

Beyond Perception: Has Romania's Governance Improved Since 2004?

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Romania and Bulgaria encounter today problems in joining the visa-free Schengen area. The main one in the public eye is corruption. Both countries pledged to improve their rule of law when signing their accession treaties in 2005, yet little progress is perceived by observers or captured with governance measurements relying on perception, such as CPI and World Bank Governance indicators. This paper explores real policy, with fact-based indicators, to trace progress in the area – or lack of it – since 2004 to the present.

Post-communist countries embarked on their EU accession path with Transparency International scores below the lowest level in Western Europe and their culture was frequently described as entirely corrupt¹. Surveys on bribing cannot fully capture the systemic nature of East European corruption, which can be defined best as governance by particularism², the systematic discretionary use of authority to the benefit of particular groups or individuals. A good proxy can be found in the ‘government favoritism’ indicator from the survey of governance by World Economic Forum. The 2009 edition did not find great differences across the post-communist region, suggesting that they may be in size rather than in kind. Czech Republic is 110 in the top of government favoritism, Hungary 112, and Romania 113, worse than Kyrgyz Republic or Kazakhstan. In other words, neither the transition, nor the EU accession has managed to restrain the capacity of *the government to distribute benefits in a particularistic manner*. Political parties, even in the most advanced countries in the region, seem to develop capacity and mobilization primarily through clientelism and state exploitation³. Spoils include four basic categories:

- a. public jobs, as the public sector is extremely politicized and each winning party fills with his own people not only the political jobs but many civil servant offices as well;
- b. public spending, for instance procurement, but also preferential bailouts, subsidies, government transfers to regional and local branches, loans from state banks;
- c. preferential concessions and privatizations from former state property; and
- d. market advantages in the form of preferential regulation.

Unfortunately we have very little systematic data collection on any of these areas, except for press reports and some occasional and sector and time limited studies by think-tanks. The only indicator allowing a comparison of 2004 with 2010 is the Control of Corruption (CC) from the World Bank, which aggregates perception scores from different expert sources (subjective sources), so a score

¹ William I. Miller, Ase b. Grødeland and Tatyana y. Koshechkina, *A Culture of Corruption? Coping with Government in Postcommunist Europe* (Central European University Press 2001).

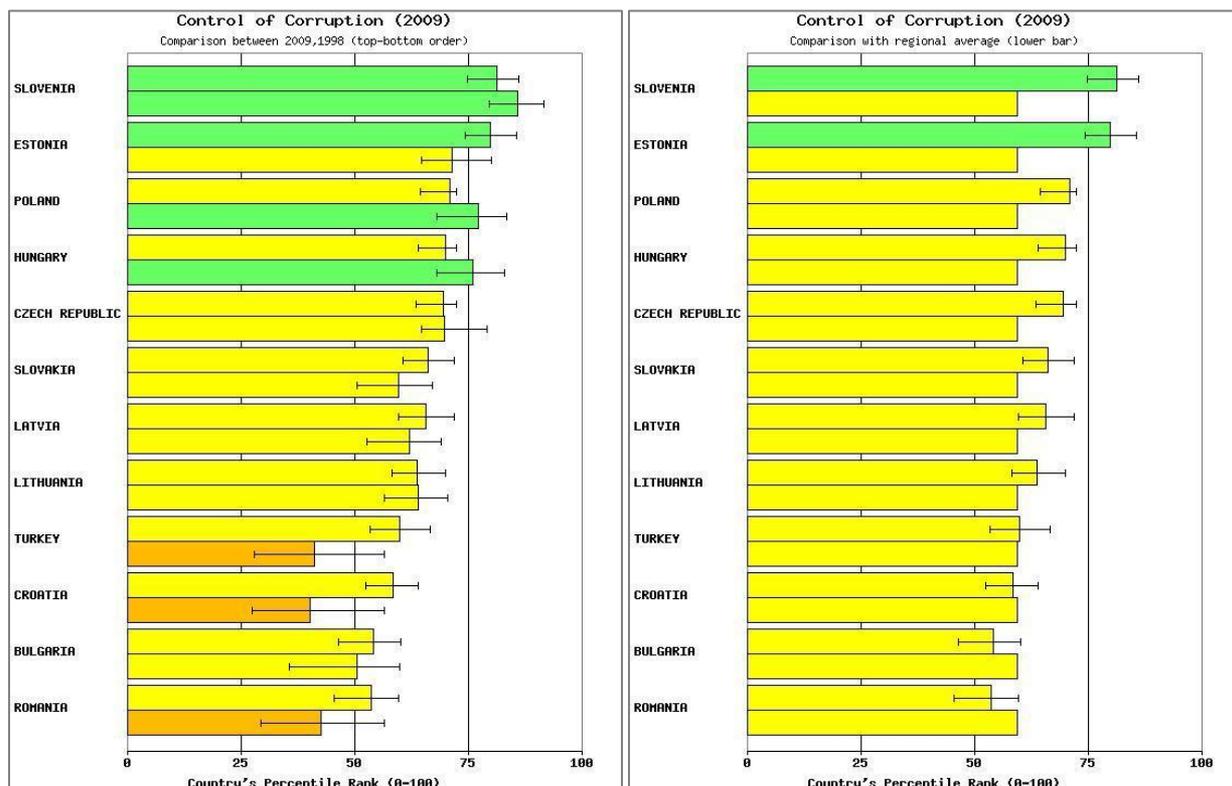
² See for a full description of particularism Guillermo O'Donnell (1996), ‘Illusions about Consolidation’, In *Journal of Democracy*, vol. 7, no.2, pp. 34-51.

³ Connor O'Dwyer (2006) *Runaway State-Building: Patronage Politics and Democratic Development*, Baltimore, Johns Hopkins University Press; Anna Grzymała-Busse (2007) *Rebuilding Leviathan : party competition and state exploitation in post-communist Europe*, Cambridge, New York, Cambridge University Press.

comparable with Transparency International's Corruption Perception Index. Which does the same. Unlike CPI, however, CC is based on a methodology which has two advantages. It allows comparison from one year to another (which cannot be done with CPI) and it allows calculating a standard error, which is actually a measurement of the distance between different aggregated sources on a country (which might disagree on progress from one year to another).

According to this indicator (Fig. 1), Romania has progressed from below 50% to above this value (orange to yellow) but the change falls within the confidence interval (at 10%), in other words this is not significant progress unless we increase the confidence interval and we accept greater disagreement among sources (Georgia is the only country to in the region to have evolved significantly in the 1998-2009 interval). Bulgaria progressed even less, but it started from a better position. The two countries are now aligned on the bottom of new EU entrants, their score in absolute figures being slightly below Turkey and Croatia, two candidate countries, (Fig. 2). The differences, however, are small across new member countries on this indicator, with the notable exception of Estonia and Slovenia, which are doing significantly better than the rest.

Fig 1-2. Comparison of each SEE country with the regional average on World Bank aggregate indicator Control of Corruption



These results are inconclusive, showing that experts cannot agree on Romania's progress. Disintegrated scores, for instance Freedom House *Nations in Transit*, show progress in 2005 and 2006, then regress and stagnation. Finding objective indicators is difficult not only due to the elusive and discreet nature of the phenomenon. On top of these, the social, economic and institutional environment has changed importantly in the process of EU accession. The nature and channels of the illicit trade of favors have changed too, which makes it difficult to compare the level of corruption at different moments of time.

To match this challenge, we need to understand that corruption is an equilibrium between resources and constraints. A lot of investment was made in raising legal constraints, but those only provide a part of the picture. A balanced anticorruption formula needs to address both resources and costs of corruption.

Corruption = Resources (Power discretion + Material Resources – Constraints (Legal + Normative)

In the formula above under resources we consider power discretion (due not only to monopoly of power, but also privileged access to influence and decision under different arrangements than monopoly, for instance cartels of parties) and material resources (public budget, foreign aid / EU funds, natural resources, state assets, public jobs). The constraints are legal (an autonomous and effective judiciary able to enforce legislation), but also normative (existing societal norms that endorse ethical universalism and sanction effectively the deviance from this norm through public opinion, media, civil society, voters). We will discuss systematically the difference between 2004 and 2009 selecting an indicator illustrative for each category.

1 Resources for corruption

The first category, **power discretion**, does not present much change. In 2004, Romania was ruled by Social Democrats who had doubled their number of mayors by recruiting opposition ones through local transfers manipulation. In 2009, the government party managed to form a majority by convincing a significant number of MPs elected on the opposition ticket to transfer their loyalties to the government. The same limited number of parties (3) dominate the political scene, with the same smaller radicals (1), minorities (1) and free rider parties (the Conservatives, who always enter Parliament running on the ticket of either left or right, as it could not pass the threshold by themselves).

An electoral reform in 2008 has not changed anything of significance at the national level: rather, due to passage from closed lists to single unit constituencies the practice to offer pork instead of parliamentary support increased importantly with public bargains going on even in toughest

austerity times. While the system is competitive, competition is nevertheless severely limited by a very high entrance threshold for new parties Romania has the highest obstacles for the entrance of new political parties (the highest in Europe): 200 000 signatures are needed to register a new party and 100 000 an independent candidate, so despite public exasperation with such behavior the current parties had managed a quite successful cartel.

The direct election of the County Council Presidents starting with 2008 visibly strengthened their role, both within their parties and in the formal and informal processes of allocating resources. As a result, both the clean part and the corrupt part of the Romanian administration were substantially decentralized, together with the political decision-making inside each major political party, for good and for bad.

Power discretion has also not evolved due to lack of enforcement of legal accountability mechanisms in the period under study. Although Romanian authorities are compelled by law 544/2001 to produce a yearly accountability report, the government does not enforce this legal provision. The General Secretariate of the government (SGG), which is supposed to be the government's chief implementing body, was unable to offer any statistics on how many such reports were filled in 2010. An independent assessment by the Alliance for Clean Government (www.romaniacurata.ro) evaluated that not even half such mandatory reports are compiled and that they are never verified or used as control instrument by the higher authorities. Out of 15 ministries, by mid-February 2011 only four had managed to fulfil the legal requirements of publishing their 2010 report on their website. This leaves great latitude to all authorities, as there is no other mandatory reporting on accomplishing goals.

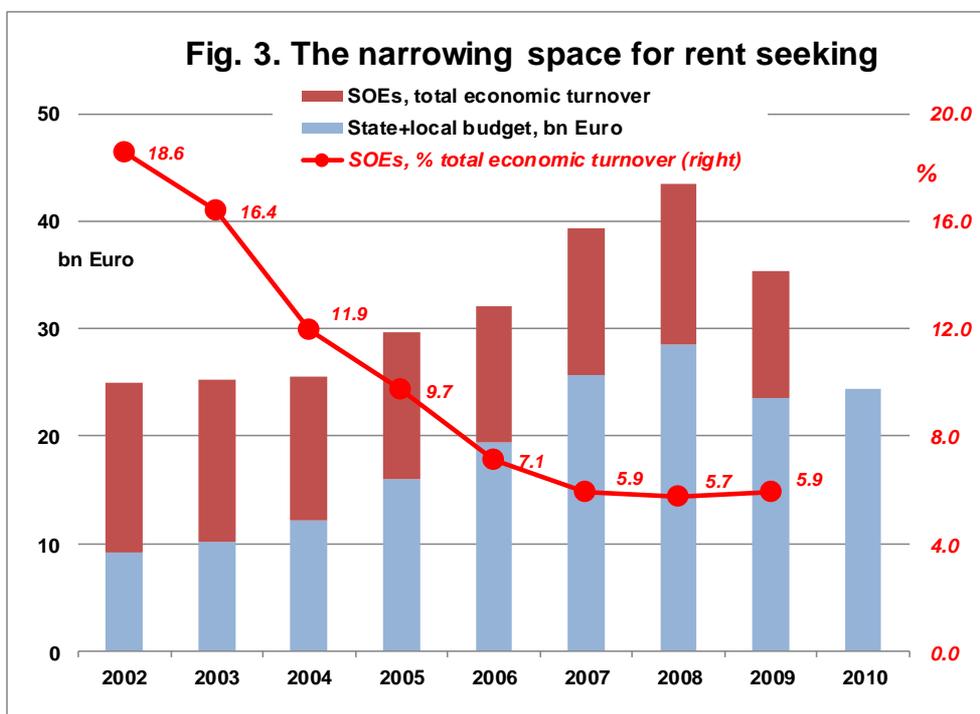
Romania's Audit Court controls only accounting, and has no prosecutorial powers. Despite the existence in quite a few laws of provisions for administrative sanctions for civil servants or sanctions for political executives there are no records of such sanctions. Ionel Blănculescu, former controller in the Năstase government (2000-2004) argued recently that custom officers charged with corruption in February 2011 had been fired before for lack of integrity, but were reintegrated in service after winning in Court due to the over-protective law of civil servants (188/1999).

Romania also has a ministerial responsibility law, but no minister was ever sentenced on its basis, despite quite a few being charged. In a notorious case, the Supreme Court of Justice acquitted the head of the State Forrest agency (also a MP) who was proved to have caused damage of millions by acquisitions with blown prices (he bought Versace tiepins for all foresters in Romania at a value of 20 000 more than their shop price). Administrative accountability also does not work.

The government produced during summer 2010 an emergency ordinance imposing social taxes payments to copyright contracts: it was full of errors and contradicted openly its own implementation norms, yet nobody was sanctioned for passing and approving it, despite thousands of people being

induced to queue at tax offices over it (the minister alone was reshuffled) The civil servants law has detailed mechanisms on their accountability, but in a system where dismissals are generally political and arbitrary such mechanisms are ineffective and controversial. As long as nobody pays for anything and only political allegiance – or lack of – is sanctioned, governance is bound to remain poor.

The second category, **material resources**, in other words the rents for private individuals and companies, have undergone important changes due to Romania’s EU accession. The processes of privatization and post-communist property restitution have more or less been completed by now (with a few notable items left in the energy sector – see Fig. 3). The networks of extraction and patronage created at the beginning of transition to benefit from them had to shift and find new opportunities. Furthermore, the gradual implementation of the EU *aquis* and, eventually, Romania’s accession, has increasingly limited the possibility to dispense openly public resources at will, as it happened in the ‘90s or shortly after.



The European competition rules (anti-monopoly, state aid) makes it more difficult to simply cancel the debts of certain private operators in 2010 compared with 2003-04, when a string of favored companies thrived on bailouts; the smaller number of state owned companies are under increased scrutiny; and the quasi-*aquis* on administrative depoliticization raises obstacles for the parties taking office which attempt to simply replace members of the civil service. Finally, the brutal onset of

the global economic crisis in 2008-2009 has forced the Romanian politico-economic environment to adapt quickly to a contracting volume of public resources available, after a few years of carefree, expansionary mindset; and to the collapse of certain economic channels used for illicit transactions (such as the real estate market).

In order to discern trends in this fluctuant environment we have focused on five indicators:

- the total potential rent;
- the profit of Romanian contractor client-companies of the Government, compared to European ones competing for public funds in Romania;
- the discretionary allocations from the Government's Reserve Fund;
- the loss incurred by main state producer agency Hidroelectrica due to insider trading to preferred companies;
- and the amount of politicization of the public sector.

The first and the last indicators are attempts to capture the overall dimension of the "corrupt market"; the other three offer case studies meant to shed a light on the actual mechanisms at play, which differ very much from sector to sector.

1.1. Our first indicator is the potential total public resource which can be allocated discretionarily, followed by the measurement of actual allocation in a few key sectors.

The amount available for rent seeking has steadily declined in industry and the financial sector. The contribution of SOEs to the total economic turnover went down from 19% in 2002, to 12% in 2004 and less than 6% in 2010 (Fig. 3). If privatizations continue, the space from rent seeking from this favorite traditional source will narrow down significantly.

What has not declined – on the contrary – mostly due to growth and the arrival of the EU funds, is the procurement budget, a category not registered as such in the budget and therefore impossible to trace accurately on a year-on-year basis. However, by adding the capital investments from the central and local budgets, with 40% of the current expenditure on goods and services, and with the EU grants, we obtain a rough estimate of 5.8% of GDP in 2004, going up to 7.6% in 2008 and 7.5% in 2010. In absolute values the increase is more pronounced, from 20 bn RON in 2007 to 27 bn RON in 2008; funds earmarked for local and regional procurement also went up, from 5 billion RON in 2006, 11 in 2007, 13 in 2008 and 18 in 2009⁴.

⁴ These calculations do not imply that *all* procurements and SOE transactions are corrupt; it only shows the volume available for rent seeking and graft.

Between 2004-2006 most of the political clientele has re-focused mainly on public tenders (for works, provision of services, etc) and learned how to bend the new, EU-inspired rules, or tried new ways to get preferential contracts from the fewer remaining state-owned enterprises (SOEs). For a few years before the crisis, against a background of buoyant public budgets (rate of increase of 15-20% per year in Euro terms), there was enough space for everyone to benefit and the reconversion was not too painful or indeed visible. And since the execution of a contract, once obtained, can be done transparently, the inordinately high margins of profit have started to show up officially in financial balance books: local companies getting preferential contracts in public works or as energy intermediaries run with annual profit rates of 30-40% or more (see Fig. 4).

1.2. This is our second indicator: profit of politically connected domestic contracting companies as compared to European established ones present on the market.

In the study interval a few Romanian-owned contracting companies (or groups) have grown and came to compete on a par with established multinationals, in terms on turnover of their business in Romania (see Chart 4). Most glaringly apparent, the high profitability was realized by the Romanian contractors, on contracts with the Ministry of Transportation (through the National Roads Company, CNADNR, mainly). By contrast, foreign companies seem to incur mainly losses – including the American Bechtel, on a contract allegedly skewed in its favor.

It is not easy to explain such puzzling trends as those shown in Charts 4-5. It may be that Romanian companies, as upstarts without powerful holdings behind them, were extremely conservative in their investment and expansion strategies and had to realize high rates of operational profits in order to finance their own development, in a period when commercial credit was either expensive or risky. Better knowledge of the local context and access to cheaper inputs, based on long-term or personal relations with their suppliers, are also reasons often quoted by the owners of these companies.

What is more, the Romanian managers also point to the fact that a large part of their profit is virtual, as many invoices they issue (and hence, have to record as realized income) go in fact unpaid for long periods of time. Political, institutional and economic uncertainties create additional costs in terms of financing any operation. In a riskier environment the interest rates are higher, and profit rates even more so. This is the normal trade-off between risk and expected profit in economic operations. Nevertheless, the same dilemma could be said to apply to all economic operators present in Romania, who all face the same level of risk, so it is not clear why only Romanian companies would require such high profitability in order to operate normally.

Fig. 4. Turnover, Romanian companies

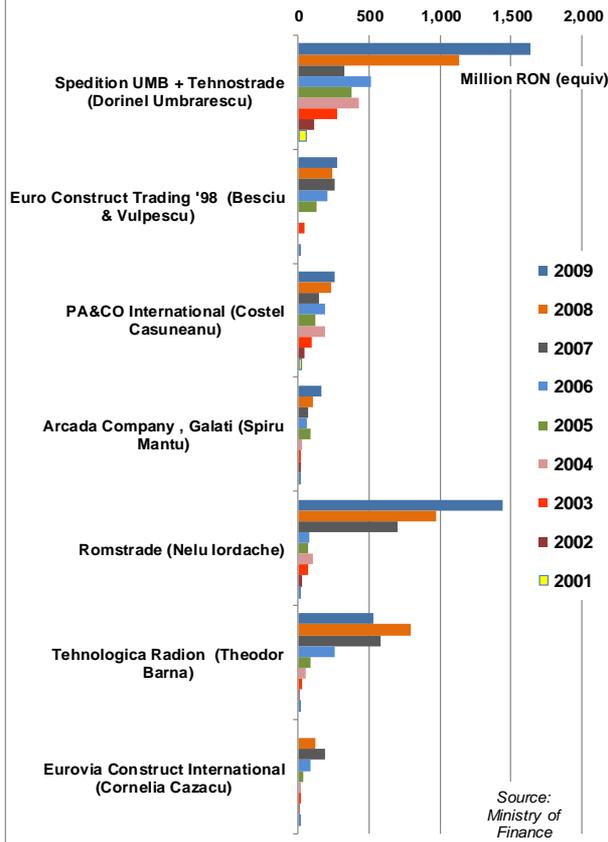


Fig. 5. Gross profit rate, Romanian companies

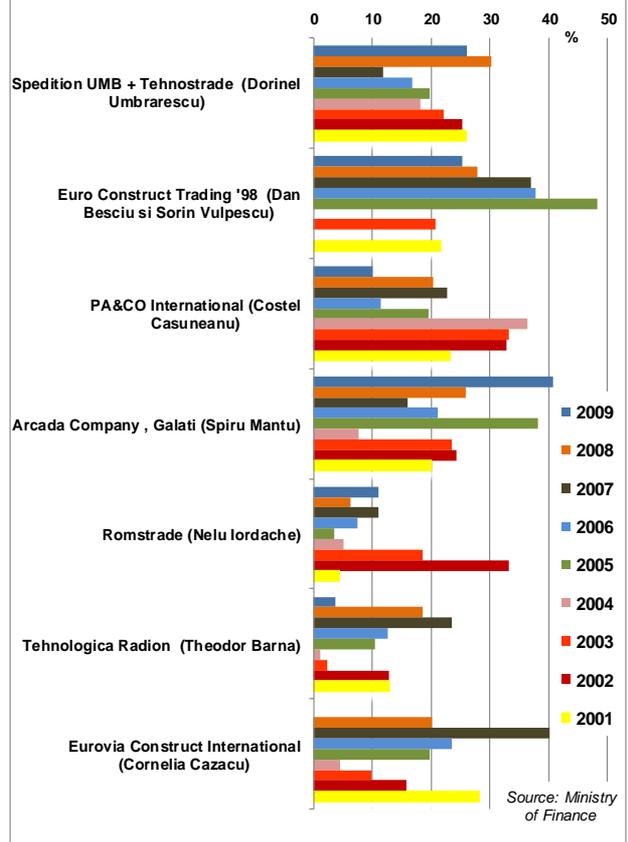


Fig. 6. Turnover in Ro, multinational companies

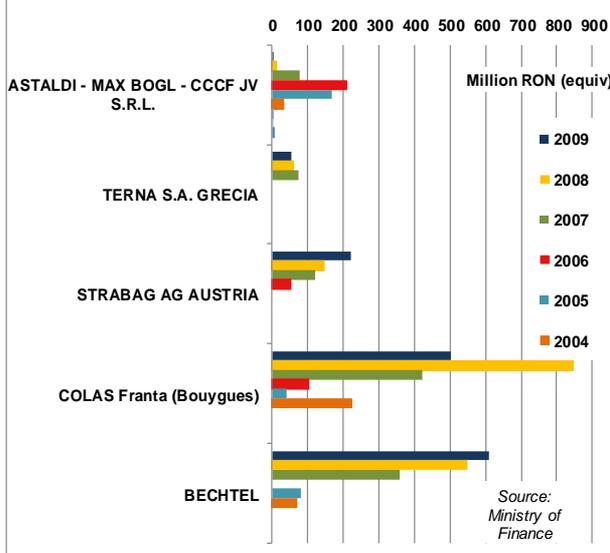
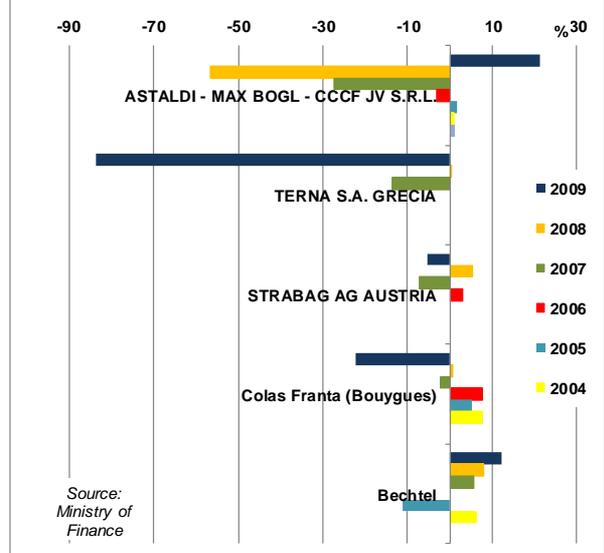


Fig. 7. Gross profit rate in Ro, multinational companies



The multinationals have been active mostly on large works contracts financed with EU Funds (ISPA); the Romanian ones, either by choice or because they were not eligible for the big projects, went for a large number of smaller contracts, a good part of which was financed directly from the national budget. In addition, the multinationals tend to get mostly large and relatively difficult works contracts, and very few framework contracts for the regular maintenance of roads (including in the winter season); the Romanians have almost exclusive access to such latter contracts, which are financed fully from national sources and hence are less cumbersome in terms of paperwork and less transparent (if only because no international partner has attributions to verify or approve anything).

Several factors may be therefore at work creating the consistent difference between the profitability rates of the two groups. Since maintenance contracts tends to bring more stable revenues over a longer period of time, while the works, especially in EU projects, tend to go in cycles, this may be the reason why the turnover and profit rate of Romanian companies look so solid and stable, when compared with the volatility of their foreign competitors. The source of the money may be very important: when CNADNR is the sole contracting authority it pays from national funds and has no controller, it may act as a much more lenient beneficiary towards its private partners: less scrutiny on quantity and quality of works, more helpful attitude in approving the claims, easier down payments – and, of course, softer when the prices are negotiated.

On the other hand, it is also possible that multinationals are better at “fiscal optimization” for their operations in Romania, while the national companies have less scope for such arrangements. After all, it is hard to understand why the large private operators continue to compete to win tenders for projects which apparently bring them only losses.

Nevertheless, the data makes it very likely that the inordinately high profit rates in virtually all Romanian subcontracting companies are not a reflection of the normal business risk, but of the existence of privileged companies in a relatively closed market, where high provision costs and preferential financial arrangements are accepted by the state, at the expense of the taxpayer.

1.3. A third indicator of discretionary, politically linked allocation can be found in the area of the Reserve fund, an emergency buffer provided for since 2002 in the Public Finance Law, for natural disasters or other unexpected situations. The general understanding was that the money from the fund would be disbursed judiciously for the purposes intended. However the law has two major loopholes: (1) it allows the unlimited increase of this fund by government decision only, during the budget cycle, by shifting money into it from other ministries; (2) it is unclear in defining the emergency situation that may justify the allocation. The combined results of the two flaws are:

- Successive governments have taken to the habit of earmarking a small amount for the Reserve Fund when the national budget is approved by the Parliament, and then supplementing it liberally by executive decision. This was increasingly the situation every year after 2002. The peak was reached in the electoral year 2008, when the fund was increased 590 times above the budgeted level, reaching 3.45 billion RON.

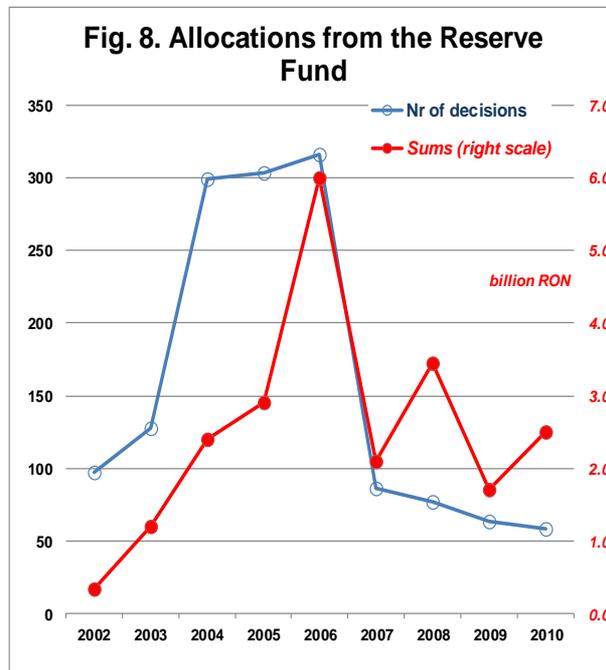


Table 1. Share of preferential allocation versus share of votes in local elections

| | 2004 (PSD) | 2008 (PNL) | 2010 (PDL) |
|---|------------|------------|------------|
| Share of preferential funds for main govt party % | 49 | 45 | 62 |
| Share of vote in local elections of govt party % | 35.5 | 16.2 | 28.8 |
| Implicit "clientelism ratio" | 1.4 | 2.8 | 2.2 |

- The cabinet can decide at any time to transfer these amounts of money from the Fund, to any central agency or local government, without the Parliament veto, by-passing the existing mechanisms of inter-governmental financing and thus undermining the policies governing local government spending and accountability.

This is bad budget practice on both counts: it reflects a lack of capacity to prepare a feasible budget, which subsequently has to be amended many times during the execution; and it opens a

broad boulevard for discretionary allocations. We therefore treat allocation of the Reserve Fund as an indicator of political partiality.

Fig. 8 demonstrates that the use of the discretionary fund went in a crescendo, both in terms of the number of allocations and sums disbursed, and declined slightly since the advent of the crisis. While the peak in 2006 may be justified by the major floods taking place that year and the year before, those in 2004 and 2008 are purely politically motivated (electoral years). This supports the politicization hypothesis.

Tab. 1 brings additional evidence, showing that an unwritten rule may have functioned in the last years that dictates that the amount of resources available must go 75-80% to the party or coalition of parties in power. This seems to be the norm. In 2004 the Social-Democrats exceeded their share of the vote with about a fifth preferential allocation. In 2008 the Liberals exceeded it by over 60%, and in 2010, at a smaller total amount due to the crisis Democrat Liberals exceeded with more than 50%. There is a flagrant lack of government impartiality in the allocation of these funds.

However, if we account for inflation and the exchange rate fluctuations, the total volume of sums disbursed through the discretionary Reserve Fund in 2009 and 2010 was below the level of 2004. The number of decisions – which are in fact back-door, executive amendments to the national budget – were also fewer in 2007-2010 compared with 2003-2004. But in the years with buoyant public budgets (2006-08) additional discretionary mechanisms were created (for example a large investment fund for schools rehabilitation which was allocated directly by the Ministry of Education with no transparent criteria, therefore functioning much like the Reserve Fund and with comparable size).

Who is to blame? The two-tier local government system of Romania generates cross-crossing political alignments, for example when the mayor belongs to the national ruling coalition, but the leadership of the County Council, which plays an important role in transfers allocation belongs to the opposition. In such situations it is hard to disentangle who is favoring (or abusing) whom when the government goes over the head of the County Council Presidents and allocates money directly to local communities: they may favor a well-connected mayor, but also compensate a local government systematically neglected by the county-level authorities. In other words, discretion in allocation is the rule at both central and county level.

1.4. The fourth indicator is in the sensitive area of energy, which has provided ample opportunities for rent-seeking on the past. The main scheme which enriched some of Romania's top billionaires – the so-called 'smart boys' is of great simplicity: buy cheap energy from the state owned companies and resell it expensively to the distributors who do not have direct access.

A top example is **Hidroelectrica**, the major state-owned production company that made headlines in recent years for suboptimal contracting practices and non-transparent deals. Hidroelectrica featured prominently in several media claims that it sells a part of its electricity production at prices below the market level to companies selected without competition. Anecdotal evidence on such practices has appeared in various newspapers. In addition to this, there is evidence that other operations of Hidroelectrica are also suboptimal. Such practices include engaging in sale contracts that exceed the production capacity or estimated production for the year, which means Hidroelectrica is then forced to purchase very costly electricity from other producers to fulfill its sale contract obligations.

Hidroelectrica has often been accused that it does not put its electricity production for competitive sale on the transparent transaction platform OPCOM (essentially, to “auction” its electricity in order to get the highest available price on the market in transparent and competitive terms). Hidroelectrica has always argued that it cannot put up for tender all this production due to the long-term contracts concluded in 2000-2004 which expire gradually in 2009-2014. Therefore, in 2009, all of its production available for the competitive market has been sold in non-competitive terms, on these previously concluded contracts. However, by the end of 2009, some of these long-term, non-transparent contracts had expired and about 2 TWh would have been available for competitive auctioning on OPCOM starting from 2010 onwards.

Nevertheless Hidroelectrica’s management approved in 2009 the extension of some of these non-competitive sales contracts to ‘smart boys’ by another five years. These bilateral contracts, both for the domestic market and exports, are non-transparent, so the clauses are not known to the general public. However, apparently, the price in these contracts is negotiated every year. It is unclear why these on-going contracts cannot be negotiated at prices comparable to those for one-year contracts on OPCOM (the results are presented in the Tab. 2 below). For 2010, Hidroelectrica traded indeed on OPCOM at end-2009 a quantity of 1.7 TWh. However, the manner in which the transaction was organized showed that it is possible to formally follow the law but yet abuse it. Thus, instead of selling competitively, which meant placing an offer for sale and wait for the highest bidder, Hidroelectrica responded to a purchase offer at a very low price (138 instead of 160 RON/MWh average price on OPCOM at the date), making a loss of 37.4 mil RON.

Table 2. Hidroelectrica: loss from non-competitive bilateral contracts in 2009

| | RON/MWh | TWh | Mil RON, total |
|--|---------|------|----------------|
| Average price, bilateral contracts domestic market, 2009 | 102 | | |
| Price for one-year electricity sales on OPCOM, Dec 2008 (for 2009) | 170 | | |
| Price difference | 68 | | |
| Quantity of electricity in domestic bilateral contracts | | 11.6 | |
| Lost revenue on domestic market | | | 788 |
| Average price, bilateral contracts for export, 2009 | 163 | | |
| Price difference | 7 | | |
| Quantity of electricity sold for exports | | 1.3 | |
| Lost revenue from exports | | | 9 |
| Total loss on non-competitive sales, 2009 | | | 798 |

Data sources: OPCOM, Money Channel. The table offers a conservative estimate, comparing Hidroelectrica's potential prices with prices on OPCOM for base load energy. In normal market conditions, Hidroelectrica's competitive advantage would be to sell the bulk (up to 2/3) of its available energy for peak consumption, which is more expensive (the premium for peak consumption varies from 20% to 200%).

Table 3. Value of Hidroelectrica's cross-subsidy to Deva, Termoelectrica and other inefficient producers (and ultimately to their suppliers)

| | RON/MWh | TWh | Mil RON, total |
|--|---------|-----|----------------|
| Average purchase price electricity for Hidroelectrica | 200 | | |
| OPCOM average price PCCB | 170 | | |
| Price difference | 30 | | |
| Quantity | | 2.5 | |
| Loss from Termoelectrica, Deva etc. by not selling on OPCOM to Hidroelectrica | | | 75 |

Data sources: OPCOM, Money Channel.

A second problem is that Hidroelectrica buys energy from other producers (notably the very inefficient Deva coal-fired plant, Paroşeni, or ELCEN) to meet its sales obligations. In 2009, Hidroelectrica produced 15.5 TWh, less than its average production in normal weather conditions of 17.4 TWh, but this decline in production was not so much due to draught and actually foreseeable (the reduction was caused by a scheduled interruption for the rehabilitation of Lotru power plant, which led to a decline in Hidroelectrica's production of around 7-8%). So Hidroelectrica should not sell electricity for higher-than-expected production, knowing that for the quantity it cannot produce it will have to purchase expensive energy on the market. 2.5 TWh of the gap in 2009 was covered from purchases from Termoelectrica (at 238 RON/MWh), Deva-Mintia (at 239 RON/MWh), Turceni (179 RON/MWh), or Craiova (195 RON/MWh). These amounts were contracted directly, without being traded competitively on OPCOM, and are at higher prices than those on OPCOM (205 compared to 190 RON/MWh on average).

The losses from these transactions, caused by the fact that Termoelectrica, Deva etc. do not sell on OPCOM and Hidroelectrica does not purchase competitively the needed electricity (in breach of Executive Order 445) are illustrated in Tab 3 and represent actual cross-subsidies mainly to Termoelectrica and Deva. This in turn allows these operators to continue with their high operating costs, inflated and eventually benefiting a network of private suppliers of the power thermo plants.

The case of Hidroelectrica allows an estimate of the economic loss due to bad governance and corruption. Its total yearly loss due to such practices in 2009 amount to almost 0.9 bn RON, in a conservative estimate, squandered by just one large SOE. Put simply, Hidroelectrica sold electricity below market prices, in quantities that exceeded its own available production, and purchased power at above market prices to cover the gap. Summarizing the tables above, in 2009 Hidroelectrica sold 11.6 TWh at 102 RON/MWh and 1.3 TWh at 163 RON/MWh, for which it needed to purchase 2.5 TWh at 200 RON/MWh. Instead, Hidroelectrica should have simply sold its own available production of 10.4 TWh at the market price of 170 RON/MWh. The difference between the two strategies amounts to a staggering 872.9 mil RON.

The almost 0.9 bn RON in revenues could have gone partly to the state Treasury, and partly in the needed investments – but instead goes mostly to a selected list of domestic insider dealers. On top of those are companies like Energy Holding (meanwhile broken into a few others), Luxten Lightning, Green Energy or Grivco, the company of the free-rider party of Mr. Dan Voiculescu. Some political links are obvious, as the change of government brought losses to some of these companies (for instance to Mr. Voiculescu, a personal enemy to President Traian Băsescu, whose suspension he is currently and publicly seeking), or impressive gains to others. Major traders like Petprod have only three employees, each responsible (for instance in 2008) of sales of nearly 30 mil Euro. So finally and when comparing 2004 with 2010 the difference is not that great. All ministers of industry in the

end approved Hidroelectrica's deals with these intermediary companies and when they intervened it was to change the profiteers, but not to change the rules of the game.

Despite a high-profile investigation by organized crime Prosecuting Department DIICOT involving a former economy minister, Codruț Seres, (from Mr. Voculescu's party), and a discrete investigation by Competition Council, most profiteers have had their contracts confirmed from one regime to another and enjoy remarkable profit rates⁵. A transcript leaked from Mr. Seres' file shows that foreign consultants charged in this case were complaining that domestic insiders are so strong and the network so perfect, including the minister, that they cannot find any way in⁶. The lawsuit is underway, but no charge of corruption was brought, so it is unclear why only these foreigners are pursued (for espionage!) and chronic domestic insider traders are not.

1.5. Finally, our last indicator is in the realm of public human resource management.

Politicization, manifested in the expensive replacements of many people in top positions in the public sector at each change in government (and indeed of government coalition composition), has continued undiminished after the EU accession, despite Romania's commitments to the contrary. If anything, transaction costs only increased as the governments had to amend the anti-politicization legislation earlier adopted at EU's bidding, a process disputed by the political opposition, the Constitutional Court and the envisaged civil servants themselves. Thousands of law suits by fired executives from the public sector have been filed after 2007 alone, despite the government solution of offering them to preserve all their privileges (therefore expenses) even when removed from office to another position.

In an exemplary case in 2009, the managers of the Proprietatea Fund were granted half a million euro stipulated in their contracts as a firing clause just to leave the positions vacant for the new government. The fund was not even under-performing at the time. Politicization, a major source of both incompetence and instability has come to include even hospital managers, despite many of them winning in Court against the government and is planned by the new education draft law to go as far as schools principals. An easiest way recently identified to shortcut legislation is seen in the proliferation of short-term contract appointments in senior government positions (directors in ministries, heads of agencies, prefects) or non-political public institutions (ex. hospitals management), as such contracts do not require open competition to fill in the office.

⁵<http://www.zf.ro/companii/vanzatorii-privati-de-energie-continua-sa-faca-profituri-uriase-energy-holding-si-a-majorat-castigul-de-pestesase-ori-4828892>

⁶ www.adevarul.ro/.../Voiculescu-Seres-privatizarilor-strategice-Tuca_0_357564854.html

To conclude, when we compare 2004 with 2007-08 and 2010 we discover that the types of resources allocated preferentially changed from 2004 to 2008 to some extent, became more subtle and professional or were partly dried up by the crisis.

But preferential allocation and government favoritism remains systemic and practiced openly. The massive distortion, involving the greatest volume of funds is the political allocation of public funds to clients, from the budgets of counties, municipalities or national companies. From counties and municipalities the money then gets to smaller, regional or local client companies.

The system is network based, the main substance of illicit trading being influence, not cash, and many politicians being themselves entrepreneurs (or their direct families). Bribing only appears when direct allocation to clients fails or a new client wants to enter the market. A survey of money spent on electoral campaigns finds a correlation between donations and winning of public contracts, but the amount of donations is so small that the real exchange is clearly not in the transparent realm.

Therefore focusing an anticorruption strategy on bribing cannot yield but limited results. The government had clear administrative instruments that it could have used, for instance in the case of Hidroelectrica, only it has repeatedly decided not to deploy them. Prosecutions should shift from corruption to mismanagement and more than one minister should be charged. As crime becomes more refined, legislation should also follow.

2 Constraints to corruption: legal and normative

A major constraint to corruption consists in the existence of an effective and just body of laws and the capacity of the law and order agencies to enforce them impartially and effectively. Romania and Bulgaria had rule of law World Bank Governance scores worse than the other new EU entrants. Romania progressed in 2005-2006 after anticommunists returned to power, but then fell back to the old practices; Bulgaria started to show good will only in 2009.

Not only politicians proved reluctant Europeanizers. In both Romania and Bulgaria Judicial Councils and judges in general were not supportive of reforms. Magistrates had been promoters of reform as long their independence from political intervention was at stake; once they became completely independent their *esprit de corps* flourished and no incentives were left to pursue self-improvement. In both Romania and Bulgaria the conservatives in the judiciary managed to make use of their administrative positions as heads of Courts to be elected into the Judicial Council or Constitutional Court in order to use their office there to oppose substantial reforms to the way these judiciaries operate.

The magistrates' pay was increased to stimulate performance and to curb corruption, but attempts to set up any serious checks on their performance did not succeed and accountability rose to become the salient problem (Freedom House 2005).

By 2007, evidence was pouring in on this count from more than one country, so the World Bank agreed that the most pressing issue has become 'ensuring judicial accountability, given newfound independence'.⁷ The European Commission then upgraded its benchmark asking for an accountable, not only an independent Judicial Council. But, unlike the government, which can lose elections for under-performing on EU accession, the Judicial Councils had no EU accession stakes.

The lack of regard of the judiciary for other interests than its own was shown blatantly in the unprecedented 2009 strike of the Romanian judiciary, when they sued and judged themselves a substantial raise of their own pay based on a bonus legally canceled years before, in a moment of dramatic budget deficit. Bulgaria's judiciary leads in 2008 in the Gallup Corruption Barometer, a global survey by Transparency International as the most corrupt judiciary in the world.⁸ Fig. 9 and 10 show that the two countries have recorded insignificant progress from 2004 to 2009, being still perceived below the level of Croatia and Turkey.

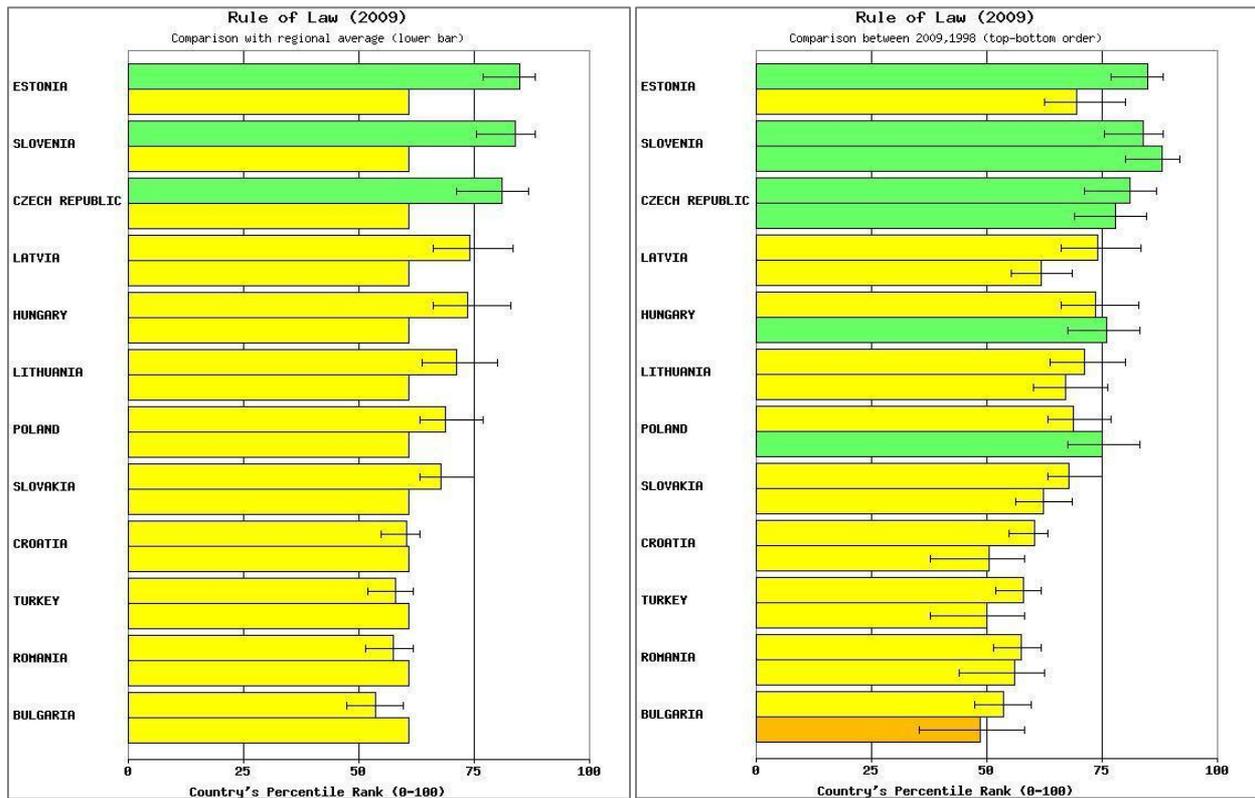
Leaving aside perception and going to direct indicators, we now examine the progress made by Romania's main anticorruption prosecutorial office, DNA since 2004 (Tab 4). There seems at first sight to be no significant improvement in the numbers of indictments and final convictions.

However, if in 2004 no high-level official was investigated by the DNA, by the end of 2010 numerous current and former Members of Parliament, Government Ministers, Mayors and County Council Presidents have been charged, some of them while in office, and sent to trial. The counter-reaction to this anticorruption campaign included political attempts to dismantle the DNA and to fire the management of the specialized body. The Constitutional Court played a very important role in two instances:

⁷ James Anderson and Cheryl Gray (2006) *Transforming Judicial Systems in Europe and Central Asia*, <http://siteresources.worldbank.org/EXTECAREGTOPJUDREF/Resources/ABCDE.pdf>, at 333.

⁸ <http://www.transparency-bg.org/?magic=0.5.0.2&year=2007>

Fig 9-10. Comparison of SEE countries with the regional average on World Bank indicator Rule of Law



- a. In 2006 the institutional set-up of the then Anticorruption Prosecution Office was deemed unconstitutional, thus forcing an institutional re-designed which slowed down the operational activity of the DNA.
- b. In 2007 it extended the immunity of ministers provided by the Constitution also to ex-ministers, thus triggering a wave of retransmission of cases involving such persons from courts to the DNA. The prosecutors were requested to obtain an approval for the start of criminal investigation and to re-administer all evidence.

In several cases, the Parliament decided to protect its members against criminal investigation. The most notable cases regard the PSD ex-prime minister Adrian Năstase and the PDL sports and youth minister Monica Iacob-Ridzi. In both cases the Parliament refused to lift the immunity against criminal investigation for these ex-ministers which were also Members of the Parliament. In another case, the Parliament refused to allow the arrest against Mr. Păsat, a member of the Chamber of Deputies, also investigated by the DNA. However, in most cases the Parliament allowed criminal investigations to commence against ministers and ex-ministers and for arrests against MPs to be requested to courts. The President issued approvals in all the cases where he was entitled to decide upon the lifting of immunity.

Another criticism voiced throughout the years was that the sentencing practice of courts is not harmonized and that sentences do not have a dissuasive effect as most of them consist in on-probation sentences, especially when they involved high-level officials. To address the first issue, two judges of the Bucharest Court of Appeal published sentencing guidelines which may be used by judges when deciding what would be the correct sentence in a given case.

Table 4. Lawsuits

| | Indictments | | Final convictions | |
|-------------|-------------|-------|-------------------|-------|
| | Files | #pers | Decisions | #pers |
| 2004 | 169 | 451 | 73 | 165 |
| 2005 | 111 | 744 | 73 | 161 |
| 2006 | 127 | 360 | 80 | 155 |
| 2007 | 167 | 415 | 63 | 109 |
| 2008 | 163 | 683 | 63 | 97 |
| 2009 | 168 | 552 | 81 | 131 |

Another useful tool for the unification of jurisprudence is Jurindex – a database of court decisions which allows judges to review decisions issued by their colleagues in similar cases. On the second issue, in 2010 the courts started to pass harsher decisions, including with regard to high-level officials (the mayor from Baia-Mare – 2 years and 6 months – the mayor of Râmnicu-Vâlcea – 3 years and 6 months, ex-senator Vasile Duță – 5 years).

While medium level corruption cases are handled by courts in less than three years, high-level corruption cases involving ministers and MPs are dragging behind in the High Court of Cassation and Justice for several years without reaching even a first instance decision. This contributes to the general opinion that high-level corruption cases benefit from special treatment from the courts. It remains to be seen if the elimination of the automatic suspension of trials when a challenge of constitutionality is raised (a method to delay trials excessively used in high-level corruption cases) will indeed speed-up the trials. Initial assessments show that the challenges of constitutionality are raised less frequently after the elimination of the automatic suspension.

The massive transfer of legislation prompted by EU did not yield the expected results. Romania, Bulgaria and Macedonia turned during their accession into the world leaders of anticorruption preparedness according to Global Integrity Index, but their systemic particularism was barely

touched⁹. A compiled index of anticorruption laws and regulations¹⁰ shows that tenths of laws were adopted since 1998, not only by candidate countries, but also by countries like Albania, who surpassed some of the new EU member countries, actually increasing the distance between the 'real' country and the 'legal' country.

As to **normative constraints**, the picture is also mixed. Romanians are very vocal in surveys against corruption and there is an overwhelming majority complaining of inequality in front of law and claiming all politicians are corrupt. However, the rally to defend Justice Minister Monica Macovei in 2007 when she was sacked, registered only about 3000 people in a city of two million inhabitants. For a more systematic analysis we reviewed the work of 50 nongovernmental organizations between 2004-2010, looking at the number of court actions against state institutions¹¹ and their outcome, at *watchdog*-type activities, the development of web platforms and surveillance campaigns.

The main mechanisms by which NGOs act as a *watchdog* is requesting information under FOIA, law 544/2001. Although there is no centralized database to reveal what is the exact percentage of applications submitted by NGOs, we can produce an overview over the annual reports, prepared by the National Agency for Government Strategies and published on www.publicinfo.ro. If in 2003, the proportion of entities accessing public information was 80% individuals and 20% legal persons, the direction has changed visibly during 2004-2008 in favor of the latter¹². While in 2004, individuals accounted for 69.99% of the requests compared to 30.01% the legal entities, in 2006, the ratio was 2-1, 65% of requests were submitted by individuals and 35% by the legal entities. The 2006 report notes that "differences on the requests of legal persons according to the administration level (39% in central government compared to over 24% in the local one) can be explained by the fact that NGOs monitor constantly, in particular the work of central institutions". In 2009, the ratio was 71% individuals compared to 29% legal entities.

The lawsuits activity is deployed most intensely in the Capital. This is due to the significant concentration of organizations in urban areas (87%) and Bucharest-Ilfov region, almost 22% of the total number¹³. NGOs such as APADOR-CH, Romanian Academic Society, Save Bucharest,

⁹See: <http://report.globalintegrity.org/globalindex/results.cfm>;
<http://www.globalintegrity.org/documents/KeyFindings2008.pdf>

¹⁰ Monica Dorhoi (2004), 'Anticorruption Assessment Index. A Comparative Review of Anticorruption Strategies', Paper presented at Midwest Political Science Association, Palmer House Hilton, Chicago, Illinois, April 15.

¹¹ The selected reasons for the actions are only related to laws such as 52/2003, 544/2001, therefore treating transparency and access to information, but also norms of ethics and integrity, corruption, public acquisitions.

¹² This category contains other legal entities also. Still, the 2006 report acknowledges the role of NGOs in accessing public information. Moreover, the intense activity of the nongovernmental organizations is proved by the significant number of monitoring reports that are based on requesting information

¹³ Civil Society Development Foundation, *Nongovernmental sector...*, p. 23.

Pro_Do_Mo etc are examples of active actors that use legal procedures. However, there are also local organizations that have acted in court public institutions for legislative issues. An example is Pro Democracy Association Craiova, which in 2008-2010 had 33 lawsuits with public institutions, of which nearly one quarter were won, 14 suspended and five dismissed. The organization producing this report (Romanian Academic Society) had better results¹⁴. Another indicator is the traffic on dedicated webpages – the leading www.domnuleprimar.ro, a forum on local governance with some watchdog activity only counts 27 000 users per day, and this is the best traffic of any NGO in Romania.

These poor results are explained by the fact that the bulk of Romanian NGOs is mostly focused on social issues, and as most EU funds come only through local or central government they avoid being involved in any activity which can be seen as critical towards government. Even from the core Coalition for a Clean Parliament, the strong alliance which contributed decisively to a change of government in 2004 due to a anticorruption campaign half the members have joined various political parties or secured official positions. NGOs involved in heritage issues and urban policy have grown from 2004, but the participation to their activities remain limited. There are no open sources of funds for anticorruption activities, as businesses are understandably reluctant to lose the favor of government.

The European Social Fund alienates the organizations from watchdog activities. The situation has worsened, as funds are rarer and harder to get, especially due to the economic and financial crisis and the redraw of the international donors. In other words, not only are normative constraints low and few anticorruption activists exist who are still in business and enjoy public trust, but the trend is negative, as there seems to be not enough funding for such activities, either from donors and Romanian business community or simply by volunteers. Romania had an active and dedicated anticorruption community only in the capital, and in insufficient numbers even there.

3 Conclusion

The methodology of this paper departs from classic studies of corruption on sectors, or of classifications such as administrative or grand, as we believe such approaches are grossly misleading. What we have tried to research here is the modus operandi of the state, to discern if it is based on ethical universalism, as any modern state should function, or rather on privileged allocations. Particular allocation seems to be the norm in Romania, and here lies the chief

¹⁴ <http://www.againstcorruption.eu/story/ngo-coalition-wins-major-battles-for-transparency>

corruption mechanism which has not changed since 2004. Addressing sectors instead of targeting the main – political – mechanism has been the approach of all anticorruption strategies of far. They do not seem to have worked.

The Romanian health system, for instance, is under financed and is characterized by a staff deficit. Physicians in the public sector make on the average under 400 Euro per month. Therefore surveys like the 2005 study conducted by the World Bank for the Romanian Ministry of Health concluding that so-called informal payments amounted to \$360 million annually only show the extent to which the state mismanages this sector. Even in percentages, Romania has the lowest budget for health in Europe, with ripe evasion of contributions paying to the politically controlled national insurance company. As hundreds of doctors were charged with petty corruption over the years and more thousands emigrated since 2007, the solution to Romania's health system is not in the realm of anticorruption. A radical reform of the sector and of its financing are the ways out. In other words, anticorruption approaches cannot be confined to prosecution, as this by itself has proved unable to solve such a gross problem.

Finally, despite the apparent lack of sustainability of European conditionality in the case of Romania's rule of law and anticorruption reforms, we believe that instruments exist to challenge these rules of the game. The Mechanism for Cooperation and Verification should continue, and postponing Romania's Schengen accession and tying it to an improvement on corruption is justified.

A successful strategy would reunite grassroots monitoring of government impartiality with top down (including from Brussels) intervention when red flags are out. EU should combine careful watching of Romania's market and act immediately when evidence exists of privileged actors. It should also encourage the funding of grassroots watchdogs, especially outside the capital, particularly when EU funds are concerned. The anticorruption legislation also must evolve in order to cover better the insider dealings which make most of transactions and not just bribing. Finally, since all government parties have proved unwilling to change the rules of the game, new political challengers are needed or the system will continue reproducing itself. These political challengers have already their program laid out: changing the current policies which only feed lack of accountability and corruption. Ironically, a "reform of the state" for better governance was also the program of President Băsescu and the current government when taking office in 2009.