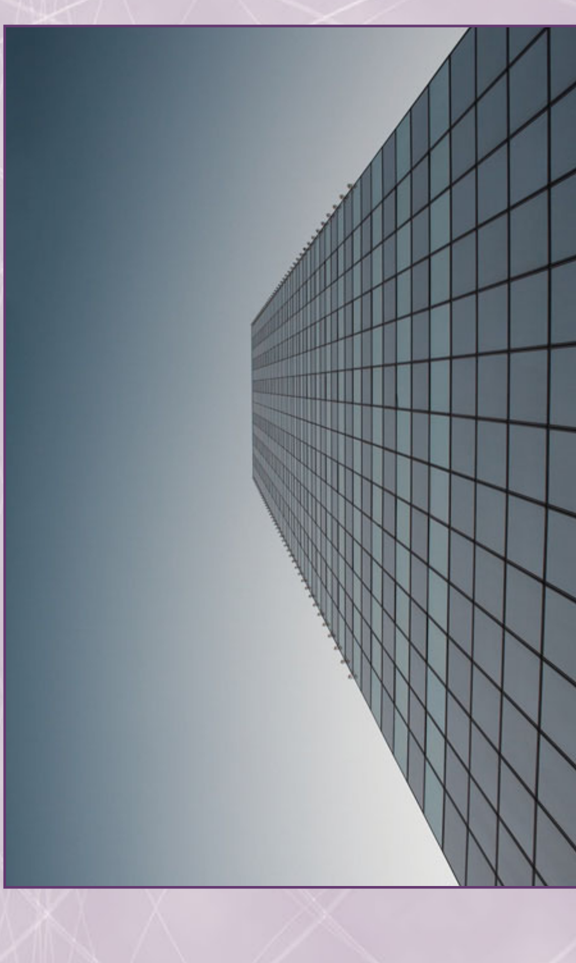
WORLD BANK WORKING PAPER NO. 115



# Administrative Capacity in the New EU Member States

## *The Limits of Innovation?*

*Tony Verheijen*



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Tony Verheijen is a Senior Public Sector Specialist in the Africa regional department of the World Bank.

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The report is part of a series of studies on current issues in public finance reform in the Central European and Baltic countries (Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia, and Slovenia—the “EU8”) which joined the European Union on May 1, 2004. These studies have been undertaken since 2005 and coordinated and edited by Thomas Laursen, Lead Economist for Central Europe and the Baltic States in the World Bank. Marta Michalska provided excellent administrative and logistical support throughout the process of preparing these studies.

# Abbreviations and Acronyms

| | |
|---|---|
| BEEPS | Business Environment and Enterprise Performance Survey |
| CAF | Common Assessment Framework |
| CIS | Commonwealth of Independent States |
| ECA | Europe and Central Asia |
| EI | European Integration |
| EU | European Union |
| HR | Human Resources |
| HRM | Human Resources Management |
| IT | Information Technology |
| OECD | Organization for Economic Co-operation and Development |
| SIGMA | Support for Improving Governance and Management in Central and Eastern Europe |
| UNDP | United Nations Development Program |
| WB | World Bank |

# Executive Summary

## Introduction and Context of the Study

The new member states of the European Union (the EU8) face significant challenges that require a strong public management system:

- The *continued* challenges of fiscal management with many of the new member states not meeting the entry criteria for the eurozone on fiscal parameters including fiscal deficit levels. This means that most states will not achieve a key policy goal which is the early adoption of the euro.
- *New* challenges of effective absorption and utilization of EU funding which will amount to up to 3.5 percent of GDP in the next financing period. This is unprecedented even when compared to earlier beneficiaries such as Ireland and Spain.
- The *future* challenge of remaining competitive inside and outside the EU-the EU8's current competitive advantage of relatively low wages combined with skilled labor will tend to be reduced as a result of economic convergence and more competition from South and East Asia.

More than two years after the enlargement of the EU administrative capacity remains an issue of concern for the new member countries. While there have been positive achievements mainly related to the attainment of EU goals these have tended to be "one-off" special efforts with considerable diversion of resources on the basis of "if it has to be done it will be" and the creation of "islands of excellence." This approach while achieving successes in relation to clearly identified objectives has not created soundly performing systems across the whole of government which will in the future ensure that in its *day-to-day management* the public sector meets the challenges it faces in an optimal fashion.

Without a strong administrative capacity states will risk not only losing the direct benefits of the structural funds but also neglecting policy agendas in other areas because of the diversionary effect of the major new task of planning and implementing structural funds on the scale envisaged. This could pose significant risks in areas that are important to economic and social development but are not included under EU funding priorities. The low uptake of funds in the current financing period (2004–06) is a reason for concern in this regard especially since the funds available in the 2007–13 period will be much greater.

A strongly performing public management system is also an essential ingredient of sound fiscal management and effective development planning which both require well developed strategic planning and policy management capacity and a stable and qualified human resource base. Responsible fiscal management and the strategic use of resources will be a key ingredient to keeping the EU8 competitive in the context of the EU. A further important element of competitiveness, the quality of public services, in particular those provided to businesses, is also determined to a significant degree by the quality of the public management system.

## The Study

Against this background, the study considers key aspects of administrative performance in three areas related to *policy, people,* and *systems.* First, in the field of *policy,* the study addresses issues of performance management, strategic planning and policy coordination and formulation. Second, as regards *people,* the study reviews human resource management practices such as recruitment and career management, incentive systems and politico-administrative relations with the aim of assessing the extent to which public administrations in the EU8 can attract and retain high quality staff in the context of rapidly changing labor markets. Finally, in relation to *systems,* the study looks into one specific aspect of public service delivery, namely the extent to which states have introduced e-Governance systems and used these effectively to enhance the business environment. A *benchmarking* exercise was conducted in each of the key aspects studied. A specific aim of the study was to identify examples of *good practice* within the region which might be replicable in other EU8 countries.

## Main Findings

The results of the study were not encouraging. The new Member States have a very mixed record in the performance of their public management systems. Whereas most states were and are effective in the management of core EU-related issues, such as for instance the transposition of EU legislation, their record in fiscal management, the planning and use of structural funds and in addressing broader issues of competitiveness remains uneven. There are, at least in part, symptoms of ill-developed management systems and the lack of an adequately skilled and sufficiently experienced civil service.

The quality of public management varies significantly between states. Whereas the Baltic States have each improved important aspects of their public sector management systems, countries such as Hungary and the Czech Republic, and, to a lesser degree Poland, have not made visible progress. Slovakia and Slovenia are both between these two extremes with Slovakia showing some interesting ministry based reforms, without having achieved progress across the system.

In relation to the three specific areas studied, the main findings were as follows:

### *Policy*

While vertical policy management on the whole was of a reasonable standard, horizontal management was—with the exception of the systems in Lithuania and Latvia—very weak. Performance management illustrated a similar pattern. The weaknesses identified in strategic planning and policy coordination in most countries in the region are of major concern not least in the context of the utilization of EU structural funding in the 2007–2013 period.

### *People*

Performance in this area was very weak across the whole region. The major problem is the unwillingness of politicians to give up their traditional relationship of power and patronage over the civil service in the interests of creating a professional merit based administration. Throughout the region there has been a retreat from the changes made pre-accession in order to meet the requirements of the acquis communautaire especially as regards horizontal management systems. *This is probably the single most serious issue identified by the study*. Incentive and management systems are generally inadequate to ensure the attraction and recruitment of high quality staff in a changing labor market which is offering more and more opportunities in the private sector and abroad. While Latvia is already seriously affected by this, it is likely to become an acute problem everywhere in the very near future.

### *E-government*

With the outstanding exception of Estonia, most countries in the region are not very advanced in the introduction of e-government systems. Poland, for example, appears very low in international rankings of e-readiness. The main reasons are a mixture of lack of strategy, institutional structure, investment and capacity.

## Benchmarking

The *benchmarking exercise* reflects these findings with most of the countries in the region receiving weak marks in all three areas of the study except the Baltic States which receive better marks in some areas often on a par with EU 15 countries (Box 1).

### *Good Practice*

It has to be said that the examples of good practice identified were few. The examples found were, however, of very high quality. They were mainly to be found in the Baltic States and were in the spheres of policy management and e-government (those identified in the field of HR were much weaker and are included with several qualifications). The examples identified are set out in more detail below.

### *Policy*

In relation to the development of effective policy formulation and coordination systems, the experience of Latvia and Lithuania stands out as a positive example. Both states have made significant progress in the establishment of state of the art policy management systems, driven primarily by the establishment of strategic planning processes, combined in both cases with a deep institutional reform of the State Chancellery.

Lithuania has opted for a top-down approach, led by the State Chancellery in close cooperation with the Ministry of Finance and rolled out throughout the central administration. Latvia has used a bottom-up approach, whereby ministries and agencies were stimulated to use policy planning tools designed by the State Chancellery, initially on a voluntary basis but from 2006 onward as an obligatory process.

The successful application of strategic planning tools has revolutionized the public management system of Lithuania. The design and enforcement of government strategic objectives and the introduction of new quality control systems for policy proposals have driven a process of qualitative improvement of policy development in line ministries and has gradually created a strongly performance-oriented public management system which can hold its own in the EU. The further roll out of the performance principles to the civil service remains to be completed. Nevertheless, the successful implementation of performance-driven

## Box 1: Benchmarking Results

| Area of study | Policy | | | People | | | | E-Gov |
|---|---|---|---|---|---|---|---|---|
| Aspect of study | Perf man | Strat planning | EI Policy Coordination | HR legislation | HR horizontal man | Politico-admin relations | Incentives | E-gov |
| Scoring system | CAF 0-5 | CAF 0-5 | Metcalfe | Sigma 1–7 | Sigma 1–7 | Sigma 1–7 | Sigma 1–7 | |
| Poland | 0.5 | 0.5 | 4 | 6/7 | 6/7 | 7 | 5 | Stage 1 |
| Hungary | 1 | 1.5 | 5 | 5 | 5 | 5 | | Stage 1 |
| Czech | 1 | 1.5 | 3 | 6/7 | 6/7 | | | Stage 2 |
| Slovakia | 1 | 1.5 | 3 | 6/7 | 6/7 | 7 | | Stage 2 |
| Slovenia | 1 | 1.5 | | 5 | 5 | | | Stage 1 |
| Lithuania | 3 | 4 | 8 | 5 | 5 | 2 | 3 | Stage 1 |
| Latvia | 3 | 3.5 | 7 | 5 | 5 | 3 | 2 | Stage 2 |
| Estonia | 1 | 1.5 | | 5 | 5 | | | Stage 4 |

The **benchmarking systems** are outlined below:

**CAF rating scale**

0-no evidence or only anecdotal evidence of an approach; 1-an approach is planned; 2-an approach is planned and implemented: 3-an approach is planned and implemented and reviewed; 4-an approach is planned and implemented and reviewed on the basis of benchmarking data and adjusted accordingly; 5- an approach is planned and implemented and reviewed on the basis of benchmarking data and adjusted accordingly and fully integrated into the organization.

**The Metcalfe scale**

9 Overall strategy

8 Establishing priorities

7 Setting parameters for action

6 Arbitration of policy differences

5 Search for agreement on policies

4 Avoiding divergences among organizations

3 Consultation with other organizations (feedback)

2 Communication to other organizations (information exchange)

1 Independent organizational decision-making

**SIGMA ratings**

1-standard achieved; 2-standard substantially achieved; 3-standard only partially achieved; 4-standard not yet achieved but progress being made; 5-standard not yet achieved; 6-standard not likely to be achieved in the medium term; 7-standard unlikely to be achieved under present arrangements.

**E-government capability ratings**

Stage 1-informational—one way communication of information

Stage 2-interactivity—two-way communication (e-mail, bulletin board etc.)

Stage 3-transactional—internal and external transactions from request to fulfilment

Stage 4-transformational—e-democracy, e-voting, interoperability, seamless integration of government agencies and citizens public management reforms is considered one of the key factors that have brought Lithuania from a laggard among transition states in 1996 to one of the best performing new Member States in 2006.

The Latvian strategic planning system, though having developed at a slower pace, may eventually have a similar positive impact on the performance of the state administration overall, which also in the Latvian case is remarkable as this followed the unsuccessful experiment with the introduction of New Zealand style reforms in 1996 which made politicians highly wary of reform. The more cautious and bottom up approach in the current round of reforms, however, appears to have brought the results that several previous attempts failed to deliver: a more coherent administration, operating based on performance principles.

## *People*

The creation of human resource management systems, able to enforce merit principles and to attract and retain qualified staff, is the area where least progress has been made in the New Member States. Indeed, this is an area where the lack of progress and the lack of serious planning for improvement are very worrying.

Civil service salary systems continue to be based on notions of seniority and job security—meaning that salaries remain low, but the compensation comes in the form of gradually increasing wages and tenure. The study shows two interesting attempts to break the vicious circle, which are Latvia and Slovakia. They are not however without their problems and qualifications and are presented here to indicate some potential future directions for change in the region.

Latvia has, since 1996, used management contracts with defined performance salary bonuses for senior staff and staff with scarce skills. "Management contracts" allowed up to 100 percent additional pay based on the fulfilment of performance objectives agreed between the State Secretary and officials. However, the lack of transparency associated with the system made it highly unpopular among citizens yet difficult to change.

Following several attempts to modify the system, the increasingly dysfunctional pay system is now being replaced with a modern pay system based on a complex job evaluation methodology, clear job classification and establishment of pay grades akin to the Austrian factor point system. This is likely to address the seniority bias in the system and, akin to the Swedish model, to create a link between the development of private and public sector pay levels, though public sector wages will continue to lag those in the private sector.

The Slovak Republic has used budgetary flexibility to allow for performance bonuses in the salary structure of civil servants. The institutionalization of flexibility in pay systems is made by making formal arrangements between the Ministry of Finance and line ministries. The arrangements allow for funds saved on vacant positions to be used towards increasing wage levels through bonuses that can range up to 100 percent of pay. This helps to circumvent the problems of formalized and seniority-based base pay systems. However, the lack of clearly defined criteria for the allocation of bonuses as well as the ad hoc nature of the system which is based on artificially construed wage budgets makes it vulnerable to politicization and risks enshrining wage budget levels that have little to do with the real needs of the administration.

The Slovak approach provides at best a temporary solution to the problems highlighted above and even in its current form needs to be better regulated (to ensure the transparency and objectivity of bonus allocations). Eventually it should be transformed into a system that ensures that the principle of equal pay for equal work, which is a fundamental principle underlying European public sector wage systems, is respected.

Apart from the problems with the wage system development, states have also struggled with the development of functioning horizontal management systems and with the regulation of the politico-administrative interface.

As regards the first point, the "traditional" continental European approach of establishing a dedicated agency to safeguard and enforce merit principles has largely failed in the new Member States. The question of how to ensure the consistent application of merit principles in public management systems that are highly centralized and have little trust from politicians remains largely unanswered and will require further reflection in the new Member States. The alternative, the emergence of a new form of "spoils system" like the ones that emerged in the early years of transition, would certainly not contribute to the development of a high quality civil service.

As regards the second point, the only states that have succeeded in stabilizing the politico-administrative interface have done so by limiting to an absolute minimum the number of political appointments at the top levels of the administration (for example, Lithuania), a solution that is generally not deemed acceptable by the emerging political class in the region and thus does not really provide a replicable model (especially since this has been tried and failed in a number of states).

In this area, therefore, there is an urgent need to reflect on how more suitable models acceptable to the emerging political elite, but still guaranteeing European principles of merit, transparency and equality, could be developed.

### *Systems*

New approaches to improve the quality and efficiency of public service delivery are a key element of sustaining competitiveness and an area where the new Member States have significant potential advantages, in particular in having a well developed IT sector. The use of e-Governance tools for various aspects of public service is a good option for countries that want to gain competitive advantage as such use provides faster and more reliable services for citizens and businesses and enhances the level of transparency.

However, thus far only Estonia has succeeded in introducing a comprehensive reform of the public service delivery system based on e-Governance tools. Significant investments in IT infrastructure, combined with the development of training facilities to enhance the necessary skills among public officials, have created a state of the art e- Governance system that includes diverse services such as e-voting, tax administration, and key business services. The latter is reflected in the very good performance of Estonia in investment climate and business environment indicators.

## The Quality of Public Management and Improved State Performance: Evidence from Recent Surveys

The study shows that countries that have effective policy formulation and coordination (Latvia/Lithuania) also perform better on a variety of indicators, including core European Integration issues, fiscal management, development planning and competitiveness. In addition, the introduction of performance-based public management systems based on a strategic planning approach will be an important asset for both countries as they define their 2007–13 structural fund priorities and are likely to give them a major advantage over the other New Member States.

The above conclusions are confirmed by the results of two key surveys related to the quality of the investment climate, which is a key element of competitiveness. The 2006 "Doing Business" report (World Bank 2006b) and the recently published "Anti-Corruption in Transition 3 (ACT 3)" (World Bank 2006a), which is based on a review of the Business Environment and Enterprise Performance Survey (BEEPS), reveal a high level of correlation between states that perform well in administrative capacity indicators and investment climate indicators. For example, whereas Latvia and Lithuania, as high performers in administrative capacity, rank among the top 25 of the "Doing Business" ratings with Lithuania performing best (ranked sixteenth), weak reformers, such as Poland (seventy-fifth), Slovenia (sixty-first) and Hungary (sixty-sixth) fared considerably worse. The Slovak Republic ranks in between (thirty-sixth).

Estonia, where e-Governance tools have significantly improved the investment climate ranks seventeenth. If one considers pure service delivery aspects, such as licensing for starting up a business, the difference between the two groups of states becomes even greater. Thus, based on the Doing Business Survey, weak administrative capacity and procedures have a serious impact on the quality of the investment climate. A review of ACT 3, which focuses mainly on issues of corruption, provides a somewhat less explicit picture, though also here three of the states that have made little progress on administrative reform (Poland, Hungary and the Czech Republic) are also among the worst performers in the "corruption as a problem for business" indicators. Thus, weak administrative capacity not only directly affects the ability to function in the EU but, more crucially, also affects competitiveness.

## *Success Factors*

The extent to which successful reform measures can be replicated in other settings depends to a large degree on the model chosen, the context and the change management processes that made the reforms work. Looking at the reforms in Latvia and Lithuania in particular, the following success factors stand out:

### *National Institutional Context*

Both Lithuania and Latvia are new states which allowed them greater flexibility in shaping their institutional systems. Whereas all three Baltic States have inherited either Nordic or Germanic administrative traditions, the fact that the development of administrative systems could start from a relatively blank sheet was important. This, however, was also the case for Slovenia and Slovakia and therefore is not a unique factor.

### *Drivers of Change*

A driver of change is crucial whether it be external (the EU) internal (e.g. a domestic economic crisis) or individual (a reforming politician). The driver of change in the Baltic States was the fiscal shock that both Latvia and Lithuania and, to a much lesser degree, Estonia, experienced in the late 1990's as a result of the Russian crisis. The scope of the fiscal problems was such that it required the implementation of radical reform measures which in Lithuania eventually formed the basis for the strategic planning and performance management system. In Latvia, there is less direct causality between the two, though in other circumstances it might have been more difficult to convince politicians to re-open the issue of administrative reform following the radical experiments of the mid-1990s.

Here a comparison with Slovakia is warranted as that country (also a new state) similarly experienced a sharp economic downturn in 1999, a consequence of four years of fiscal mismanagement. Slovakia also responded with the initiation of public management reform measures (as part of a larger package of structural reforms), but was unable to follow through on these, except for a few cases of successful ministry-based reforms. Hungary (in 1995) also responded to a fiscal crisis by trying to reform its public management system, but did not get beyond across-the-board expenditure cuts. This was also true for Poland (2001–02).

### *Political Support and Administrative Continuity*

Arguably the most important single factor is continuity and quality in the top levels of the administration and a relatively smooth pattern of politico-administrative relations. Lithuania and Latvia are the only two cases where public sector reforms have been followed through consistently under governments of different political color and where one core group of senior officials was entrusted (and in Lithuania actively supported) by politicians in successive governments with the reform of the policy management system.[1] Rapid turnover of governments in these two countries has not had the same negative effect on administrative reform continuity. This is a factor that has been clearly lacking everywhere else in the region including in Slovakia, which otherwise shares more or less all of the same features seen in Latvia and Lithuania.

### *Center of Government*

A strong and reformed center of government appears to be an essential ingredient in driving successful reform processes in policy formulation and coordination. It is, however, exactly this institution that has remained largely unreformed or weak in many states, which in part explains why less progress has been made there. In Poland strengthening of the center of government would have to be combined with strengthening of regional/local government and improvement of the link between the center and the regions.

### *Performance-based Logic*

It is particularly important to note the performance-based logic present in each of the successful reform cases. Whether it is e-Governance in Estonia, strategic planning in Latvia and Lithuania, or the Ministry of Finance reform in Slovakia, all successful reform cases have elements of performance-based public management. This is a crucial point because

1. In Lithuania this extends beyond the top level of the admintration: in the civil service has decreased significantly in recent years as public perception of the public administration has improved.

the use of performance-based public management tools in the context of Central and Eastern Europe has often been questioned. However, it appears that the dynamic of the labor markets in the new Member States has created a culture where performance is seen as a logical and acceptable aspect of organizational management, including in the public sector. Thus, whereas performance-based approaches are indeed at odds with the institutional tradition of these states, this appears to have been counterbalanced by the dynamism and flexibility inherent in most of the economies in the region. Thus, politicians should be encouraged to be bolder in the type of reforms they introduce.

### *Strategic Approach*

All three Baltic countries relied on a strategic approach with an overall strategy, detailed action plans; recognized implementation structures both at the center and in the ministries and strong methodologies. This coherent "road map" approach to change management is one of the most important success factors and one of the most important lessons for other countries in the region attempting to achieve similar changes. Realistic time scales (i.e. long-term planning) and a willingness to adapt the strategy in response to failures and changing circumstances was also key.

### *Adaptation of External Models to the Local Context*

Lithuania and Latvia both based their reforms especially in the area of strategic planning on external models but in each case they substantially modified the models to their local reality and needs. Moreover they did not rely on only one model but systematically "cherry picked" from the good practice of other countries.

### *Staff Resources*

While external consultants helped with the initial launching of reform initiatives Lithuania and Latvia rapidly took ownership of the reforms and developed their own teams with the capacity to see the reforms through. It is this people aspect which is one of the most impressive features of the Lithuanian and Latvian success stories.

While it is clearly not possible or indeed necessary for all of the above success factors to be at work it is desirable that as many of them as possible are in operation consistent with the local context in which they are being applied. Key factors are:

- A suitable model adapted as necessary to the local context and needs.
- Driving forces to initiate change and to see it through (political, institutional and personal).
- Sound and consistent change management processes.

A word of caution is also in order in relation to the Baltic "tigers." While their innovations and achievements in the three areas studied are impressive they are by no means complete or totally secure. Lithuania's achievements in strategic policy management are hindered by the failure to introduce performance oriented HR policies. Latvia's achievements in this sphere are by no means fully embedded in the system and its ambitious experiment in remuneration policy which is only at the beginning of the road is both complex and contentious—it will take very careful change management to see it through to completion. Estonia's achievements in E-government are coming up against cost constraints and are not matched in the policy or HR spheres. In all three countries further development of the systems depends very crucially on continued political support.

## Conclusions

It is evident from the results of the study that *renewed impetus for public sector reform is needed* in the EU8 with the aim of introducing soundly performing systems of day to day policy making, HR management and service delivery across the whole of government. This is especially important in Poland which—although it is the largest of the EU8 and will benefit most from the structural funds—is sadly lagging behind instead of acting as a role model for the rest of the region. There is also a need for continued improvement in the Baltic States which despite their generally good performance and their impressive achievements in some areas cannot be complacent since their successes need to be sustained while at the same time there are other areas of their systems where improvements are just as necessary as in the other countries in the region.

The *priorities* are clear. Most countries need to improve horizontal policy management and e-government but the main priority affecting all countries is the urgent need to develop professional merit based and independent civil services. The lack of sufficient progress in the reform of incentive systems, which has only recently been starting to get attention, and the merit principles across the civil service are key weaknesses in most of the public management systems in the region. Two main challenges need to be overcome if this issue is to be addressed, one of which is technical and the other political. First, the design of systems that reflect the new labor market realities in the region, based on performance principles, properly designed and linked incentive systems and fair and transparent application of rules. Second, the development of a common understanding among politicians that a well functioning civil service is a public good rather than an extension party politics, and the development of a set of principles politicians commit to abide by when addressing civil service staffing issues. Without a commitment by politicians to accept the notion of the civil service as a public good, little progress can be made on this issue.

Unfortunately it appears that there are *no effective drivers of change* in operation at present. External forces like the European Union do not seem to be performing this role as in the past; the European Commission has accepted that the EU8 meet the requirements of the acquis and seems disinclined to apply pressure in this area despite the fact that soundly performing administrative systems—with the emphasis on systems—will be necessary to ensure optimal use of the Structural funds and despite the evidently poor performance of those systems during the 2004–06 period. As Bank funding is replaced in the EU8 by EU funds the Bank too has less influence for change than in the past. There are moreover no signs of any government which is willing of its own accord to carry through the substantial reforms which are needed in the public sector. It may be that an external or internal "shock" of some kind may be required to bring home the need to invest in real change. It would be better, of course, if change could be initiated more "strategically" and coherently throughout the region and if shocks could be avoided.

Effective *strategies* for public sector reform are almost entirely lacking. A few countries have strategies but they have not so far been implemented effectively. Equally worrying is the fact that generally speaking there appear to be no roadmaps for reform emerging from the process of programming the structural funds as might have been expected. This is especially disappointing because such programmes could have been exactly what were needed in the region—long term, consensual, well- funded strategies with strict external controls and inputs of external expertise but combined with local ownership and a continuity spanning political horizons.

*Centers of government* are generally weak and horizontal management of both policy and HR systems is virtually absent. This is a serious concern because the conclusions of this study point to a scenario in which system reforms in a step by step process starting from core government institutions with political leadership and support and a coalition between politicians and a core group of senior officials are likely to have the greatest success. Unfortunately it is these institutions that in most states have been heavily politicized and, in the cases of Poland, the Czech Republic and the Slovak Republic severely weakened. Therefore rebuilding core government institutions as bodies of professional excellence is an important condition for successful systemic reform. It remains to be seen whether there would be much appetite for this but past experience is not encouraging as Poland's many failed attempts to strengthen the center of government demonstrate only too clearly. Moreover as indicated earlier especially in a country of the size of Poland local government and its relations with central government would need to be taken into account.

In terms of the *models* which might be adopted it would be desirable to rethink some aspects of the systems which have been promoted up till now. With regard, for example, to the people dimension there is a clear need to think outside the traditional civil service box. In particular ways need to be found to marry the emerging market culture of the new member states with the notions of merit, impartiality and equality which are the core principles for the development of a stable and high quality civil service. This in our view means that civil service systems need to rely much more than is currently the case on performance based approaches in recruitment and career management. The Slovak example of the Ministry of Finance provides a good illustration of how this could be done. However at the same time performance principles need to be counterbalanced by checks on the respect for merit principles and for this cross government structures are required. The design of cross government structures that fit the institutional and political context of the new member states stands out as a serious challenge to be addressed in the coming years. Traditional EU models do not work in this context but a suitable alternative has yet to emerge.

More important, however, than the models chosen are two further aspects of the change process namely 1) *political commitment* and 2) *effective change management*. As regards political commitment for reforms to be successfully implemented a broad, non partisan political dialogue is essential. As noted from the Latvian, Lithuanian and Estonian (on e-Governance) cases the continuity in the direction and implementation of public management reforms has been a huge factor in bringing success. If a common direction does not emerge organically as it did in the Baltic States, a formal process in which politicians and senior officials engage with the academic and business communities on the design of a common vision for the development of the public management system should be put in place. This would need to be based on: i) the understanding of the urgent need for improvement in public management systems if these systems are to meet the challenges set out in the introduction to this study; ii) the notion that public management systems will need to reflect a balance between principles of performance, merit and impartiality; iii) that resources will need to be committed, and that there should be a common understanding across the political spectrum that this will be done irrespective of who is in government; and iv) that any strategy or vision would need to be a medium term one, spanning at least five years. Without the emergence of a process of this type it is likely that successes will remain limited to those few states that have already shown progress and that the others run a serious risk of facing the negative consequence of inadequate public management systems; missed opportunities in the use of structural funds, continued weak fiscal management and eroding levels of competitiveness.

Most important of all is the process of *change management*, the detailed and long term process by which the planned changes are embedded in the day to day operations of ministries. It is this aspect of the good practice of the Baltic States which could be most valuably replicated in the other countries in the region. Some efforts have been made by the Baltic States to transfer this expertise to other countries in transition but mainly in an ad hoc way to non-EU countries such as Macedonia. It would be desirable if the EU8 and indeed the candidate countries could systematically learn some lessons from this study and especially from the change management experience of the Baltic States.

CHAPTER 1

# Introduction, Context, and Approach

## Context

More than two years after the enlargement of the EU administrative capacity remains an issue of concern for the EU8. On issues that are directly linked to the management of EU affairs, most New Member States continue to perform well as they did during the accession process. However, indications that all is not well with their administrative systems overall continue to be present. These are expressed in a diverse set of indicators, including overall fiscal performance, where several states do not meet Eurozone entry criteria, have low EU fund absorption ratios, and show an uneven performance in key business environment indicators.

Specifically, the EU8 countries face three key challenges that require a strong improvement in administrative capacity:

1. The forthcoming "step increase" in EU funds, which in the next financing period will amount to up to 3.5 percent of GDP. This is unprecedented, even when compared to earlier beneficiaries such as Ireland and Spain. If they lack a strong administrative capacity, states will not only risk losing the direct benefits brought by these funds but will also risk the neglect of policy agendas in other areas owing to the sheer volume of the task of planning and implementing structural funds. This could pose significant risks in areas that are important to economic and social development but are not included under funding priorities. The low uptake of funds in the current financing period (2004–06) is a further reason for concern in this regard.
2. The continued challenges of fiscal management. Many of the New Member States do not meet the entry criteria for the Eurozone on fiscal parameters, including fiscal deficit levels. This means that states will not achieve a key policy goal, which is the early adoption of the Euro.

3. Competitiveness, and in particular the question of what the Central and Eastern Europe states will focus on as their competitive advantage of relatively low wages combined with skilled labor will be reduced as a result of economic convergence and more competition from South and East Asia. Administrative quality, as expressed in the quality of the business environment, will be a key element of competitiveness as other elements of comparative advantage, such as lower labor costs, will gradually decline in importance.

This study reviews the direction of administrative development in the first two years of EU membership in the EU8 and includes a review of general trends in administrative development as well as a benchmarking exercise for a sample of states on selected criteria that illustrate capacity for public management innovations. The study will draw conclusions on ways to address the identified issues and problems in the development of the public management systems of the EU8, with a focus on systems and instruments that would help address the three challenges set out above.

## Administrative Capacity Two Years after Accession: Mixed at Best

The experience of the New Member States in the EU over the last two years has been mixed. Whereas most states have proved to be able to cope with the workload generated by core EU issues, their ability to effectively plan and use structural funds and to address broader issues of competitiveness remains in doubt. This includes uneven performances in recently published investment climate and business environment ratings.

### *Strong on Core EU Issues*

The pattern of administrative performance in the EU8 varies strongly depending on the issue reviewed. Whereas in some core aspects of participation in the EU, such as the transposition ratios of EU directives, the New Member States have all done (unexpectedly) well.[2] The picture becomes more diverse and less positive once one reviews performance in issues not directly related to core EU business, ranging from structural fund absorption, through fiscal management to investment climate and business environment ratings.

With regard to the transposition of directives (one of the main measuring sticks of administrative performance used by the European Commission) all New Member States perform well and some excellently (see Table 1.1). Whereas this has broader significance than "ticking boxes" (in particular in terms of the reliability of the legal framework for economic management), it still remains a limited indicator of broad administrative performance.

In addition to being a narrow form of measurement of administrative performance, this also reflects an earlier established pattern of administrative development. In issues related directly to the EU management affairs, the EU8 have always performed well and have developed capacities on par with or even exceeding those of the old member states, in particular during the high pressure build-up period to membership. However, whereas

2. Lithuania ranked as the best performer among all Member States in the Commission League Tables published in February 2006.

**Table 1.1. Transposition: EU-25 Member States**

**EU-25 Member State Transposition Deficit, as of 1/12/2005—1635 Directives**

| Member State | LT | DK | HU | FI | PL | SE | CY | LV | MT | SI | NL | DE | EE | SK | UK | AT | ES | FR | BE | IE | CZ | IT | PT | EL | LU |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Transposition Deficit (percent) | 0.4 | 0.7 | 0.7 | 0.8 | 0.9 | 0.9 | 1.1 | 1.1 | 1.2 | 1.2 | 1.2 | 1.3 | 1.3 | 1.4 | 1.4 | 1.5 | 1.5 | 1.7 | 1.8 | 1.8 | 2.5 | 3.1 | 3.1 | 3.7 | 4.4 |
| Number of Directives | 6 | 11 | 12 | 13 | 14 | 14 | 18 | 18 | 19 | 19 | 19 | 22 | 22 | 23 | 23 | 24 | 25 | 28 | 29 | 30 | 41 | 50 | 50 | 60 | 72 |

**Infringement Cases against EU-15 Member States, as of 1 October 2005**

| Member State | DK | FI | LU | SE | NL | IE | PT | AT | UK | BE | EL | DE | FR | ES | IT |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Number of open infringement cases | 31 | 36 | 36 | 41 | 44 | 51 | 53 | 59 | 66 | 66 | 99 | 101 | 113 | 115 | 157 |

**Infringement Cases against EU-10 Member States, as of 1 October 2005**

| Member State | LT | LV | SI | EE | HU | SK | CY | CZ | MT | PL |
|---|---|---|---|---|---|---|---|---|---|---|
| Number of open infringement cases | 4 | 7 | 7 | 8 | 10 | 10 | 11 | 14 | 14 | 18 |

*Source:* European Commission: Internal Market Scoreboard 14bis.

**Table 1.2. Fiscal Deficit Levels, 1995–2006 (GG deficit, ESA 95% of GDP)**

| | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006F |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| CZ | −13.4 | −3.4 | −3.9 | −5.1 | −3.8 | −3.8 | −5.8 | −6.9 | −6.7 | −2.9 | −2.6 | −3.8 |
| EE | 0.4 | −2.0 | 1.7 | −0.4 | −3.7 | −0.4 | 0.3 | 1.0 | 2.4 | 1.5 | 1.6 | 0.8 |
| LV | −2.0 | −0.5 | 1.5 | −0.6 | −5.3 | −2.8 | −2.1 | −2.3 | −1.2 | −0.9 | 0.2 | −1.5 |
| LT | −1.9 | −3.6 | −11.4 | −3.0 | −2.9 | −3.6 | −2.0 | −1.4 | −1.2 | −1.5 | −0.5 | −1.2 |
| HU | | | | | −5.5 | −3.0 | −3.5 | −8.4 | −6.4 | −5.4 | −6.2 | −8.0 |
| PL | −4.4 | −4.9 | −4.6 | −4.3 | −1.8 | −1.5 | −3.7 | −3.2 | −4.7 | −3.9 | −2.4 | −2.4 |
| SI | | | | | | −3.9 | −4.3 | −2.7 | −2.8 | −2.3 | −1.8 | −1.9 |
| SK | −0.9 | −7.4 | −6.2 | −3.8 | −7.1 | −12.2 | −6.5 | −7.7 | −3.7 | −3.0 | −2.9 | −3.2 |

*Source:* Eurostat.

the "islands of excellence" in European Integration Management have often been praised, few among the New Member States have managed to expand the best practice approaches used in the preparation for EU membership to their public administration systems at large.

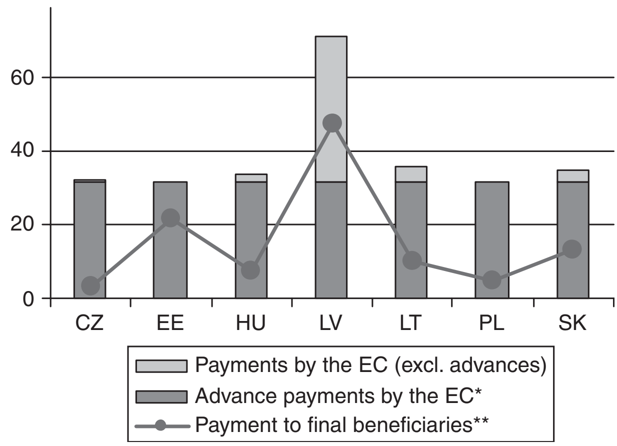
## *Weak on Areas Requiring Broader Capacity*

Looking at the situation from a broader perspective, and reviewing the overall economic and fiscal performance, the EU8 continue to outpace the old member states, which would appear to be an indication that the EU8 remain economically highly competitive. However, serious concerns remain regarding core aspects of economic management. Fiscal discipline remains weak in many of the New Member States, with Hungary being the main outlier with a fiscal deficit that could exceed 10 percent of GDP in 2006 and only five of the New Member States meeting the targets required for joining the Eurozone (see Table 1.2).

A further indicator of administrative performance, related to the absorption capacity of EU funds, reveals more significant problems with administrative capacity. Fund absorption rates have remained well below the desired levels (see Figure 1.1). Poland, Hungary and the Czech Republic all stand out as problem cases, while Latvia is the only state with a satisfactory performance, although even in the Latvian case it is difficult to say to what degree commitment levels translate into actual payments.

Finally, on key service delivery indicators (such as investment climate assessments) documented in the "Doing Business 2007" report (World Bank, 2006b) and the "Anti-Corruption in Transition 3" (ACT 3) (World Bank, 2006a), the performance of the EU8 is at best mixed. The most recent data indicate the emergence of two sets of states in the region: on the one hand, those that rank among the best performing OECD states (all three Baltic States), and on the other hand those (Hungary, Poland) that are in league with states such as Moldova, Azerbaijan (in the BEEPS surveys), Pakistan and Nicaragua (in the Doing Business Surveys). In relation to the latter survey, which reviews issues such as access to credit and taxation alongside classical service delivery related issues such as business registration and issuing licenses, the performance gap is even more significant when only service delivery features are considered (see Table 1.3).

**Figure 1.1. Absorption of EU Structural Funds, September 2005 (In percent for appropriations of 2004–06)**




* Advance payments to New Member States in the amount of 10 percent of total allocations in 2004 and 6 percent in 2005.

** Verified public expenditure—expenditure of the final beneficiaries verified by the managing or intermediary authority (excluding Estonia).

*Source:* World Bank-EU8 QER, February 2006.

## Conclusions and Approach

In view of the above, a discussion of ways of addressing the remaining problems involved in developing well-functioning public management systems is urgent. This is important not only because states stand to lose significant amounts of funding if they do not improve

**Table 1.3. Service Delivery: Evidence from "Doing Business" and "ACT 3"**

| Country/indicator | Doing Business ranking 2007 (out of 175 states) | Doing Business ranking 2006 (out of 175 states) | 'Corruption as a problem': ACT 3 (26 countries in Europe and CIS only) |
|---|---|---|---|
| Czech Republic | 52 | 50 | 21 |
| Estonia | 17 | 17 | 4 (with negative trend) |
| Hungary | 66 | 60 | 8 (with negative trend) |
| Latvia | 24 | 31 | 6 |
| Lithuania | 16 | 15 | 12 |
| Poland | 75 | 74 | 13 |
| Slovak Republic | 36 | 34 | 5 |
| Slovenia | 61 | 56 | 1 |

their public management systems, but also because weak administrative capacity, as expressed in deficiencies in service delivery, will have a negative long-term impact on their competitiveness. The Czech Republic and Poland stand out as particularly weak performers in this regard, followed by Hungary.

This study will aim to "unpack" the issue of administrative capacity by considering three key aspects of administrative performance. First, we will address issues of systemic performance, which includes the extent to which states have introduced performance management and strategic planning approaches in their public management systems, as well as reviewing the strengths and weaknesses in their policy coordination systems. The extent to which strategic planning and performance management systems are well established determines the ability of a country to carry out effective fiscal management and development planning. Both are crucial aspects of the forthcoming 2007–13 EU fund planning period. Finally, performance management approaches, if well framed, can help improve the quality of service delivery, in particular in areas important to the investment climate such as the issuing of permits and licenses, business registration, etc.

Second, we will review the "people" aspect of public management by assessing HRM systems and practices. This review aims to assess the extent to which public administration can attract and retain quality staff, in particular in the context of the dynamic labor markets in the EU8.

Finally, we will look into one specific aspect of service delivery, namely, the extent to which states have introduced e-Governance systems. Together with the above -mentioned introduction of performance management tools, such systems can make a major difference in creating an enabling investment climate for a country (World Bank 2006a).

The approach taken in this review relies on accepted tools and methods that can be used to conduct comparative assessments in each of these areas. While such assessments can never be exact when it comes to public management systems, they will help indicate which states have performed well and in what aspects of public management. In the final chapter we will draw conclusions regarding the replicability of some of the innovations that countries have introduced with the aim of defining a possible approach for other countries to follow.

CHAPTER 2

# Reviewing Main Trends in Administrative Development

An overall review of administrative development in the New Member States points to some success stories in introducing public management innovations but also reveals an overall backsliding in the core issues of administrative development. Success has been achieved mainly in the introduction of strategic planning and performance management systems, particularly in Lithuania and Latvia and in innovations in service delivery through the use of e-Governance tools, mainly in Estonia. Some agency specific reforms, in particular in the Slovak Republic, also stand out as best practices. Apart from these innovations, the trend in the development of the civil service and the public administration systems is not positive. Weaknesses in policy coordination, unsettled political-administrative relations and outdated incentive systems stand out as particular problems.

## Public Management Innovations Continue to be Rare and Relatively Isolated

The review of administrative development in the EU8 reveals some interesting innovations, especially in performance management and e-Governance.

### *Performance Management: A Basis for Long-term Improvements?*

The strategic planning initiatives in Lithuania (launched in 1999) and Latvia (launched in 2000) were initially defined as a response to serious fiscal problems and as a way of meeting the requirements for the improved management of the EU accession process. Five years on, strategic planning has become the anchor for a broader move towards the introduction of performance management systems in both states. Lithuania has opted for a top-down approach, led by the State Chancellery in close cooperation with the Ministry of Finance and rolled out throughout the central administration. Latvia has used a bottom-up approach, whereby ministries and agencies were stimulated to use policy planning tools designed by the State Chancellery, initially on a voluntary basis but from 2006 onward as an obligatory process.

The review of the two cases shows that Lithuania's top-down approach has led to faster results, as there has been a strong push for ministries to adapt to the new system which has led to a relatively quick roll-out of the system (Brown, Rimkute, and others 2006). This is also reflected in improved budget management, organized around strategic planning principles, led by the Ministry of Finance. The Latvian strategic planning system has developed at a slower pace but is also expected to cover the entire central state administration by the end of 2006.

The introduction of performance-based public management systems based on a strategic planning approach will be an important asset for both countries as they define their 2007–13 structural fund priorities and is likely to give them a major advantage over the other New Member States.

In addition, the investment climate ratings presented in the previous chapter illustrate the improved performance of both states in service delivery to businesses. Latvia and Lithuania rank well above all other New Member States, except for Estonia, when it comes to investment climate ratings and they also outperform a number of OECD states. In addition, the two states rate even better in those aspects of the investment climate that are directly related to administrative performance, such as business registration, licensing, etc.

The next step in the development of performance management systems is to bring performance criteria to the level of individual officials and link these to career advancement. This will be a difficult step, as HRM systems remain weak in both states (see the discussion of HRM coordination in Chapter 3) and the outdated incentive systems in place are ill-suited to the requirements of a performance driven public management system. It should be noted that Latvia has already initiated a wage system reform process, thus taking a further step towards completing a full-fledged performance management system. The radical reform of Latvia's wage system was driven by concerns by both the government and investors over the high rate of turnover in the civil service.

One important success factor in the development of performance management systems is manageability, which in this case means setting simple and realistic performance targets at the institutional level so that individual performance criteria can be distilled from this relatively easily. Creating systems of performance target setting that are too complex is likely to increase resistance to innovations which in turn will stifle their successful introduction. Furthermore, in setting performance targets for individual civil servants it is important to reflect routine tasks (in particular, for those mostly engaged in service delivery) as well as developmental tasks, in order to ensure that aspects of policy implementation are reflected in an appropriate manner. This means that individual performance appraisal will necessarily continue to be a mixture of strategic goals at the institutional level and the more routine aspects of service delivery.

## *Service Delivery: Using e-Governance Tools, the Estonian Exception?*

The use of e-Governance tools for various aspects of public service delivery is a good option for countries that want to gain competitive advantage as such use provides faster and more reliable services for citizens and businesses and enhances the level of transparency. Estonia has been the front runner in applying e-governance approaches among the New Member States.[3] Significant investments in IT infrastructure, combined with the development of training facilities to enhance the necessary skills among public officials, have created a state-of-the-art e-Governance system that includes diverse services, such as e-voting, tax administration, as well as key business services. The latter is reflected in the good performance of Estonia in investment climate and business environment indicators, in which the country outperforms all other New Member States except Latvia and Lithuania.

Whereas the Estonian comprehensive approach is difficult to replicate in terms of the speed and comprehensiveness of its introduction, a more selective approach would be feasible across the EU8, focusing on key business services and on the corruption-sensitive aspects of service delivery, but to date this has not found widespread application.

## Structural Flaws Have Reappeared

### *Coordination Systems Are Weakening*

The last years before accession saw a strongly enhanced overall system of policy coordination and the emergence of stronger horizontal management regarding such issues as HRM, driven in part by the EU accession process. The review of the state of play two years after accession reveals a worrying trend, particularly in the latter aspects of coordination.

A review of overall policy coordination capacity, based on the Metcalfe coordination scale applied in four selected countries (see Chapter 3 for details) reveals two patterns:

1. Coordination capacity in core EU affairs has generally declined, but to different degrees.
2. Overall coordination systems remain weak and well below the required level for advanced administrative systems, with HRM coordination particularly at risk.

*Weakened EI Coordination.* European Integration (EI) management systems formed the administrative backbone of the accession management process in the EU8 and have been widely praised for their effectiveness. However, moving from the management of the accession process to the management of membership requires a significant change of approach and the need to roll out specialized EI capacity throughout the state administration. The in-depth review of four countries and the literature review of other selected countries reveals a pattern that ranges from dismantling the EI management system as it previously existed (Poland and the Slovak Republic), through the transformation of the systems in Latvia and Lithuania, where the former has been significantly weakened and the latter has retained much of its previous capacity. Based on additional discussions, the Hungarian system would most likely fit the Lithuanian pattern of consolidation, while the Czech EI management system would fit the declining pattern of Poland and the Slovak Republic (Brown, Rimkute, and others 2006; Staronova and Brown 2006).

3. Some more specific initiatives (such as electronic feedback possibilities for citizens on policy proposals) have been introduced in the Slovak Republic and Latvia, and progress in the provision of e-services has also been noted in the Czech Republic (Vidlakova 2006).

*Overall Coordination Systems Have Not Caught Up.* The decline of specialized EI management structures is a cause for concern but could be compensated for by improvements in the overall policy coordination system, which arguably is a more significant determinant of administrative performance than specialized EU coordination. However, based on a review of four countries according to the Metcalfe scale, most countries remain well below the desired coordination levels, at levels between "communication and information provision" (2) and "consultation" (3). Coherence in policy design and effective policy implementation in areas that involve several government institutions require coordination systems at least at level 5 (bottom-up search for agreement) or 6 (arbitration of differences) (Metcalfe, 1994). Of the four countries reviewed in depth, only Lithuania and Latvia come close to these levels, and none of the four countries reviewed on the basis of desk research fare better than Poland or the Slovak Republic (both between levels 2 and 3).

*Rolling Back HRM Coordination Systems.* The concerns over the development of policy coordination systems are exacerbated by the general roll-back of horizontal management systems on key issues such as HRM systems. Across the board horizontal management systems, "personified" by civil service agencies and central departments for HRM, have been either watered down or simply removed, with Poland, the Slovak Republic and the Czech Republic as the main examples. In none of these cases has the previous central authority been replaced with at least a "light" coordination mechanism, which basically buries the notion of a "professional civil service" as a concept. The situation in Estonia and Hungary is similar, with no central authority to guide civil service development in place. Latvia and Lithuania constitute a positive exception, as some central HRM capacity remains in place in both states.

The abolition of HRM systems so soon after their creation poses serious questions of the right "fit" of these systems compared to the economic and political realities of the New Member States. The legislation and civil service management systems established in the early years of this decade were modeled on the traditional approaches to civil service development prevalent in the old member states, which may simply not have been suitable in the context of Central and Eastern Europe. The focus on legislation and formal institutions, advocated by the EU, in this regard has prevented the development of more urgent strategic approaches to developing stable and competitive HRM systems. It is important that this is recognized, in particular by the EU. What is needed is urgent consideration within the New Member States on how to design and implement systems that do fit their realities, and in the EU on its approach to current and future candidate states in this particular area.

## The Return of Politicization

Politicization is generally seen as a key impediment to successful administrative development (Verheijen 2001; Pierre and Peters 2003), as it runs contrary to the principles of merit, professionalism and permanence that are essential ingredients of a functioning civil service. The last years before the EU accession saw a move in most candidate states towards the formalization of politico-administrative relations and the introduction of constraints to politicians' freedom to appoint and dismiss senior officials at will. Moves to de-politicize top level appointments were strong, particularly in Lithuania, where the number of politically appointed positions was reduced to that of Deputy Minister, and in Poland, where the 1999 Civil Service Law set strict limits on the power of politicians to appoint and remove those recruited under the new law. However, increased political influence on top level appointments was noted for Hungary (Meyer-Sahling 2004), and the adoption of legal frameworks limiting politicization in the Czech Republic and the Slovak Republic was not followed through consistently in implementation.[4]

Our review of the HRM practices two years after EU membership points to the return of politicization, particularly of top level appointments. Civil service agencies in the Slovak Republic and Poland are being dismantled, and with this any checks and balances on politicians' right to appoint senior officials will effectively disappear. The Civil Service Law in the Czech Republic has still not become effective, and it may never work as initially planned (Vidlakova 2006), while the trend towards increased political interference in top level appointments in Hungary that had begun with the Orban government (Vass in Verheijen 2001; Vass 2005) appears to have continued. The other four New Member States do not show a similar negative trend, though continued high levels of politicization in Slovenia have been noted (Hacek 2006).

## *Incentive Systems: Still Looking for a Balance*

Apart from the introduction of merit-based public administration systems, the development of incentive systems that would make the public administration a sufficiently attractive employer for talented staff remains a key issue. In the run up to the EU accession, administrations were able to retain talented staff through "postponed rewards" of future positions in EU institutions, or through strong latent private sector demand for those involved in EU accession preparation. Post-accession this particular incentive no longer applies. States have since grappled with the issue of how to attract staff in an increasingly politicized civil service system.

With two exceptions civil service incentive systems continue to be based on notions of seniority and job security—meaning that salaries remain low, but compensation comes in the form of gradually increasing wages and tenure. The latter has been eroded owing to increasing levels of politicization; the former holds little attraction for the talented and increasingly sophisticated young workforce in the New Member States. Fiscal constraints, particularly in those states intending to rapidly join the Eurozone, make an overall increase in wage levels virtually impossible, and electoral considerations make politicians reluctant to increase civil service wages. The civil service thus remains locked into a vicious circle of low attractiveness which remains difficult to break.

The review of five of the eight New Member States revealed two interesting attempts to break with the above situation. Latvia has used management contracts with defined performance bonuses for senior staff and staff with scarce skills. The Slovak Republic has used budgetary flexibility to allow for performance bonuses.[5]

In the Latvian case, the so-called "management contracts" which allowed up to 100 percent additional pay based on the fulfillment of performance objectives agreed between

4. In the Slovak case the situation is worse, as the transfer of competencies for the appointment (and dismissal) of officials to politically appointed heads of offices, without any checks and balances, is likely to increase politicization significantly.

5. The Lithuanian case, not discussed here, is one example of a more marginal improvement to the existing system, which, however, is said to have a positive impact on the competitiveness of the civil service as an employer (World Bank 2004).

the State Secretary and officials, were instituted in the mid-1990s as a way of keeping talented staff in the administration. However, the lack of transparency associated with the system made it highly unpopular among citizens yet difficult to change. Following several attempts to modify the system, the increasingly dysfunctional pay system is now being replaced with a modern pay system based on a complex job evaluation methodology, akin to the Austrian factor-point system. In the context of this reform the level of performance bonuses will be reduced to a maximum of 20 percent of total pay. This is likely to address the seniority bias in the system, and in a way comparable to the Swedish model, to create a link between the development of private and public sector pay levels, though public sector wages will continue to follow those in the private sector from a distance.[6]

The Slovak case is one of the institutionalization of flexibility in pay systems. Other states, such as Poland, operate with some degree of flexibility in pay levels based on bonuses, but the Slovak Republic is the only case among the eight to have institutionalized this in formal arrangements between the Ministry of Finance and line ministries. The arrangements allow for funds saved on vacant positions to be used towards increasing wage levels through bonuses that can range up to 100 percent of pay. This helps to circumvent the problems of formalized and seniority based base pay systems. However, the lack of clearly defined criteria for the allocation of bonuses as well as the ad hoc nature of the system, which is based on artificially construed wage budgets, makes it vulnerable to politicization and risks enshrining wage budget levels that have little to do with the real needs of the administration. Thus, the Slovak approach provides at best a temporary solution to the problems highlighted above and even in its current form needs to be better regulated (to ensure the transparency and objectivity of bonus allocation). Eventually, it should be transformed into a system that ensures that the principle of equal pay for equal work, which is a fundamental principle underlying European public sector wage systems, is respected. In its current form, however, this is not an approach that would be advisable for replication.

A further interesting aspect of Slovak reforms, important from the perspective of mitigating corruption risks, is the initiative to create "posts of superior importance" that have a 50–100 percent bonus to basic pay but at the same time have a more rigid regime for asset disclosure. This was used for the following five posts quite successfully: Head of the State Treasury, Head of the Debt Management Agency, Chief Economist at the Ministry of Finance, Head of the Anti-corruption Unit at the Government Office, and Head of Programming of Structural Funds at the Ministry of Labor, Social Affairs and Family.

In conclusion, even though some progress is being made in reforming incentive systems, overall these remain outmoded and unfit for attracting and retaining the high quality staff that was pivotal to the successful EU accession process. Large-scale systemic changes such as that in Latvia will be difficult to replicate and would require significant time and political will to actually carry out, while most ad hoc approaches intended to introduce flexibility, such as that attempted in the Slovak Republic continue to pose a serious risk of further eroding objective merit principles and of freezing historical budget allocation levels, unless they are regularized on the basis of the introduction of performance appraisal systems and a review of actual staff needs.

6. It is noteworthy in this regard that Serbia is introducing (so far successfully) a simplified version of the Austrian/Latvian model, which provides further evidence that the introduction of relatively advanced pay and employment systems in the region is a real possibility.

CHAPTER 3

# Comparing Innovative Capacity

The previous chapter reviewed the overall direction of administrative development in the eight New Member States. For a number of key aspects of public management, the trends are not positive and some are a cause for serious concern about the future competitiveness of the states, as reflected in their investment climate ratings, and their ability to effectively function as EU member states.

However, in order to define the relative level of development of public management systems across the EU8 it is important to review the main elements of their systems in relative terms. It is generally accepted that the performance of public management systems is determined by three main factors: systems, people and resources. In this study we will focus on the first two aspects, while budget management and resources are addressed in a separate study.

In relation to "systems" we will review two main issues: first, the degree to which management systems are in place that will ensure the reliability and coherence of government policy and the quality of its delivery; second, the degree to which innovations (such as e-Governance solutions) have been introduced.

Regarding the "people" dimension, the discussion will focus on the generally agreed determinants of well-functioning public management systems including: (i) recruitment and career management systems; (ii) incentive systems; and (iii) the organization of the politico-administrative interface.

## Identifying Comparators

Measuring administrative capacity in comparative terms is not straightforward, and until recently there were few generally accepted methods and approaches for conducting comparative assessments. However, over the last 15 years significant progress has been made in this area. This includes the work of the global Civil Service Research Consortium, which has developed a methodology for the qualitative comparison of civil service systems (Toonen, Bekke, and Perry 1996), the work done by OECD/SIGMA to define benchmarks on key aspects of administrative performance in the context of European Integration (OECD 1999), and, finally, the development of the quantitative Common Assessment Framework (CAF). The latter was initially designed for use in the context of the EU (and related to the Lisbon Competitiveness Agenda) but has in the meantime become a global tool for benchmarking administrative performance (Staes and Thijs 2006). In addition, several approaches to comparing the introduction of e-Governance systems have also been designed, including the Global Information Technology Report and other ratings.

This study will use elements of the different tools mentioned above to review the relative progress made in establishing modern public management systems in the eight states discussed here. It will look at the four main aspects of the development of systems (performance management, strategic planning, policy coordination and the introduction of e-Governance solutions) as well as the main elements of the "people" aspects of public management (recruitment and career management, incentives, and politico-administrative relations).

1. *Performance Management and Strategic Planning.* Performance based public management systems tend to be better able to absorb innovation and drive change. Thus, the introduction of performance based systems, even if in an incremental manner, can be a significant step forward in improving administrative capacity in complex areas such as structural fund planning. It can also significantly enhance transparency in public management.

   Strategic planning capacity in this context is an important pre-condition for the development of an effective performance management system at the level of government and individual government institutions.

   Whereas performance management and strategic planning are aspects of public management in their own right, and are often reviewed as separate issues, we have opted here to review them together. The reasons for this are that the introduction of strategic planning and performance management systems in the EU8 has been strongly intertwined, making it difficult to review them separately, and that if we are to reflect the general trend in the ECA region it is necessary to treat these two aspects of system development as interrelated aspects of the same agenda.[7]

   The comparative indicators for performance management and strategic planning systems will be based on the World Bank paper Increasing Government Effectiveness (2005), which includes a digest of international practices and sets out a set of key principles against which policy management systems can be benchmarked.
2. *Policy Coordination, both Vertical and Horizontal.* Coordination capacity is one of the main factors determining policy coherence and reliability, both of which are key to ensuring an enabling investment climate. In addition, adequate coordination—both

7. This, for example, has also been the case also in countries like Kazakhstan and Russia, both of which have started the introduction of an administrative modernization agenda based on interrelated performance management and strategic planning agendas.

regarding horizontal and vertical aspects such as the planning and implementation of structural funds—is crucial to effective participation in the EU policy process (Wessels and Mittag 2003).

In reviewing both aspects, the Metcalfe Coordination Scale (Metcalfe 1994) was applied to arrive at a relative ranking of the case studies as well as to set a benchmark for adequate performance on this criterion. While the Metcalfe scale is not easy to apply, it is the only available and usable tool for comparing coordination systems across states.

3. *Human Resources Management.* The absence of a well-functioning HRM system is generally seen as one of the most serious impediments to the creation of-state-of-the-art public administration systems. In defining comparators in HRM systems, two possible approaches can be taken. First, the SIGMA baseline criteria, which have been the generally accepted assessment instrument during the accession process, still provide an acceptable framework for assessing HRM systems. An alternative approach would be to use the HRM ratings used in the Common Assessment Framework (CAF). Whereas applying the latter would have the advantages of using a more advanced approach, the CAF framework has undergone changes recently, which makes it difficult to use for benchmarking over time. Thus, we will use the SIGMA approach, with some added elements to assess incentive systems based on World Bank wage system reviews.
4. *E-Governance Innovations.* The application of e-Governance solutions to improve internal management in public administration and strengthen service delivery can be an important element of competitiveness, and is thus discussed as a key aspect for the reform agenda.
5. E-Governance systems are somewhat more difficult to assess in a comparative context than other elements of the public administration system. Even if e-readiness rankings exist, for example in the Global Information Technology Report, this does not necessarily reflect the ability of states to use e-Governance tools for service delivery. Thus, on this issue we will attempt to benchmark mainly against phases of the development of e-Governance systems.

## Defining the Sample

The study focuses mainly on five of the New Member States, for which we aimed to define best practices in key aspects of the public administration systems. Reviews of other states were limited to desk research. The five cases reviewed in depth, Estonia, Latvia, Lithuania, Poland and the Slovak Republic, were chosen for the following reasons:

- Poland is the largest of the New Member States; it also was one of the earliest administrative reformers in the region on certain aspects of civil service development and some elements of administrative restructuring. At the same time, the continued high degree of political polarization in Poland has set strong limitations on the ability of reforms and innovations to take root. Nevertheless, the Polish case was expected to generate benchmarks on issues such as HRM systems and structural fund management.

- Estonia is generally recognized as one of the European pioneers in the development of e-Governance, including the application of e-Governance solutions to public service delivery.
- Latvia and Lithuania are known for their attempts to reform policy management processes based on performance principles. These two states have taken fundamentally different approaches and in both cases important progress has been reported. In terms of the implementation of structural funds and overall policy coordination capacity, these are highly significant reforms.
- The Slovak Republic conducted a partially successful restructuring of the central administration in 2000–01, followed by a number of high profile single agency reforms in the Ministries of Finance and Labor, in particular.

The other three EU8 countries lack similar distinct reform initiatives that could provide best practice examples. The Czech Republic remains a laggard in administrative reform issues, while Slovenia, though often seen as an example by former Yugoslav states, has shown little progress in administrative reform implementation, at least until recently. Hungary was the earliest reformer among the EU8, but reforms have seen little progress since the mid-1990s, when Hungary was advanced in civil service reform and in the introduction of strategic planning, only to have progress stalled in the late 1990s when other states moved forward (Vass, 2005). Some noteworthy attempts at innovation, such as the introduction of a Senior Executive Service, have been caught up in political polarization (Vass, 2005; Meyer-Sahling, 2006) and have not yet come to sufficient fruition.

## Performance Management and Strategic Planning

Performance management and strategic planning both are important ingredients of high quality public administration systems in their own right. For the reasons outlined above, in this study they will be reviewed together.

### *Performance Management Approaches and Their Application*

Performance based approaches to public management have their origin in the English-speaking countries of the OECD, but have been successfully introduced in Northern Europe as well as in traditional Continental public administration systems such as Austria. Many other systems have experimented with the introduction of performance management systems in single agencies or sectors (for example, France).

Moreover, the CAF which was designed as the agreed system for administrative quality assessment for the EU Member States,[8] is based on a performance logic, which makes the introduction of performance principles in public management an even more logical step for the New Member States. Finally, well-designed performance management systems

8. The CAF was first adopted in 2001 and has gradually been rolled out across the EU; a third amended version of the instrument was recently completed and is being used in more than 800 public sector organizations in the EU.

can significantly enhance transparency and thus mitigate the risks of corruption. The development of a performance based approach to public management requires some significant investment in capacity, and its successful introduction strongly depends on the quality and realism of its design.

Introducing performance based systems holds important advantages for New Member States. With the disappearance of EU accession as an overriding policy priority, New Member States would need to re-define their strategic priorities and establish policies that would contribute to their continued competitiveness in the context of the EU and would ensure that they would become successful member states. A performance based framework, based on strategic priorities, would help in retaining some of the discipline that characterized the public management systems in the final years of the accession process and would also ensure continuity in institutional development.

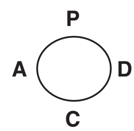
*Defining Comparators.* The World Bank publication Increasing Government Effectiveness (2005) provides a digest of best practices in performance management and highlights 11 benchmarks for successful performance management systems (World Bank 2005, pp. 92–93 and Box 3.1). Four of the EU8 countries were reviewed according to these indicators. For comparative purposes we will apply an overall rating based on the five point rating system used in the Common Assessment Framework (www.eipa.nl/CAF), presented in Figure 3.1.

The eleven comparators outlined in Box 3.1 basically break down into four main features; clarity and comprehensiveness of the framework (points i to iii); accountability (iv to vi); flexibility and delegation (vii and viii); and capacity (ix to xi). These four main categories will be used to group the assessment of the selected cases below.

**Box 3.1: Performance Management Benchmarks**

i. Performance expectations are clearly articulated and linked to government, ministry, agency, department, and individual levels.
ii. Government and ministry performance goals contained in ministry strategic plans are reflected in individual performance contracts, particularly at the senior management level.
iii. An objective framework exists within which performance rankings are assigned.
iv. Clear lines of accountability exist–for each expected result, the person being evaluated knows to whom they are responsible for producing that outcome.
v. Performance expectations are shared in advance–it is unfair and dysfunctional to assess individual performance if the expected results have not been stated with sufficient clarity beforehand.
vi. Accountability is a two way street–performance expectations must be feasible and the necessary resources must be made available.
vii. Sufficient flexibility exists within the framework to account for and adapt to unforeseen circumstances or unanticipated events.
viii. Appropriate levels of delegation exist–if someone is accountable for producing a particular result, then they must be delegated sufficient authority and resources to realize the desired result.
ix. Sufficient capacity exists within or can be recruited into the civil service to accept increased responsibility and meet demands for improved performance.
x. A central agency function exists to review and continuously improve performance management and measurement.
xi. Internal audit systems exist to ensure ministry compliance and improve performance.

**Figure 3.1. CAF Rating Scale**

| | | |
|---|---|---|
| 0 | No evidence or only anecdotal evidence of an approach | |
| 1 | An approach is planned | PLAN |
| 2 | An approach is planned and implemented | DO |
| 3 | An approach is planned and implemented and reviewed | CHECK |
| 4 | An approach is planned and implemented and reviewed on the basis of benchmarking data and adjusted accordingly | ACT |
| 5 | An approach is planned and implemented and reviewed on the basis of benchmarking data and adjusted accordingly and fully integrated into the organization |   |

*Source:* Based on the CAF framework presented on www.eipa.nl/CAF

## *Performance Management Practices in the EU8: Partial, Incremental, but with Some Promise*

The in-depth review of the four states highlighted three interesting and diverse examples of attempts to introduce performance management systems. Two of these are government-wide (Lithuania and Latvia), and one is institution-specific and concerns the Ministries of Finance and Labor[9] (Slovak Republic). There is no evidence of the systemic introduction of performance management approaches as yet in Poland, nor has there been an in-depth review for the other three states.

*Clarity and Comprehensiveness.* In terms of the clarity and comprehensiveness of the framework, only Latvia and Lithuania have initiated the development of government-wide systems, while the Slovak Republic has put in place performance management systems in selected individual institutions.

The Latvian system is based on a set of central methodologies and guidelines provided by the State Chancellery. The system is built on a radically reformed State Chancellery which under the management of Gunta Veismane was transformed from a largely administrative body to a center for innovation in policy planning, coordination and impact assessment. An individual performance appraisal system has been in place for top level officials since 1996, but the so-called management contract system functioned more as a rationale for paying higher salaries than as a proper performance appraisal system (Brown, Rimkute, and others 2006). For those officials not on management contracts, no adequate performance appraisal system was in operation. This will be addressed through the introduction of a new wage and performance appraisal system, planned for 2007, which is based on a competency framework and will better reflect the needs of a performance based system.

9. Only related to the management of service delivery.

The Lithuanian system is centrally led by the State Chancellery and the Ministry of Finance, and has gradually evolved from a relatively simple expenditure prioritization system to an effective policy management system in the run-up to EU membership. An effective link between government-wide and institutional priorities is in place, and a link with medium-term budget planning has been in operation for the past four years.

Lithuania has become an outstanding example of how to effectively run a performance-based policy management system. What remains is the adoption of a satisfactory individual level performance appraisal system, which, regardless of serious efforts to ensure its introduction over the last three years, is still not effective. Based on the Latvian example, this would probably require an overhaul of the wage and job classification system, which has been proposed (World Bank 2004) but not yet implemented.

Regarding the Slovak case, some ministries have experimented with performance management systems internally, particularly the Ministry of Finance. The lack of a strong central driver for institutional reform overall (regardless of the establishment of a Reform Unit in the Office of the Government in 2002) has led to a decentralized approach to institutional reform that has created strong disparities in overall government capacity and has reduced the overall effectiveness of the public management system (Staronova and Brown 2006). However, those ministries that have introduced performance management practices provide a strong example of how an integrated system of organizational and individual performance objectives can operate.

On this first issue, none of the three states that have experimented with performance management approaches have put in place a full-fledged system, though Lithuania and Latvia both have a strong potential to do so. The Slovak case depends more on the approach that the new government will take to public management innovations: if there is a concerted effort to roll out performance based practices, building on previous ministry-based approaches, the potential to build performance based management systems is in place—but significant investments would be required in enhancing central management structures and building capacity in lagging ministries.

*Accountability for Performance.* Latvia and Lithuania have established strong accountability and reporting mechanisms at the government-wide and institutional levels, but this has not yet been brought down to the level of individual officials.

Latvia is the most advanced among the EU8 in designing a new and state-of-the art individual appraisal system, but this is not yet operational and its previous "management contract" system is far from being an example of good practice. Lithuania's system remains weak at the level of measuring individual performance. Among the other states reviewed in detail, the Slovak Republic does not have a government-wide performance appraisal system. Poland, regardless of having the longest record, among the five states studied in-depth, of implementing the civil service law, has yet to put in place a consistent approach to performance appraisal at the individual level. The desk review of the other three states does not reveal any further cases of particular interest.

*Flexibility and Delegation.* The Medium Term Budget Planning system in Lithuania as well as that planned in Latvia include sufficient flexibility to adapt budgets to unforeseen circumstances, as budget ceilings will provide ministries with enhanced flexibility in meeting performance targets. The Slovak Republic has experimented with its own brand of flexibility, allowing ministries to use savings on wage bill funds to provide enhanced incentives for well- performing staff, although this effort has been largely limited to wage fund allocation.

In terms of adequate levels of delegation of responsibility this remains problematic across the board. In part, this issue is reflected in problems regarding policy coordination, which will be discussed in the next section.

*Capacity.* Capacity constraints remain a serious problem for the introduction of effective performance management systems. Capacity is defined in the criteria above as human resource capacity, central management capacity and management control capacity.

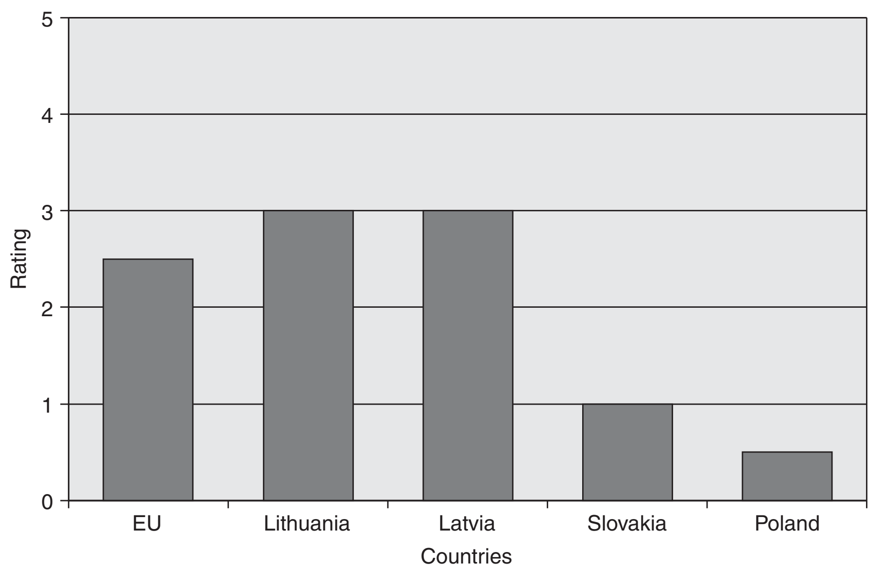
Regarding central management capacity, Latvia and Lithuania have performed well, as both have invested significantly in their central management institutions to drive the establishment of a performance culture in public management, which is weak in the other states. Reform attempts in the government offices of the Slovak Republic (2002–03), Poland (1996–97) and Hungary (under the last three governments) have failed to achieve results in terms of improved central management of the administration. This is due mainly to coalition politics interfering with the need to establish a strong center of government (Peters, Vass and Verheijen 2005).

Human resources capacity also remains an issue, as turnover ratios in the civil service have remained stubbornly high in Latvia, Poland and the Slovak Republic, though less so in Lithuania (World Bank 2004; Brown, Rimkute, and others 2006). Establishing a public management system based on performance principles requires institutional stability as well as training and staff development. Institutional stability has remained elusive in most of the EU8 states owing to continued politicization (in Poland, Hungary and the Slovak Republic in particular) and to the lack of sufficiently strong incentive systems (in Latvia and to a lesser degree Lithuania). Even for the most advanced public management systems, (those in Latvia and Lithuania) questions remain as to how they can grow without a serious change in incentive systems (Brown, Rimkute, and others 2006).

Regarding the development of management control capacity more progress has taken place as this was a significant element of the EU membership preparation process. Internal audit systems are a key administrative capacity requirement and a sine qua non for the allocation of EU funds. While this was a new aspect of public management for all of the states concerned, internal audit systems were established before EU accession and are functional.

*Rating.* If we extrapolate the above qualitative analysis to the CAF rating scale in Figure 3.1, it is obvious that no EU8 country has established a fully fledged performance management approach (see Figure 3.2). Both Lithuania and Latvia would have a good rating at around level 3 on the CAF rating scale, with a planned, implemented and reviewed performance management system in place, even if not yet fully functional across all elements of the system. Whereas in the Slovak case the Ministry of Finance would rate between level 2 and level 3, the system as a whole would rate at level 1, with a performance management approach planned following the 2000 "audit" of the central administration (www.ineko.sk) but never fully rolled out. Poland would rate at level 0.5, with no structurally planned approach in place as yet. Based on desk reviews, Hungary, the Czech Republic, Slovenia

**Figure 3.2. Performance Management Benchmarked Against the EU Average**




and Estonia would not rate above level 1; although their performance based approaches may have been planned, they have not yet been introduced.

A good proxy for performance management systems would be the average of European organizations that have participated in the CAF and posted their evaluations on the CAF web-site (www.eipa.nl/CAF), as all nine CAF indicators relate to performance based approaches. The latest rating across the EU (from February 2005) comes to an average of approximately 2.5 on all scores. It should be noted that entire government approaches are more difficult to implement, but nevertheless the CAF provides a good relative indication of where the New Member States stand. While Latvia and Lithuania exceed the European average, the other New Member States would fall below the European average when it comes to overall performance management approaches.

## *Strategic Planning*

Reviews of best practices in strategic planning, as presented in Increasing Government Effectiveness and further specified in the pilot country study on Poland conducted in the context of this study, point to the good practice indicators on strategic planning systems presented in Box 3.2. The comparison across the countries reviewed will also be based on the CAF rating system, as the CAF provides a specific rating for strategic planning capacity. As with other issues, this relates to the performance of individual organizations rather than the government as a whole, but the comparison with European averages nevertheless provides a good approximate point of reference for strategic planning in the New Member States.

**Box 3.2: Strategic Planning Benchmarks**

i. A **high level decision making forum** exists within which the necessary policy and fiscal trade-offs can be made.
ii. Consistency and coherence are reflected in the key **public vehicles** through which the government announces its policy and financial goals.
iii. An approved publicly released document links **ministry strategic plans** to their budget.
iv. **Codified procedures and standards** exist to guide ministries in the preparation of materials that succinctly provide decision makers with realistic options and clearly express the policy and fiscal impacts of these options.
v. **Central agencies** ensure that the process is well managed and provide a quality assurance role.
vi. **Policy and impact assessment instruments** are used to precede and/or accompany the review of complex legal instruments.
vii. **The policy and financial review procedures are coordinated,** although it is not unusual for governments to undertake these reviews separately; ultimate approval must be informed by both assessments.
viii. **The policy and legal impact reviews are coordinated.**
ix. **Active agenda management for cabinet and sub-committee meetings**—deadlines for proposals are set well in advance; progress is monitored and significant delays in the preparation of reviews rarely occur.

### *Strategic Planning Practices: How to Move Beyond the Accession Process?*

Strategic planning was the starting point for institutional reform in Latvia and Lithuania. Over the last seven years the strategic planning process in both states has moved from being a filtering mechanism in the decision-making process to a comprehensive policy management system that includes fiscal and regulatory impact assessment. The latter was driven by EU accession considerations and was born out of the process of defining negotiation positions and enhanced public consultation mechanisms and an improved policy planning-budget linkage. Capacity building efforts have reached down into the ministries, and in Lithuania, the Lithuanian Institute of Public Administration has become a key vehicle for the roll-out of strategic planning capacity to lower levels of the administration. In addition, Lithuanian municipalities have engaged in strategic planning processes of their own (though, in many instances, these have been based on the central strategic planning manual), with Vilnius considered one of the leading examples of strategic municipal planning in Europe. Considering the benchmarking criteria above, Lithuania performs well in virtually all aspects of such planning, particularly in the performance of high level decision making bodies (the Strategic Planning Committee of the government) and central structures (the Strategic Planning Department at the State Chancellery) and in impact assessment (driven mainly by the EI coordination unit), and has reviewed and upgraded its practices over time.

The Latvian strategic planning process was anchored in the 2001 Public Administration Reform Strategy. As in the Lithuanian case, strong emphasis has been placed on policy impact assessment, and, more specific to Latvia, on public consultation. This includes posting all government policy proposals on the government's web-site for comments and inputs. One aspect in which the Latvian strategic planning process is more at risk of reversal is that of the political decision-making structure, which is less well enshrined than the Lithuanian Strategic Planning committee and more prone to ad hoc political intervention (Brown, Rimkute, and others 2006). The ministerial capacity to effectively conduct strategic planning is still constrained by high turnover and limited capacity, an issue that is expected to be addressed through the introduction of the new wage and job classification system in 2007.

The other two states that were reviewed in-depth, Poland and the Slovak Republic, have not introduced over-arching strategic planning systems. Poland has no over-arching government strategic planning document and no high level strategic forum to coordinate trade-offs. It suffers from weak policy coordination, a high degree of formality in legal and fiscal impact assessment (employing process orientation rather than strategic orientation) and a lack of steering capacity in the government office (World Bank, 2006a). Thus, Poland would fail in virtually all of the benchmarks for good strategic planning.

The Slovak case is somewhat different. The foundation for a strategic planning system was laid in 2001 with the establishment of a Central Policy Planning Unit in the Office of the Government, tasked with the design and implementation of policy impact assessment systems and policy planning guidelines. However, the reduced influence of the Office of the Government after 2002 led to the eventual abandonment of many of the innovations that had been planned. One element of strategic planning that has been introduced is the mandatory preparation of analytical papers before the preparation of legislation, which aims to remove the 'legal bias' from the policy process and improve fiscal and legal impact analysis. In addition, some institution-specific innovations, particularly in the Ministry of Finance, should be noted. Deficiencies in the policy management process constitute a major risk regarding the ability of the Slovak authorities to effectively plan and use structural funds; it is therefore crucial for the incoming government to re-launch the stalled process of public management reform.

Reviews of the other EU8 states did not provide further examples of effective strategic planning processes. Hungary pioneered strategic planning in the mid-1990s (Verheijen and Coombes 1998), but attempts to strengthen the Prime Minister's office as a locus for strategic planning have fallen foul of increased political polarization. Similarly, reforms in the Czech Republic and Estonia have failed to bring significant change to the policy process and in the former country have given rise to concerns about structural funds planning.

*Rating.* Using the same rating scale as applied above on overall performance management practices, Lithuania and Latvia would rate at 4 and 3.5, respectively, while the Slovak Republic's rating would be 1.5 compared to Poland at 0.5 (see Figure 3.3). Ratings of other EU8 states, based on the available information, would not exceed the Slovak 1.5, which signifies that some strategic planning implementation measures have been taken but that the approach remains at the planning stage.

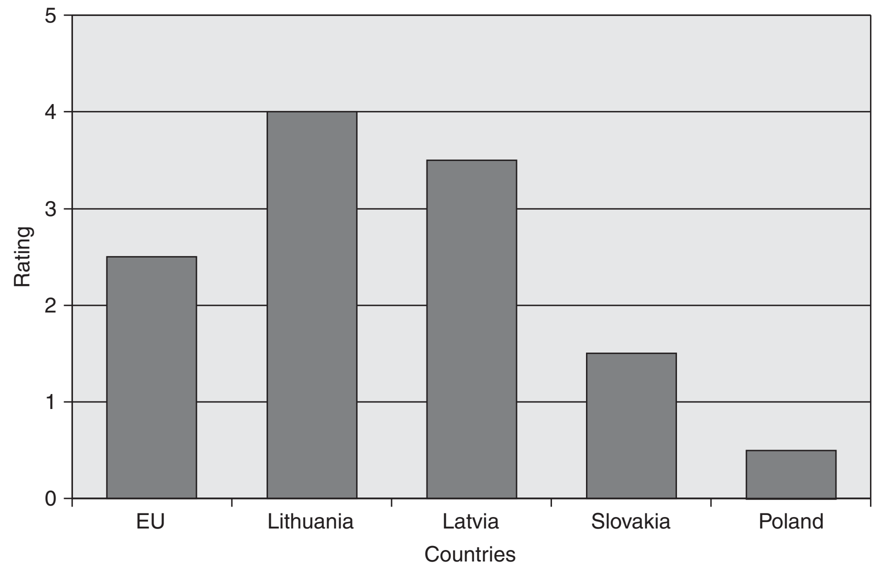
Comparing these ratings with the average European public sector organizations mentioned in the February 2005 CAF report, the average rating for strategic planning was 2.6 out of 135 organizations that provided data. Thus, apart from Latvia and Lithuania, the other states would rate significantly below the average. [10]

## Policy Coordination

The main comparative tool for coordinating capacity is the so-called Metcalfe Coordination Scale, designed by Professor Les Metcalfe in the 1980s as part of the analysis and assessment

10. This of course would not rule out the possibility that individual organizations in these states could attain a higher rating.

**Figure 3.3. Strategic Planning Benchmarked Against the EU Average**




work following the Spanish and Portuguese entry to the EU. The nine point rating scale (Metcalfe, 1994), presented in Figure 3.4, is suitable for assessing both horizontal and vertical coordination processes and is a cumulative (Guttman) scale, well suited for comparative analysis across states.

## *Reviewing Coordination Practices: A Dangerous Sub-Optimum*

The review of four states included in this study highlights the following three main issues:

**Figure 3.4. The Policy Coordination Scale**

9. Overall Strategy
8. Establishing Priorities
7. Setting Parameters for Action
6. Arbitration of Policy Differences
5. Search for Agreement on Policies
4. Avoiding Divergences among Organizations
3. Consultation with other Organizations (Feedback)
2. Communication to other Organizations (Information Exchange)
1. Independent Organizational Decision-Making

*Source:* Based on Metcalfe (1993).

- Overall coordination patterns are sub-optimal in three of the four states reviewed, especially when compared to Metcalfe's rating of the old member states in 1994 and the fact that most of these states have evolved since then.
- There is still a strong qualitative difference between specific EI coordination processes and overall coordination practices in the policy process, though in stronger performing states (such as Lithuania) the gap is narrowing.
- There appears to be a strong correlation between the introduction of innovations such as performance management systems and the quality of coordination.

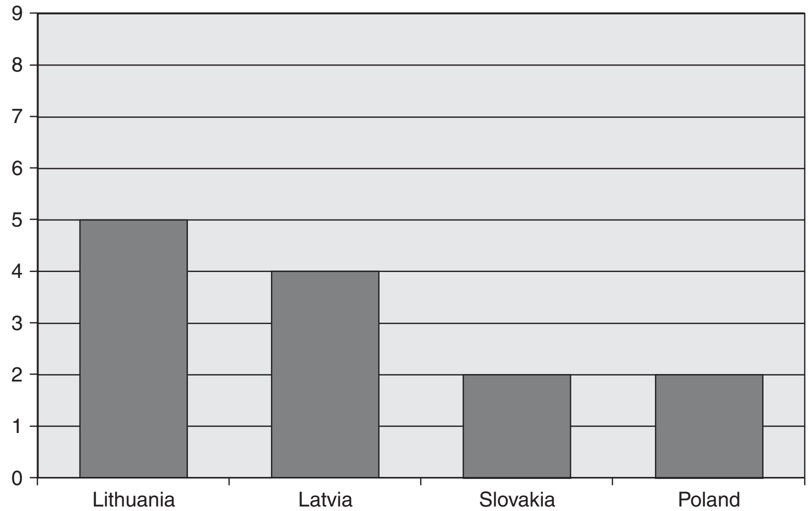
On the first issue, the review work conducted for four states found that only Lithuania would rate at level 5 or 6 (the desired minimum level of policy coordination, depending on whether a state has a more bottom-up or more top-down policy management system). The Slovak Republic and Poland would not rate higher than level 2 (well below the levels that would be considered effective for domestic policy formulation). In neither of these two states is there evidence that standard processes for policy coordination have worked effectively, and there is little proactive coordination beyond information exchange which is due largely to the lack of effective delegation within the public administration systems of both states. This, in turn, is determined by the general lack of progress in settling key aspects of politico-administrative relations.

In the case of Poland, the degree of vertical coordination between levels of government, which is an important determining factor for the successful implementation of EU structural funds, is rated higher at level 5 (Search for Agreement on policies). However, if horizontal coordination issues at the center are not addressed, the impact of this on effective performance in structural fund implementation is likely to remain limited as the planning process involves a large number of institutions at the central government level.

The Latvian case is less straightforward, as there are different interpretations of the way in which the Latvian system of domestic policy coordination functions. Initial reviews led to the conclusion that level 3 would be the most appropriate classification for the Latvian system, though other expert opinions rated the system at level 4 (Brown, Rimkute, and others 2006) (see Figure 3.5). The full introduction of the Policy Planning Guidelines from 2007 is likely to enhance coordination levels in the system.

Regarding the second point above, ratings change significantly if EI coordination systems are considered separately (see Figure 3.6). Latvia and Lithuania would both rate at very high levels (7 and 8, respectively), akin to advanced EU member states such as Denmark and the United Kingdom in the initial Metcalfe study (1994). Using the same criteria, the Polish system would rate at level 4, which signifies a reduced level compared to what would have been the case before EU accession. Poland had one of the strongest EI coordination systems among the EU8, but it has been gradually dismantled. The Slovak system would rate lower at level 3, slightly higher than the domestic policy coordination system, but not significantly, which also in this case expressed a weakening of the system following EU accession as the EI unit at the Office of the Government has gradually lost influence as well as qualified staff. Of the states not studied in depth, the ratings of the Czech Republic would not be expected to exceed the Slovak ratings, while Hungary would rate higher (around level 5) on European issues. Like the two Baltic States, Hungary had a strong EI coordination system in place.

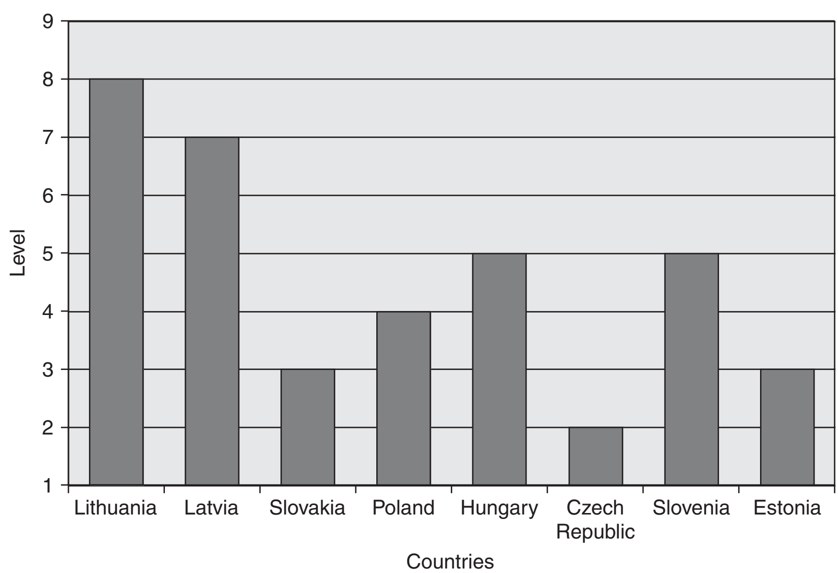
**Figure 3.5. Overall Coordination Levels**




The correlation between the introduction of performance management systems and the quality of policy coordination is clear, as the states with the most advanced performance management systems also have a stronger record on policy coordination.

In general, the policy coordination systems of the states reviewed follow the pattern of the EU-15 where EI policy coordination is concerned, with Latvia, Lithuania and Hungary

**Figure 3.6. EI Coordination**



following the pattern of advanced states such as the United Kingdom, Denmark and Finland, while Poland, the Czech Republic, the Slovak Republic and Estonia would rank in the less advanced group of states, which would also include Italy and Greece.

The Polish case remains somewhat unusual, as several recent high profile cases over the last six months of Poland pursuing its national interest create the impression of a well-coordinated machinery, based on a well-elaborated set of priorities. However, it should be noted that these cases involved issues related to high politics, and thus were mainly driven by members of the government at a personal level. In addition, even on these issues the way in which the negotiations were handled provided an indication of weaknesses in the internal coordination process in the administration, as the positions taken were in most instances not realistic and not well underpinned in substantive terms. The Estonian case is interesting because, as the smallest of the EU8, the country's coordination issues might be expected to be less problematic. However, the SIGMA Civil Service Review of 2003 (SIGMA 2003) as well as later assessments (Sootla 2005) highlighted coordination issues as being one of the major problems of the Estonian public management system (as was the case in Poland), in spite of the strong performance of the country in preparing for EU membership.

The main concern is that the quality of the domestic policy coordination process (which is the main vehicle for policy implementation, including structural fund implementation) continues to lag behind the more advanced EI coordination mechanisms. This provides further evidence that innovations introduced in the EU accession process have not transferred successfully to the general policy process and appear to be eroding in several of the states discussed here, thus posing further risks of backsliding in administrative development and for the implementation of EU funds.

## HRM Systems

In terms of HRM systems, the SIGMA baseline system (although mostly based on a formal-legal assessment) is still the most applicable benchmarking system. This is reflected in its increasingly broad application, which goes beyond the immediate group of EU candidate states through self-assessments in Ukraine and baseline reviews at the federal level in Russia as well as in some five Russian regions.

The main elements of the HRM baseline assessment are summarized in Box 3.3. The baseline assessment was originally conducted on the basis of a seven point qualitative rating scale;[11] this was later abandoned and led to a fully narrative evaluation that posed risks of subjectivity to the application. In addition, the emphasis on the use of the assessment tool changed from a focus that was largely on HRM to a greater emphasis on administrative procedures and processes.

In the context of this study, we will focus specifically on the development of horizontal HRM systems (item 4), and on conditions of service (particular incentives) and politicization (all under item 5).

11. The rating system ranged from level 1: standard achieved; level 2: standard substantially achieved; level 3: standard only partially achieved; level 4: standard not yet achieved but progress being made; level 5: standard not yet achieved; level 6: standard unlikely to be achieved in the medium term; to level 7: standard unlikely to be achieved under present arrangements.

**Box 3.3: The Main Elements of the HRM Baseline Assessment**

1. **Legal Status of Public Servants**

   Does an appropriate legal basis exist defining the status of public servants responsible for advising on and implementing government policy, carrying out administrative actions and ensuring service delivery, in a way compatible with prevailing standards in EU member states?

2. **Legality and Accountability**

   The general legal administrative framework and administrative practices guarantee the principle of legality in administrative decision-making and are sufficient and appropriate to guide civil servants and make them accountable for their performance.

   2.1. Do all actions taken by public servants have a clear basis in law or in appropriate regulations?

   2.2. Are public servants responsible to their superiors under public law?

   2.3. Are effective accountability mechanisms in place?

3. **Impartiality and Integrity**

   The necessary conditions are in place to ensure that officials can act independently of political influence and an effective ethical infrastructure is in place to prevent bias in administrative decision-making.

   3.1. Are administrative actions taken independently of the personal interests of public servants and without favoring any other illegitimate interest?

   3.2. Is corruption and are other abuses of power subject to effective disciplinary and penal remedies?

   3.3. Are salary structures legally defined and salary levels openly disclosed?

   3.4. Do public servants act independently of party and organized political influence?

4. **Efficiency in Management of Public Servants and Control of Staffing**

   A cross governmental structure and system for personnel management is established and ensures the application of homogenous standards across the administration.

   4.1 Is a cross-governmental structure and are systems for personnel management established?

   4.2 Do management practices ensure that public servants are motivated to perform well?

   4.3 Are the numbers of staff and personnel costs controlled and published?

   4.4 Do staff representatives participate in the decision-making and control concerning personnel management matters?

5. **Professionalism and Stability of Public Servants**

   Legal frameworks, management practices and reward systems ensure the development of a merit based system.

   5.1 Do legal frameworks and management practices provide for the open and competitive selection of public servants based on merit and transparent criteria?

   5.2 Do conditions of service and career opportunities ensure that public servants with appropriate knowledge and skills are recruited, developed and retained?

   5.3 Do sufficient and reasonable mechanisms (basically mobility, training, and motivation) exist for good performance and career development within the civil service so as to make it attractive?

6. **Development of Civil Service Capacities in the Area of European Integration**

   6.1 Have adequate staff resources been assigned to units charged with coordinating and managing EU affairs?

   6.2 Do incentive systems and other mechanisms (e.g., staff rotation systems, secondment) ensure that European Integration functions are staffed by sufficiently qualified civil servants and that a high level of stability in staff is achieved?

   6.3 Are special training programs in place to prepare the civil service for the implications of EU membership?

### *HRM Systems, In Overall Decline*

HRM systems have remained the Achilles' heel of public management systems in the New Member States. While progress, or at least selected innovations are evident for most aspects of public management in each of the EU8 states, there is still too little progress in HRM system development.

*Legislation: Backtracking.* Civil service laws were adopted in all New Member States before accession, as this was one of the few sine qua non of EU-related administrative capacity requirements. However, this did not imply that laws needed to be effective as of the date of membership. For example, in the Czech Republic the Civil Service Law has still not become effective more than two years after accession, and following the 2006 elections there are serious doubts as to whether it will ever be implemented (Vidlakova, 2006). The laws in the Slovak Republic and Poland are on the point of either being revoked or made ineffective.

The situation in Latvia and Lithuania is marginally better, as legislation adopted in 2001–02 has been implemented and the legal framework for the civil service in Latvia could see a significant further improvement once the new Law on Civil Service Wages becomes effective in 2007. Among the eight New Member States, these are the only two cases in which there has been a certain degree of consistency in the legislative framework for the Civil Service over the last five years.

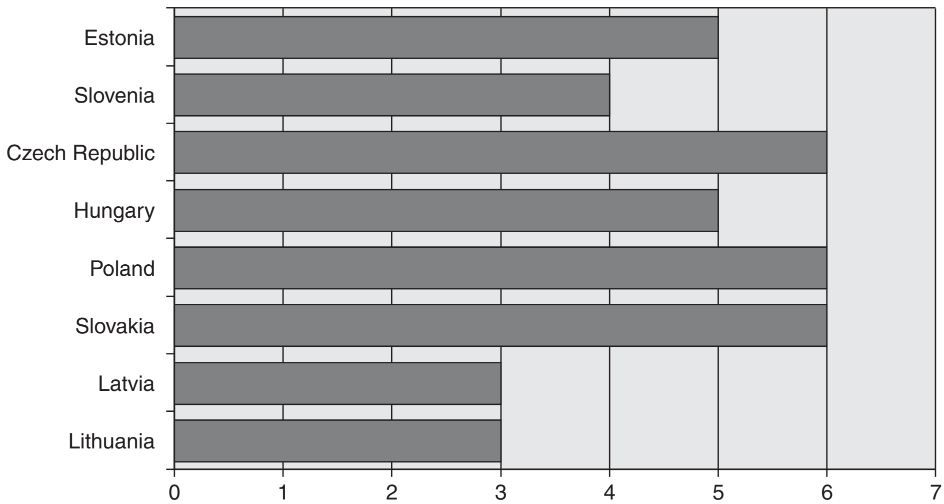
The implementation of Slovenia's Civil Service Law started just before the EU accession and has not led to a major change of direction in what remains a strongly politicized civil service system (Hacek 2006).

In conclusion, whereas all but one of the EU8 would have achieved the baseline for legislation at the time of accession (the Czech Republic was the only country not to have a civil service law in effect at that time), a repeat assessment in 2006 would provide a rather more sober picture, with three of the EU8 (Poland, the Slovak Republic and the Czech Republic) having revoked the legislation or rendered it ineffective and two states (Hungary and Estonia) having failed to resolve the deficiencies noted in the last SIGMA assessment conducted in 2003. Thus, if a SIGMA review were conducted today, the majority of the EU8 countries would fall in the "baseline not yet achieved" category, with a negative trend of "baseline unlikely to be achieved in the medium term" for Poland, the Slovak Republic and the Czech Republic, which would put them at point 6 or 7 on the seven point rating scale (see Figure 3.7).

It is important to draw the right conclusions from this development. One of the main points brought out in discussions with officials and experts from the New Member States is that the legislation adopted under pressure from the EU is not suitable for the specific political and economic conditions in Central and Eastern European states. The polarized political process combined, in most states, with a highly dynamic labor market makes static employment models based on job security unpopular among both potential candidates for civil service positions and politicians. Thus, a new model that would provide more incentives (for example, rapid career growth possibilities and performance elements), with some degree of flexibility in appointments and dismissals, would probably be more viable at the current stage of development.

*Horizontal Management Systems: In the Process of Being Dismantled.* In a similar way to the legislation on which they were based, many of the horizontal civil service management

**Figure 3.7. Civil Service Legislation**




*Note:* Level 1 is the highest and, level 7 is the lowest rating.

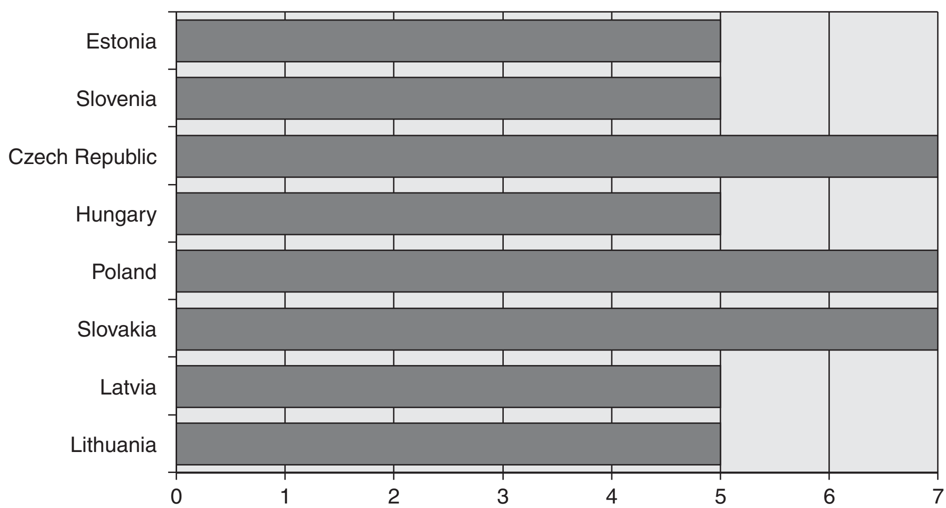
systems that were put in place before EU membership have been gradually dismantled after accession.

Apart from the move to abolish the Civil Service Offices in Poland and the Slovak Republic (discussed previously), the role of the Civil Service Policy Department in the Ministry of Interior in Hungary has gradually diminished, leaving virtually no central policy function in place on human resources issues, while the Civil Service Department under the Ministry of Interior in Lithuania has thus far not been able to establish itself as the single authority on HRM issues. The Latvian Civil Service Administration never moved beyond being a purely administrative office, which is further illustrated by the fact that amendments to the Civil Service Law introduced in 2002 moved the responsibility for personnel policy to the State Chancellery, thus rendering the Civil Service Administration further irrelevant.

The lack of a strong central authority on HRM issues, coupled with the lack of investment in the development of ministerial human resource units, has created a situation in which politicians basically have few restrictions imposed on them in terms of hiring and firing, which opens the door for the return of the highly politicized civil service systems that existed in the mid-1990s at the start of the administrative reform process.

In a context in which continuity and predictability in governance are key elements determining performance in the EU as well as competitiveness, the return to the politicized and unstable systems that marred economic management in the mid-1990s in the Slovak Republic, the Czech Republic and the Baltics is highly undesirable but becoming a fact in a growing number of states.

**Figure 3.8. HRM Systems**




*Note:* Level 1 is the highest and level 7 is the lowest rating.

The development of the central management systems was always rated as a weak element of the civil service systems in the New Member States, and the last SIGMA report issued in 2003 (OECD 2003) highlighted the existing weaknesses in the horizontal management of the civil service system across the board. However, at that time the trend was towards strengthening horizontal management, at least in the Czech Republic, the Slovak Republic and Slovenia. In the three years following the assessment, the trend became decidedly negative, with none of the EU8 countries having a solid horizontal management system for the civil service in place. This has led to a general erosion of merit principles and has opened the door to increasing levels of politicization of senior appointments. Thus, in terms of SIGMA ratings all would rate "not yet achieved" (level 5 in the seven step rating), except for Poland, the Czech Republic and the Slovak Republic, which would rate "not yet achieved and will not be achieved under current arrangements" (level 7 in the rating (see Figure 3.8).

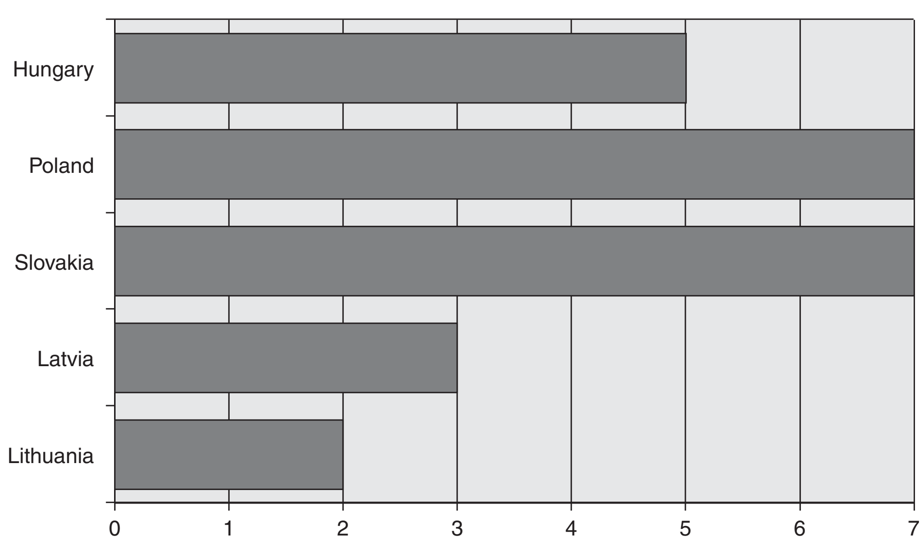
As in the case of legislation, it is important to read the right signals from this direction in institutional development. The argument generally made is that the civil service agencies as they were conceived in the early years of the decade were focused too much on legislation and control functions and too little on strategy and management. Thus, functions such as labor market research, career tracking and related issues were neglected, although it was these issues that were important in the development of the civil service as a professional institution. Civil service agencies were perceived as overly administrative and conservative and found little support when politicians moved to dismantle them. A new generation of management structures, lighter in approach and with a focus on supporting the development of a more dynamic civil service, would need to replace them, since leaving administrations without any central management function is certain to pose a danger of further erosion of the nascent civil service systems in Central and Eastern Europe.

*Politicization on the Return.* Political appointments have been re-institutionalized in most of the EU8 countries, either directly, as in Poland and the Slovak Republic, or indirectly, as in Hungary. In the latter case this was done through the creation of a special core group of civil servants for which recruitment and dismissal was subject to a higher degree of discretion than for other civil servants (Meyer-Sahling, 2004, and Vass, 2005).

Latvia and Lithuania are the two main counter examples on this issue. Lithuania has limited political appointments under the Civil Service Law and the Law on Public Administration to Deputy Ministers only, and each ministry can have no more than one such position. Lithuania also has a significantly lower rate of staff turnover when compared to other states. For example, in 2004 over 70 percent of civil servants had served between 3 and 12 years, and only a small proportion of civil servants had less than 3 years of experience (World Bank 2004). These are highly unusual figures for this group of countries. Latvia is putting in place a competency based system for job classification under the new Law on Civil Service Wages. These two states constitute the main exceptions to the general trend towards increasing politicization of appointments and career management.

When put in terms of the SIGMA assessment model, Lithuania would rate "substantially achieved" (level 2), while Latvia would rate one level below that (see Figure 3.9). Of the countries for which sufficient information is available to justify ratings, Hungary would rate "not yet achieved" (level 5), while the Slovak Republic and Poland would rate "not yet achieved and not likely to be achieved under current arrangements" (level 7).

**Figure 3.9. Politicization**




*Note:* Level 1 is the highest and level 7 is the lowest rating.

*Incentive Systems: A Continued Search for a Solution.* Together with the development of horizontal management systems and the stabilization of politico-administrative relations, incentive systems were the third main area identified as problematic in the 2003 SIGMA assessment. The difficulty in defining incentive systems that are geared towards attracting and retaining talented staff reflects three main factors: fiscal space, political will and tradition.

With regard to the first point, fiscal space remains limited in the EU8 countries, especially as states try to meet the Eurozone entry criteria. Improving salary levels for the Civil Service would not be a major issue in itself, as the civil service takes up only a small share of the Public Sector Wage Bill, (typically, 5–10 percent). However, the perceived linkage between civil service wages and wage levels in the broader public sector, especially in centralized sectors such as education, typically sets constraints on wage policy options.

The second point is that politicians are generally not ready to "sell" wage increases for civil servants, even if these are part of broader systemic reforms in the system. This has not been helpful, if we look at the negative response of citizens to the introduction of bonus schemes such as the management contract system in Latvia. Among the EU8 countries, only Hungary has followed an explicit policy of wage level increases based on the argument that effective participation in the EU requires a high quality civil service. Lithuania improved its wage levels with the introduction of the new Civil Service Law in 2002, which also simplified the system and enhanced the proportion of merit elements in pay as opposed to seniority. The new system made the civil service more competitive and was considered a significant improvement over the previous practice (World Bank 2004). Overall pay levels still lag significantly behind private sector pay levels, but the improvements introduced in 2002 were sufficient to re-attract staff to the civil service (World Bank 2004). The Slovak Republic employed "flexibility" in the use of wage bill budgets to operate a bonus-based system, which, though more transparent than the Latvian system, still raises issues of subjectivity and transparency in the use of budget resources. It could be a basis for a longer term solution to the problems of wage system management provided it is properly institutionalized.

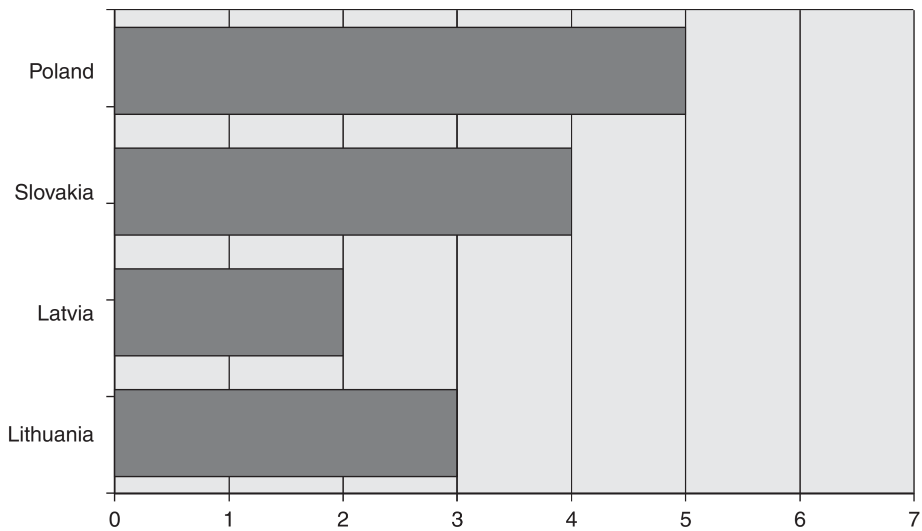
Finally, tradition makes the reform of incentive systems highly difficult. Under both the pre-communist systems and the communist regimes, the seniority principle was key to wage development in Central and Eastern Europe, and was driven by both classical notions of wage systems in the public sector (ensuring objectivity though relying mainly on seniority) and egalitarianism. Replacing systems that were based mainly on seniority by competency frameworks or performance-based wage systems has proved to be highly controversial in the region, though some progress has been made more recently in Latvia and Lithuania.

In terms of incentive systems, the assessment would be slightly more positive than for the other issues reviewed here. In terms of ratings, the Latvian system would rate at 2, "baseline substantially achieved"; Lithuania would be one level below that, and the the Slovak Republic would have a positive rating compared to the situation in 2003. However, Poland would remain at level 5 ("baseline not yet achieved") (see Figure 3.10).

## *Conclusions on HRM*

The creation of functioning HRM systems and approaches is undoubtedly the main area of failure in public management reform in the New Member States. Systems and legislation that were created in the early years of this decade in advance of EU accession

**Figure 3.10. Incentive Systems**




*Note:* Level 1 is the highest, level 7 is the lowest rating.

have been dismantled or have never been fully implemented. There is little or no evidence of success in any of the key aspects of establishing functioning HRM systems (in particular, if we look at issues of politicization, incentives and stability). The general view expressed on this issue is that the systems advocated by the European Commission in the pre-accession period were not suitable for the New Member States for two main reasons:

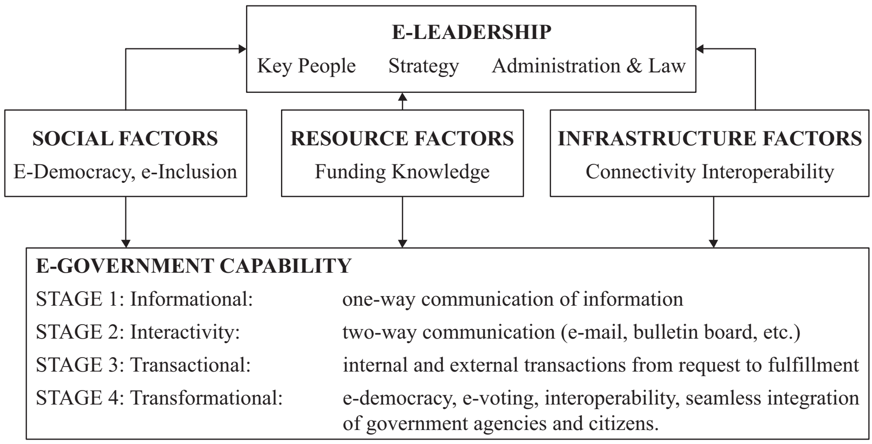
- Labor markets are inherently different, and, especially, they are more dynamic than in the old member states. This means that the needs and requirements for HRM systems are different.
- Politicians demand a certain degree of flexibility in staffing decisions that is much more pronounced than in the old member states, and the acceptance of permanence as a principle is low.

Overall, what is needed in HRM issues is "new thinking" as to both legal frameworks and institutions—a need to think in terms of strategic approaches rather than legal rights and obligations and a recognition of the fact that the old EU models do not fit the realities of the New Member States, at least not at this stage in their development. This does not mean that a full laisser-faire model should be introduced, but rather that the purpose and nature of legal and institutional frameworks needs serious reconsideration.

## E-Governance Applications

The final element of the public management systems reviewed in this study is the use of e-Governance tools in public service delivery. Two selected states, Poland and Estonia,

**Figure 3.11. Analytical Framework for e-Governance Applications**




*Source:* Estonia e-Governance Report (Combe and Brown 2006).

were reviewed using the framework in Figure 3.11 for analyzing e-Governance service provision, rating both at their stages of development.

E-government systems have been assessed in terms of enabling factors, (leadership, social, resources and infrastructure) capability and application (stages 1-4 in Figure 3.11). The findings from the review are that Estonia and Poland largely reflect two groups among EU8 states: on the one hand, Estonia and the Czech Republic, which are ahead of the other EU8 states and on a par with some of the more advanced OECD countries such as Sweden, the Netherlands and Finland; and on the other hand, a group of states including Poland and the Slovak Republic[12] where for a variety of reasons e-Governance approaches have not been mainstreamed. The only state that does not fall easily within these two categories is Slovenia, which, based on the Economist Intelligence Unit's report and other ratings (Combe and Brown 2006), falls in between.

## *Contrasting Poland and Estonia: Phases in e-Governance Capability*

The review of Poland and Estonia was expected to reveal the causes behind the difference in the spread of e-Governance applications.

First, it is important to establish how e-readiness ratings can reflect the implementation phase of the e-service regardless of their limitations. There is obviously a difference between the applications of e-Governance tools in different areas of public service delivery. The review of Poland (Brown, Silbergh, and others 2006) includes an assessment of 16 key aspects of e-public services, ranging from internal communications inside government through taxation, social security, civil and land registries, public access points and the

12. With Bulgaria and Romania notably further below.

provision of computer laboratories to schools. Of these 16 core services, only three were rated positive (land registry, social security and computer laboratories in schools) and a further three were rated partially positive. In all other areas (including public health, vehicle registry, judiciary, the e-government portal, the educational portal, taxation and procurement), implementation had not moved beyond phase 1, or in some cases has not even reached this phase. Thus, apart from isolated innovations, there is no consistent approach to the introduction of e-public services, let alone any attempt to move beyond this to a phase 4 type of interaction, such as e-voting.

Based on information from other elements of the case studies, the situation would appear to be similar to that in other states: whereas there are advanced cases in individual sectors/areas,[13] there is no overall move towards introducing e-Governance solutions. This is the case despite statements of intent, the adoption of strategic documents (Poland) or the conduct of an in-depth assessment on e-Governance potential (Lithuania).

This contrasts strongly with Estonia, where a similar review of key areas of potential e-public service delivery revealed progress in all areas assessed,[14] including complex aspects of e-Governance such as e-voting, which even advanced OECD states have often failed to introduce successfully (Combe and Brown 2006). Estonia has bundled e-public service delivery in the e-citizen system, which includes business services such as environmental permits, business registration and licences, and public health and social security systems. These are areas in which, in Poland, either progress was partial or no progress was reported.

In more advanced areas of e-Governance, such as e-voting and e-democracy, classified above as phase 4 areas, Estonia is further ahead and is classified among the most advanced OECD states as the only one among the EU8 states (Combe and Brown 2006). It should be noted that Latvia and the Slovak Republic have also shown progress in some aspects of e-democracy through their policy feedback portals.

Thus, generally, Poland (along with most other EU8 states) remains in phase 1, with some exceptions in individual policy areas, while Estonia could be firmly placed in phase 4, for establishing a functioning e-Governance system.

## *Explaining Variations in Progress: The Four Factors*

More important than the general assessment of progress given above and the best practice illustrations found in the background material (Brown, Silbergh, and others 2006; Combe and Brown 2006), is the assessment of why Estonia is well ahead of other states and to what degree the others are likely to be able to catch up.

Estonia has several important advantages over the other New Member States when it comes to the introduction of e-Governance tools, some of which are due to its geographical position and small size and others which are a result of strategic planning and effective public-private partnerships.

13. For example, in Latvia the e-portal allows citizens to comment on policy proposals; Lithuania has electronic tax administration; and the Slovak Republic provides for the publication of and commenting on annual reports of government institutions on the Internet.

14. The areas assessed do not fully overlap, though the majority are the same. In Estonia, just seven areas were reviewed, but one of these, e-citizen, included virtually all individual sector services reviewed separately in the Polish case (see Brown, Silbergh, and others 2006; Combe and Brown 2006).

First, Estonia has followed a consistent policy regarding the introduction of e-Governance over much of the last decade, and even if there is no strong top-down coordination system in place to ensure that this strategic goal is followed through, the introduction of e-Governance solutions has been consistent across the board. Informal coordination and “coaching,” together with the existence of an over-arching strategic goal, has worked well in this particular area.

Second, Estonia has paired strategy with capacity building, most importantly with the initiative of establishing the e-Governance academy (co-funded with the UNDP and the Soros Foundation), which has become a lead institution on e-Governance issues in the region. Thus, since the government has a state-of-the-art training institution at its disposal, it has been able to build on its already strong human resources base in IT.

Third, partnerships with the private sector have played a key role. This has been particularly important in relation to the banking system. The PIN code system designed for e-banking has been an important and suitable identification tool for e-Governance applications (for example, for e-voting, which would not have been feasible without this). More than 80 percent of the Estonian population uses e-banking services, thus allowing for a very wide use of tools such as e-voting.

Finally, Estonia has used its strong fiscal performance to allow for investment in strategic IT infrastructure. Estonia is the only state among the EU8 to have run a consistent (small) fiscal surplus and has thus been able to make strategic choices for investment, unlike its Baltic neighbors which both suffered from high fiscal deficits in the late 1990s, or the Slovak Republic, which needed to bring its fiscal deficit under control in 1999–2001.

As noted above, some of the factors discussed are unique to Estonia, and the country has been helped by its relatively small size and population. However, although it is important, this factor is not considered the main success factor, as the other state that has performed well in this area, the Czech Republic, is one of the larger states among the EU8, both geographically and in terms of population size.

In terms of the four factors highlighted in Figure 3.11, leadership, social factors, resources and infrastructure, leadership and fiscal resources would appear to be key issues. These are areas in which Estonia has been consistent while Poland and other states have not. In this regard, e-Governance is much like other aspects of administrative reform: leadership, consistency and medium term vision are all crucial. The strategic planning process related to the 2007–13 structural funds programming provides a unique opportunity for governments to both define and follow through on an e-Governance agenda, as well as to generate some of the necessary resources.

Resources are a second key issue. This issue has two aspects, of which the importance of human resources is often underestimated. In principle, all new member states have a good human resources base in IT issues, but moving from the availability of technical skills to their application in e-Governance solutions is not an easy step. The Estonian decision to invest in the establishment of an e-governance academy has given it a distinct advantage in this regard, though it should be emphasized that this is a regional institution open for use by other governments (and actively used especially by CIS states). The use of this capacity building facility is therefore a key factor in defining the Estonian success.

This points to a larger issue, which is that Central and Eastern European states continue to under-use capacity building as a change instrument, especially where issues of public sector reform are concerned. The use of e-Governance tools requires a serious capacity building and re-training effort—a point very often underestimated. This is also where problems arise in other states, such as the Slovak Republic, which does not have a well-functioning training infrastructure, or Lithuania and Poland, which have training systems geared mainly towards more traditional legal and procedural training programs.

Fiscal resources are a further issue, especially for those states that are struggling to meet the Eurozone entry criteria. However, as noted above, the structural fund planning window would provide a strategic opportunity for states to obtain the necessary counterpart funding and add to national resources. The fact that a capacity building facility has been added to the programming cycle could also help address some of the human resource issues outlined in the previous section.

Finally, the importance of functioning public-private partnerships is not to be underestimated, especially when it comes to more advanced applications, such as e-voting and other aspects of e-democracy. The use of secured systems developed in the private sector, especially in the banking system, would save governments significant resources and would facilitate the broad rolling out of e-services to the public, as banking systems tend to cover states as a whole. In addition, attracting strategic investment (a method successfully used by Estonia and, previously, by Ireland) will have a knock-on effect on the ability of states to define and implement e-Governance solutions.

In conclusion, even though the Estonian case is often seen as unique, this review of some of its success factors highlights the fact that these factors are not all unique to Estonia and many could in theory be replicated in other states. However, the strategic vision and political will that is required, as well as some of the strategic decisions on human resource development that need to be taken, have been in short supply in other states. Catching up with Estonia in e-Governance innovation therefore is a possibility, albeit a long-term prospect, for other states provided that they can make some of the decisions outlined above and follow through on them.

CHAPTER 4

# Replicability and How to Design a Successful Reform Agenda: A Review of Alternatives

How to design successful public management reforms is an increasingly topical question among the EU8, especially as the 2007-13 funding framework is making new resources available for capacity building. As highlighted in the previous sections, most of the successful reforms in the EU8 have been implemented step-by-step referred and, in some ways, have been opportunistic in nature, while attempts at more comprehensive design have often failed. While we accept this point, it is nevertheless important to review the reasons why certain elements of reform remained and others did not. In the previous chapter we discussed in detail the reasons for the general lack of success of civil service reforms, an area in which most states will need to rethink their options. More important, however, is the need to reflect on those reform initiatives that worked, and to determine why they worked.

## Innovations and Factors in Replicability

The public management innovations discussed in this report can be subdivided into two types: systemic changes, mainly in Latvia and Lithuania, and changes that are either institutionally confined or are concerned with specific aspects of public management such as service delivery, and which relate mainly to the Estonian and Slovak cases. While we recognize that systemic reforms have in most instances started with smaller and more contained initiatives, establishing why they developed into systemic reforms is important.

Looking at the case materials (Brown, Silbergh, and others 2006; Brown, Rimkute, and others 2006; Combe and Brown 2006; Staronova and Brown 2006), the extent to which reforms are replicable depends on several factors:

1. Driving forces, situation-specific or general.
2. Politicians and civil servants, cooperative or antagonist models.
3. Planning process, incremental or design-based.
4. Scale of reforms and fiscal requirements.

### *Replicability of Systemic Reforms*

The two cases of overall systemic reform are Latvia and Lithuania. Even though neither of these countries has fully completed its new public management system, both are sufficiently advanced to enable us to speak of successful administrative transformation.

One common element in both cases is that relatively contained but successful initiatives were used as the basis for designing broad reform strategies after the initial phase of reform had been completed. A second common element is that in both cases the reform of the State Chancellery was the starting point for broader institutional reform. Finally, the need for fiscal prudence and the demands of the European Integration process helped sustain the reform processes.

In terms of the management of the reform process, the importance of the emergence of a coalition for reform between senior officials and politicians stands out. Whereas this is more pronounced in Lithuania than in Latvia, it is a fairly unique feature in a region generally plagued by ill-functioning systems of politico-administrative relations.

Strategic planning of the reforms, though helpful, does not appear to have been a major factor in determining success, as Latvia's and Lithuania's systemic reforms emerged from more specific and contained institutional reforms. Broader reform strategies appear to have mattered only after the initial successful steps had been taken.

The main lesson from the Latvian and Lithuanian cases, therefore, would be that step-by-step reform processes, supported by both politicians and civil servants, can be a good basis for successful systemic reforms. While there were certain unique circumstances (European Integration, the convergence of interests between politicians and officials, etc.) that ensured the initial success of reforms and their expansion, there is no obvious reason why a similar approach could not work in other states, in particular considering the challenges many of them face at the current time.

### *Replicability of Selected Public Management Tools and Agency Specific Reforms*

*E-Governance Tools for Service Delivery.* In terms of innovations in using the public management tools, the Estonian e-Governance case stands out as a key example among the EU8. The success of the Estonian reform process is generally attributed to strong political leadership, a strong skill base, strategic prioritization and public investment, as well as private sector leadership in issues such as e-banking which opened up the possibilities for public e-services.

In terms of skill base, there is little that is exceptional to Estonia, at least in terms of reform potential. The IT skill base is generally strong among most of the EU8 countries, thus providing a strong enabling environment for the introduction of e-Governance based innovations. However, what is unique is the combination of a strong skill base with political leadership and strategic vision, which ensured that Estonia, unlike most other EU8 countries, capitalized on its comparative advantage.

Private sector leadership in sectors such as banking has been a further factor in the advancement of e-Governance services, as the secure electronic PINs provided by the banks gave the government a ready-made solution to some of the identification issues related to complex aspects of e-governance such as e-voting. Eighty percent of Estonian citizens use e-banking services, thus greatly facilitating the identification of e-services.

Finally, one factor that is relatively unique to Estonia is fiscal space. Estonia is the only state to have run a consistent fiscal surplus over a prolonged period of time, thus allowing for some of the necessary public investments in the e-Governance system to be made, without being hindered significantly by resource constraints. In the current fiscal context of the EU8, this is a feature that certainly limits short term replicability.

Considering the above, a fast replication of e-Governance innovations akin to that in Estonia is possible, even if not easy. Whereas basic conditions in terms of capacity are in place in most of the EU8 countries, fiscal space is limited everywhere, and political leadership is lacking in many of the other states (especially Poland and Hungary).

*Agency-Specific Reforms.* The review of the New Member States highlights a number of examples of successful agency-specific reforms, and most states have at least a few relative success stories of such reforms. One of the most interesting cases is the Slovak Republic, where the initial horizontal functional review or "audit" of the central government conducted in 2000 yielded an overall institutional reform agenda combined with agency-specific recommendations which were to be followed up by individual ministries. These reforms were introduced specifically in the Ministry of Finance, where the organization of the Ministry was fully overhauled, including the personnel management system, and in the Ministry of Labor, which conducted a fundamental reform of the service delivery system in employment and social protection.

The main question concerning the replicability of these innovations is why they would "travel" abroad if they were not replicated inside the Slovak Republic. This, indeed, is both the strength and the weakness of these examples: they could be replicable in other similar agencies in other states, but owing to their specific nature (and their linkage to the political leadership of the institutions concerned), they are more than any of the other reforms discussed here unique in their nature.

The main factor that would positively influence replicability is that most of the EU8 states continue to have administrative systems characterized by fairly autonomous ministries and agencies, thus giving ministers and managers significant leeway for conducting institutional reforms in their own organizations. This limits the chances for the successful implementation of systemic reforms (and is one of the reasons why, in Latvia, the roll-out process of systemic reforms has been greatly drawn out) but makes it easier to conduct reforms in single institutions. It is interesting to note that the Ministry of Finance reforms in the Slovak Republic would have fit quite well into the performance management systems of Latvia and Lithuania, but for several reasons the former was not rolled-out in the administration, while the latter two have found it difficult to introduce some of the personnel management reforms that were successful in the Slovak Ministry of Finance.

## *Conclusions Regarding Replicability*

The conclusion drawn from the review of these cases has to be that the more holistic, systemic reforms attempted in Latvia and Lithuania are in the long term likely to be more viable than agency driven approaches such as that chosen for the Slovak Republic. The reason for this is mainly political volatility and the fact that single agency reforms are easier to reverse than to replicate, while systemic reforms implemented over a longer time period are more likely to be sustained, even under relatively radical changes of government.

However, at the same time, it is important to note that systemic reforms in Lithuania and Latvia started from more contained process reforms, which only later were transformed into systemic reforms. What made the difference was: (i) the presence of relatively broad support for change among officials and civil servants, which existed in Latvia and, especially in Lithuania, and (ii) the fact that reforms were based in the center of government, which has an unique advantage in being able to push down systemic reforms provided the process is credible. Starting from the line ministries, or even the Ministries of Finance, could be a much more difficult path, especially in the context of the strong ministerial autonomy in Central and Eastern Europe.

CHAPTER 5

# Conclusions

A review of administrative capacity development in the New Member States of the EU provides a mixed picture of overall setbacks, especially since accession, with some promising innovations, particularly in the Baltic States. The setbacks identified are of serious concern, as they affect key aspects of the public management system, primarily the civil service. However, they are also strongly related (with hindsight) to the lack of "fit" of the models propagated by the EU in the run up to membership. This point in particular should be seriously considered by the states that are next in line.

Instability in the civil service, combined with weak policy coordination systems as identified in the review, are important risks for the successful implementation of EU funds and a threat to effective policy management overall. They also have the potential to endanger some of the economic and social gains made over the last decade.

The reforms introduced as a part of membership preparation have in many instances not "stuck" and, in particular, in Poland and the Slovak Republic (but also in Hungary and the Czech Republic), there appears to be a very strong risk of the reversal of the reforms. One important general question is why this has happened.

On the basis of the review conducted, one important factor is in some countries the hasty design of ill-fitting reforms (in the Slovak Republic in particular) under the pressure of the EU accession timetables. This prevented the formation of an adequate level of consensus on the reforms and produced solutions that were in some instances technically not sufficiently sound and that in others did not fit the realities of political and economic conditions in the countries concerned.

This appears to have been an issue in particular in contexts in which there was a fear that the EU might use the administrative capacity argument as a reason for postponing membership. This affected the Slovak Republic as a late reformer, in particular. The question is now whether a new reform program can be built around some of the successful reforms that have been piloted in individual agencies and ministries, while merit and professionalism are re-instated as principles in civil service management.

In most of the states backsliding appears to be due largely to the lack of a broad underlying consensus on the direction of reforms (Poland, Estonia and possibly Hungary) or a general lack of interest in public management reform among politicians (the Czech Republic, in particular). It was also in the Czech Republic that EU leverage was weakest, as the country could count on its economic record and political considerations to gain membership and was less dependent than the others on merit.

The lack of underlying consensus has been clearly visible in the merry-go-round of reforms in the civil service in both Poland (with successive adoption and abolition of civil service legislation and related management institutions) and Hungary (with the machinations surrounding the introduction of the Senior Executive Services between 2000 and 2004). This may not come as a surprise, as these states are politically highly polarized. Why this has had less effect on the Slovak Republic, also a polarized state, may simply reflect the high degree of continuity in government between 1998 and 2006.

Estonia remains a more difficult case to explain, as there is neither very strong polarization nor a strong political interest in the status quo. Unfortunately, we were not able to find a real answer to the lack of overall progress in administrative development in this particular case.

The six cases of stagnation and backsliding tell us something about the drivers of reform (the need for consensus, technically sound design, motivation and fit with political and labor market conditions). This was by and large confirmed by the two more successful cases in terms of policy management reforms (Latvia and Lithuania).

The case of Latvia is particularly interesting considering the administrative chaos created by the experimentation of the mid-1990s—although Lithuania is hardly less interesting, as it was deemed at that time to have one of the most unreformable administrative systems among the EU candidate states. EU pressure was significant in both cases, and membership was not guaranteed until relatively late in the accession process. This would suggest a parallel with the Slovakia Republic. However, the latter only began to deal seriously with administrative capacity issues in 2000–01, following two years of severe structural economic reform and had to design its reform mostly with outside help, as the internal administrative capacity was either not available or impossible to mobilize. In contrast, the Lithuanian reform process started in 1998, while in Latvia much of the basic work was initiated even earlier. Lithuania and Latvia therefore had advantages in all three areas: relative consensus (paired with a relative lack of polarization), strong technical design (and the presence of a critical mass of reform-minded officials) and motivation.

The cases also provide some important lessons for both the process and the substance of reform. For the reform process, consensus, technical capability and motivation are essential features, and, based on the Latvian and Lithuanian cases, it may take years (and relative administrative stability) to achieve them successfully. Whereas EU membership is a motivator (see the Slovak Republic), membership on its own is insufficient because: (i) EU pressure on administrative capacity does not carry sufficient credibility owing to the way in which it has been used; and (i) membership time horizons are often too short for the completion of a full cycle of administrative reform, at least for the EU8.

These two factors limit the relevance of EU motivation in driving sustainable reforms. Thus, while an effective administration is of great importance to gaining the benefits of membership and remaining competitive, it is also important to recognize that the administrative reform process should continue after accession if systemic reforms are to be brought to a successful conclusion. Hardship experiences that are due to failed reform experiments (Latvia) and/or economic problems (Lithuania and Latvia) may in this regard be a more important motivator and may also lead to an enhanced consensus on reform agendas.[15]

The availability of technical capacity is an interesting factor as well. The Latvian and Lithuanian reforms were built around a relatively small group of reform-minded officials who managed to gain and retain the trust of politicians regardless of their political orientation. This type of professional, non-partisan elite appears to have been missing in most other states, where expertise was and is politicized (and thus deemed insufficiently trustworthy by opposing political factions), is not available or is not available to government. Technical capacity and consensus thus appear to be strongly intertwined in most of the states concerned, and Latvia and Lithuania have been an exception to this rule, although there is no a clear explanation for this.

Where do these conclusions leave us on the question of introducing a "road map" for reform? First, it is an encouraging fact that successful reforms appear to have been built mostly on more limited and contained initiatives. Second, the fact that these reforms were strategically driven (this applied to both the systemic reforms in Latvia and Lithuania and the introduction of service delivery tools in Estonia) emphasizes the importance of political leadership and the need to build coalitions between politicians and at least a core group of senior officials. Third, and perhaps less encouraging, is the fact that all three cases of successful reform were driven by, or based in, a central government institution, which in the cases of Latvia and Lithuania was itself first reformed.

These conclusions point to a scenario in which system reforms as a step-by-step process starting from the core government institutions is likely to have the greatest success. Unfortunately, it is these institutions that in most other states have been most politicized and, in the cases of Poland, the Czech Republic, and the Slovak Republic, severely weakened. Therefore, rebuilding central government institutions stands out as an important condition for successful systemic reform.

As a second point, modesty in design is also crucial. Large-scale reforms have not worked well in most of the EU8 countries, which may be due in part to the vagaries of coalition politics and the low coherence of governments, which make these states unique. In this type of political context, grand designs are less likely to work well than in more centralized systems.

In terms of the people dimension, there is a clear need for new solutions. Labor market conditions and the political environment in the EU8 countries, at least at this point in time, are not conducive to the replication of classical civil service models. However, this does not mean that elements of such models should not be retained. Ensuring consistency in recruitment and career management across the civil service and safeguarding to the highest degree possible the "equal pay for equal work principle" are elements of civil service systems that need to be re-introduced. In addition, equilibrium between political discretion and civil service independence is still elusive in most of the states reviewed, and

15. The relative success of the Serbian reforms in the last two years without a strong EU motivation factor may point in the same direction.

**Box 5.1: Conclusions and Recommendations: Summary**

On Reform Processes:

1. Reform processes of the nature and complexity of those in post-communist states always require more than one government cycle. Consensus building therefore is the most essential pre-condition for successful reform. An effective dialogue between politicians and senior officials is key.

On Reform Substance

1. Process innovations, such as strategic planning and performance management, have been under-emphasized in administrative reform. Nevertheless, the experience of Latvia and Lithuania provides a clear testimony to the potential gains that such innovations can bring in enhancing the efficiency and effectiveness of public expenditure and in achieving effective EU participation. The introduction of system reforms is best based on a reformed central government structure, which provides the best chances for a successful roll-out of new management tools across the entire government.
3. Simplicity is key to success. Starting with the definition of simple and easy to apply guidelines for setting institutional goals will enhance the chances of buy-in. Some of the cases reviewed clearly show that even if foreign models are used for reforms, breaking them down into easy-to-use guidelines will help gain support.
4. A renewed effort to define key principles underlying civil service management is essential. Recognizing that attempts to introduce Continental European style career systems have failed, a dialogue should be opened regarding the alternatives. Northern European style approaches, based on private sector modalities, could be an option, but only if the issue of politicization is first addressed. Without this the creation of spoils systems with all their negative consequences is a real risk.
5. On incentive systems, the definition of new pay systems will remain key. The Latvian experiment with a factor-based remuneration system will be worth following, as will the Serbian variant on the same model. Both are slated for introduction in 2007. In our view, this approach, even if it is labor and time intensive, provides the only long-term solution for redefining incentive systems.
6. E-Governance approaches will remain attractive in principle, but the review of the Estonian case shows the difficulties in replicating this example. Step-by-step approaches, starting with targeted innovations (as already applied in many states) constitute the best starting point in a context of fiscal constraints. A combination of the introduction of performance based management tools and e-Governance instruments would have significantly better chances of success.

without this equilibrium the desired increase in the quality of the civil service will not materialize. Thus, reform programs should aim to create “light” monitoring and safeguard mechanisms that will ensure respect for the principles of merit and quality while providing some space within these principles for politicians to decide on appointments and dismissals. The contract-based systems for certain categories of senior officials, which some states have started to experiment with recently, may be a viable solution in this regard.

Finally, in considering service delivery mechanisms, the lesson drawn from this study, combined with the recent Doing Business and Anti-Corruption in Transition reports, is that improved service delivery requires a combination of a performance driven administration and the use of innovative tools (in particular e-Governance tools) in service delivery. The performance of the Baltic States in these two sets of investment climate and competitiveness indicators provides ample food for thought in this regard. Whereas the introduction of both types of reforms is not easy to achieve, the benefits in terms of improved competitiveness can be clearly noted. Box 5.1 summarizes the above conclusions.

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