THE FAILURE OF THE EU REGIONAL POLICY IN ESTONIA?

Tanel Oppi and Erik Moora

Abstract
The main objective of the current paper is to evaluate the ability of Estonian local governments to apply successfully for financial aid from the instruments of the EU. Socio-economic status of local governments and its impact on their participation in the pre-accession programmes are elaborated more closely. As a result of the analysis, a conclusion can be drawn that socio-economic status of a local government plays an important role in its ability to participate in regional aid programmes.

1. Introduction
In May 2004, 10 new member states (NMS-s) of European Union (EU) will obtain official status as equal participants in the construction of new European Union. Since the early days of the integration of former Soviet Bloc members to EU policies and institutions, there has been considerable concern whether they would be able to participate equally and decorously in political processes of EU. The question of eligibility has, to large extent, been justified and meaningful.

To overcome this problem, EU has fostered the development in Central and Eastern Europe via different financial support programmes: Phare, ISPA (Instrument for Structural Policies for Pre-accession), and SAPARD (Special Accession Programme for Agriculture and Rural Development). The overall objective of these instruments is to assist the applicant countries of Central and Eastern Europe in their preparations for joining the European Union and help them through a period of extensive economic restructuring and political change.

These support programmes form a part of the wider framework of EU-s regional policy. European Union has declared economic and social cohesion as one of its main objectives. To imply the importance of regional policy for EU, the growth in funding of Structural Funds in has grown from their relatively insignificant role to one-third of the overall Union budget (Allen 1997).

Balancing regional differences has also been one of the main purposes of EU-s financial assistance to NMS-s. These investments should alleviate not only regional differences in Europe as a whole, but also within the NMS-s themselves. NMS-s are known to demonstrate even more significant intrinsic regional disparities than different regions across Europe. In this respect, low administrative capacity of local government units (in most NMS-s) is one of the key problems and challenges. Principles of democracy and subsidiarity force the policy-makers to turn their eyes to the local governments as the appropriate level of solving sub-national development inequalities.

As experiences with pre-accession financial aid programmes imply, the ability of regional and local governments to benefit and participate in these programmes is one of central issues. Quite often, the conditions of assistance have been too strict for weak and fragmented local governments of CEE.

Therefore, the strength and effectiveness of local authorities is one of the main indicators of regional development. Keeping that in mind, NMS-s have a quantity of challenges to meet. Set aside the fact that Estonia as a whole is part of the most lagged-behind region in new EU, it has considerable disparities within its territory. The large number of weak municipalities (most of them in constant financial difficulties) poses a treat of not being able to absorb the funds assigned to NMS-s by European Union. Current paper aims to illuminate the success or failure of so-far pre-accession instruments in levelling regional and local disparities, focusing on the relationship between allocating practices of EU regional funds and strength effectiveness of Estonian local governments. Authors believe, also, that the risks of mismanagement of EU funds are best visible in local authorities.

Main problem addressed by the research and paper is whether and how local governments of Estonia are capable of applying for and purposefully managing of the EU funds assigned to regional development and investments

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in NMS-s. Does current practice of allocating EU-s regional assistance alleviate or deepen the inequalities between Estonian local governments? What obstacles to purposeful use of these funds are identifiable and how to overcome these problems? The preliminary hypothesis is that the objective of EU structural policies – to alleviate regional inequalities – may remain unattainable due to several factors that characterize local governments in NMS-s and due to the operating principles of pre-accession financial instruments. Even the opposite – EU-s pre-accession funds may even deepen intra-state regional differences – may prove to be true.

Current paper is part of an ongoing research that attempts to evaluate the capacity of Estonian local governments to participate in policy-making and implementation processes of common European administrative space. So-far experience of Estonian local governments’ independent participation in EU assistance programmes is so insufficient that strong and statistical conclusion about the eventual failure or success of EU-s regional policy cannot be drawn yet. We fully acknowledge that the criticisms presented in this article do not undermine the need for and usefulness of EU-s regional assistance policies. We simply point out that certain aspects of these may have shortcomings that could increase the disparities within NMS-s. We are, also, well aware that local governments are not the most important level of solving these problems, most of the aid is administered by national agencies.

The paper consists of 4 different chapters. First of all, we outline the main aspects of EU-s regional policy. The policies towards candidate countries are also described to present the main principles and objectives of the assistance to states of Central and Eastern Europe. After that, the overview of Estonian municipalities and their position in the public administration system of Estonia will be briefly presented.

While our main purpose is to discuss the effect of EU-s financial aid programmes on the socio-economic misbalance among local authorities, the index of socio-economic managing will be developed and used to assess the current situation of Estonian local authorities. Having done that, we present the Estonian experience in participating in EU-s pre-accession financial instruments. The focus on local governments forces authors to concentrate on a small number of specific programmes. In the following analysis we shall demonstrate that so-far experience shows that most of the regional funds is allocated among the municipalities that are relatively successful and well off. Those with the sharpest social problems are often unable to participate in these programmes. Finally, we point to several reasons for this contradiction in objectives and consequences of assistance policies and suggest few possible solutions.

2. The Regional Policy of in the European Union

For Estonia, as well as for the 9 other NMSs, the situation regarding the regional policy of the EU is unique: it is still a subject of EU’s policy for the accession countries and at the same time with accession into the EU, it will become a part of the regional policy of the EU.

2.1. Overview of Regional Policy in EU

Regional policy of the EU refers to a set of activities the aim of which was actually phrased in 1957 in the Treaty of Rome: “… to strengthen the unity of their economies and to ensure their harmonious development by reducing the differences existing between the various regions and the backwardness of the less favored regions”. The Single European Act rephrases the ‘harmonious development’ to ‘economic and social cohesion’ but the idea remains the same: how to reduce the regional disparities within the Union itself and the member states. (Allen 1997) Since the whole chain is as strong as its weakest link is, the importance of the regional cohesion is obvious.

The primary tools of the EU’s regional policy are the Structural Funds (the Funds) and the Cohesion Fund.

The aim of the Funds generally is supporting of regions suffering from low GDP, high unemployment or industrial or agricultural decline. The currently the underlying principles of the Funds are described with the Council Regulation laying down general provisions on the Structural Funds (EC No 1260/1999). The Regulation identifies four financial tools of the Community referred to as the Funds:

- European Social Fund (ESF) – mainly provides assistance under the European employment strategy;
- European Regional Development Fund (ERDF) – concentrates on regions whose development is lagging behind and those undergoing economic conversion or experiencing structural difficulties;
- European Agricultural Guidance and Guarantee Fund (EAGGF) Guidance Sector – deals with the development and the structural adjustment of rural areas whose development is lagging behind by
improving the efficiency of their structures for producing, processing and marketing agricultural and forest products;
- Financial Instrument for Fisheries Guidance (FIFG) – supports restructuring in the fisheries sector.

The history of the Funds reaches back to the beginning of the Community. Two sector-based funds of the current Funds – ESF and EAGGF – were set up in 1958. With the accession of Denmark, Ireland and the Great Britain and the worsened global economics situation the need for clearer cohesion policy became even clearer. In order to respond, ERDF was created in 1975. The main function of the ERDF was to redistribute a part of the member states budget contributions to the poorer regions.

The most important turning point in the development of the regional policy of the Community took place in mid-1980’s. In 1986 the SEA lays the basis for a genuine cohesion policy: to offset the burden of the single market for southern countries and other less favored regions. In 1988 three separate funds (ESF, EAGGF and ERDF) were brought together under the same framework to form the Funds and funding allocated to them was raised up to ECU 68 billion.\(^2\)

In 1993, the Edinburgh European Council adopted two important decisions regarding the Funds. First was the creation of the FIFG, the fourth of the current structural funds and the second was allocation of one third of the Communities budget to cohesion policy. (Peterson and Bomberg 1999)

The last reform of the Funds took place in 1999 on the Berlin European Council we re the current principles of the functioning of the Funds and Cohesion Fund were laid down. Part of the reform was narrowing down of the objectives of the funds from previous 7 objectives to current 3:

- Objective 1 – promoting the development and structural adjustment of regions whose development is lagging behind;
- Objective 2 – supporting the economic and social conversion of areas facing structural difficulties;
- Objective 3 – supporting the adaptation and modernization of policies and systems of education, training and employment. Third objective also provides financial assistance outside the regions covered by Objective 1 and provides a policy frame of reference for all measures to promote human resources in a national territory without prejudice to the specific features of each region. (Peterson and Bomberg 1999)

The total budget allocated to the Funds for 2000-2006 amounts up to €195 billion. (Commission 2004a)

The second tool of the EU’s regional policy besides the Funds – the Cohesion Fund – was created in 1992 with the Treaty on European Union. The main purpose of Cohesion Fund was to support projects in the fields of the environment and transport in the least prosperous member states: Greece, Ireland, Portugal and Spain. For the period 2000-2006 is €18 billion allocated for the Cohesion Fund. (Commission 2004a)

2.2. The EU’s Pre-accession Programs for the Candidate Countries

In the light of the widest enlargement in the history of the EU three pre-accession programs have been introduced by the European Communities to assist the CEE applicant countries\(^3\) in their preparations for joining the European Union (Commission 2004b):

- The Phare programme (Poland, Hungary Aid for Restructuring of the Economy) is the main assistance programme of the EU to the CEECs in their preparation for joining the EU. The Phare Programme has two main priorities: Institution Building and \textit{acquis}-related Investment;
- SAPARD (the Special Accession Programme for Agriculture and Rural Development) is a Community support for pre-accession measures for agriculture and rural development in the CEE applicant countries in the pre-accession period;
- ISPA (Instrument for Structural Policies for Pre-Accession) aid is directed mainly towards aligning the applicant countries on Community infrastructure standards, particularly in the transport and environmental spheres.\(^4\)

\(^2\) the so-called Delors packet
\(^3\) The other 3 candidates, Cyprus, Malta and Turkey benefit from separate pre-accession funding.
\(^4\) As such ISPA can be seen as a pre-accession analogue to the Cohesion Fund.
The Phare programme was created in 1989 in order to assist the CEECs in reforming and democratization of their post-communist societies. As response to the Luxembourg European Council’s launching of the enlargement process in 1997, was Phare in 1998 refocused entirely on pre-accession priorities highlighted in each country’s Accession Partnership. In this sense the Phare Programme is broadly focused on two main priorities: Institution Building\textsuperscript{6} and \textit{acquis}-related investment.

These basic orientations were adjusted in 1999 to reflect the initiation of SAPARD in agriculture and rural development and of ISPA in transport and environment infrastructure. Phare’s freed funds were redirected towards tackling the issue of economic and social cohesion.

The development disparities between the candidate countries and the existing member states are substantial. CEECs per capita GDP range from one quarter to three quarters of the EU average. This makes the issue of economic and social cohesion one of the most critical issues in the EU’s pre-accession relations with the applicant countries. Phare’s objectives for economic and social cohesion are:

- Strengthening of the candidate countries programming and administrative capacities through institution building support across their entire national territories so that they are capable to absorb the Structural Funds upon accession.
- Using of investment in support of institution building, and closely coordinated with it, to begin to make an impact on development disparities and to allow pilot testing of integrated development programmes similar to Objective 1 and Community Initiatives at national and/or regional level. (Commision 2004b)

SAPARD and ISPA are new Community programmes for the applicant countries in CEE. Both programmes are implemented since 1\textsuperscript{st} of January 2000.

SAPARD provides Community support for agriculture and rural development during the pre-accession period in the applicant countries of Central and Eastern Europe, in order to contribute to the implementation of the \textit{acquis communautaire} concerning the common agricultural policy and related policies and to resolve priority and specific problems for the sustainable adaptation of the agricultural sector and rural areas in the applicant countries. Both, public or private sector organizations or firms promoting eligible projects can apply for co-financing in the form of grants. Implementation of the SAPARD programme is the responsibility of the competent authorities and entities responsible for implementation in the applicant countries.

ISPA co-finances investment projects in the transport and environment sectors in the CEE applicant countries in form of grants (subsidies). Beneficiaries can be only public organizations / public undertakings.

2.3. \textit{Main Principles of the EU-s Regional Assistance}

Another change made in 1999 by Berlin European Council was the strengthening of the operation principles of the Funds (Commission 2004a; EC NO 1260/1999):

- \textit{Programming} is the preparation of multi-annual development plans and has to be undertaken through a partnership-based decision-making process until the measures are taken over by the public or private bodies entrusted with carrying them out. Programming involves (a) a precise description of the current situation in the region, (b) a description of the most appropriate strategy for achieving the stated objectives and (c) indications as to use and form of the contribution from the Funds;
- \textit{Concentration} is the principle of concentrating of the Funds on priority objectives, especially for promotion of regions whose development is lagging behind. 69.7\% of the total funding for the Funds is allocated for the Objective 1;

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\textsuperscript{5} Originally Phare involved only Poland and Hungary, later the programme was expanded also to other CEECs currently benefiting from the Phare programme. Until 2000 the countries of the Western Balkans (Albania, Bosnia & Herzegovina and The Former Yugoslav Republic of Macedonia) were also beneficiaries of Phare. However, as of 2001 the CARDS programme (Community Assistance to Reconstruction, Development and Stability in the Balkans) has provided financial assistance to the Western Balkans.

\textsuperscript{6} Institution building includes support for adapting and strengthening democratic institutions, public administration and organizations that have a responsibility in implementing and enforcing Community legislation. Development of relevant structures, human resources and management skills were targeted. Around 30 \% of Phare funds were used to meet Institution building needs.
• **Partnership** is the approach to include the regional and local authorities, the economic and social partners and other competent bodies throughout all stages, starting with approval of the development plan;

• **Additionality** is the requirement of additional national funding next to the Community assistance;

• **Management, monitoring and evaluation** is the requirement to the Member States to set up a managing authority and Monitoring Committee for each programme;

• **Payments and financial controls.** The Member States have to appoint a payment authority for each of the programmes, which acts as intermediary between the financial beneficiaries and the Commission. The Member states also have to improve checking arrangements: on-the-spot checks and financial audits.

3. **Local Governments in Estonia**

Local self-government denotes the right and the ability of local authorities, within the limits of the law, to regulate and manage a substantial share of public affairs under their own responsibility and in the interests of the local population (Council of Europe). Local government as such is the government of the community: it is the social, economic, and political ordering of people’s activities where they live and work (Banovetz 1998). Local government is the closest administrative level to citizens providing the very basic services to the community. In the modern and democratic state local government is the instrument of democracy not a mere agent of the central government (Redcliffe-Maud and Wood in Kungla 1999).

3.1. **Local governments in the Administrative System of Estonia**

These basic concepts about local self-governance are also reflected in the role of the local governments in the Estonian administrative system. In accordance with the general principles of local government laid down in the Constitution of the Republic of Estonia Art. 154 section 1 “All local issues shall be resolved and managed by local governments, which shall operate independently pursuant to law.” and Art. 155 section 1 “Local governments are rural municipalities and cities.” there are 39 cities and 202 rural municipalities in the local government system of Estonia (Ministry of the Interior).

The cities and rural municipalities are community based administrative units, which form the first layer of the administrative system in Estonia. The second layer is the central government, the state. Besides the 241 local governments in Estonia also divided into 15 counties, governed by county governors. Although 15 counties can be seen as regional governance units, they cannot be seen as administrative levels: as by law they are parts of central government which are financed directly from the state budget and are subordinated to the central government. They are not autonomous administrative units but extensions of the central government at regional level. Therefore Estonia has a two level administrative system with one central government and 241 local governments.

The task of local governments, provided by Local Government Organization Act, is to organize the following: social welfare and related services, care for the elderly, youth work, housing and public utilities, water supply and sewage, property maintenance, territorial planning, public transport within a municipality or town, garbage collection and street cleaning in municipalities or towns. The function of a local government is also to organize the maintenance of pre-school child care institutions, basic schools, secondary schools, hobby schools, libraries, community centres, museums, sports facilities, shelters, care homes, health care institutions and other local agencies if such agencies are in the ownership of the local government.

Local governments compose their budget independently. The council of the local government confirms the budget, the central government has not right to intervene into the process of composing or accepting local budgets. The main income sources of local governments are the personal income tax (35% of total revenues), support provided by the central government (25%) and own incomes (18%) and the main expenditures are education (35%), investments (20%), economy (14%) and general governance expenditures (10%) (Liivik and Jõgi 2003). In 2002 the expenditures made by the local governments constituted to the GDP 10.6% and the revenues of local governments amounted up to 9.9% of the GDP (Ministry of Finance).

Although the overall economical indicators of revenues and expenditures indicate healthy financial situation of local governments, the actual situation varies a lot. The 241 local governments in Estonia vary to great extent in their size, economical indicators and ability to fulfil their functions.
The 39 cities have a total population of 914,663 (67.5%) inhabitants (of which the population of Tallinn, the capital of Estonia, is 397,150 inhabitants) and in rural municipalities have a total population of 441,382 (32.5%) inhabitants (Statistical Office of Estonia). The population 197 local governments out of 241 is less than 5000 inhabitants and in 125 local governments its even less than 2000 inhabitants. Most of the very small local governments (less than 2000 inhabitants) are rural municipalities (119) and the in category of local governments with population less than 5000 inhabitants 183 out of 197 are rural municipalities (Ministry of the Interior).

In principle most of the revenues of a local government should come from the personal income tax paid by the inhabitants of the local government. At the same time most of the local governments are small or even very small. But they all have to carry out the same tasks as provided by the law. It can be assumed that the actual ability of local governments to fulfil their tasks and to contribute the local development varies to a great extent.

3.2. The Socio-economic Division of Local Governments

As it has been stated above, Estonian local governments are fragmented and at different developmental level. To say something about distribution of European funds among different municipalities, we have to specify and measure the position of every municipality.

In order to estimate the level of development, socio-economic potential and sustainability of every given municipality, one would need integrated criteria and measurable indicators. It has always been an arguable issue, how to assess the level of development of different administrative units objectively. Mostly, the methods and indicators that are used in evaluation processes reflect the interests and needs of the evaluator. There is no internationally accepted way to measure socio-economic potential or ability to manage the local life.

Therefore, in this article, we shall compare different local governments with each other. First of all, several indicators will be chosen that should demonstrate different aspects of regional development. The choice of indicators depends on the availability and comparability of data. Until now, there exists no national-level common elaborated system for evaluating the situation and development of local governments. Different authorities use different indicators (Hirmo 2003).

The framework for assessing Estonian local governments will be in line with the research by Ministry of internal Affairs (Suvi 2001). This report is the most condensed synthesis of different aspects of local governments. The managing capacity of all Estonian local units is measured by an Index of Local Management Capacity. This index integrates 4 different aspects of different local governments:

- **demographic potential of the population of the given municipality.** It is operationalised through the ratio of children to elderly persons (number of persons aged 0-15/number of retired persons) and the Labour Pressure Index (calculated as follows: number of people aged 5-14/number of people aged 55-64). The mean of these two indexes shows the demographic potential of the municipality. If this integrated index had value over 1,4, the demographic potential of the municipality was rated good (3 points). If it was less than 1,1, it was rated poor (1 point). 1,1-1,4 was average (2 points). For every following index the points are attributed in a similar way – 3 means “good”, 2 “average, 1 “poor”;
- **economic activity of the population of the given municipality.** It is operationalised as an amount of personal income tax per capita, collected in the territory of the municipality. In Suvi (Suvi 2001) they were divided into 3 equal groups according to the value of collected income tax per capita. The same is done in this study, only the ranges are different. If per capita income tax for given municipality is above 2800 EEK, it is rated good (3), if 2000-2800 EEK average, and if it is below 2000 EEK, the municipality’s economic activity is rated poor (1). This indicator is important, since the income tax per capita reflects most adequately the living standard and general development of municipality (Hirmo 2003);
- **relative economic independence of the municipality.** This is measured as a ratio of municipality’s own revenues to the administrative and social security expenditures. If it is more than 1, it means that municipality has potential to invest without external assistance. If this ratio has a value above 2,5, it is rated good; if it is 15-2,5, it is rated average, and ratio below 1,5 means that the relative economic independence of the municipality is rated poor;
- **location index.** It is calculated by Estonian Land Board and describes the value of the location. It is complex index to assess the value of the location of every municipality (full data in Suvi 2001). The rating system is similar to that described in case of previous indexes. The importance of location must be especially stressed – the distance from capital Tallinn correlates clearly with most of the social, economic, and demographic indexes (Hirmo 2003).
The average of these 4 indexes creates an index that demonstrates the relative management capacity of different local governments. In the following analysis the same measures are used. Where necessary, the data is updated. For example, the income tax per capita is updated according to the information about year 2003 provided by Estonian Tax Board (Estonian Tax Board). Also, several mergers of different municipalities have taken place since 2001. These are also taken into account and adjusted.

Following graph describes the distribution of local governments according to the Index of Local Management Capacity.

**Figure 1: The Distribution of Estonian Municipalities According to Index of Local Management Capacity**

According to the Index of local management capacity, all Estonian municipalities are divided into 4 groups with different levels of socio-economic potential. Following table presents the division of local governments into 4 groups according to their socio-economic potential.

**Table 1. Socio-economic capacity of Estonian municipalities**

<table>
<thead>
<tr>
<th>Group</th>
<th>Index of Local Management Capacity (max 3)</th>
<th>Number of municipalities in group</th>
</tr>
</thead>
<tbody>
<tr>
<td>Group 4 (Highest potential)</td>
<td>2,75-3</td>
<td>35</td>
</tr>
<tr>
<td>Group 3 (High potential)</td>
<td>2,25-2,75</td>
<td>63</td>
</tr>
<tr>
<td>Group 2 (Low potential)</td>
<td>1,75-2,25</td>
<td>74</td>
</tr>
<tr>
<td>Group 1 (Lowest potential)</td>
<td>1-1,75</td>
<td>69</td>
</tr>
</tbody>
</table>

Having divided local governments into 4 different groups according to their socio-economic capability, further analysis becomes possible. First of all, by evaluating different groups and local governments these groups are composed of, the relevance of the population size of the local government becomes clear. The Socio-economic capacity of bigger municipalities is quite clear. For example, 20 of the biggest local governments of Estonia belong to group 3,35 on average. 20 of the smallest (in terms of population) belong to group 1,51 on average.

The significance of the size becomes even clearer if one looks at the average number of people in the municipalities of different groups. The results are presented in Table 2. It demonstrates that local governments with higher socio-economic capacity to manage their problems are bigger than those with lower living standard and lower ability to deal with their problems. Note that capital Tallinn (by far the biggest local government unit with 378 000 inhabitants) is excluded from the calculation in Table 2. The analysis suggests that regional policy programmes should focus mainly on smaller municipalities, if they served the purpose of balancing intra-state disparities.

**Table 2. Socio-economic capacity groups and average sizes of municipalities**

<table>
<thead>
<tr>
<th>Group</th>
<th>Group 1 (Lowest)</th>
<th>Group 2 (Low potential)</th>
<th>Group 3 (High potential)</th>
<th>Group 4 (Highest)</th>
</tr>
</thead>
</table>

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The second important factor is the difference between towns and rural municipalities. The socio-economic potential of the urban local governments is higher than of the rural ones. The average value of the Index of local management capacity in towns was 2.33 and in rural municipalities it was 1.9 respectively. The average group of socio-economic potential of towns was 2.9 and average rural municipality belonged to group 2.1. This is considerable difference.

Table 3 presents the belonging of towns and rural municipalities into different groups. As it shows, nearly 77 percent of towns have high or the highest socio-economic management potential (in other words, they belong to groups 3 or 4). The respective number for rural municipalities is less than 34 percent. It shows that the need for regional assistance is more severe in rural municipalities; their ability to cope with socio-economic pressures and challenges is lower. This should direct the European assistance also mostly to rural areas.

Table 3. Socio-economic capacity groups and type of local government

<table>
<thead>
<tr>
<th></th>
<th>Towns</th>
<th>Rural municipalities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of towns</td>
<td>% of all towns</td>
<td>Number of rural municipalities</td>
</tr>
<tr>
<td>Group 4 (Highest potential)</td>
<td>11</td>
<td>28,2</td>
</tr>
<tr>
<td>Group 3 (High potential)</td>
<td>19</td>
<td>48,7</td>
</tr>
<tr>
<td>Group 2 (Low potential)</td>
<td>3</td>
<td>7,7</td>
</tr>
<tr>
<td>Group 1 (Lowest potential)</td>
<td>6</td>
<td>15,4</td>
</tr>
<tr>
<td>Total</td>
<td>39</td>
<td>100</td>
</tr>
</tbody>
</table>

4. The EU Regional Policies in Estonia

4.1. Pre-Accession Programmes and Estonia

As Estonia is one of the CEECs accessing the EU on the 1st of May, Estonia has participated in all the pre-accession programmes of the EU for the CEECs – Phare, SAPARD and ISPA.

Phare programme has been opened for Estonia since 1991: in the beginning for re-orientation on functioning market-economy; later, as an applicant country and after re-orientation of Phare’s focus on preparations for CEECs joining the EU, aid was targeted on institution building and investments. Through the years 1991 to 1999 the EU has supported through Phare’s several sub-programmes with €198.27 mil. Phare’s focus for the programming period 2000-2006 is in Estonia on economic and social cohesion. The re-orientation on economic and social cohesion was reflected also in allocated support: Phare’s aid in 2000-2001 for Estonia was €62.83 mil.

ISPA and SAPARD were introduced as new pre-accession programmes in 2000. ISPA focus is on assistance to environmental and transport sector. Already in 2000, the first year implemented, ISPA support amounted to €24.62 mil. Following the support of €40.46 mil in 2001, the ISPA support to Estonia in 2000-2001 amounts up to €65.1 mil.

Also SAPARD opened on the year 2000 for Estonia. Because of administrative reasons first payments were made in 2001 and they amounted up to €12.35 mil.

The total Phare assistance to Estonia in 1991-2001 has been €338.53 mil. (Ministry of Finance)

4.2. The Pre-accession Programmes and Local Governments

The implementation of the EU’s pre-accession programmes is in Estonia regulated by the regulation of Estonian Government on applying and using, monitoring and evaluation of foreign aid. As laid down in the regulation the applicant for Phare assistance in Estonia is centrally the Ministry of Finance, which coordinates the programmes with other ministries. The same applies for ISPA and SAPARD. Therefore the local governments cannot apply for Phare, ISPA or SAPARD directly – they can only co-apply with one of the Estonian ministries or the can be the beneficiaries.

The local governments can in principle participate in the ISPA programme by applying through the Ministry of Economic Affairs and Communications. As the minimum size of the project assistance is applied for is at least €5 mil. In 2000-2002 several environmental projects where local governments are beneficiaries have been
finance. However, in most of the cases local governments have not been directly the co-financing part in the projects. Mainly the co-financing side has been a local firm where local governments are one of the shareholders.

SAPARD programme is mainly targeted for the private and non-profit sector. Local governments can apply for funding only under one of currently five opened measures. The sixth measure of SAPARD is opened (also for local governments) for the first time and the deadline for funding applications is in September 2004.

Although the Phare programme in general has been targeted on institution building and investment at national level in order to prepare Estonia like other applicant countries for the EU membership, has Phare been the main possible funding source from the pre-accession programmes for the local governments.

4.3. Programmes for Local Governments

The analysis of the participation of Estonian local governments in European pre-accession regional programmes will focus on a very limited number of sub-programmes. The reasons for such a narrow perspective is presented in this section. The authors of current research set up a list of criteria that the programmes should meet.

First, which is most important, these programmes have to be open for local governments as applicants. Second, the programmes suitable to the research would have economic and social cohesion and regional development as their main objectives. There exist (within Phare, for example) several sub-programmes that are oriented to advance certain policy area. For example, the funds oriented for dealing with specific environmental or education problems. Third important criterion is the availability of information, preferably for longer period. Only then, meaningful conclusions about the policy as a whole can be drawn. Fourth, these programmes should not be with very narrow scope – aimed at specific problems or policy areas. If that was true, it would distort the results – different local governments could not participate on equal basis.

CBC, Cross-Border Co-operation programme, is one of the few Phare financial instruments especially targeted on regional development and local governments (however, local governments are only one of the possible beneficiaries, also other bodies like county governments can apply for funding). It has been the programme that is best suited for this research. The aim of the CBC is to promote co-operation in the Baltic Sea region. Assistance is provided for projects which involve institutions of more than one country in the region and which should possibly lead to wider co-operation in Baltic Sea region. In Estonia CBC is opened since 1994 and since 1997 CBC cover the whole territory of Estonia. CBC’s small project fund and medium-sized project fund, as flexible and focused on regional/local level, are especially suitable for local governments.

PPF, project preparation facility, a Phare financial instrument that is focused on preparation of the countries joining the EU for absorbing of Structural Funds. PPF provides financial assistance to projects in order to ensure a sufficient number of eligible projects for applying assistance from the Funds. Focus is on several kinds of preparatory surveys, training etc. All possible applicants eligible to apply for funding from the Funds can apply for assistance from the PPF. In Estonia special attention is paid on local governments in the framework of PPF. To keep our analysis more informative and reflective, PPF (2001) was also included to analysis. The round of application has been held only once until now, but local government participated rather actively and it is illuminative of the developments in The EU regional assistance policies.

Phare ESC 2001: Tourism Infrastructure Grant Scheme, which has also been open for local governments, might also be include into analysis but too few projects have been put into practice. Therefore, one cannot evaluate their regional political dimension. There has been only one application round that has been open to local governments. Only seven cases of local governments’ successful application for the funds of the ESC 2001 Tourism Infrastructure Grant Scheme are available. These have also been distributed mainly to the municipalities with highest level of development and competitiveness (4 of them belong to Group 4 municipalities).

INTERREG III B and INTERREG III C have also been open for Estonian local authorities and there have been 18 occasions of participation by Estonian local governments in different projects run under these programmes. But mostly these are projects run by some national or regional agency from other European countries, Estonian local governments have only participated in these projects. As a matter of fact, merely 2 local government units (capital Tallinn (Group 4) and town of Narva (Group 3)) have successfully applied for European funds under INTERREG programme. It is surely not enough to involve them into the analysis.
The focus on the capacity of local governments to apply for the Union funds and manage regional or local projects on their own excludes two main pre-accession instruments from our attention. Both ISPA and SAPARD have not included measures or financing schemes that are directly open to local governments. The funds allocated through ISPA programme are allocated through national institutions. To be more precise, initiative may originate from the local unit but respective ministries compile the applications and the projects shall be presented to the European Commission by central coordinating unit (CFCU- Central Financing and Coordinating Unit, a separate department of the Ministry of finance). Of course, local governments have benefited considerably from ISPA programmes. But their role in ISPA financing mechanisms is passive.

SAPARD has been overwhelmingly oriented towards rural entrepreneurs; only in 2004 one of the measures (Measure 6 - investment support for regeneration and development of villages) open to local governments as direct applicants has been initialised. Until now, no decisions of allocation have been made. Therefore, ISPA and SAPARD programmes have had significant and positive outcomes for different regions within Estonia but the effect on the independence and strength of local governments has not been so significant.

Therefore – the major units of analysis will be Phare CBC (data available for period of 1994-2001, CBC 2002 is currently announced and open for application) and PPF (data available for only one year – PPF 2001).

5. Estonian Local Governments and EU-s Regional Aid. Analysis

During the period of 1994-2001, CBC funded total of 88 projects. The amount of financial aid attributed to different Estonian applicants was in total. Out of these 88 projects, local governments were main applicants in case of 27 (31 % of total).

In terms of the money distributed, local governments were more successful –out of the total 20 691 195 € local governments have used 9 053 728 € (44 %). This number shows that, in general, local governments have been rather successful applicants in CBC programme, if compared to other types of applicants.

The development of the local governments’ preparedness in time cannot be drawn out, because of too little number of projects in different periods. During the period 1994 – 1998, the overall number of CBC projects in Estonia was 24 (less than 5 projects per year) but in 2001 it was 40 (but in 2000 only one project was funded). Therefore, the shifts in the participation level of different types of local governments might not be representative.

PPF 2001 is a recent project (the second round PPF 2002 has just been announced) and several of the projects are still ongoing. Therefore, no statistics about the size of assistance is publicly available (the evaluation report of PPF 2001 has been declared confidential). But the programme gives another kind of useful information – the percentage of the applications that have found endorsement. In PPF 2001, total of 209 applications were submitted and 32 % of them by local governments (68). The total amount of contracts made to this day is 28 (and even 19 of them with local governments). It shows, once again, that local governments are rather successful applicants.

5.1. Socio-economic Status of Local Governments and European Regional Aid

The main question for this paper is how these funds are distributed in terms of socio-economic capacity of different successful applicants. The results that can be drawn out seem to affirm the preliminary hypothesis that regional assistance meant to deal with regional differences works rather in the opposite direction. If we investigate the distribution of the European assistance funds among the 4 groups of socio-economic capacity, it can be assured that richer and more successful local governments have “collected” most of the benefits of European assistance.

In CBC programme, 29 projects with local governments as contract partners have been distributed along the lines of socio-economic capacity groups as presented in Table 4. The number of projects is clearly biased towards more well off local governments. Therefore, on a large scale, these projects have supported those with best capacity to manage their social life on their own. Only 2 successful applications by group 1 (lowest potential) municipalities demonstrate the low impact of CBC funds in alleviating regional inequalities. If the amount of funds is taken under consideration, the results are even more in favour of the municipalities of groups with higher socio-economic potential.

Table 4. The distribution of CBC assistance and socio-economic capacity groups
In PPF, the distribution has been more indifferent to the groups. Several reasons for that could be drawn out but the most important of these were pointed out by Head of the CFCU Klas Klaas in interview (Klaas 2004). First and foremost, the independent consultants, helping local governments to write better applications, have appeared. In most cases, these are private companies that offer the service of writing well-reasoned applications and, in some cases, also managing the projects themselves. This has helped local governments with lower administrative capacities to benefit from the EU assistance. Following Table 5 describes the distribution of PPF funds among local governments.

<table>
<thead>
<tr>
<th>Group 4 (Highest potential)</th>
<th>Number of projects</th>
<th>% of municipalities’ projects</th>
<th>Funds for the group (€)</th>
<th>% of municipalities’ funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Group 3 (High potential)</td>
<td>6</td>
<td>20,7</td>
<td>2 524 767</td>
<td>27,9</td>
</tr>
<tr>
<td>Group 2 (Low potential)</td>
<td>6</td>
<td>20,7</td>
<td>725 420</td>
<td>8,0</td>
</tr>
<tr>
<td>Group 1 (Lowest potential)</td>
<td>2</td>
<td>6,9</td>
<td>140 204</td>
<td>1,5</td>
</tr>
<tr>
<td>Total</td>
<td>29</td>
<td>100</td>
<td>9 053 728</td>
<td>100</td>
</tr>
</tbody>
</table>

Table 5 The distribution of PPF assistance and socio-economic capacity groups

<table>
<thead>
<tr>
<th>Projects</th>
<th>Number of projects</th>
<th>% of municipalities’ projects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Group 4</td>
<td>5</td>
<td>27,8%</td>
</tr>
<tr>
<td>Group 3</td>
<td>6</td>
<td>33,3</td>
</tr>
<tr>
<td>Group 2</td>
<td>6</td>
<td>33,3</td>
</tr>
<tr>
<td>Group 1</td>
<td>1</td>
<td>5,6</td>
</tr>
<tr>
<td>Total</td>
<td>18</td>
<td>100</td>
</tr>
</tbody>
</table>

5.2. The Type and Size of Local Governments and European Regional Aid

The analysis of socio-economic capacity of different local authorities demonstrated the sharp difference between urban and rural municipalities. The logic of regional policy would suggest that most of the assistance is directed towards rural municipalities but the analysis of the results proves, once again, the opposite. In case of CBC, 29 successful projects are distributed as follows: 22 of them were conducted by towns and 7 by different rural municipalities. It means that rural municipalities have managed to obtain CBC aid less than once a year (duration of CBC has been 9 years).

If the amount of aid is considered, the results are even more in favour of the towns. As much as 92 % of the total assistance was received by towns and only 8 % was left over for rural municipalities.

In case of PPF, the results are, once again, more balanced. 13 of the total 18 projects were submitted and carried out by rural municipalities and 5 by towns. If the percentage of the success of applications was taken into account, the rural municipalities would prove to be even more successful than towns – 30 % of their applications were selected (13 out of 43). In case of towns the percentage was 20 (5 out of 25). Once again, the role of independent consultants should be emphasised, the decision-making procedure focuses mainly on the writing quality of the application (Klaas 2004). Hence, the possibility of poorer local governments to compete for the regional assistance seems to be improved but it is too early to ascertain it with considerable credibility.

5.3. The Obstacles of Local Government Participation

So far, we have demonstrated that regional aid of EU has been distributed mostly to the municipalities that already have higher administrative capacity and more resources. The analysis of fundamental reasons for that would require different research and more space. But considering the socio-economic aspects of local governments, the type and character of pre-accession aid programmes, following three general problems impeding the local governments of participating in the programmes can be pointed out:

One of the main problems for most of the local governments is the additionality principle of the EU financial aid programmes. As pointed out earlier most of the revenues of the local governments forms the part of personal income tax assigned for the local governments (56% of the persona income tax). Considering the fact local governments are mostly small rural municipalities suffering also under the problem of unemployment, it is clear that they cannot be well off regarding their financial situation. This is reflected also by the fact that the second
biggest income source for local governments is financial aid provided by the central government. Also the socio-economic analysis of local governments confirms that.\(^7\)

The second biggest problem hindering the participation of local governments in the financial aid programmes is their administrative capacity to compose eligible projects. The requirements concerning applying for different EU programmes for financial aid are the strict: projects have to meet clearly the expressed purpose of the programme, precise description of activities and budget have to be provided etc. Certainly already writing of a successful project requires special knowledge of the EU programmes, further also good project management skills are of use. The smaller local governments have problems with that, and there are also problems with basic English skills. The decision-making procedure focuses mainly on the writing quality of the applications and decision-makers clearly lack the administrative capacity to evaluate the real need for assistance. The formal congruity is over-valued and the real situation in applicant local government is under-valued. County level advisory board that estimates the necessity of each project could help to overcome this obstacle.

Another problem regards to the aid programmes themselves. The analysed pre-accession programmes were mainly targeted to the national level, not for the regional development. Even if the programmes were opened to the local governments, they had to compete with NGOs and other regional institutions. It has caused the situation, when most of the municipalities have no experience and skills to apply for European assistance.

6. Conclusion

Since the Treaty of Maastricht economic and social cohesion of regions Europe has been one of the justifications of the EU. Considering the fact that one third of the Community’s budget is allocated for the purpose of elimination of disparities between regions within the EU and also within the Member States, economic and social cohesion can be regarded as one of the main goals of the EU as a whole. If one looks at the experience the EU has had in the field of economic and social cohesion with Ireland, Spain, Portugal and Greece it is obvious that strategy chosen has been successful – although there are still remarkable differences between the regions in Europe, it is clear that without the regional policy of the EU the disparities would be even deeper.

With the 1st of May 2004 the EU is looking at another challenge in the field of regional policy – the accession of 10 new member states. The challenge is even bigger than the previous challenge with Ireland, Spain, Portugal and Greece. The disparities between “old” and “new” member states are huge, even within the new member states the differences are remarkable. In overcoming these problems the Funds and Cohesion Fund play a central role. Having in mind the success of the Funds and the Cohesion policy so far, it is clear that the main question is whether NMS are capable to absorb the potential finances provided via different financial instruments.

In the case of Estonia the focus of our paper has been on local governments and their ability to apply for finances from the different financial instruments now opening also for them. We have asked the question, whether European regional assistance has helped to eliminate regional disparities within the country. Our focus has been on local governments, since they, taking into account the principles of subsidiarity and democracy and considering their role in Estonian administrative system, are one of the main triggers of regional development within Estonia.

We evaluated the success of local governments in pre-accession programs in order to estimate the probable success or failure of regional policy of the EU with regard to the regional development within Estonia. Because Phare, ISPA and SAPARD have been targeted mainly to national level and are still “new”, we narrowed the focus of our research down to cross border co-operation (CBC) Phare sub-programme (and in addition the recent PPF (Project Preparation Facility)), which is one of the few Phare programmes where local governments have been one of the main target groups.

As our analysis shows, the socio-economic status of a local government can be considered to be one of the central factors in its participation in the regional aid programmes. Although the logic of regional policy would suggest allocating funds to regions or local governments that are more lagged behind, the experience of the selected cases (programmes) shows the opposite. European funds, to this day, have been distributed mainly to those local governments that have higher socio-economic potential and that belong to the more developed part of Estonia.

\(^7\) Also the NDP of Estonia expresses the concern regarding the ability of local governments to bring up needed investments
The research has demonstrated convincingly that mainly towns (instead of poorer rural municipalities), larger local government units (instead of more lagged-behind smaller ones), and those municipalities with higher level of socio-economic potential (instead of the more stagnant and vulnerable ones) have managed to obtain most of the resources available. It is serious threat for the post-accession structural policies, as well. Pointing our finger to that threat was one of the main objectives of this paper. This paper is part of an ongoing study that investigates not only the objective data about participation of local governments in European assistance programmes, but also the opinions of local governments about the availability of European regional assistance.

The threat of deepening of regional intra-state differences requires attention of the policy makers. The paper did not aim at saying that EU policies in NMS-s have failed – most of the assistance has been directed straight to the severest regional problems but the funding of projects submitted by local governments deserves to be revised.
References