

**LITHUANIA'S CAPACITY TO ABSORB THE EU STRUCTURAL AND
COHESION FUNDS ASSISTANCE**

Summary

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Vilnius, 2002

DESCRIPTION OF THE PROJECT

The main purpose of the project was to:

- Determine the additionality basis, or the amount of Lithuanian public or equivalent structural expenditure made during the period of 1999-2001;
- and
- Determine Lithuania's co-financing capacity after accession to the EU according to investments made during the period of 1999-2001 from main sources of state and municipal expenditure eligible under the Structural funds and the Cohesion fund.

ACTUAL RATE OF CO-FINANCING THE EU STRUCTURAL ASSISTANCE

Principal co-financing ceiling of the EU Structural funds assistance for Objective 1 regions is 75 per cent of the total eligible cost. In member states covered by the Cohesion fund and certain other regions the co-financing rate can be as high as 80 per cent of the total cost.

However, within these ceilings the co-financing rate can vary according to other criteria:

- with regard to investments in private enterprises under state aid rules, a maximum rate of assistance from Structural funds is 35 per cent of the total cost. Taking into consideration co-financing from the EU member state, a highest rate of public assistance to private enterprises can be around 47 per cent (may be higher for SMEs and other cases), while the remaining percentage of the project cost should be covered from own sources of private enterprises;
- with regard to investments in infrastructure generating substantial revenue (at least 50 per cent of the project cost), a maximum of 40 per cent of the total eligible cost (50 per cent in the member states covered by the Cohesion fund).

Hence, due to the aforementioned limitations, but also because of the fact that not always all expenditures are found to be eligible, an average rate of Structural funds co-financing in the EU member states, which are covered by the Cohesion fund, reaches about 2/3 thirds of the total eligible cost.

DRAFT PROPOSAL TO LITHUANIA CONCERNING THE NASCENT ASSISTANCE OF THE EU STRUCTURAL AND COHESION FUNDS IN 2004-2006

In the draft financial proposal by the European Commission to the candidate countries we find that the estimated total structural assistance to Lithuania in 2004-2006 stands at **1485.05 mln euro**, of which:

- **579.52** mln euro – from the Cohesion fund (average between lower and higher brackets),
- **871.67** mln euro – from the Structural funds for the Objective 1 programme, and
- **22.16** mln euro and **11.70** mln euro from Community initiatives INTERREG and EQUAL respectively.

As previously mentioned, an average rate of Structural funds co-financing in the EU member states, which are covered by the Cohesion fund, reaches about 2/3 thirds of the

total eligible cost. Therefore, to absorb the indicated 1485.05 mln euro (i.e., 2/3) of the EU structural assistance, Lithuania would have to invest approx. 731.44 mln euro (i.e., 1/3) of national co-financing. Hence the estimated maximum national co-financing of Lithuania stands at **2525.52 mln Litass in 2004-2006**, or **841.84 mln Litass on average annually**.

FINDINGS OF THE RESEARCH

Lithuania's co-financing capacity

The research revealed that the amount of state and municipal expenditure, which may be eligible for co-financing the EU Structural funds and Cohesion fund, is 5 373 mln Litass. Hence the annual average stands at 1 791 mln Litass, which exceeds the estimated co-financing requirement (i.e., 841.84 mln Litass) by 949 mln Litass. Therefore, the study concludes that potential Lithuania's co-financing capacity to absorb the EU Structural funds and Cohesion fund should be sufficient, provided that eligible national expenditure is allocated for co-financing purposes.

However, the distribution of eligible expenditure according to sectors of the economy is not in line with the situation of EU Cohesion countries. For instance, eligible assistance to industry and business (including both direct assistance to private enterprises and support for business infrastructure) amounts to 81.3 mln Litass, i.e. only 1.5 per cent of all national eligible expenditure. To compare, in Portugal assistance to the private business under state aid schemes (business infrastructure excluded) amounts to about 25 per cent of all expenditure by the EU funds.

Moreover, after accession to the EU Lithuania will receive about 579.52 mln euro from the Cohesion fund (average between highest and lowest brackets), which would amount to about 40 per cent of all the EU structural assistance to Lithuania. It is expected that 50 per cent of this amount (or 290 mln euro/ around 1 000 mln Litass) will be allocated for the environmental sector (water/sewage, waste and air measures). According to the analysis, expenditure eligible to co-finance these measures in the period of 1999-2001 amounted to 4.5 per cent of all national eligible expenditure and comprised 241.6 mln Litass in total. The revealed co-financing capacity is not sufficient – at least 334 mln Litass (or 1.5 times more than was available during the period of 1999-2001) should be allocated to co-finance the EU Cohesion fund assistance in the area of environment alone (i.e., without regard to how much more might be needed to co-finance relevant Structural funds' assistance). However, it should be noted that expenditure for environment is increasing after 2001, mainly due to the support from the ISPA pre-accession instrument.

(in thousand Litas)

	1999	2000	2001	Total	Average
1. Infrastructure	1 289 530	985 551	991 011	3 466 490	1 155 497
<i>1.1. Transport</i>	605 330	484 744	332 296	1 422 370	474 123
National and regional roads	124 844	109 617	36 239	270 700	90 233
Local roads	219 910	222 574	74 756	517 240	172 413
Railways	165 959	74 159	85 614	325 732	108 577
Air transport	23 656	14 297	14 808	52 761	17 587
Water transport/port	70 961	64 097	120 879	255 973	85 324
<i>1.2. Telecommunications</i>	2 172	3 075	1 207	6 454	2 151
<i>1.3. Energy</i>	431 344	342 722	460 514	1 234 580	411 527
District heating	91 534	47 840	73 124	212 498	70 833
Gas	16 076	32 434	22 557	71 067	23 689
Electricity	271 469	213 517	314 591	799 577	266 526
Oil	0	0	0	0	0
Ignalina NPP	52 265	48 931	50 242	151 438	50 479
<i>1.4. Environment</i>	96 992	75 022	81 468	358 650	119 550
Water and sewage	38 542	32 402	38 365	214 477	71 492
Solid waste	5 179	8 695	10 458	24 332	8 111
Air quality	189	534	2 081	2 804	935
Natural resources	900	218	519	1 637	546
Drainage	52 182	33 173	30 045	115 400	38 467
<i>1.5. Health care</i>	66 552	23 525	61 819	247 126	82 375
<i>1.6. Urban infrastructure</i>	87 140	56 463	53 707	197 310	65 770
2. Human resources	502 870	370 232	536 069	1 435 964	478 655
<i>2.1. Science and education</i>	275 636	260 629	278 936	815 201	271 734
<i>2.2. Training and employment</i>	75 783	63 915	91 995	231 693	77 231
<i>2.3. Research and development</i>	136 633	14 563	120 987	272 183	90 728
<i>2.4. Information society</i>	3 700	10 199	26 926	40 825	13 608
<i>2.5. Sport</i>	5 007	5 476	4 486	14 969	4 990
<i>2.6. Culture</i>	6 111	15 450	12 739	61 093	20 364
3. Productive sector	180 030	155 331	120 806	456 167	152 056
<i>3.1. Agriculture</i>	130 803	106 863	74 294	311 960	103 987
Agriculture and rural development	123 984	97 250	68 203	289 437	96 479
Fisheries	6 819	9 613	6 091	22 523	7 508
Forestry	0	0	0	0	0
<i>3.2. Industry and business</i>	24 239	32 278	24 827	81 344	27 115
<i>3.3. Tourism</i>	24 978	16 187	21 685	62 850	20 950
<i>3.4. Other services</i>	10	3	0	13	4
4. Other	3 656	6 234	4 301	14 191	4 730
Total:	1 976 086	1 517 348	1 652 187	5 372 812	1 790 937

The distribution of eligible expenditure between the levels of central government (the state budget, the Privatisation Fund, loans on behalf of the state and guaranteed by the government, own revenues of state-owned enterprises) and local governments (municipal budgets, loans by municipalities and municipal enterprises, municipal extra-budgetary funds, and own revenues of municipal enterprises) represents a 9:1 ratio with very small

annual deviations from the average (in 1999 - 89 per cent, in 2000 – 90 per cent and in 2001 - 90 per cent national expenditure came from the central government).

Determination of the additionality basis

Additionality basis (financial table summarising national public or other equivalent structural expenditure in Lithuania as nascent Objective 1 region) was a result of calculations, based on a stricter interpretation of the eligibility (e.g., ability to prove, that expenditures were eligible indeed) as well as methodological remarks presented by the European Commission in Working paper no.5 “The verification of additionality for Objective 1”. Notwithstanding, the following table represents an estimation. Final version of the additionality calculations will be available when the draft Objective 1 Single Programming Document for Lithuania is ready, as it will become clear then which categories of expenditure ought to be included.

(in thousand Litass)

	Annual average 1999-2001		
	National/ Central level	Local government and public enterprises	Total
1. Basic infrastructure	445 247	322 732	767 979
Transport	258 431	117 529	375 960
Telecommunication	50	1 042	1 092
Energy	41 608	178 025	219 633
Environment and water	86 795	23 857	110 652
Health	58 363	2 279	60 642
2. Human resources	330 575	6 268	336 843
Education	206 345	5 108	211 453
Training	56 235	1 126	57 361
RTD	67 995	34	68 029
3. Productive environment	112 317	1 150	113 467
Agriculture/rural development/fisheries	77 747	162	77 909
Industry	19 277	706	19 983
Services	3	282	285
Tourism	15 290	0	15 290
4. Other	39 766	23 104	62 870
TOTAL	927 905	353 254	1 281 159

Therefore, it was estimated that additionality basis (years of reference: 1999-2001) in Lithuanian case amounted to 1 281 mln Litass annually (1999 prices); while it was already mentioned, the national co-financing requirement in 2004-2006 constitutes 842 mln Litass per year (1999 prices). Moreover, calculations are based on the very unfortunate years, when due to fiscal difficulties, that appeared as a result of Russian crisis, public expenditure has been substantially curbed. Therefore, it is very likely that, as situation

improves, when calculations are repeated with 2002 (and probably 2003) taken as a year of reference, the additionality basis to be declared in the draft SPD is going to be larger.

RECOMMENDATIONS

Although the very potential to co-finance the EU Structural funds and Cohesion fund assistance is sufficient, national expenditures intended to be used as such co-financing still have to be allocated and used in an effective manner. That is, if Lithuania actually is to use these expenditures (which in general are eligible to be used for that purpose) as co-financing after 2004, it is necessary to foresee the relevant measures in the SPD and to ensure a sufficient “project pipeline”: these factors play an important role in determining the absorption capacity.

Since development of larger projects (from project idea to fully documented project, ready for implementation) may take more than a year, the building of “project pipeline” shall start as soon as possible, so as to enable to start the implementation of such projects already in the beginning of 2004. Moreover, it is important to note that many projects to be financed under the SPD will be of comparatively small size (i.e., smaller infrastructure projects, structural assistance to farmers or SMEs). Considering the experience of the EU member states, it could be estimated that Lithuania would need to prepare about 1000 projects (of which 20-40 projects – to be finance from the Cohesion fund, which supports projects larger than 10 mln euro).

At the same time, it is important to ensure the existence of a convenient system of state aid schemes, which would serve as a background to issue state assistance from Structural and Cohesion funds. The analysis of this study indicates that the greatest need for additional national co-financing might arise in the area of productive environment, where state assistance as of this moment comprises only approx. 1.5 per cent of total eligible expenditure (while experience of the EU member states indicates that at least 10 per cent of all EU Structural funds assistance is used for the latter purpose).