = N_n(X\beta, \sigma^2 I) \quad (2)$$

where  $X = [X_1, X_2, \dots, X_p]$

X- nxp matrix of

Y-nx1 matrix

$\beta$ - px1 vector of coefficients

$\sigma$ - unknown constant (positive value)

Every potential subset of choices is indexed in a vector. The subset of predictors with very small estimators are eliminated.

$$\gamma = (\gamma_1, \dots, \gamma_p)' \quad (3)$$

$\gamma_i = 0$ , if  $\beta_i$  is small and  $\gamma_i = 1$ , if  $\beta_i$  is large

The following prior mixture is used to model the selected predictor, where  $\gamma$  is unknown and  $q_\gamma$  ( $q_\gamma \equiv \gamma'1$ ) is the dimension of the  $\gamma$ -th sub-set:

$$\pi(\beta, \sigma, \gamma) = \pi(\beta/\sigma, \gamma)\pi(\sigma/\gamma)\pi(\gamma) \tag{4}$$

$\beta$  is modelled as the prior realisation with a multivariate normal distribution and we get the model for the  $\gamma$ -th subset:

$$\pi\left(\frac{\beta}{\sigma}, \gamma\right) = N_p(0, \mathfrak{N}_{(\sigma, \gamma)}) \tag{5}$$

The  $i$ -th element on the diagonal matrix  $\mathfrak{N}_{(\sigma, \gamma)}$  is the best choice for which the coefficient is 0 or 1. The specification of  $\mathfrak{N}_{(\sigma, \gamma)}$  helps us in determining the properties of the hierarchical priors. The residual variance  $\sigma^2$  associated to the  $\gamma$ -th model is actually a realisation of an inverse gamma distribution for that prior:

$$\pi\left(\frac{\sigma^2}{\gamma}\right) = IG\left(\frac{\vartheta}{2}, \frac{\vartheta\tau_\gamma}{2}\right) \tag{6}$$

The last equation can be rewritten as:  $\frac{\vartheta\tau_\gamma}{\sigma^2} \sim hi_{\vartheta}^2$  (7)

It is advisable to decrease the value of  $\tau_\gamma$  when the number of predictors in the subset grows.  $\tau_\gamma$  is used as prior estimator of  $\sigma^2$  and  $\vartheta$  is the prior for the sample dimension. If we do not have any information about  $\sigma^2$  prior, we select  $\tau_\gamma \equiv s_{LS}^2$ , where  $s_{LS}^2$  is the OLS estimator for  $\sigma^2$ .  $\vartheta$  is selected to have a high probability for  $\pi(\sigma^2/\gamma)$  on the interval  $(s_{LS}^2, s_Y^2)$ , where  $s_Y^2$  is the dispersion of Y.

In fact,  $\gamma$  can be modelled as a realisation of any prior  $\pi(\gamma)$  from the  $2^p$  values for  $\gamma$ , we chose the following expression for it :

$$\pi(\gamma) = \prod w_i^{\gamma_i} (1 - w_i)^{(1-\gamma_i)} \tag{8}$$

$\pi(\gamma_i = 1) = 1 - \pi(\gamma_i = 0)$  represents the probability that  $\beta_i$  is large enough to be selected in the final model.

The marginal posterior distribution  $\pi(\gamma/Y)$  contains important information for variable selection. The data series for Y is known, the posterior distribution  $\pi(\gamma/Y)$  updates the prior probabilities for any value of  $\gamma$ .

The prior hyper-parameters, especially  $\mathfrak{N}_{(\sigma, \gamma)}$ , are selected in order to have high probabilities for  $\pi(\gamma/Y)$ .

SSVS procedure uses Gibbs sampling in order to simulate a parameter sequence when  $\vartheta_{0\gamma(i)} > 0$ . The distributions are conditioned by the last generated values for parameters:

$$\pi(\beta/\sigma, \gamma, Y) \tag{9}$$

$$\pi(\beta/\sigma, \gamma, Y) = \pi(\sigma/\beta, Y) \tag{10}$$

$$\pi \left( \frac{\gamma_i}{\beta}, \sigma, \gamma_{(i)}, Y \right) = \pi \left( \frac{\gamma_i}{\beta}, \gamma_{(i)} \right) \quad (11)$$

where  $i=1,2,\dots, p$

These conditional distributions are standard distributions that can be easily simulated. The form of  $\beta$  is constructed as:

$$\pi(\beta/\sigma, \gamma, Y) = N_p((X'X + \sigma^2(D_\gamma R_\gamma D_\gamma)^{-1})^{-1} X'Y, \sigma^2(X'X + (D_\gamma R_\gamma D_\gamma)^{-1})^{-1}) \quad (12)$$

$((X'X + \sigma^2(D_\gamma R_\gamma D_\gamma)^{-1})^{-1})$  is calculated again by choosing the new values for  $\sigma^2$  and  $\gamma$  is based on Cholesky decomposition.

### 3. Determinants of monthly inflation rate in the USA since 2008

We used the Consumer Price Index for All Urban Consumers which measures the average monthly modification in the goods and services prices for urban consumers between two periods. It expresses the buying habits manifested by the urban consumers. In the USA this index refers to 88% of the total American population. The weights used in computing the index expresses the importance in a certain group spending. The consumer price index is used to identify the inflation or deflation periods.

The Bayesian procedure is applied for several monthly macroeconomic variables that are presented in the following table. The data were registered for the period from January 2008 to March 2015. The objective is to determine the factors that have influenced the inflation rate (dependent variable) during this period. The explanatory variables are: the unemployment rate, the exchange rate, the crude oil prices, trade, the real disposable personal income, the expected inflation and money stock (M2).

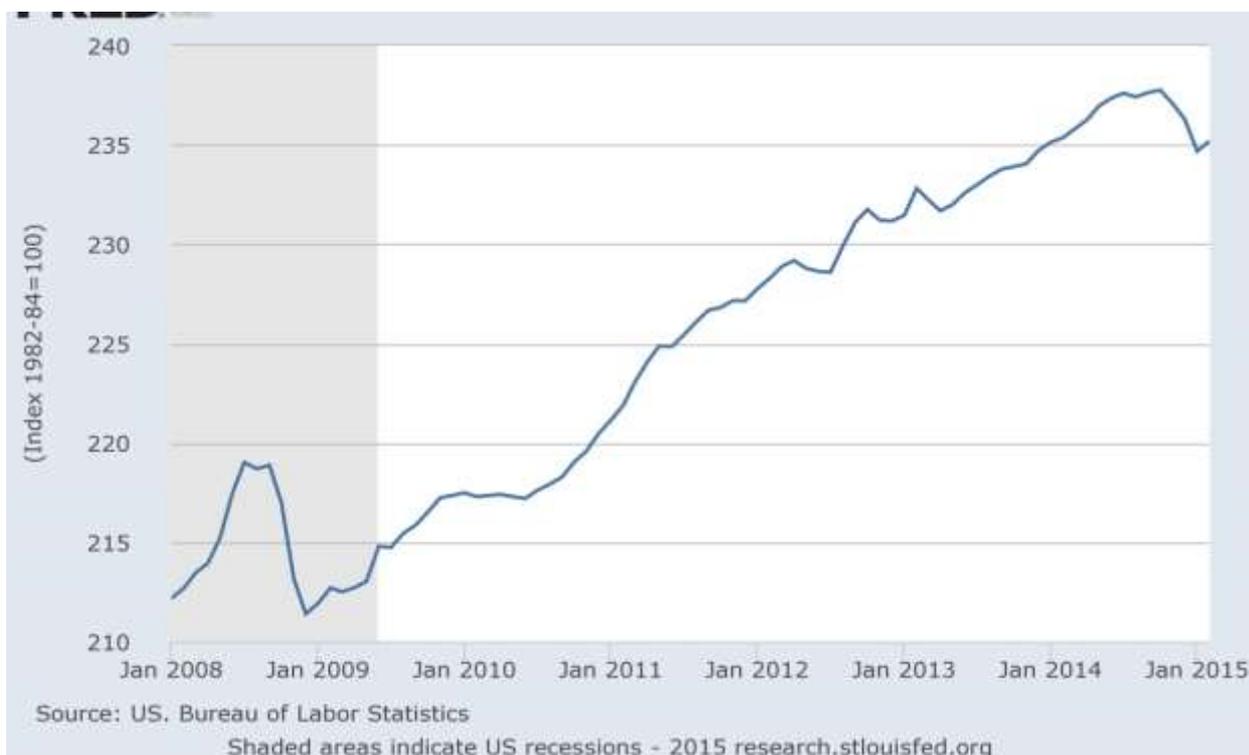
**Table 1-The inflation rate and its potential determinants**

Variable	Notation
Inflation	V
Unemployment rate	v1
Exchange rate	v2
Crude oil prices	v3
Trade weighted U.S. Dollar Index	v4
Real Disposable Personal Income	v5
Expected inflation rate (University of Michigan)	v6
M2 Money Stock	v7

Source: author's notations

According to the graph made by the US Bureau of Labour Statistics, a very low inflation was observed in the context of crisis triggering at the end of 2008 and at the beginning of 2009. Then, inflation began to increase slowly, but a constant increase was not registered.

**Figure 1-The evolution of the monthly consumer price index in the USA (January 2008-March 2015)**



Source: author's graph

The Bayesian algorithm indicated the exclusion of two variables for an acceptance probability of 0.3: Real Disposable Personal Income and Expected inflation rate provided by the University of Michigan. So, during January 2008 and March 2015, the monthly inflation rate was influenced by:

- Unemployment rate;
- Exchange rate;
- Crude oil prices;
- Trade weighted U.S. Dollar Index;
- M2 Money Stock.

The coefficients values (posterior means) in the refined regression model indicated that the exchange rate had the highest impact on the inflation rate while M2 money stock had the lowest influence. The hierarchy of high influence on the inflation is continued by the following variables in this order: unemployment rate, trade and the crude oil prices.

**Table 2- The estimation results- for the model with all regressors**

Variable	Coefficient	Posterior mean	Posterior standard deviation
Constant	C(0)	1.989	2.964
v1	C(1)	1.076	0.130
v2	C(2)	4.704	2.385
v3	C(3)	0.173	0.020
v4	C(4)	0.389	0.071
v5	C(5)	0.003	0.000
v6	C(6)	0.078	0.294
v7	C(7)	0.005	0.000
	Variance	2.705	0.432

Source: author's calculations

Very low coefficients were registered for v5, v6 and v7. For v5 and v7 the posterior standard deviations was null.

**Table 3-The inclusion probabilities for all variables**

Coefficient	Posterior mean	Posterior standard deviation
Tau(0)	0.545	0.498
Tau(1)	1.000	0.000
Tau(2)	0.949	0.221
Tau(3)	1.000	0.000
Tau(4)	1.000	0.000
Tau(5)	0.026	0.159
Tau(6)	0.175	0.380
Tau(7)	0.990	0.099

Source: author's calculations

The regressors v5 and v6 were excluded. The inclusion probabilities were indeed very small for these variables (0.026 respectively 0.175). The constant and the regressors v 1, v2, v3, v4 and v7 were chosen in refined regression.

**Table 4- The estimation of the refined regression model**

Coefficient	Posterior mean	Posterior standard deviation
C(0)	4.619	3.205
C(1)	1.454	0.189

C(2)	6.984	2.645
C(3)	0.329	0.020
C(4)	1.102	0.051
C(5)	0.006	0.000
Variance	6.681	1.089

Source: author's calculations

The results are in accordance with the economic theory. The changes in the exchange rates affect the international price of goods and services. In the case of depreciation in the exchange rate, the inflation rate will increase. The consequences of this fact are:

- A higher domestic demand (the demand for USA exports will increase because of the cheaper exports and the domestic aggregate demand will grow);
- Imported inflation (it is more expensive to buy from abroad and the price of goods from import will grow);
- Reduction of the incentive to cut costs (the competitiveness will improve in exports without any effort of the manufacturers).

The trade-off between inflation and unemployment implied by the Phillips curve suggests that policymakers may target low unemployment or low inflation rates.

An important fact for USA investors is that they return to the inflation trade from 2014.

Higher oil revenue or higher price will increase the government revenues and also the domestic liquidity. Therefore, we have higher inflation and an increase in demand. Since 2009, the growth of the oil prices has generated higher inflation in the USA. Excepting energy, the price growth was quite stable.

## Conclusions

In this study, the determinants of the inflation rate in the USA for the crisis period, starting with 2008, have been identified using a Bayesian procedure. The traditional methods used in literature to select the inflation determinants use only the objective Statistics and Econometrics. Therefore, this research brings, as a novelty, the consideration of a Bayesian selection of the inflation's main determinants.

Since 2008, the monthly inflation in the USA has been determined by: the unemployment rate, the exchange rate, the crude oil prices, trade weighted U.S. Dollar Index and M2 Money Stock. The results are correlated with the economic theory. The changes in the exchange rates have affected the

international price of goods and services. The study might be continued by considering other potential determinants the inflation rate.

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## COORDINATES AND REPRESENTATIONS OF ARCHITECTURE FOR A REGIONAL CROSS-BORDER DEVELOPMENT STRATEGY

Marcela SLUSARCIUC\*

**Abstract:** *The general objective of the wider research this paper is part of is to analyze in a multidisciplinary framework the economic development poles of the Romanian border areas and to identify the ways to building a viable strategy in a cross-border framework. One of the specific objectives is to design a complex model that shapes an adequate architecture for a development strategy for a cross-border area. A result that meets this objective is an architectural tridimensional model for building a development strategy for a cross-border area that is presented in this paper, based on the growth/development poles. The description includes the main coordinates and representations of the model, where the building framework is the institutional system layered on many levels, the main levels being structured by the economic sectors and where the solidity points are the growth/development poles from the cross-border area.*

**Keywords:** cross-border; development poles; economic development

**JEL Classification:** P25; P48; R11

### Introduction

Most of the cross-border areas are weakly developed, mainly in the context of the gravity towards the national centers. The differences between the administrative structures and competences, between fiscal and social legislation, the cooperation difficulties between SMEs based on a lack of cross-border suppliers and markets, differences between legislation and spatial planning, differences between the environmental and waste legislation, the differences between the exchange rates, the existence of different transport systems, labour markets, wages levels, social security systems, the natural emergence of a special type of "cross-border tourism" based on economic interests and with impact on the environment protection, the existence of preconceptions, stereotypes or tensions in the communities from both parts of the border, the distance between center and periphery – all these are putting pressure on cross-border areas and constitute challenges of a cross-border region that aims to balance economic and social development on long term.

Moreover, we should consider the changes in Europe – that becomes a meeting place for diversity in many fields – economic, political, institutional, cultural or professional. Therefore, we notice the increase of border permeability inside the European Union in parallel with the decrease of border permeability between the European Union and its neighbours, issuance of financial incentives,

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legal pressure, ideas and paradigms more focused on the cross-border cooperation process, re-shaping of the role of national governments as "guardians" of cross-border relations, the reconfiguration of the border status between two sovereign states from separator of countries to a mixture of functional spaces, such as economic, social, legal or identity.

Considering this framework, the governance of the cross-border regions cannot be approached in the traditional political or territorial sense, an approach placed in the context of networks of public and private actors that bring together different social systems based on different value systems being more appropriate instead, decisions being less dependent on the national level. The cross-border regions become forms of institutional building due to difficult changes along the borders, to involvement of different types of local governance and to interactions among multilevel governance networks - local, regional, European and even global. In the configuration of these regions it is worth retaining that on one hand the cross-border transfer of the organizational knowledge is most effective when the needed knowledge is simple, explicit and independent, on the other hand the differences between the individualist and collectivist cultures influence the process of knowledge transfer (Bhagat *et al.* 2002). Repeated and good quality interactions, based on principle involvement, favour trust, mutual understanding, internal legitimacy and mutual commitment, therefore it generates and sustains a capacity for joint projects.

## **1. Research issues**

This paper is part of a wider research that aims to analyze in a multidisciplinary framework the economic development poles placed in the Romanian border areas and to identify how viable development strategies in a cross-border context can be built. Still, even if the research was focused on a specific territory, the proposed theoretical model is based on a wide general literature and it can be considered as well in any European territory, for other cross-border regions. Our endeavours are based on a few hypotheses. Firstly, the cross-border areas are peripheral areas but with good potential that can be capitalized on, in conditions of proper solutions. Secondly, the theoretical literature about regional development, growth and development poles, clusters and other similar aspects, offers many approaches, models and solutions that can be adapted to a cross-border context. To this we add a third hypothesis, one that considers that the empirical studies about cross-border cooperation at different borders between Members States or between these and partner countries offer real models of cross-border cooperation rich in lessons learnt and potential solutions for specific issues that can be adapted to other cross-border areas. The fourth hypothesis is based on the fact that the cross-border areas have

some specific features and their approach needs a multidisciplinary analysis framework that should consider issues as regard to at least geopolitical, legal, sociological, administrative science or innovation systems. The fifth hypothesis considers distinctions between the cross-border areas between Member States and the cross-border area between Member States and EU partner countries, as having different characteristics, if we consider at least legislation differences and the permeability degree of the borders. The last hypothesis relies on the fact that, in conditions of cooperation and joint development will in cross-border areas, a model can be identified for building a long term strategy for developing a cross-border area.

With these hypotheses in mind we had four research questions: which are the actors that should be involved in building a development strategy for a cross-border region?; what are the steps that can be made in building a development strategy as being viable – adapted to the region needs, assumed by the actors involved in implementation, realistic, based on real existing or potential resources and able to capitalize the existing potential of the cross-border region?; can a complex model that catches a proper architecture for building a development strategy for cross-border regions be shaped? What is the role of the growth and development poles and what is the meaning that we may assign to it? From this we established four research objectives:

- Objective 1 – to identify the relevant actors that may be involved in building a development strategy for a cross-border region and also their role in an institutional system;
- Objective 2 – to identify the coordinates and stages for the building of an institutional development strategy;
- Objective 3 – to create a complex model which should comprise a suitable architecture for the elaboration of a cross-border region;
- Objective 4 – to determine the role that the growth and development poles have in the process of preparing a development strategy of a cross-border region.

The actual paper provides answers to three out of the four objectives and describes one of the important results, the tri-dimensional architectural construction model for the development strategy of a cross-border region respectively, focused on the growth/ development poles, shortly named DEV-CBC. The other results of the wider research are: a theoretical model for the institutional structure of actor networks which are involved in the elaboration of a development strategy for a cross-border region, a theoretical model structured in the stages to be followed in the elaboration of a development strategy for a cross-border region, two research instruments in the field in order to obtain the necessary data for the elaboration of a cross-border development strategy, a pre-implementation

assessment tool of the development strategy of the cross-border region and a framework for validation and update of the architecture, in a certain cross-border region, namely Suceava- Botosani-Chernivtsi.

It is important to keep in mind that in our research we give a larger meaning to the notion of the development pole, by including, besides the notion outlined by the theoretical framework and by the different entities, structures or entities which constitute activity concentrations and which have as their aim community development – urban areas, growth poles, clusters, urban development poles. We have chosen this extended approach while considering that the previously mentioned points generally have economic development potential, and they usually include either entities with a research-development and innovation capacity (universities, research institutes, excellence centres), they have an adequate business infrastructure or at least the development potential for it, they are accessible (by vehicle, train, airplane or by ship), they include entities which offer public services and they have the capacity of administrative association.

In this paper, for a first representation of the architecture we propose an architectural tridimensional model for building a development strategy for a cross-border region, based on development/growth poles.

## **2. Literature review**

The existence of much research about the regional economic growth and development poles and also the increasing importance of this field led to the identification of features and experiences, out of which just a part are referred to in this paper, the conclusions being relevant for our research.

The approach of the economic development of cross-border regions may start from the usual regional economy theories (Solow, 1956) (Swan, 1956) (Richardson, 1973) (Armstrong and Taylor, 2000) (McCann, 2001), economic growth (Myrdal, 1957) (Romer, 1986) (Lucas, 1988) (Kaldor, 1970) and development poles (Perroux, 1995) (Neubauer, 1976) and it may continue with their adaptation, still considering a few specific elements: geographical placement in the neighbourhood of main cities or development of economic areas with a high potential, cultural differences between communities from each part of the border, historical events more or less controversial that mark the actual diplomatic relationships, legal differences, provisions of the treaties or agreements between the two countries, etc.

The analyzed theoretical frame offers us much needed indications in our endeavor, referring to the dependence between productivity and the technological progress, a faster innovation rhythm and

promotion of investments in human capital contributing significantly to the development process. The change of the nature of the international trade relations from the competitive advantage to the competitive advantage based on a better use of inputs, in a more productive way, gives a new sense to the knowledge economy (Asheim, 2000) and it increases the importance of the perspectives and strategies that guarantee the innovative capacity of the region for the economic growth, contributing to the openness of the economies to the external markets, macroeconomical stability, increase in governance and public institutions quality, enforcement of the law, increase in corruption level, orientation to the economic principles of the competitive markets, losses in governmental expenses and so on, as factors evaluated by Bari. Beyond these, we can consider also the accumulation of the capital goods and human capital in regions, efficient distribution of resources and technological endowment, if we are concerned about the investment need in a higher professional qualification and in innovation promotion, as long as services companies and institutions are opened to this (Iordan, Pauna, & Andrei, 2008). The efficient use of ICT benefits supposes an ongoing competition in infrastructure, networks and connected applications, fact that supposes a fructification of the innovative potential of the universities and research centers, but in cooperation with profit entities, in view of calibration with real market and consumer needs.

The development of the regional economies can be significantly stimulated by concentrating the public investments in a limited number of cities and by supporting the network of growth poles, both in urban and rural areas, through directing significant funds towards the local development poles (Dobrescu and Dobre, 2014). A proper vision pursues the integration and implementation of the collaborative networks in polycentric territories, through the cooperation among areas and small and medium cities, both, at the borders inside the European Union and at the borders between the European Union and neighbour countries. The networks of urban development poles, together with the networks of growth poles can form polycentric systems that balances the negative space generated by the concentration and economic development, plus, the support networks of growth poles, from rural and urban areas, can support these if the local investments are directed strategically and complementary in the region. Cities are seen as growth poles because they have the capacity to induce a rapid economic growth, to create jobs, to stimulate productivity growth, to influence the development of small and medium cities and the neighbour rural areas, and therefore can contribute to the development of the regions where there are located. Moreover, the functional area of the cities goes most of the times beyond the administrative area, therefore the cities' growth can lead to an enlargement of the functional area around (Banca Mondiala, Ministerul Dezvoltarii Regionale Si Administratiei Publice, Ministerul Fondurilor Europene, 2013). If a pattern of polycentric

development is respected, that includes more growth poles, we can notice that the economic areas can be larger and, in the long term, the urban development can stimulate the rural development.

As to what concerns the clusters as growth and development sources, one of the conclusions relevant for our research, based on the information about clusters in Romania, on the scientific literature and also on Porters' remarks, is that, as regard to the cross-border areas between Romania and its neighbours, there is a starting potential for building a cooperation network that may include clusters as long as in the regions along the borders there are clusters covering a variety of fields. A second conclusion is that, both the scientific literature and experience offer guiding marks for an investigation tool for the potential of a cross-border cooperation network that includes clusters. Some issues that should be worth investigating are: the potential competitive advantages through knowledge, relationships, motivation; the existence of multiple links and synergies between industries and institutions from both countries; the innovative potential generated by universities, research centers or active companies in the innovation area; the potential usage of the historical heritage that can be preserved and recovered in relation with tourism, urban development, environmental management; the level of cooperation among enterprises, local and regional administration, research institutes, business associations (as catalysts), in each country and at cross-border level, between entities from both countries; the potential of including multinational companies, urban centers, the level of support for companies from the local and regional administration and, not the least, the motivation or objectives concerning cross-border activity, in the neighbourhood or toward other common markets. In a separate paper we investigated the clusters issue in the scientific literature and experience and the conclusions of that review were mentioned (Slusarciuc and Prelipcean, 2014).

The existence and development of clusters draw some significant effects for region development, namely, the considerable involvement of the institutions and government, job specializations for a certain industry that can be a competitive advantage for the region, continuous innovation – sophisticated methods, advanced technologies, unique products or services. The innovation potential of clusters is generated mainly by including the academic and research institutions, educational institutions, innovation and engineering centers, excellence centers and active innovative enterprises, as members (Romanova and Lavrikova, 2008).

On the other hand, the clusters by themselves are not enough to cover the weaknesses of the business environment; a solution could be in this case to include them as part of a strategy for competitiveness increase, based on regional strengths and clear and coherent objectives (Anicic *et al.* 2013). Also, it should include actions for capacity building in mutual cooperation at local level and

network approach, that ensure an extension of business relations, monitoring of development trends, share of information about enterprises strategies, openness to new ideas, collaboration with successful business, in order to save time and other resources.

Apart from the remarks above, the existence of some approaches in the cross-border relationship among clusters, based on the neighbourhood of the countries or on identification of common target markets, confirms to us one of the research hypotheses, namely, the existence in the practical field of models and solutions that can be adapted to the cross-border context (Altmann, 2014). An important conclusion, based on the lessons of the reviewed examples (Slusarciuc and Prelipcean, 2014), refers to the fact that, as long as a consistent potential for cross-border networks can be identified, a future strategy for developing a cross-border area should include tools for collective knowledge and learning inside networks, for detecting and improving the management abilities of clusters and for strengthening of cooperation inside and around clusters.

The review of these approaches and some other multidisciplinary approaches allowed us to identify necessary guiding marks in shaping the proposed models and it confirmed some of the research hypotheses, namely the fact that the cross-border regions have some specific characteristics and their study needs a multidisciplinary frame of analysis that should include also geopolitical, legal, sociological, administrative issues and also the fact that the cross-border areas placed between European Union member states have different characteristics compared with the ones placed between European Union and partner countries, at least from the point of view of legal differences and borders permeability (Slusarciuc, 2015).

### **3. Coordinates and mapping shaping DEV-CBC**

In the beginning of this section we consider relevant to delimit the meaning of a **cross-border region** in the framework of this research and of the models, instruments or recommendations that we propose. The architecture that we set was build having in mind the geographical areas placed along any of the Romanian borders (in our specific study case) with neighbouring countries and which includes at least one county in Romania and an equivalent administrative unit on the other side of the border: regions in Bulgaria, districts in Serbia, counties in Hungary, regions in Ukraine and departments in Republic of Moldova. The same delimitation can be considered regardless of the border, inside the European Union or with its neighbours, containing NUTS 3 units. Also, for cooperation cases among more restricted geographical areas, our proposals are valid but the implementation needs to be simplified as the case may be.

The proposed architecture for building a development strategy for a cross-border region has as *skeleton-structure* the institutional system layered on more floors, *the main levels* are formed by the economic sectors and *the abutments* are the development/growth poles placed in the cross-border region.

In our endeavours we take into consideration **two sets of coordinates**: the first set refers to the strategy from the point of view of the economic sectors and the exploitation of opportunities from each economic sector and the second set refers to the approach through levels/ layers of the entities and it is the one in which we can identify the poles or relevant “nodes” on which a regional cross-border development strategy can be built. The two coordinate sets have common elements represented by either the domains approached or the entities that are interest “nodes”. Besides the coordinate sets we propose a series of reinforcement marks which bring long-term value, flexibility and stability to the development strategy.

Regarding the first set of coordinates, structured on the main economic sectors, the strategy DEV-CBC should target the identification and usage of the opportunities for each economic sector, setting up objectives in the following areas:

- The primary sector – agriculture, fishing (based on the Local action groups – LAG – and the transfer of the working models where is the case), forestry (through joint restocking projects or projects based on alternative materials as sustainable development approach). The poles or “nodes” used in this sector are LAGs, local/regional administrations, rural administrations, agricultural or local producers associations, etc.
- The secondary sector – support for existing small enterprises production or starting new ones in those fields that can represent competitive advantage of the cross-border region, support for use and revival of the traditional crafts, including the construction technology, identification of technologies or innovative products that can be developed at regional level based on existing resources, etc. The poles or “nodes” used in this sector are the commerce chambers, business associations, enterprises, universities, research and development centers, clusters and local/regional administrations, as support entities for economic development by incentives or facilities offers.
- The tertiary sector – the development of tourism services at regional level, support services for the productive sector, etc. The poles or “nodes” used in this sector are the commerce chambers, business associations, enterprises, universities, research and development centers, clusters and local/regional administrations, as support entities for economic development by incentives or facilities offers.

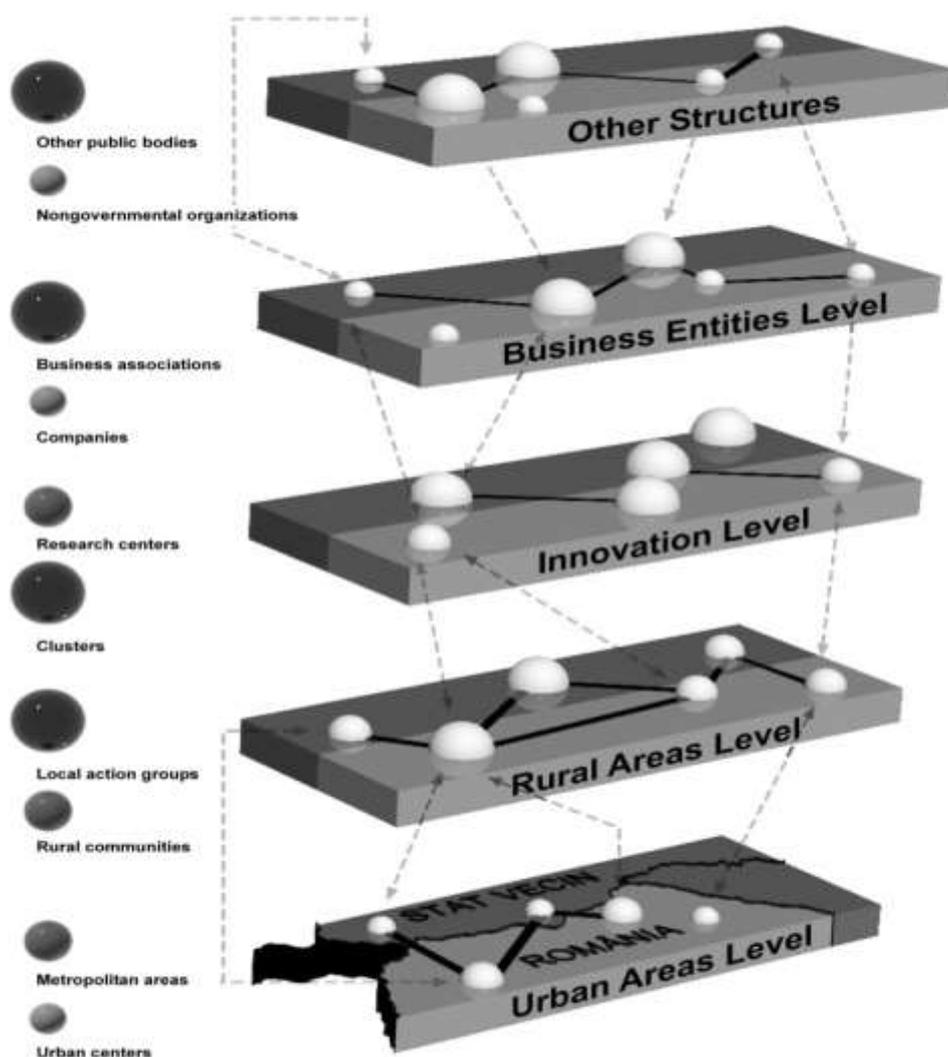
- The quaternary sector – it intervenes as support for the basic sectors mentioned above and it is focused on: building a good governance at regional level among all the actors involved in DEV-CBC building, cooperation development in research areas, initiation of cultural and educational exchanges that indirectly facilitates consolidation of the cross-border partnerships at regional level and the knowledge transfer among the partners from both sides of the border, the involvement of the civil society and the nongovernmental associations as legal entities that represent the citizens and promotes their interests and needs in different fields.

The second set of coordinates is built on levels/layers and on each layer we can identify the relevant poles/nodes. In **Figure 1** below, the representation of the tridimensional model based on planes, main poles/nodes for each plane and examples of possible relations between these is shown.

Therefore, we distinguish five levels, ordered from bottom to top, taking into consideration the priority in establishing the development objectives and building of the DEV-CBC:

- *The level of urban areas* – the main actions are: to identify the growth/development poles in the area, the metropolitan areas, in both states, to identify the existing partnerships and the potential ones, the main cross-border projects implemented or planned. The main actors are the local and regional administrations from towns/cities.
- *The level of rural areas* – the main actions are: to identify the local action groups in the member state (Romania in our study case), the agricultural and local farms associations, the rural areas, both in the member state and in the neighbour state, to identify the existing and potential partnerships, the main cross-border projects implemented or planned. The main actors are the rural administrations, LAGs and agricultural or local farms associations.
- *The level of innovation* - the main actions are: to identify the research and development centers or the ones with high innovative potential, both in the member state and in the neighbour state, to identify the existing and potential partnerships, the main cross-border projects implemented or planned. The main actors are universities, research and development centers, and clusters.
- *The level of business entities* – the main actions are: to identify the relevant business crowdings, the main enterprises or multinational companies in the region, the representative entities for the business sectors, and it has as actors the enterprises, chambers of commerce, business associations and clusters.
- *The level of other structures* – the main actions are: to identify the institutions and organizations acting on relevant fields for the region, such as public health, environmental protection, civil defense, social institutions and NGOs or border and custom institutions.

**Figure 1 - The tridimensional model of DEV-CBC planes/layers**



Source: Own representation<sup>1</sup>

Concerning the possible relations among the actors we can identify the following **types of connections**:

- *Connections type 1 – connections between entities from the same country and the same plane* – these are the simplest type and usually are long term connections, therefore the partnership has been calibrated and consolidated;

<sup>1</sup> The structural and informational concept belongs to the author of the paper and the electronic design was prepared by Sergiu Dascalu, implementation and monitoring officer in the Regional Cross-Border Cooperation Office of the Romanian-Ukrainian Border.

- *Connections type 2 – connections between entities from the same country and different planes* – we cannot establish the characteristics, these may be traditional partnerships, with solid ground, but may be new partnerships, initiated lately. Most of this type connections are traditional;
- *Connections type 3 – connections between entities from different countries and the same plane* – in this area there are already significant partnerships, due to the cross-border cooperation programmes on each of the five borders of Romania, already at the fourth programming generation<sup>2</sup>. These partnerships already passed through at least two implemented joint projects and they identified a proper cooperation way. Also, in this category we may include new partnerships, at their first cross-border partnership exercise;
- *Connections type 4 – connections between entities from different countries and different planes* – in this area most of the partnership are new, at their first partnership exercise, constituted usually as consequences of the other types of connections.

A complete tridimensional representation of all the existing and potential connections in a cross-border region is difficult to design with respect to simplicity and clarity of the representation, but, as an easy way of working we recommend the deconstruction by maps representation for each of the five levels and by maps for the connections type:

- map of urban centers and metropolitan areas,
- map of rural areas and LAGs,
- map of business structures and enterprises crowdings,
- map of clusters, universities and research & development centers,
- map of other institutions and organizations acting in relevant fields for the region,
- network-map of the existing partnerships,
- network-map of the potential partnerships.

The last ones may be also deconstructed in maps that combine fewer levels, especially the ones with common “nodes”. Also, if it will be the case, a map of disadvantaged areas for which relevant objective may be set could be prepared.

The maps are relevant in order to identify the existing resources concerning development/growth poles that may attract in the development process other entities from different

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<sup>2</sup> The first pilot initiative was represented by EBI - External Border Initiative Programme (2003), followed by the Neighbourhood Programmes (2004-2006), then Joint Operational Programmes (2007-2013) and now started or are under preparation and approval the future Joint Operational Programmes for 2014-2020.

levels. Also, the potential of the cross-border region in terms of partnership and cooperation or new development areas that had not previously been optimally used may be identified.

Complementary, next to the sets of coordinates, we propose some **stiffening marks** that bring value, flexibility and stability for DEV-CBC in the long term. These marks may be used depending on the specificities of the cross-border region and on the real state of facts when the analysis for the strategy will be prepared:

- The initiation of reconciliation activities in order to overpass the disadvantageous historical context deeply imprinted in the memory of the communities from the cross-border area;
- The use of the significant contribution that national minorities may bring for building an improved framework for cooperation in the border area;
- The identification of twin or pair cities, placed nearby the border, on each of the two sides, and the intensification of the collaboration between them, through formal and informal actions;
- The identification of the metropolitan areas located nearby the border and their integration in the DEV-CBC with specific measures or actions;
- The identification of natural sites as cooperation themes, the sites being a space for solving, in a cross-border context, some international environmental protection issues, with the support of previous actions that NGOs ran;
- The identification of joint projects that may be implemented in more stages in a longer period of time;
- The set up or identification of formal existing network structures that may be used as starting points for building the institutional system that ensures continuity and attracts financial resources;
- The initiation of setting up branches of representative business associations on both sides of the border;
- The identification of ample events that can be organized jointly;
- In the long term, the identification of cooperation opportunities between three countries that cover a certain cross-border region.

The two sets of coordinates, together with the marks and representations described above, constitute the basic architecture for a development strategy in a cross-border area, built around development/growth poles.

## Conclusions

This paper confirms one of the main hypothesis of our larger research, namely that, beyond the differences inside the cross-border region, between the communities from both sides, under the condition that a strong will for cooperation and joint development of the cross-border area exists, a model for approaching a long term strategy building for a cross-border region has been identified.

One of the main representations of the architecture proposed is a tridimensional model for building a development strategy in a cross-border region, based on growth/development poles.

The architecture proposed for the construction of a development strategy for a cross-border region has as framework-structure of the institutionalized system situated on several levels, where the main levels are composed by the economic sectors and in which the strong points are the growth/development poles situated in the cross-border region. In our approach we take into consideration two sets of coordinates: the first set refers to the strategy from the point of view of the economic sectors and the use of opportunities from each economic sector and the second set refers to the approach through layers/plans of the entities and it is the one in which we can identify the poles or relevant “nodes” on which a regional cross-border development strategy can be built. The two coordinate sets have common elements represented by either the fields they activate in or by the entities that are interest “nodes”. Besides the coordinate sets we propose a series of stiffening marks which bring long-term value, flexibility and stability to the DEV-CBC.

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## THE EUROPEAN UNION LOOKING FOR THE FUTURE. NEW FORMS OF ACCOUNTABILITY AND GOVERNANCE

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**Abstract:** *The European Union is more capable than any of its Member States, individually to meet the major challenges of the XXI century. It is a political and economic partnership that represents a unique form of cooperation among sovereign countries. The challenges can only be properly understood or addressed in a regional and global context. EU decision-making processes and the role played by the EU institutions vary depending on the subject under consideration. EU interests and values common to all its Member States and their defense on the international scene can be more effective with a common, the European approach, rather than a single voice in each state.*

**Keywords:** government; system; accountability; development; aid

### Introduction

The European Union (EU), with 28 member states and 500 million citizens play an important role on the international stage and are constantly striving to promote its core values in the world. International trade, human rights, help in crisis situations, close relations with its neighbors, promoting good governance and democracy are just a few examples of how the Europeans engage in world affairs. “The European Union (EU) is a political and economic partnership that represents a unique form of cooperation among sovereign countries. The Union is the latest stage in a process of integration begun after World War II, initially by six Western European countries, to foster interdependence and make another war in Europe unthinkable.” (Archick, 2015, p.6). Since 2004, EU membership has grown from 15 to 28 countries, bringing in most states of Central and Eastern Europe.

It maintains that the enlargement door remains open to any European country that fulfils the EU’s political and economic criteria for membership. Nevertheless, in the longer term, some European leaders and many EU citizens are cautious about additional EU expansion, especially towards Turkey or countries farther east, such as Georgia or Ukraine. The last twenty years have left nothing untouched: how we work, how we consume, how we travel, how we relate to each other, the reasons we empathise, the issues that scare us have all been transformed. And most of these changes have caught us by surprise.

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Today, we live an age of insecurity. “The challenges which Europe faces today stem as much from developments outside its borders as they do from the EU’s timidity in responding to them. If the Union is to secure its future, it will need to adjust its objectives and policies to cope with this fast-changing world.” (Project 2030, p. 12). There is much talk about strengthening the European Union, and its institutions as well as about enhancing the efficiency in being closer to its citizens.

In the current international context, “the EU aspires to be more visible and effective globally, to assume increased responsibilities on the world stage, an objective that can only be achieved by creating a united Europe, thus the EU could offer its unique model of integration based on diversity, freedom and solidarity” (Jinga, 2008, p.30). The European model is challenged by changing patterns of global power and interdependence which question the legitimacy and effectiveness of the EU’s international posture, arousing doubts on the role the EU should play in the global arena. The absence of the EU as a global player is not just a problem for Europe, but also for the world. For global governance to work, it is necessary to have actors that are willing and capable of taking initiatives and pushing the agenda forward. “In the past the EU has played such a role when confronted with issues like human rights, multilateral trade liberalization, climate, and the regulation of financial markets.” (Balfour and Raik, 2013, p.12)

In a world characterized by rapid change and a significant probability of major upsets, attempting to look ahead to 2030 is as difficult as it is necessary. (ESPAS, 2015, p.15). From the global perspective, the European Union continues to be a center of wealth and considerable economic strength, the development model is very inhomogeneous so that economic and social disparities remain substantial, growing after recent enlargements. Throughout most of its existence, the EU has been a pole of internal stability, brought peace, democracy and a consistent level of prosperity half of the continent after World War II. In time, it included the other half of Europe through a process of unprecedented political and economic integration.

These successes allowed the EU to become the greatest economic power in the world, including a market and a single currency. However, Europeans are moving towards a future increasingly complex and uncertain, with a lack of common purpose that characterized the initial postwar integration. “The European Union has a claim to be a front-runner in the new democratic age, because of its diversity, transparency and political experience acquired over decades of cooperation, compromise, coalition building, social dialogue and an active and respected civil society.” (ESPAS, 2015, p. 64). The challenges facing Europe today are generated as much by developments outside its borders and inside the EU, particularly in tackling their shyness. If the Union wants to secure its future, it will have to adjust its objectives and policies to address a rapidly changing world. So, we

hope that, by 2030, the European Union's strategic interests should probably be expressed more clearly, since fragmentation and global insecurity may well force the Union to take on more responsibilities for its security and possibly its defence.

### **1. Accountability and European Union governance**

Accountability is one of the cornerstones of good governance; however, it can be difficult for scholars and practitioners alike to navigate the myriad of different types of accountability. Recently, there has been a growing discussion within both the academic and development communities about the different accountability typologies. This note outlines the present debate focusing on the definition and substance of different forms of accountability and considers the key role that legislatures play in ensuring accountability. "Accountability ensures actions and decisions taken by public officials that are subject to oversight so as to guarantee that government initiatives meet their stated objectives and respond to the needs of the community they are meant to be benefiting, thereby contributing to better governance and poverty reduction" (Stapenhurst and O'Brien, 2005, p.1). As the European Union is turning into a polity, issues of accountability increasingly have found their way onto political and academic agendas. One recurring issue is whether these new multi-level forms of governance require new forms of accountability. The article explores the meaning of new accountabilities and whether these would help to overcome possible accountability deficits.

Anyone studying accountability will soon discover that it can mean many different things to many different people. Moreover 'accountability' often serves as a conceptual umbrella covering various other often highly contested concepts. For example, the European Commission uses 'accountability' rather loosely. It serves not only as a synonym for 'clarity', 'transparency', and 'responsibility', but it is also equated with much broader concepts such as 'involvement', 'deliberation', and 'participation. (Bovens, 2007 p.105). If one takes a narrow perspective on accountability for European governance, "the distinction is first of all a distinction between vertical and horizontal accountability, or between actor–forum relations that have a principal–agent character and relations that do not have such a character. The mechanism of political accountability operates precisely in the opposite direction to that of delegation." (Bovens, 2007 p.109).

"In terms of development cooperation and global social justice, we are living through times of profound change, especially during this pivotal year 2015, the European Year for Development. The global community is counting down to the adoption of an ambitious and comprehensive new framework of Sustainable Development Goals (SDGs), which will be recognizing and building on

undeniable achievements of the Millennium Development Goals (MDGs) while at the same time acknowledging and addressing their weaknesses and shortfalls.” (Wanders, 2015, p.1). The first step towards improving accountability of public institutions is to improve citizens’ access to key information about the most critical issues in their lives, the issues that touch their lives directly. Other literatures have been concerned with problems of accountability and legitimacy as well. A major problem in the international relations literature on ‘governing without government’ has been the accountability deficit – that is, the fact that ‘most collectivities in globalized space are not accountable for their actions’ (Shore, 2009, p. 32), whether they be multinationals, nongovernmental organizations or international organizations.

A European sphere of publics will provide democratic legitimating to the extent to which the idea of democratic accountability or control will have penetrated European governance processes, as a function of specific institutional procedures and decision-making practices. “Procedures on which accountable governance can be based in the framework of the Council of Ministers include three types: accountability towards national legislatures; transparency regulations of Council deliberations; co-decision making with the European Parliament.” (Liebert, 2001, p.11-12). The EU is faced with the challenges of fashioning practices and institutions that reconcile the conflicting demands on political representatives from their international partners and their domestic constituents. “The dilemma of political and institutional reform in the EU can then be stated as follows. Starting with where we now are, is it possible to construct a political order that guarantees the substance of continuing democratic accountability within the member states, whilst simultaneously reinforcing adherence to the political obligations that those same member states have taken on?” (Weale, 2015, p.1).

Since accountability is an ambiguous and contestable concept, the contribution first analyses the concept and then narrows it substantially before discussing the meaning of these new forms of accountability. “New forms of accountability are diagonal or horizontal in character and include accountability to administrative forums, to citizens, clients, and civil society.” (Saurer, 2009, p.17). Increasingly, accountability forums seem to come together to form multi-level accountability networks, in which expertise and information is shared and in which European and national forums work together to hold European actors to account. First of all, diagonal or horizontal forms of accountability do not of themselves enhance popular control of governance, because most of the forums involved are not democratic forums. “New forms of accountability can provide alleviations of some sorts of accountability deficits in EU governance, but certainly not of all. They may enhance learning and provide formal and informal checks and balances, but they are no alternative to

traditional forms of popular control. However, they can at the least help to provide additional information for democratic forums. What we need regarding European governance therefore, are traditional and new forms of accountability.” (Héritier, 2002, p. 26).

The conclusion is that new forms of accountability enhance policy learning and provide a series of formal and informal checks and balances but they are no alternative to traditional forms of popular control. We, therefore, need traditional and new forms of accountability regarding European governance.

## **2. Global Governance for Development**

While the importance of global governance has been acknowledged, we are witnessing the increasing need to manage global problems more effectively in the face of increased interdependence. European construction necessarily led to the transfer of authority from the state domains into the European and toward the sub-state. “The European Union is itself an actor on stage plus European policy which increases its complexity. Multiple governance process involving political actors at European, national and sub-national it is called multi-level governance.” (Adshead, 2002, p. 132). “Global governance encompasses the totality of institutions, policies, norms, procedures and initiatives through which states and their citizens try to bring more predictability, stability and order to their responses to transnational challenges.”(Committee for Development Policy, 2004, p.vi). Global governance has become a domain with many different players including: multilateral organizations that have a universal character, such as the United Nations General Assembly; elite multilateral groupings such as the Group of Eight and the Group of Twenty; different coalitions relevant to specific policy subjects (such as climate change); informal multilateralism and regional formations” (Committee for Development Policy, 2014, p.52). Effective global governance can only be achieved with effective international cooperation. As the world becomes more interdependent, global governance, including global economic governance and the governance of the global commons, is increasingly relevant for achieving sustainable development.

The implementation of the post-2015 development agenda ultimately depends on the political will of Member States. Success will depend on whether all countries contribute to the reform of global governance and use their policy space to implement policies for achieving common goals. Generally, governance refers to the steering of societal processes by governing procedures and institutions in a democratic manner. “‘Good governance’ is a specifically normative usage that prescribes certain steering procedures and institutions — based on principles, values and norms (such as participation,

transparency and rule of law) — that should be adopted to achieve preferred outcomes.” (EUROSTAT, 2015, p.318). The EU Sustainable Development Strategy addresses good governance in various sections, namely in the sections on policy guiding principles, better policy-making, and financing and economic instruments. Advancing global partnership for development has been one of the core Millennium Development Goals. Presented as the eighth MDG, the global partnership for development reflects mutual responsibilities for both developed and developing countries to achieve the other seven MDGs which focus on with poverty, education, gender equality, child mortality, maternal health, poverty diseases and the environment. The new global partnership for development in the post-2015 development framework provides an opportunity to address these global economic, social and environmental issues in a coordinated, coherent and collaborative manner. In this way, the global partnership can promote a more effective, coherent, representative and accountable global governance regime, which should ultimately translate into better national and regional governance, the realization of human rights and sustainable development. At the same time, putting in place an enabling and inclusive system of global governance would create an international enabling environment and would thus strengthen the global partnership for development in many ways, translating into a more coherent framework for achieving sustainable development at regional and national levels.

Furthermore, 2015 is the European Year for Development. This year was chosen for two reasons: the MDGs were to be reached by 2015 and it also marks the beginning of a new era of development co-operation since the debates about the design of the Post-2015 Development Agenda are supposed to culminate into Sustainable Development Goals. This is of particular importance for addressing ongoing and emerging challenges for meeting the Millennium Development Goals (MDGs) in 2015, for securing the reforms for global governance identified above, and for sustainable development in the post-2015 era. Implementation of the post-2015 development agenda ultimately depends on the political will of Member States to carry it through. The extent to which the post-2015 goals will identify the most important development needs over the course of the next decade will determine their effectiveness, a key element for their ultimate legitimacy as goals.

## **Conclusions**

The EU remains a central reference point, an alternative model to traditional interstate relations, and a transnational legal community that has brought prosperity and cohesion to all regions. The impact of EU external action will depend largely on its ability to adapt to the many challenges it will

face in 2030. A European sphere of publics will provide democratic legitimating to the extent to which the idea of democratic accountability or control will have penetrated European governance processes, as a function of specific institutional procedures and decision-making practices. Another option to consider is the integration of global governance targets and requirements within each of dimensions of the 2015 development agenda as a way of supporting improved implementation and accountability. The global partnership for development can contribute to achieving this vision by integrating global governance targets firmly into the post-2015 development agenda. In a more interdependent world, a more coherent, transparent and representative global governance regime will be critical to achieve sustainable development in all its dimensions.

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## THE CONSOLIDATION OF EU GOVERNANCE: THE EUROPEAN SEMESTER AND THE EVALUATION OF EUROPEAN INTEGRATION DEEPENING

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**Abstract:** *Once it was introduced as an instrument for deepening European integration, the legitimacy, opportunity and utility of European Semester were repeatedly questioned from the perspective of its contribution to the institutionalization of European governance. Also, there is a strong and direct link between the further deepening of the European Union's political and economic integration on the one hand, and the development of a culture of evaluating policies and programs on the other. Taking these aspects into account, the following questions arise: does the European Commission have, in its position as manager of the European Semester, a real capacity of evaluating all aspects regarding the deepening of European integration? Can the European Semester be a means for diffusing evaluation practice at the level of Member States? This is why, in this paper, we propose to give answers to these questions.*

**Keywords:** European Semester; governance; evaluation

**JEL Classification:** D04; D78; F42; O20

### Introduction

The financial, economic and social crisis of the last decade has generated the need for the consolidation of the EU governance. To this end, the Europe 2020 Strategy is implemented through the European Semester, its priorities being to ensure a smart, durable and inclusion oriented economic growth. The European Semester is thus seen as an instrument for facilitating the implementation of structural reforms in the Member States. In line with this, the European Commission's instruments for evaluation (guides, methodologies etc.) are meant to support the efforts for improving policy coordination, in order to achieve greater effectiveness. In the actual economic and political context, the governance architecture generates and channels towards the Member States solid concerns regarding the exercise of greater control by EU institutions (Armstrong, 2012). Such control manifests at the expense of the flexibility Member States benefit from both in the internal policy process, as well as regarding the management of European structural and investment funds. In this regard, the European Semester is often characterized as a negative integration instrument.

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In the context of the consolidation of the EU's economic governance, as well as in that of implementing the provisions of the Europe 2020 Strategy, the European Semester is used both as an instrument for coordinating economic policies, as well as for monitoring and evaluating these policies which are targeted according to the Strategy's objectives (for example employment, education, research, innovation, energy or social inclusion). On the one hand, the role of the European Semester is to synchronize functional inter-dependencies between different areas and dimensions of the Union's policies, thus generating a new socio-economic governance architecture. If during the last decade, when policies were guided according to the objectives of the Lisbon Strategy, the coordination of policies was conducted *ex-post*, in the context of the European Semester, the synchronization is conducted *ex-ante* (Delors *et al.*, 2011). This perspective offers a more predictable and realistic framework for implementing structural reforms at the level of Member States. On the other hand, the European Semester leads to the realization of ample processes for changing the arrangements which define relationships between EU institutions and the Member States. Thus, Member States have started to request the use of the intergovernmental approach for European policy making more frequently (Zeitlin *et al.*, 2014, p. 55). However, in the last few years the European Commission has significantly consolidated its administrative capacity for conducting all processes related to the European Semester, thus diminishing pressures coming from the Member States related to invoking intergovernmental prerogatives. Yearly adjustments regarding the calendar and next steps demonstrate the fact that Member States have accepted this mechanism of synchronization.

After being institutionalized in 2011, the European Semester proved, following the four exercises which have already been conducted that, apart from the measures for coordination and monitoring economic and social progress, there is a need for in-depth evaluations of policy impacts. Consequently, the European Commission's approach from October 2015 on stated that, in the following exercises of coordination and monitoring, there is a need to place a greater accent on the consistency of the deepening of economic integration (completion of EMU) with performances registered in the social and employment fields (European Commission, 2015b). In its communication, the European Commission also highlights the fact that there is a need for a more obvious promotion of the convergence between the two dimensions of integration, by establishing a set of criteria and by identifying and disseminating best practices. Therefore, evaluation exercises have the capacity to offer the necessary evidences and justification for supporting convergence processes. That is why the European Commission's capacity of conducting these types of exercises in all policy domains is questionable.

The argumentative discourse of this paper is focused on the analysis of the connection between the further deepening of the EU's political and economic integration on the one hand, and the development of an evaluation culture regarding policies, programs and EU's institutions on the other hand. In the first part of our paper we describe the way in which the premises for initiating and developing an evaluation capacity within the EU's institutions and policies were formed. In the second part, we discuss the way in which the European Commission took the role of disseminating evaluation practices in the Member States, including through the use of the European Semester. We also reflect on the characteristics of the contingency approach in evaluation as an alternative to the centralized administrative tendency and we analyze the way in which it can facilitate the deepening of European integration, in the context of the new socio-economic governance architecture.

### **1. Fostering European political integration – European views and practices on evaluation**

The application of EU policies is based on the synergy of several elements, ranging from ranking action priorities by establishing a smaller number of initiatives at the level of EU institutions until EU regulations are improved, to the selection of adequate and current methods of implementation. All these elements are destined to respond to the needs of Member States which are in a perpetual dynamic, thus requiring a periodical refresh. For example, with the purpose of improving policies, the European Commission (2015a, p. 3) expressed its intention to “further open up policy-making and listen and interact better with those who implement and benefit from EU legislation”. This has implications such as (European Commission, 2015a, pp. 3-13):

- Greater openness, transparency and accountability – by using online facilities for permanently consulting citizens regarding the opportunity of proposals for regulation and by including feedback in debates circumscribed to the decisional process;
- Giving more detailed information to stakeholders of policies and programs – by offering in real time sources for documentation regarding the substantiation of legislative proposals and the implications of each stage of application;
- Improved policy instruments – after “all significant impacts – whether positive or negative, quantifiable or not – should be analyzed and considered” (European Commission, 2015a, p. 6);
- Shared responsibility of the EU institutions in relation to decision making, which would support the evaluation of the impact of measures, their participative and inclusive revisions and, ultimately, the adoption of clear, fit for purpose and current regulations.

For example, the adoption of the Financial Regulation and its Rules of Application was based on similar principles. Being revised in order to better adapt to the economic and social reality of the EU, they place the accent on changes for simplifying budgetary rules and procedures which are applicable to European funds, enhancing the role of robust ex-ante evaluations for each measure, which will represent the basis for strong financial management and increased transparency (European Commission, 2013). The current state of affairs is the result of measures which have been implemented by the European Commission in the last three decades regarding the strengthening of its administrative capacity.

The process of developing the EU's own evaluation culture was initially based on the experiences which were accumulated over time by Member States regarding the use of evaluation in internal public policy making. In spite of this, from the point of view of political conditionalities, the Single European Act established the premises that are necessary for initiating the process of developing a supranational evaluation culture for community interventions (especially for community policies and by establishing the multiannual budgetary planning). The Maastricht Treaty played a considerable part in strengthening this process. The institutional reforms which were carried out in the first part of the 1990's, for preparing the EU's vertical and horizontal expansion, entailed the institutionalization of a series of new policy instruments. In order for these to be efficient, effective, relevant and adequate, the European Commission needed to conduct veritable evaluation exercises (Stern, 2009, p. 45). When the vast institutional reform evaluations were sporadically conducted within the European Communities, starting from 1995 the use of evaluation increased. The European Commission upholds the practice of evaluating the EU's interventions by periodically issuing communications to Member States, thus contributing to the initiation of a centralized process of developing both the EU's, as well as the Member States' evaluation capacity.

When following the development of evaluation in Europe, referencing the North American space, where the domain of evaluating policies, programs and organizations has been strongly theorized, is unavoidable. In response to the need of explaining the way in which funds are spent and which programs are worth running, evaluation first sought to identify the causal chain, focusing on the "experimental methods applied in a conscious self-critical way" (Campbell, 1991, p.143), and trying to identify, before evaluating a program, what a good quality program would look like.

In Europe, the preoccupation for evaluating policies, programs, projects, organizations and other aspects connected to the public space developed in a different manner from that observed in the North American space. The European Union's role as a determinant actor and a stimulus for developing the preoccupation for evaluation can be noticed, because one of the most prolific fields

for evaluation in Europe is represented by the interventions which are implemented through the policies and programs of the European Union. The EU played a central part in disseminating the practice of evaluation by including evaluations in the implementation cycle of European programs, which consistently influenced the management of programs (Pollitt, 1998, p. 2017).

For example, a European Commission document from 1996 stipulates the fact that “the Commission has identified, as a priority, in the framework of the Sound and Efficient Management Initiative (SEM2000), that the evaluation of such programs should take place on a more systematic, timely and rigorous basis” (European Commission, 1996). Thus, after applying the first multiannual budgetary planning exercise (Delors package I) and carrying out the reform of structural and cohesion funds, the European Commission established as its priority to strengthen the evaluation capacity both within its own institutions, but as well as within the Member States.

In spite of all these facts, the mechanism of propagation of the evaluation practice within the Member States was different from the one in the United States of America. In the North American space we have to take note of the crucial role played by the different professional communities (which were initially interested in the quality of the educational process, the efficiency with which public funds were spent and in the results of social programs) (Tavistock Institute, 2003, p. 10). These communities began to theorize and use evaluation in order to improve programs, extending later to other domains. On the other hand, in Europe, with certain exceptions (some Northern countries, Germany, and the United Kingdom, which were interested in evaluating democratic governance, and budgetary and political reforms), the field of evaluation was less developed. The widespread propagation of evaluation came steadily from the European Union, both as a consequence of the European Commission’s power strengthening process, in the context of the EU’s institutional reform in the beginning of the 1990’s, as well as a consequence of the acceleration of the European integration process. Thus, the development of an evaluation capacity within the Member States and implicitly of the European Union’s gained a centralized process, especially for the states which did not have such a practice at the central, regional or local levels. Among the founding Members of the EU the most relevant example is that of France, where, due to the Napoleonian administrative culture, the practice of evaluation was institutionalized much later than in the other Western countries, and the process of institutionalization began from the local and regional levels, encouraged by the EU’s regional development funds (Duran *et al.*, 1995, p. 135). In the opposite direction, at the beginning of the 1990’s the United Kingdom, the Scandinavian states and even Spain had already developed a strong internal capacity for evaluating public interventions. These countries consistently motivated themselves from the process initiated by the US beginning in the 1960’s, so that in the beginning of

the 1990's the internal public policies of the EU Member States mentioned above were founded more and more on evaluations which were conducted in the ex-ante and ex-post policy implementation stages. This process was also accelerated by the context of the reforms which are specific to New Public Management, which entailed the undertaking of consistent and rigorous evaluation exercises (Pollitt, 1995, p. 56), so that the new interventions would become more efficient and would meet the needs of beneficiaries adequately. At the same time, the European Community and later the European Union, based their focus on citizens, thus creating the European citizenship and a new generation of common policies, such as those for a better life (environment, education, employment etc.), which created the need for consistent ex-ante evaluations.

In this context of thematic and geographical expansion of evaluation practices, several European approaches regarding the methods and techniques used for evaluating public interventions were developed. One of the most well-known approaches is the *illuminative evaluation* (some authors include Parlett, Hamilton), which uses methods and instruments derived from anthropology, psychology and sociology, its purpose being "illumination", or the clarification of the elements and processes which are analyzed. Other well-known approaches are the *democratic evaluation* (MacDonald, Walker) or the *personalized evaluation* (Kushner), which focus on negotiation, the pluralism of values and the diversity of stakeholders. What is more, there are certain approaches which focus prominently on the *culture of dialogue in evaluation* (Karlsson) or the so-called *realist evaluations*, which criticize both positivist, as well as constructivist approaches, highlighting instead the roles of regulations, stimulants and information (Vedung) (Stame, 2013, pp. 356-362). In spite of this, in the last period, the positivist current is gaining a little more pronounced effervescence in conducting evaluations at the level of EU policies, especially in the case of intervention regarding economic, social and territorial cohesion (Hoerner, Stephenson, 2012, p. 699). The determining role in using evaluation in the European Union at a systemic level was played by the evaluation requirements through the regulations regarding Structural Funds. To this end during the years 1995 to 2000 the European Commission carried out the *Means for Evaluating Actions of a Structural Nature* program, within which a group of independent experts elaborated a six volume set of handbooks on monitoring and evaluation approaches and techniques (Gaffey, 2013, p. 196). The initial efforts laid the foundations of a process of diffusing evaluation practice, both within the services of the European Commission, as well as at the level of Member States. Consequently, a framework of horizontal and vertical convergence was gradually created. In our opinion, the successful application of current governance instruments, such as the European Semester, depends

mainly on the initial foundations of the process of institutionalizing the use of evaluation in the process of deepening European integration.

## **2. Contingency view as an alternative for dealing with the centralistic administrative tradition**

As it can be seen from the practice in the field, “current tendencies in the practice of evaluation tend to follow situational logic, that of choosing the approach which is most adequate to each case, but also to the *complexity of the levels of interaction it entails*. Of course, preferences for certain approaches are inherent, but budget and time constraints do not allow them to become implacable rules in practice” (Stavaru, 2015). There are several fundamental elements which play a part in the development of an evaluation process and which have the capacity to discriminate between approaches and models, such as: a) ontological and epistemological positioning; b) the positioning regarding objectivity; c) the purpose of the evaluation; d) the object of the evaluation; e) the utilization of the evaluation process and results; f) the type of evaluation design; g) the role of evaluators and of the epistemic evaluation community; h) the inclusion or non-inclusion of values and i) the inclusion of the client and stakeholders in the evaluation process. All these elements have proven to be determinants of the process of creating and maintaining the construction of an evaluation capacity (European Policy Evaluation Consortium and Technopolis France, 2005) and culture within the European Union (Williams *et al.*, 2002), thus strengthening its polity regime characteristics and the new socio-economic governance architecture.

If in the initial stages the centralized approach for developing the evaluation capacity within the European Union was needed in order to begin the process, in time it came to generate the effect of searching for a gold standard for methods and instruments which are used for evaluating the Union’s interventions. Thus, the centralized approach, which was mainly favored by the centralized administrative culture of the Member States, led to the widespread use of methods and instruments for evaluating EU interventions. This process of dissemination was transposed within the central, regional and local administrations of the Member States, as well as candidate and associate states. For example, through the Eastern Partnership, as well as the European Neighborhood Policy, approaches regarding the need for using evaluations in the process of substantiating public policies have made their way into the Republic of Moldova or in Ukraine (Toderas and Stavaru, 2013, p. 475). The recent evolutions regarding the EU’s institutional reform, and the desire to create a veritable EU

social and economic model, encompass the following phenomena regarding the process of deepening European integration:

- The implementation of a program or common policy should be regarded as an open system, which is sensible to a certain degree to interferences coming from the Member States, as well as from external contexts (social, economic and political crises, disasters, strategic preferences etc.);

- The dynamics of transforming an initial state to a proposed state through a program depends on the dynamics of the national administrative environment, but also on the stimulants and conditionalities which derive from the process of regulating and implementing common policies.

In the context of the increased accent placed by the EU in the last few years on on-going evaluation, we consider that three major aspects need to be highlighted. Firstly, based on the idea of evaluation processes continuity, we consider that the usefulness of evaluation can be increased by using it, alongside with achieving its other assumed roles, as a mechanism for continuous learning, both in the phase of programming, as well as in the phase of implementation, during the policy and program cycle. Thus, through this reorientation, both Member States, as well as the European Union's institutions can develop a more interactive and adequate framework for learning from public interventions that have been implemented. What is more, the usefulness of such an approach is evident in the Member States' public administrations (central, regional and local) institutional innovation process (Stame, 2007, p. 10), a context in which the learning process ensures the convergence of the approaches, practices and instruments which are used in public policy making. The recent financial and economic crisis, and the actual social crisis, point out to the fact that learning from public policies has to be continuous, flexible and deliberate, and evaluation exercises, be they retrospective or prospective, need to offer a wider choice of options and alternative strategies and actions. This is why, in order to strengthen its evaluation capacity, as well as that of the Member States, the European Commission has been placing a pronounced accent in the last few years on a complex set of instruments included in the Better Regulation Package (European Commission, 2015a), as well as on new types of evaluations, such as Fitness checks. The latter instrument is concerned with analyzing the ways in which the sets of legislative or normative provisions in a given field have contributed to fulfilling or not fulfilling the objectives of a policy.

Secondly, based on the idea of increasing flexibility and on the characteristic of a process which is reactive to ongoing changes, and taking into consideration the complex characteristics and the wide reach of European policies and programs, we consider that evaluation needs to keep up with these characteristics and that a contingent approach to evaluation can respond to this need in an efficient manner in order to optimize programming and implementation processes with the aid of various

evaluation exercises. The European Commission, as well as other institutions within the European Union, has not promoted such an approach. However, under the pretext of increasing the comparability of evidences and processes, the centralized system was created in the last part of the 1990s in order to develop an evaluation culture and capacity within all the Member States, as well as those which were in the process of adhering.

Unavoidably, the creation of the centralized system also led to a unique understanding regarding the use of evaluation methods and instruments. For example, the predominance of counterfactual analyses in the regional development of the Member States is a consequence of this process, and public servants and experts from central public administrations incorrectly apply the logic of “this is how the European Commission requires [it]”, even though the European epistemic community frequently presents the shortcomings of it (Stame, 2010, pp. 381-382). Taking this situation into account, Picciotto considers that in the last two decades the quality of the evaluations that have been conducted on the structural and cohesion funds of the European Union has not improved significantly due to the lack of diversity of methods and instruments which are specific to the evaluation process, even though the evaluation results had a significant impact in establishing policy priorities (Picciotto, 2007, p. 126). It is possible to obtain added value by exploring a wider range of evaluation concepts, models, methods and instruments, and using them based on choices which are made when deciding on the actions which are most appropriate to the emerging situation. This is consistent with the contingent evaluation approach, which points out to the fact that “there is never a way which is always the best for conducting an evaluation, but, instead, choosing the approach and methods should be based on the characteristics of every situation” (Chen, 2005, pp. 11-12).

Taking into consideration the fact that Europeanization is based on a diversity of processes and policy actions and strategy alternatives, this phenomenon can be seen from a contingent point of view. This is why the use of the contingency perspective will lead to a better anticipation of probable evolutions for a range of expected events (such as economic governance and the European Semester), but also of the conditions in which quantitative, qualitative or mixed methods will prove more useful for evaluators and for beneficiaries (EU institutions, Member States, citizens’ communities etc.), based on which expected events will take place towards consolidating policy convergence. Even though the European Semester was initially conceived as an instrument belonging to economic governance, the need for synchronizing different interventions from the macro-economic field inevitably creates externalities towards other interventions, such as those from education, employment, energy or environment.

Thirdly, we consider that using a contingency approach in evaluation is opportune, especially in order to counterbalance the perpetuating of the centralized administrative culture, which entails the need to wait for indications from the central administrative level on the way the processes of public interventions need to be carried out. Thus, the contingency approach opposes the idea that there is only one way of conducting evaluations (Stame, 2013, pp. 367-368), in this case, the one which is indicated by the central administration. The openness to non-universal approaches would facilitate innovation in the field of evaluation models, methods and instruments and, implicitly, the contribution of theorists and experts to the development of the field of evaluation and of an evaluation culture, thus leading to the deepening of European integration.

In summary, the contingency view entails the analysis of the different characteristics of evaluation processes, which requires to identify the range of variations and possible combinations, so that, by following situational logics, through deliberative - participative contexts, one can choose the most adequate alternative, the objective being to obtain a more efficient and adequate model subsequent to the context of European integration. In this way, the results of evaluations would offer the premise for interventions which are closer to the communities of beneficiaries and sustain the process of consolidating the European polity public space.

At the level of Member States we can notice two situations regarding the use of evaluations in the process of reporting progresses which have been registered during an exercise specific to the European Semester. A first situation refers to Member States in which evaluation has been used since the 80's (Kallemeyn *et al.*, 2015, p. 341) or those which have significantly consolidated their internal evaluation culture (such as Portugal or Spain). In the case of these countries, exercises of reporting on the progress or regress registered in the context of objectives specific to the Europe 2020 Strategy assumed through National Reform Programs are generally conducted based on solid evaluation exercises, and policies are substantiated based on valid and periodically collected evidences. This is why, in the case of these countries, evaluation exercises which use the counterfactual method have a high level of validity.

A second situation refers to countries in which the maturity of evaluation culture is still very low, as in the case of Romania. Reports within the European Semester are rather based on pseudo-exercises of evaluation. Furthermore, the substantiation of policies is made based on the political desideration of political parties which are governing at one point or another.

In the case of Romania, recent research regarding the maturity of the national system for evaluating public interventions, which was conducted at the central government level, pointed out the fact that the current administrative culture is tributary to the ambiguous understanding and rare use

of evaluations (Stavaru, 2015, p. 214). Thus, in spite of the fact that over time the European Commission has encouraged governmental authorities to strengthen their evaluation capacity, at the internal level this issue was not considered to be sufficiently important. Consequently, evaluation exercises have been conducted sporadically in the last few years, which mainly focused on conditionalities regarding the implementation of structural and cohesion funds (as in the case of the Operational Program for Regional Development, or the program for Development of Human Resources). With regard to national programs which have a tangency to the objectives of the Europe 2020 Strategy which are assumed through the National Reform Program, evaluations are rare, and the ones which are conducted are expressly required by the European Commission, the World Bank or the International Monetary Fund. In general, the quality of the evaluations is low, and evaluation results are rarely used for substantiating interventions. With regard to reports by the ministries of results subsequent to the objectives of the National Reform Program, these are conducted based on general information, without being supported by evaluations of impact studies.

Thus, in the case of Romania, the European Commission has not succeeded in strengthening the evaluation culture through the European Semester, neither in the case of programs with European financing, nor in the case of programs financed from the national budget, but which have a direct connection to the objectives of the Europe 2020 Strategy.

In the case of the European Commission's services, as well as that of the Member States' central administrations, it becomes more and more difficult to argue that a single evaluation model can offer the most appropriate answers in all the situations when a policy or a program, specific to European integration, are evaluated. For each and every case different elements, dimensions and aspects which are useful to the evaluations' beneficiaries can be used and combined. In the logic of European integration it is important that the evaluations of interventions are not conducted by the European Commission itself, but to implicate wider consortiums of organizations whose main activity is to evaluate public programs and policies. What is more, a contingency approach to evaluation has the role of strengthening the European Union' values. By invoking the values, principles and objectives of the European Union, the Member States (in the name of their own citizens) decide to transfer more competencies to the European Union, and from this process citizens expect a significant improvement of the common policies for a better life. In reality this is translated by EU policies becoming close to the expectations and needs of European citizens and in consequence the democratic deficit which is characteristic to the process of deepening European integration is perpetually diminished.

## Conclusions

The development of an evaluation culture and capacity in the context of deepening European integration has taken place during the last three decades through a mixed process. In the first stage, up to the middle of the 1990's this process was carried out through a bottom-up mechanism, from certain Member States to the Community institutions. The second phase manifested itself through a top-down mechanism (from the supranational to the national level) as a commitment of the Member States, based on the agreements which were settled at the supranational level. The second phase proved to be much more consistent and oriented towards achieving convergent results, which would facilitate the deepening of European integration. If in the first phase the process was rather intergovernmental in nature – with the purpose of improving the relevancy and efficiency of the interventions which were carried out through structural and cohesion funds – in the second phase the regulatory character strengthened the supranational dimension, with the purpose of contributing to the fulfillment of the convergence and cohesion of objectives. Consequently, the European Commission, together with international organizations such as the UN, OECD, World Bank etc., has become a true promoter of evaluation within Member States, both through regulatory practices, as well as by promoting the cases of qualitative practice (a process which has been stimulated especially through the Open Method of Coordination). Because of this, there are certain cases when the evaluations of EU policies and interventions are conducted after a series of patterns, without ensuring the diversification of methods and innovative instruments. What is more, through an isomorphic process, the Member States' central administrations have transposed the same approach into their internal policies and interventions, thus perpetuating the use of the same evaluation models, methods and instruments.

In the context of further deepening the European political integration and of developing its own social and economic model, the EU has to offer as much and as relevant evaluation as possible to its own policies and initiatives so that the objectives of integration become achievable. Furthermore, the deepening of European integration entails the fact that the evaluation process does not end when the final results are identified. Instead, a new method of prospective thinking has been learned, which is based on knowledge and experience that has been accumulated. This method can be used for present implementations and for the future programming period, thus allowing a restart of the policy cycle. We have illustrated the need for the European Union's institutions to offer a wider framework for the diversification of the evaluation approaches, methods and instruments which are used. Such a shift in paradigm would enable the offering of a much more democratic and participative European public

policy making framework, and will lead to a decrease in the democratic deficit, which is characteristic to some EU institutions and to the results of the integration process. For example, the European Semester is an instrument which facilitates the consolidation of evaluation capacity and culture at the level of Member States. In spite of the fact that in the context of the EU governance architecture from the post-Lisbon period the European Commission has created and implemented innovative instruments such as the European Semester, Fitness Check, or complex packages from the Better regulation series, it can be noticed that some Member States, such as Romania, still do not have a good capacity for evaluating public policies and programs connected to the objectives of the Europe 2020 Strategy.

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