MOLDOVA: CO-OPERATION IN REGIONAL DEVELOPMENT

Review of Moldova's Regional Development Legal Framework

Background paper 6: Regional Development Financing

DRAFT: NOT FOR QUOTATION

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Abbreviations

AIP	Annual Implementation Plan
CHU	Central Harmonisation Unit
DFID	Department for International Development
EU	European Union
FY	Financial Year
GoM	Government of Moldova
GDRD	General Directorate for Regional Development
IPP	Institute for Public Policy
OPM	Oxford Policy Management
M&E	Monitoring and Evaluation
MCRD	Ministry of Construction and Regional Development
MDRD	"Moldova: Cooperation in Regional Development" Project
ME	Ministry of Economy
MoF	Ministry of Finance
MTEF	Medium Term Expenditure Framework
NBS	National Bureau of Statistics
NDS	National Development Strategy
NCCRD	National Coordinating Council for Regional Development
NFRD	National Fund for Regional Development
NPC	National Participatory Council
NSRD	National Strategy for Regional Development
PPA	Public Procurement Agency
RD	Regional Development
RDA	Regional Development Agency
RDC	Regional Development Council
RDS	Regional Development Strategy
RDL	Regional Development Law
ROP	Regional Operational Plan
SADI	Small Area Deprivation Index
SAI	Supreme Audit Institution
SPD	Single Programming Document
WG	Working Group

Introduction

This paper is part of a broad legal review of RD law and regulations, undertaken between October 2010 and February 2011 by the DFID & SIDA funded MDRD project, together with the MCRD and other Moldovan government stakeholders. The review focuses on the Regional Development Law and on Regulations to this Law as well as on other documents governing the regional development interventions. The purpose of the review is to draw lessons from progress to date in the implementation of the RD policy and propose areas where the RD law can be strengthened.

A key aim of the review is to look for ways to simplify procedures. But the papers elaborated for the review also focus on the institutional framework and conceptual matters and their mutual relationships or implications. This is because the institutions and concepts are important for RD policy and its implementation and because the legislation – even if well designed – need not cover all situations.

The objectives of the Moldova RD legal framework review are to:

- identify and analyse good practice and strengths of the current RD legislation in order to build on them in the development of RD policy and interventions;
- identify and analyse weak points and problem areas in the current RD legislation and implementation, including the conceptual and institutional framework;
- propose areas where the Law on Regional Development and RD regulations need to be changed; and,
- provide recommendations for the further improvement of RD policy and its implementation.

Background

The Regional Development Law, adopted in February 2007, was elaborated over a period of two to three years, mainly with the assistance of a previous EU Technical Assistance project, the largest and third such EU TA project in the field of regional development in Moldova stretching back to around 2002-3. The same EU project elaborated a large part of the secondary legislation which, subject to certain amendments, was not adopted definitively until 2010. The focus of the primary RD Law – and indeed of a very large part of the secondary legislation - is mainly on designating key functions, institutions and instruments. The RD Law made almost no direct mention of the process of project preparation, appraisal, and selection. The focus was on programming, not on projects per se. The secondary legislative documents – notably the Framework Regulation on Regional Development Agency, the Framework Regulation on Regional Development Council and even the Regulation on the development and usage of the National Fund for Regional Development resources (all of 8 February 2010) focus on institutional and procedural issues of a mainly legal-administrative nature. Among the secondary documentation is also the Manual for the National Fund for Regional Development which provides the most elaborate description of the project and programming cycles. The development modalities of the project cycle (and to some extent the inter-related programming cycle) were not covered in detail.

The Regional Development exercise for 2010 was considered by all concerned as an exceptional exercise, driven by severe time-pressure. It was never envisaged by anyone involved in the process that the 2010 exercise would be the normal manner in which to articulate either the programming or project cycles. Under pressure of time and in view of the embryonic nature of regional structures, certain instruments were introduced which had never been foreseen in previous planning. Primary among these were a "national call for project proposal" identical across all regions, a straight-forward and time-pressured project submission process and a rapid and mainly national project appraisal and selection process.

Issue 1: National Fund for Regional Development

Main findings

The National Fund for Regional Development (NFRD)[1] is defined as *'the financing source for all programmes and projects aiming to achieve regional development objectives'* set out in the single programming document. It should be clarified that the NFRD currently only funds programmes and projects under the Law on Regional Development in the Republic of Moldova; it does not extend to all programmes and projects with a possible regional development perspective or impact.

The institutional framework for financing regional development is provided for in the Law on Regional Development in the Republic of Moldova and applicable regulations. The NCCRD approves the annual implementation plan and annual financing of the NFRD.[2] The NCCRD includes representation from key central government and regional development council representatives.

The NFRD is replenished annually with a one percent levy of the state budget and this is based on revenues rather than expenditure. In other words, if there is a fiscal deficit in that expenditure exceeds revenues, the levy is not applied to additional borrowings. This is a fiscally responsible approach to the management of the NFRD. The law provides that the fund may comprise any other financial sources from the public and private sectors at the local, regional, national and international levels, including EU assistance (donor)

[1] The Law on Regional Development in the Republic of Moldova, English translation, Article 1: Basic terms, draft, dated 19 June 2008.

[2] The Law on Regional Development in the Republic of Moldova, English translation, Article 5 (6).

programmes and private donations.[3] However, the regulations do not detail the processes by which those additional sources of funds are to be accounted for and how any possible conflicts of interest are to be addressed with sponsorship funding from the non-governmental sector.

The Fund is a line item under the existing GoM budget of the MCRD which has overarching responsibility for regional development. That the NFRD utilises existing GoM budget and capital, works, policies and systems is both an advantage and a disadvantage. It is an advantage in that the NFRD can rely on standard systems and procedures which most officers are well versed with and it is compliant with the Paris Declaration requirements. It is a disadvantage in that the current GoM policies and systems are not flexible and could not react to a changing capital works environment.

The Ministry of Finance (MoF) is focused on resource planning (budgeting), management of the funds (cashflow) and meeting payment obligations. The MoF is very supportive of the NFRD and considers that it may attract additional donor funding as it demonstrates the Government's commitment to regional development.

The Minister for Finance sits on the NCCRD so there is a level of coordination in terms of NFRD activities. For 2011, the projects will be distributed according to sectoral groupings, for example, transport and the environment. Once the projects are approved, the projects appear under the capital works budget, with the MCRD as the beneficiary. The key issue for the NCCRD is that the projects are approved before August of the preceding year to be included in the budget.

The MoF intends to shift the NFRD towards the medium-term budget which will focus on a '1 plus 2' planning process.[4] That is, the current budget year plus two out-years. This will impact on the planning processes for the NCCRD and the MCRD such that they will have to consider a rolling three-year programme consistent with the MTEF and updated annually to reflect any shift in funding levels. Once the forward planning processes are established for the NFRD, this will be a positive outcome for regional development and strategic planning.

With regard to unpsent funds being carried forward, there is a memorandum signed by the Minister that states that unspent funds can be carried forward and hence the fund can continue to grow and meet existing and planned project commitments.

Currently, the Court of Accounts has the responsibility for the annual financial attest audit of the accounts on behalf of Parliament. The capacity of the CoA to undertake audits at the RDA level is limited. As we understand it, their capacity is limited to an audit once every three years. Therefore, the application of NFRD funding is a concern in that the external audit function does not have sufficient capacity to undertake annual audits.

There is a line of thought that the RDAs should focus on regional development strategy and devolve the procurement process down to the beneficiaries. This is more fully discussed in

[3] Regulation on the development and usage of the National Fund for Regional Development resources, Appendix No. 4 to the Government's Decision No. 127, 8 February 2008.

[4] For example, in 2010 the MCRD had a budget line item (147.15.2) for the NFRD of 135,400.0.

Issue 4 on public procurement. One problem with direct beneficiaries managing the public procurement process is the capacity for oversight of NFRD funding at that level. In terms of audit, the Court of Accounts will need to plan audits of many local authorities (rayons) rather than at one RDA. Each local authority may have slightly different processes and systems and may not be as accessible as the RDA, although we would assume that GoM processes should apply for payment and procurement. One of our recommendations is that the MCRD Internal Audit unit undertake some of the oversight activity in the absence of an annual Court of Accounts financial audit. However, if the proposal to devolve procurement to local authorities is considered, we would have to consider an alternative oversight function to cover the absence of the Court of Accounts and that the MCRD Internal Audit function would not have any jurisdiction over local government (or indeed the capacity). It is possible that the Public Procurement Agency (PPA) can undertake periodic checks of procurement.

To resume, the NFRD financial management is satisfactory for the regional development objectives of the Government of Moldova and adopts a national approach. The NFRD financial management processes are established within the overall GoM budgetary and accounting systems and therefore are managed within an existing accountability framework. However, there are a number of key issues that limit the effectiveness of the NFRD financial management and accountability. First, there is a lack of audit capacity to undertake annual reviews of NFRD funding. Second, if direct beneficiaries are involved in the procurement process, the oversight of NFRD funding will need to be extended to this level.

Options or Solutions

The solutions could be

- The oversight function for NFRD funding needs to be reinforced. As stated, there is not an annual audit function that will attest to the application of NFRD funds and this is a key problem, not in terms of financial legislation and regulation, but in terms of capacity (resources). We have recommended that the Internal Audit Unit undertakes this responsibility until such time as the Court of Accounts has sufficient capacity for annual reviews.
- If we introduce direct beneficiaries into the procurement function for the NFRD, we are introducing an additional actor into the process and hence one further step away from being able to audit the application of NFRD funding. We will then need to consider additional support to the Court of Accounts, PPA and/ or to local authorities.

Recommendations

- That the Internal Audit Unit has responsibility for the audit of RDAs and the procurement process at that level. The reports would be provided to the Minister and copied to the Director Regional Development (GDRD) for action. The Court of Accounts would have access to these reports as required.
- If we were to pursue the devolution of the procurement function from the RDAs to local authorities (direct beneficiaries), we recommend that a review of their capacity

to carry out these activities be undertaken.. We would also have to consider additional options for audit oversight of the application of NFRD funds at the local level, including a spot check role for the PPA.

Issue 2: Overlapping of other state funds with the NFRD and also of the NFRD with other budget lines

Main findings

Currently the funding of local/regional projects partly overlaps; e.g. the State Environmental Fund provides financing for sewage systems, while sewage systems elsewhere may be financed by NFRD.

The GoM has a number of funds to support policy initiatives in Moldova. These include the National Road Fund, the Environmental Fund, the NFRD and the Social Investment Fund, which are off-budget funds, unlike the NFRD. This issue considers an effective approach to coordinating an overall strategy where a number of funds are contributing to regional development whether at the national and/ or local level. In some cases, projects have commenced with one Fund and completed through resourcing from another Fund.[5]

For example, the National Environmental Fund (NEF) is a division of the Ministry of Ecology and Natural Resources. The National Road Fund (NRF), under the Ministry of Transport and Communications, is focused on national roads and supporting infrastructure.

An example of overlap is that water supply and waste management projects could be potentially funded through either the NFRD or NEF. Whilst the project stakeholders and objectives would tend to be different, the engineering and infrastructure would be similar. For example, a waste management project can have both local and national outcomes. Hence, funding could be through both the NEF and the NFRD. Is this a problem? We do not believe so in terms of funding sources. If a project can support both national and local goals then this is a positive outcome. The concern is that local authorities will seek funding from multiple funds through articulation of project objectives to comply with each fund's overarching objectives when it is only fundamentally one project. Potentially, one project proposal can receive many sources of funding and accumulate more additional project funding than is required for the completion of the development. However, the key to this issue, if indeed it is an issue, will be the coordination of funding decisions at the ministry level (see Paper 3: The role of other ministries and departments in RD). The other issue is to ensure that each of these GoM funds has defined parameters in terms of what it will fund and what it will support. This will allow a greater level of clarity and efficiency in the coordination of the various funds.

[5] In the interview with the Director General, Financial, National Accounts and Capital Investment, he mentioned the example of Balti which started with the Environmental Fund and finished the project through the NFRD.

The key issue is that all GoM development funds should have defined parameters and be coordinated. A greater level of coordination will facilitate improved decision making and, by implication, allow less potential for fungibility.

Options or Solutions

The key solutions are:

- The coordination process between the different funds needs to be reviewed and formalised. We believe that the coordination process is essentially in place as the same key stakeholders, including the Ministry of Finance, sit on the respective decision making bodies. There may need to be an additional process whereby RDAs are informed of projects presented to other funds for approvals for its particular region. We would also suggest that the reporting format should, to the extent possible, be common to all funds with the beneficiary and nominated (beneficiary) officer clearly specified, the project outcomes and capital and estimated recurrent costs for maintenance clearly specified. There may need to be a common approvals timetable for all funds.
- There must be a level of clarity with GoM funds as to what they will fund and won't support. The parameters of each fund must be reviewed and defined to reduce overlap and poor coordination. For example, the National Road Fund (NRF) could only be involved in national roads and motorways and not local roads. However, one can envisage issues where a new national road is built but local roads are not connected due to poor planning. There must be coordination at both the decision making (approval) levels and also at the operational (RDA and other stakeholders) levels to support an overall integrated approach to (infrastructural) development. The Director General, Financial, National Accounts and Capital Investment supported the view that the RDA must have information on all approved projects from other funds and how they are connected to national planning. The RDA Evaluation Committee should check with the national plans on roads and/ or sewerage to support a coordinated response to development.
- Over time more examples of "over-lapping" will emerge. We do not believe they will pose any major operational problems for some time to come (i.e. until the volumes of money become large). However as they do emerge, this will provide the opportunity to clarify what is "regional/local" and what is more properly national/sectoral. To seek clarity at this stage is probably too ambitious and when this issue arose in preparing the RD process it was clear there was little understanding of it. Over time it will become a real issue and will necessitate that increasingly the NFRD should seek to define the more specifically regional/local dimension to a series of sectoral interventions, where through other mechanisms, the State may also intervene but perhaps more directly (eg transport, environment, but also in time, enterprise development, labour market and human resource etc)

- To support the coordination process, the application to one fund must also state that other fund proposals have been lodged for the same project. In fact, if a project can clearly identify both national and local outcomes, this should strengthen its claim to approval by the NFRD.

Recommendations

- That RDAs are informed by other funders of proposed projects as part of the approval process for NFRD funded project proposals. The projects proposed to the NFRD are likewise copied to other funds.
- Common reporting systems are utilised.

Issue 3: Use of multi-annual planning of state budget expenditures for RD projects funding

Main findings

The RD projects are planned in general for a period of up to 2 years, but expenditures are approved on an annual basis according to the legislation. This may cause uncertainty for beneficiaries and it is not in line with the medium-term expenditure framework. The need and possibility for coordination with (or the use of) the MTEF for the regional development projects should be considered and recommendations prepared.

The MCRD develops the three year single programming document (Article 10) which is then approved by the NCCRD (Article 5, Section 6[b]). The NCCRD also approves the Yearly Implementation Plan, in compliance with the NFRD financial resources available (Article 5, Section 6[e]). The Ministry of Finance have commented that they would like to see the NFRD shift to a three year budget, which would require the NCCRD to approve three year implementation plans with funding drawn from the NFRD line item in the MTEF. This would require a slight change in the legislation[6] to support this change. It is also important to note that this will be a rolling three year implementation plan as we cannot effectively plan for the out-years if there are major changes in budgeted revenues. The three year implementation plan must be a rolling plan consistent with the MTEF. The budget and planning processes should be coordinated such that both NFRD and the MTEF (Capital Works) are aligned. On the ground any shift towards a three-year planning cycle, will require a much more robust approach to project development. There will be serious problems if projects are programmed for three years but are clearly unable to be implemented within that period.

Options or Solutions

[6] The Law on Regional Development in the Republic of Moldova and attendant regulation on the National Coordination Council for Regional Development

- The enabling legislation and/ or regulation are amended to reflect an approval process for a three year rolling single programming document and annually updated implementation plans, consistent with the National Regional Development Strategy. The regulations and operational manual will also need to be amended to reflect a longer planning period, which will impact on RDC and RDA regulations. This will include Article 4 (2d), Article 5, section 6, Article 6 (1), Article 7 (6a) in the Regional Development Law. The regulations for NCCRD, RDA and RDCs will also have to be reviewed and, if necessary, amended.

Recommendations

- The regional development law should be amended to bring the implementation planning process into line with the MTEF.

Issue 4: Public procurement in the regional development

Main findings

The public procurement process has not been fully tested as yet, as agreed projects are only at the working group formation stage. The process appears overly regulated and may, in itself, create delays in commencing projects due to the number of steps and 'actors' within the process.

There is a line of thought that the RDAs should focus on supporting wider regional development activities and project development and devolve the procurement process down to the beneficiaries (practically, in most cases, rayons). There are distinct advantages in a direct beneficiary undertaking the public procurement process and assuming real ownership and making a contribution (whether financial or other staff resourcing). This usually helps ensure the project meets the needs of the beneficiary as they have determined.

It also allows the RDA, with its limited resources, to focus on regional development activities and to facilitating project preparation rather than to become overloaded by administrative tasks of direct project management.

Following on from the above, the oversight function for NFRD funding would have to be considered. As discussed in Issue 1, there is not an annual audit function that will attest to the application/use of NFRD funds. If we introduce direct beneficiaries as the procurement function for the NFRD, we are introducing an additional actor into the process and potentially limited oversight on NFRD funds.

Another issue is that the PPA has the responsibility to manage the contracts process in all public institutions. However, once a contract is signed they have no responsibility and/or capacity to undertake snap audits and checks on the contracts. The PPA comments that if there is a contractual problem at the local authority level, the authority can request the contract to be suspended. However, if the problem is with the Local Authority, they are unlikely to request the PPA to do anything. The Corruption Commission was mentioned as a possible check on local authorities however once the CC is called in, in terms of accountability, it is generally too late!

An advantage with having local authorities undertake the procurement process is that they will have a higher level of ownership of the project. It is therefore important for the local authority to be involved in the process from the beginning and undertaking the procurement process will ensure buy-in. This argument has been advanced by other papers. Pending a shift to this model, it will be essential that the beneficiary is involved actively in project management by being a member of an effective project steering committee that meets regularly and reviews progress.

Direct beneficiaries (local authorities) would be the most appropriate level for NFRD funded procurement activities to be carried out. However, the capacity of the local authorities to undertake this responsibility would need to be assessed and potentially additional support offered to local authorities to gradually take up the RDA procurement responsibilities.

The key issues are the unknown capacity of direct beneficiaries (local authorities) to undertake procurement and the increased lack of oversight over the application of NFRD funds. Whilst, the Court of Accounts will undertake financial audits of local authorities, these are at best once every three years. In our opinion, there is a need to have an annual audit at all levels of government, including project procurement by local authorities.

Options or Solutions

- There are distinct advantages in allowing a number of actors to perform public procurement as part of the regional development (NFRD) process. However, the capacity of direct beneficiaries to undertake procurement on behalf of RDAs is unknown. A review can be undertaken of their capacity to carry out these activities. A flexible programme would need to be developed to incrementally transfer this function to local authorities that have the capacity. As the capacity of individual beneficiaries progressively improves, both in terms of skills and resources, the programme can be extended to other beneficiaries. To achieve this, the GoM needs to amend the current procurement related regulation[7] to allow for actors other than the RDAs to undertake procurement activities with support from the RDA and possibly MCRD.
- It is our position that there is a need for an annual audit by the Court of Accounts at all levels of Government. However, in the short to medium term, this is not a feasible option as the Court of Accounts does not have the capacity for annual audits and, if we devolve some procurement to beneficiaries, the current proposal for MCRD internal audit to provide some coverage will not be applicable. Therefore, we need to consider a range of compensating oversight controls whereby the PPA could undertake periodic (random) checks at the local authority level, the MCRD Internal

[7] Specifically, Article 4 of the Framework Regulation on Regional Development Agency, Appendix No. 3 to the Government's Decision No. 127, from 8 February 2008.

Audit unit would cover the RDAs, the RDAs would report to the NCCRD (including the Ministry of Finance) and the Court of Accounts would perform financial audits once every three years.

Recommendations

- If devolution of the procurement function from the RDAs to local authorities (direct beneficiaries) is to be considered seriously, we recommend the need to undertake a parallel review of their capacity to undertake these activities.
- The current procurement regulation should be amended to include direct beneficiaries as procurement agents on behalf of RDAs.
- Additional options for audit oversight of the application of NFRD funds at the local level should be identified and considered, including encouraging the PPA to undertake a programme of spot checks on procurement at all levels of Government.

Issue 5: External (donor) financial support and possibilities to include these external funds in the NFRD or to co-ordinate the actions of the NFRD with the donors

Main concerns

This issue relates very much to co-ordination role of the MCRD and to co-ordination mechanisms of regional policy and external assistance in general. There are many donors operating in Moldova. Most of them have their own rules that have to be followed, which leads to a situation where every donor has its own programme, often with competing objectives. The Paris Declaration supports donors using existing Government systems and processes for the management of donor funding. The coordination of donor programmes and projects is also critical and can be managed through increased coordination with other funds (as per Issue 2), common reporting and timeframes and with donors supporting Government coordination efforts.

The current financial management processes for the NFRD are appropriate for increased external funding, although the audit oversight may concern donors. However on the assumption that budgetary support is the preferred manner by which donors will want to support RD, then donor contributions will need to be integrated into the NFRD system. This will inevitably involve more and more donors in discussing how the NFRD actually works. This issue may be anticipated by asking a general question of the donors: what kind of procedures currently in the NFRD might make the fund more or less attractive to them?

Issue 6: Grant mechanism to fund regional development activities, in addition to public procurement mechanism for RDAs

Main Findings

There are usually two possible ways how to finance the regional development activities – (i) support those public investments and development activities (eg labour market support) undertaken by public bodies directly (i.e. themselves with their own internal capacities) or indirectly, through procuring the services, supplies or works of outside contractors and providers and (ii) provide limited financial support of a non-reimbursable kind (grant) to bodies outside the public administration system but whose activities can contribute to RD public policy objectives. There are some intermediate cases (eg partial grants to public bodies which must them provide some co-finance from their own (tax) revenues) but we do not deal with these here.

Because different public regional actors such as RDAs, rayons or communities play a massive and primary role in regional development in Moldova, direct transfer of financial resources from the State Budget to these subjects is used as a main tool in the current system in Moldova. This is all the more pertinent since rayons do not have any substantial resources of their own.

However, regional development is not primarily a financial transfer mechanism. It is a development process and, as such, seeks to mobilise the efforts of all relevant actors in the territory of the region in favour of its development. It seeks to deliver outcomes which the market will not or cannot easily provide. But at the same time, it is not the case that public bodies can provide everything in this area. There are specific development outcomes which the public sector need not or cannot provide and which often correspond to the efforts of citizens and civic society working in a structured manner. Many NGOs operate in this space and provide goods which are relevant to the RD process.

Moreover, situations occur where market actors, acting primarily out of motives of profit, contribute to RD outcomes, especially by creating employment. It therefore is important that RD promotes a strong market sector, especially if this does not already exist. In this situation there may arise a rationale for using public money, given by public bodies, as some form of partial subsidy to investment to enterprises or as an incentive for enterprises to improve their performance through, for example, training or better internal processes. This is a complex area of intervention requiring very clear conditions and governed by State Aid regulations.

The two examples above however point up two main cases where – outside of the public administration – a situation may arise where it is appropriate to further RD objectives by providing some form of financial support to non-public actors. This poses the question of how such "grant assistance" can and should be structured.

In such cases various grant mechanisms are used to support such activities and allow different actors to develop and submit appropriate projects. For purposes of this paper we will use the term "grant scheme" to refer to mechanisms that award non-reimbursable grant to non-public actors.

Although we understand that at the national level some grant systems are currently used – i.e. the National Environmental Fund or the Social Development Fund and although the NFRD regulation generally allows grants to be used,[8] there are no grant systems currently in place at this moment within the field of Regional Development as supported by the NFRD.

There are a number of specific or typical aspects to grants. Usually:

- a grant is not given at 100% but rather only "enough" grant is given to create an incentive for a particular actor to carry out an activity (of which, he/she is the owner)
- grants are usually given to many actors – it would be unnecessary to create a grant scheme to fund just one large project (which in any case is unlikely to be undertaken by non-public bodies). Usually grant schemes seek to incentivise many bodies to carry out (usually) small activities and the aggregate of these activities constitutes a RD outcome (e.g. many NGOs carrying out information and training services to excluded groups; many enterprises investing in new machinery which makes them and the region more competitive)
- in the specific case of enterprises, it is illegal (under EU legislation and probably in the eyes of all donors) to provide 100% grant to an enterprise for anything. Practically most grants to enterprises are rarely above 50% of cost (issue of State Aids legislation)
- grants are sometimes given to encourage new forms of development activity and therefore may encourage innovative approaches. As such grant schemes can often support innovative practice.

It should be noted that in the case of grants, the actual "results of the project"- whether these are physical assets, training materials, strategies or whatever - are the property of the beneficiary, i.e. the body that received the grant (and usually) provided a part of the co-finance itself.

Options or solutions

The grant system to support different actors including private entrepreneurs and NGOs to develop and implement regional development activities can be setup in a several different ways. These are distinguished according to how and at which level the projects are selected.

1. There can be provided **direct support to strategic projects** which are agreed according to a regionally based, extensive consultative process, and not in a competitive call for proposals. The consultative process has to be is transparent and has to involve all key regional actors. This option, though it can be used for distributing grants, is more usual

[8] The Regulation on NFRD, Article 12,

for public investment projects which means that the grant system is not usually necessary in this case.

2. **Grant schemes** can be established either at national or at regional level. Grant scheme is a system, where the administrator sets narrow set of rules, including objectives and expected results, in a certain problem area and then launches a call for proposals for potential applicants. There are different types of grant schemes:
   - GS for a certain regions (for example GS for communities in area hit by floods, or communities within a certain region with unemployment higher than 40 % etc.);
   - GS for a specific types of activities (GS for community marketing activities in specific region or nationally set up); and,
   - GS for a specific target group (GS for NGOs providing services for disabled people, eligible for all regions or just launched in a specific region).

When using the grant scheme, the amount of money for the scheme shall be decided upon in advance. For example, the Ministry can announce that it will use 50 mil. Lei to launch the call for proposals to support infrastructure projects in the next year and the relevant body, i.e. the Parliament, will approve this amount as a part of the NFRD budget line, and the call for proposals will be launched afterwards for the stipulated sum of mones, or there is no universal and exact rule (or set of rules or criteria) to decide which way/form of grant scheme shall be used. The type of grant shall be always chosen according to the problem identified or objective that should be achieved. Nevertheless, a general guidance can be provided.

Altogether, grants help motivate and support different regional actors, to take their part in the regional development along with public bodies. When introducing a grant mechanism the ministry should keep in mind several issues that needs to be clarified before the system will be established.

Targeted priorities and target groups – Any grant mechanism needs to have a clear objectives and priorities. From the point of view of transparency it is necessary to have a clear and if possibly very detailed criteria set up for projects selection so that everyone can see from the very beginning what kind of project will be favoured.

Size of Project – it is important to indicate the number and size of projects that may be funded. Many funding bodies are afraid to do this. They claim it is too risky. But in fact it is often risky not to do this. There is no need to be fully prescriptive but rather indicative: e.g. it is envisaged that the likely size of most projects will range from 30-100,000 and that in all probability no more than around 30 projects will be funded. Or alternatively indicate the likely level of monies to be disbursed under the scheme which with an indication of size will allow applicants to measure their chances.

Effective and user friendly implementation system – one of the most important part in the preparation of grant mechanism is the implementation system. According to the target group described above, the ministry should setup a management system that should on one hand be as much effective as possible to avoid a bureaucracy, on the other hand should be user friendly (give advance information, not require too much documentation etc)

Also in cases where the support will be aimed to activities like social services etc. it would be also best to have the implementation at the lower so that the applicant won´t have to travel to the central administration authorities.

The implementation system should therefore consider also a regional subsidiaries/ implementation bodies in certain areas, such as RDAs.

Project pipeline -It should be also ensured that the target groups are ready to apply within the call for proposals and that they have enough projects ready or they will be able to prepare the projects. This is best done through some form of support to project development, perhaps upstream from the actual launch of the scheme. The current "Partners for Projects" initiative undertaken by MDRD project provides a model for this.

Effective system of control – when introducing grant mechanism, it is also necessary to have a clear idea how and who will control that the applicants use the funds in line with the rules of the particular mechanism. The ministry should therefore have a clear idea how all applicants will account for the grant given and how the accounting will be controlled. It should be also clarified in which cases and how the applicants should deal with public procurement requirements.

Recommendations

As a basic suggestion the MCRD and all other relevant ministries should consider adjusting the financing system, so that also system of grants will be allowed.

The system should be adjusted because current system of transfers of financial means to public bodies is suitable just for some kind of projects and applicants; that's why it is suitable for solving limited kinds of problems.

Grant scheme systems should be considered especially for regionally targeted interventions where communities, NGOs or businesses will be supported. In many cases there is a need for a system of support for smaller initiatives implemented by NGOs and the private sector that will complement or optimise the impact of larger projects funded through different modalities (e.g.. marketing, training etc.). The system may also be suitable for funding preparatory works of (larger) projects, such as feasibility studies, technical designs etc.. The ministry should therefore have a tool to support such type of projects. As the system should be also opened to NGOs or private entrepreneurs, a change in the respective laws will likely be needed..

Because there is unlikely to be enough financing for many grant schemes at this moment, the system should be pilot tested – perhaps as a support to smaller activities that complement other, larger projects in the regions or that target very specific needs.. The RDAs could take over the preparation and implementation of a grant schemes, focused on regional problems subsequent to implementation of a successful pilot.

We would not envisage that in the foreseeable future more than about 10-20% of all NFRD monies should be considered for grant schemes since there remain many needs directly incumbent on public authorities.

Finally it is strongly recommended to keep NGO grant schemes fully separate from Enterprise Grant Schemes. These latter are intrinsically more complex, require a lot of expertise and are governed by State Aids rules.

Issue 7: Other Activities funded by the NFRD

Main findings

Under the current call for proposals, funding is provided mostly for investment projects. Initial discussions have shown that activities to prepare investment projects (such as designs, studies, even project development) should also be considered eligible, at least in case of small beneficiaries with low or missing capacity (including financial capacity) or in case of large projects where technical design and preparatory work are very costly.

Regional development is not just about infrastructure projects, it can also extend to studies and other soft measures related to regional development such as strategic planning, training and project development or other support activities such as marketing activities and capacity building.

Options or solutions

Making provision for project preparation especially for technical and economic/financial studies is essential, since otherwise there will not be enough adequate projects prepared. It is evident this is already a real problem in Moldova.

There is also the additional problem of ensuring that enough resources are available for supporting capacity building to development processes (Issue 2 Project Development Paper). For this we recommend that donors be mobilised to support this through projects focused on the RDA. From the interviews as well as from the information available it is clear that the capacities and skills of local/regional actors are very limited. It is therefore recommended that the support system should focus on supporting the capacity – skills improvement, knowledge acquiring, new competencies development – of regional actors.

Recommendations

As a general rule we recommend that the RDA manage a small financial allocation derived from the NFRD) corresponding to a TA priority within each RDS. This should be used for two principle purposes:

a) financing and contracting out specific studies required for those projects whose concept is proposed to the RDC and which are deemed to merit this support

b) capacity building activities requiring external expertise and resource.

The RDA should seek approval from the RDC for any expenditure proposed under either of these categories. Activities at (a) should be synergetic with proposals in Project Development Paper Issue 1 (project concept and regional project process).

The .activities at (b) should ideally seek to mobilise donor support as well as a small allocation from the NFRD.

The RDA should be responsible for tendering and contracting this form of assistance. Over time it may be appropriate to allow beneficiaries access to small grants through which they can tender/contract external experts to assist project development. However Moldova is currently in the situation where it is essential to establish appropriate standards and practice for economic and financial analysis of projects, environmental impact assessments etc and until this is done, it would be unwise to leave recruitment of experts to beneficiaries.

Issue 8: Financial contribution of beneficiaries

Main Findings

Currently the state provides 100% of project financing. This can have an adverse effect, as beneficiaries are not necessarily fully engaged or responsible in the project implementation (construction) phase.

According to European experience this can also lead to situation that the applicants do not have any reason to prepare economically effective projects that use only the best value for money solution

Another issue is a support for international projects such as cross boarder projects that are asking for financial contribution but the Moldova partners are often in a situation that they do not have enough financing on their own.

On the other hand it must be recognised that regional and local bodies, including public bodies, currently have almost no capacity to provide any significant co-financing.

Options or Solutions

The co-financing system asking beneficiaries to provide match or co-funding should be approached very sensibly and should take into consideration the financial possibilities of local actors as it could lead to a discrimination of mainly smaller subjects that do not have enough financial means.

In such cases, even project preparation is very costly for such applicants and no other financing should be asked otherwise there are unlikely to be any projects ready in regions or priorities where small applicants are supposed to be the one who should prepare and implement projects.

In order to strengthen the buy-in of beneficiaries the possibility of in-kind contribution could be considered. There are many cases how to approach this issue; however in all cases the ministry should consider whether the in-kind contribution will really lead to the improvement of the applicant's involvement or whether it will just increase the bureaucracy for the applicant and the ministry itself.

For example when the applicant will provide itself technical documentation, it could be accepted as it is understood that the applicant has in fact already contributed to the project. On the other hand when the applicant suggests that he will use staff costs of his accountant, it is questionable whether this will increase the applicant involvement as he needs to pay the accountant even in case that he does not have any projects.

Generally when introducing any co-financing system, the ministry should consider following issues:

- The more the system would be open to other projects than top strategic or priority projects, the more the system should be balanced, so that only "necessary" and sustainable projects will be proposed and financed. The system should therefore ask for financial or in-kind contribution based on what kind of projects are to be supported.
- To set up a system of financial contribution for regional development projects by local beneficiaries (rayons, communities), there should be knowledge of the available financial means at the local level so that the requirement of financial contribution will not exclude (small, poor) local communities or will not disadvantage them in preparation of projects. It is important to bear in mind that such small communities, NGOs and other applicants are often even unable to gather enough resources to prepare the necessary technical documentation so the system should not ask financial contribution in priorities, calls for proposals and grant schemes where such small applicants are supposed to apply for support..
- In some cases also "in-kind" contribution should be considered due to the fact that the local communities and regions have limited financial resources. In such case the system could also accept contribution for example in terms of provided land for the project development etc.

There is also an issue how to support potential applicants that are planning to participate on international projects such as cross-borders projects or European initiative projects once they will be opened also to Moldova applicants.

In such cases the applicant needs usually between 10-25 % co-financing of the total costs. International projects often require pre-financing which leads to situation that many of potential applicants won't be able to participate at all. Unlike the pre-financing of projects, the national contribution to international projects can be covered by the NFRD within the framework of the regional development policy. However the NFRD Regulation does not seem at this moment to allow such a match funding.

Recommendations

The in-kind contribution should be made possible in the grant system in case the interventions will be planned to require the beneficiaries to contribute financially when implementing the project. If that is possible a clear system should be set up, how this type of contribution would be controlled and administered. To allow this, following legislation should be changed or adjusted:

- Existing legislation would have to be changed including Article 6 (6), Article 8 (4), and Article 12 of the Law on Regional Development in the Republic of Moldova.
- Existing regulation would also have to be changed including Article 9 (4) (6) of the Framework Regulation on Regional Development Agency.

Also to support the participation of Moldova partners at international projects a specific support tool should be introduced to help the potential partners with the co-financing of such projects.

The best way to do that is to reserve a specific amount of NFRD financial means for this purpose and allow each successful participant which will succeed with his application in any international project to apply for a support for the co-financing. As most of the international grants are opened just for public bodies and NGOs there is no problem with the support to private companies and the ministry should therefore consider giving to the applicants all remaining 25%-15 % co-financing as they will have to pay already all the preparatory costs and secure the pre-financing for the projects, if necessary.

There is no need for any competition within this support system as the projects have been already competing with other projects when "fighting" for the support at the international level and the ministry will already support the successful ones and therefore the ones that fits the international selection criteria and priorities. Applications could be made to the RDA/RDC who should annually dispose of a small amount to co-finance such projects (no more than about 400,000 EUR). RDS and ROPs and SPDs to formalise this simple mechanism.