STREAMLINING THE BUDGET PROCESS BY PRIORITIZING PUBLIC INVESTMENT PROJECTS

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Abstract:
The substantiation of the state budget for 2014 has also considered some measures to improve budget planning activities by prioritizing public investment projects. The prioritizing approach of public investment projects in the budget process is a particularly important and complex one, involving a set of coherent and responsible evaluation, selection and prioritization activities of such projects based on a well defined prioritizing criteria and mechanism. It was started in 2012, unfortunately not as an undertaking of public decision makers in Romania, but as a requirement of the World Bank and International Monetary Fund in order to improve the budget process. The reason is the fact that not considering public investment projects a priority produced negative effects on the budget process, on the whole Romanian economy after the events of 1989, characterized as a lack of vision in terms of the public investment approach. Unfortunately, these negative effects persisted after Romania joined the European Union and has resulted in the low level of access to funds.

Key words: *budget planning, public investment, prioritizing investment projects, sustainable development, prioritization mechanism*

1. Introduction

In the sense of European regulations (regulation (CE) No. 2.223/96 of the European Council in June 25, 1996, with its subsequent amendments and supplementations), "public investment is the investment made by or on behalf of a central public authority, of a local public administration in the case in which the project is co-financed from funds allocated from the state budget through national programs or of an economic operator over which the State has control and is reclassified in the government sector". A public investment scheme is held also by investments achieved from bank loans guaranteed by the state, as well as investments that are the subject of a form of public-private partnership (in Romania, based on art.6 from Law no. 178 from October 1, 2010 about the private-public partnership, through the private-public partnership contracts, liabilities can be transferred to a private company, which are a form of private-public partnership such as: design, starting with the technical design phase, construction, development, rehabilitation, operation, maintenance, financing an investment objective).

After the events of December 1989, the public investment approach in Romania lacked vision, negatively affecting the budget process, namely the efficient allocation of public financial resources. Following this reality, at the request of external donors (EC, IMF, WB), the process of prioritizing public investment projects has been started by analyzing support documentation - pre-feasibility studies, feasibility studies, technical and economic memoranda or substantiation notes - for the purposes of readiness assessment of projects and mainly of their affordability and sustainability.

Without doubt, the approach is necessary and at the same time complex given the multitude of project proposals made by the main credit release authorities, who after prioritizing the significant ones, these are to be approved by the Government through memorandum. In our opinion, in order to give more strictness to the approach, it would be important that the document is approved by the legal authority.

The approach underlines the effort to align Romania to the practice of developed European countries, concerned with the issue of ensuring an efficient management of public investment. For example, in Italy, the Public Investment Evaluation Unit operates within the Ministry of Economic Development and provides technical support to governmental entities in programming public investment projects and investment prioritizing in the UK is carried out by the Treasury Department.

2. The Need for and Benefits of Public Investment Project Prioritization

Public investment in Romania requires a rigorous evaluation, selection and prioritization process if we consider that it decreased in the years 2012-2013, motivated by the fact that the allocated amounts were adjusted negatively in a context where the budget revenue performance was low and investment financing from European funds did not offset the reduced investment from the state budget. The risk of recording a low absorption rate of EU funds persists in 2014, if we consider that the new programming cycle is not rigorously prepared even if in the approved budget for 2014 there is foreseen a growth of 6.2% of GDP compared to 5.1% as was provided in 2013.

From the stated perspective, a correct evaluation and selection, followed by significant investment prioritization of public projects for their admission to funding, is necessary because, currently, projects that funding is applied for are in excess (about 5000) and most of them have little chance of implementation given the limited public resources (for example, in the budget on 2014, there are included 104 significant public investments that meet the analysis conditions regulated by OUG 88/2013, and the estimated time for finishing these would be 12 years, a time exceeding a way long the medium horizon of time estimated for finishing this type of projects, namely three-five years, http/zf.ro, accessed on 06.03 2014). Moreover, some of them are not in line with the national strategic priorities, they have a minimal impact on the economy and are no longer justified in terms of appropriateness and necessity.

In the expressed sense we find the conclusions of the World Bank, which has identified the main reason explaining the low level of absorption of structural and cohesion funds as the inefficient management of public investment projects, namely projects underfunding and long service implementation.

Aspects inconsistent with what sustainability means by financing public investment projects appear in the substantiation note accompanying the draft rules concerning the prioritization of public investment projects (HG (project), about the methodological norms regarding public investment project prioritization, published Mar 3, 2014 on mfinante.ro, accessed on 10.03.2013, approved through HG no.225/26 March 2014 for approving methodological norms regarding public investment project prioritization published in the Official Gazette no. 0249 from 07.04.2014), which states that, by doing so, it aims to increase the efficiency of the mechanism for prioritizing objectives of public investment, given the constraints of the fiscal space, the increased transparency in the decision to allocate investment spending and the need for close monitoring of their implementation.

Public investment projects prioritization is a necessary step due to the following reasons:

- The new and on-going public investment projects portfolio to be financed from public funds should be linked to government priorities through systematic approach for the coherent managing of public investments in Romania;
- Public funding should consider projects with high economic and social benefits a priority, for which to ensure achievement conditions within the time limit and public funds limit provided each year, according to the fiscal budgetary strategy and the fiscal framework;
- To reduce the risk of delays in the implementation of public investment projects;
- To strengthen the central decision-making process regarding public investment coupled with the potential of annual budgets and the institutional capacity of public entities to manage public investment projects.

The advantages of public investment project prioritization are given by the fact that:

- they provide conditions for the creation of an efficient management system of public investment (public investment management is formed from a series of legislative acts - laws, GOs, regulations, orders and procedures – that regulate organizing and monitoring means of the public investment process), through which to manage public investments in Romania by setting the steps to follow and the institutional framework responsible for prioritizing them for funding;
- they correlate objectives of public investment projects with national objectives in a given period of time required for implementation: and, very important, with public funds from the state budget each year, according to fiscal budgetary strategy and the fiscal –budgetary framework;
- they ensure rigor and strengthen the decision making process at government level regarding public investments contained in the budget process;

- they contribute to strengthening the institutional capacity of public entities to develop, substantiate, evaluate and implement public investment projects;
- they impose a code of identification of investment projects which the Ministry of Finance allocates to a project, having the role of identifying and rigorously monitoring project progress in the management system of public investment in the substantiation and execution of the state and local budgets.

3. Classification of Public Investment Projects, Principles and Prioritization Criteria

From the considered statements, there results that the legislative incident act (OUG No. 88 September 18, 2013 about adopting some fiscal budgetary measures in order to fulfill the commitments agreed by international bodies and the amending and supplementing of certain acts, published in the Official Gazette no. 593 from September 20, 2013) is important in that public investment projects are ranked in the public investment program based on overall records, ensuring their transparency and monitoring.

From a technical standpoint, investments in the “C” category: “other investment expenses” and public investment projects in the national defense, public order and national security, whose particularization contains classified information are exempted from the prioritization procedure. Public investment projects as a result of regulations issued by specific legislation (Ibidem,chapter II art.40) are classified into three groups as follows:

- ***Significant public investment projects*** with a total estimated value of over 100 million;
- ***Average public investment projects*** with a total value estimated at 30-100 million;
- ***Low public investment projects*** **-** the total estimated value below 30 million.
- In connection with this classification note that, by detailed rules, public investment projects can be classified into categories based on the manner of implementation, and the level of risk in relation to project objectives.
- Principles and criteria established for prioritizing significant public investment projects are:
- ***Project opportunity*** having as analysis criterion the relevance of project objectives in the context of national or sectorial strategies;
- ***Social-economic justification of the project***, justified by supporting documents: pre-feasibility studies, feasibility, technical and economic memoranda, substantiation notes, that concern the impact on the environment, according to specific legislation.
- ***Affordability and financial sustainability,*** having the following analytical criteria: the need for funding the project realistically estimated and correlated with the

resources available to affected sector, how the public investment project meets the requirements of Law 500/2002 on public finances (art.43 line(9)), or, as appropriate the requirements of Law 273/2006 on local public finance (art. 45 line(2)), the level of co-financing from the state budget and the quality of financial arrangements to cover the operating and maintenance costs after project completion;

- ***Arrangements for the implementation and deployment performance***, having as criteria: the degree of maturity in project preparation (substantiated technical economic indicators, documents of ownership, lease, etc., how to define progress and performance indicators for the monitoring and evaluation of project and the existence of a project management structure to ensure implementation progress and respond to it.

In complementing these principles relating to new projects, on-going projects below prioritize on the basis of an ***additional principle*** which has as criteria: the time remaining until the project finishes, the time remaining for implementation and especially the associated costs arising from a possible restructuring, suspending or closing a project.

4. Roles and Responsibilities in Prioritizing Public Investment Projects

In the prioritization process of significant public investment projects, a major role is played by the Public Investment Evaluation Unit within the Ministry of Finance which provides the technical secretariat and performs the following tasks:

- Pre-feasibility study analysis, technical economic memos or substantiation notes in terms of affordability and sustainability of proposed projects to financing;
- Assessing the readiness and maturity of public investment projects;
- Analysis of the main credit release authorities for including investment projects in the annual budgets following prioritization;
- To propose to the ministry for the approval or rejection as appropriate, of the credit release authorities request to pass to the drafting stage of the feasibility study, except that, without the approval of the Ministry of Finance they will not be able to get to this stage.

In relation to the government and the authorizing officers, the Ministry of Finance has the role of managing the flow of information to ensure the consistency of the public investment prioritization process (see art. 45 from OUG no. 88 from September 18, 2013 line(1), which states that the Ministry of Public Finances presents the prioritization results to the government until June 30, respectively September 30 of each year, with a view to approving by memorandum the list of prioritized projects and line(2), which regulates that the main credit release authorities are to send the Public Finance Ministry the list with prioritized investment projects until May 15, respectively August 15 of each year, the latest), within the time limits set by the budget calendar.

5. Capital Investment Planning and Budgeting at the Local Level

The prioritization of public investment projects should bring clarification, support and coherence to the multi annual investment planning that is carried locally as **current practice for the preparation of multi-annual programs and investment budgets beneficial on sustainable local development**.

Also, the entire process must be integrated into specific legislation in the field of public finances (Law 500/2002 about public finances and Law 273-2006 about the local public finances) and fiscal and budgetary regulations provided by the law on fiscal budgetary responsibility (Law 69/2010 which imposes the following restrictions to the public investment process: investment allocations to other destinations will not be purchased during budget execution, public institutions will set multi-annual spending limits and the Government's development of the fiscal strategy until May 30, each year for the next three years).

Multiannual investment requirements at local level meet a set of tools called ***"CIP Toolkit"*** applicable to local communities that, by the resulting document, ***the plan of capital investments***, as a management tool within the reach of local government, having legitimacy by nature of stakeholder endorsement, support the investment process in the private sector as well.

The multiannual programming toolkit involves the following steps:

- Determining the organizational structure of an interdisciplinary working group;
- Establishing work procedures and personal instructions;
- Evaluation of investment needs;
- Analysis of local financial capacity;
- Preparation and analysis of applications that propose projects for funding;
- Setting priorities for local investment;
- Evaluation of financing options;
- Developing the investment program and budget;
- The publishing to debate of the draft of the Capital Investment Plan;
- Approving the investment plan and budget;

The toolkit has been proposed by GRASP experts (The GRASP program („Governance Reform and Sustainable Partnerships" – Reforma administraţiei publice locale prin parteneriate durabile) has proposed, starting with **July 2003**, technical assistance packages for capital investment planning and budgeting at the local level) as a result of assistance programs conducted under the authority of the U.S. Agency for International Development - USAID).

The benefits of planning and budgeting the capital investment is demonstrated by the fact that:

- It provides local sustainable development of communities through the development of local programs of investment in the social infrastructure, education, transportation, waste management, water and sanitation supply networks, etc.;
- It puts in direct relation public investment with development programs of economic operators and with national strategies;

- It correlates a community development objectives with its financial capacity based on financial planning;
- It provides information to residents and stakeholders on the needs and investment objectives and contributes to the public support for investment projects;
- It strengthens the financial credibility (creditworthiness) and provides stability by controlling taxes, while avoiding unanticipated loans and maximizing the range of alternative financial options;
- It identifies the most efficient and most economic sources of financing investment objectives.

6. Conclusions

Through the regulatory legal framework created to prioritize the significant public investment, rigor and effectiveness is added to the budget process. The approach is necessary to ensure the viability of public investment projects financed from the state budget and local budgets and to produce economic and social effects in conjunction with the standards expected for sustainable development in an optimal time.

The prioritization is important due to the fact that:

- It ensures greater transparency in the decision to allocate public funds;
- It provides public decision makers with a mechanism for prioritizing the significant public investment, which should be extended to medium and small projects for public investment, to finance with priority efficient projects and to suspend the non-performing;
- It details and regulates unitarily the evaluating process of the degree for preparing a new public investment project and introduces specific elements of analysis of their effectiveness based on some economic performance indicators (indicators of cost / benefit) and social utility (indicators of cost / utility);
- It considers identifying financing opportunities for investment project from other sources than the state budget (European grant funding, public-private partnerships, etc.)
- It establishes elements of analysis and evaluation or re-evaluation of the excessive portfolio with public investment projects with a view to finance the significant ones who meet the minimum score of freezing/waiver bad projects as appropriate;
- It provides opinion leaders, civil society and especially budgetary obligation payers with a transparent set of information needed to analyze the efficiency of the budget process.

The success of the prioritization process for funding and implementing public investment projects, subject to the limits of expression of the state budget remains dependent on how it will ensure consistency, stringency and independence towards political factor interference, detrimental to their correct evaluation on the basis of economic and social targets.

7. References

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