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Issues on Accessing EU Non-refundable Funds by SMEs in Romania

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Abstract

Admission of Romania to European Union in 2007 meant for Small and Medium Enterprises (SME) a perspective to access a new funding source at low costs, but with beneficial economic effects for this. Providing funding sources is vital for any company whether being at the beginning of its activity, or in progress, such as facilitating SMEs access to available financial resources represents an important instrument of the economic development.

Starting from the SMEs position in the economy, this paperwork intends to emphasize the problems they encounter in procurement of necessary financial resources and the need to ensure access to finance. Eventually, it highlights the issue raised by accessing and implementing projects financed by European non-refundable funds.

Keywords: *European non-refundable funds; small and medium enterprises, implementation*

JEL Classification: *M21*

Introduction: Barriers to SMEs Development

Providing funding sources is vital for any company whether being at the beginning of its activity or in progress, so that funding programs provided by European non-refundable funds, accessible to Romania after joining the European Union (EU) represent an opportunity not to be neglected by Small and Medium Enterprises (SME), which they must resort to when eligibility requirements are met.

Procuring resources to finance the activity, as well as the cost of procurement represent on ongoing concern; this aspect targets the traditional SMEs that do not have a long-term strategy and address to a local or regional restricted market; it concerns, also, the modern ones that use advanced technologies and are in search for new markets and pursue continuously to streamline their business.

Whether we discuss about traditional SMEs, those that do not have a long-term strategy and address to a local or regional restricted market, or about the modern ones that use advanced technologies, which are in search for new markets and pursue continuously to streamline their business, procuring resources to finance their activity, as well as the cost of procurement is an ongoing concern. Access to funding sources and national and international credits represents an important barrier both at their incorporation and during their development and, not for a few times, a cause for termination of their activity.

Limited resources may also reduce access to new technologies and innovation which are essential in business efficiency and maintaining the small enterprises on the market.

SMEs access to finance is inextricably linked to the cost of its funding and financial structure of the applicant. Bank credit represents a source of funding which the small and medium enterprising apply to frequently. Accessing bank loans is hindered by the reluctance manifested by the financial intermediaries in providing small business financing as they consider SME financing a high risk activity and low earning capacity. The reluctance of the financial intermediaries for SME financing is accentuated by a number of factors. (World Bank, 2008):

- Administrative costs related to granted loans. Regardless of the amount of the granted loan and the borrower entity type, creditors may support a number of fixed costs (the applicant's file analysis, registration and monitoring) when granting the credit. From this perspective, the high administrative costs associated with small loans make the SMEs lending not to be considered a lucrative business for the financial intermediaries;
- Lack of goods as assets that may be used as collaterals. SMEs are considered high-risk borrowers because of insufficient assets held, vulnerability to market fluctuations and high mortality rates;
- Lack of SME's experience in providing financial statements or business projects slows down the assessment process of investment proposals.

The decrease of banks' interest for small clients, higher costs of credit, as well as more stringent requirements and creditworthiness of applicants, the legislative instability, the sharp drop in demand for goods and services, high taxation have determined SMEs to reduce the investments, to postpone or waive certain investment projects, to renegotiate contracts with suppliers, to restructure/ reduce activities and, thus, to reduce staff and salaries.

In order to reduce barriers regarding the financing and supporting the SMEs development, our country has initiated and supported various action programs and packages of financial instruments (guarantee funds, loan products, etc.) oriented to facilitate SMEs access to funding resources. In addition, the European Union of membership status entitles our country to benefit from a number of EU funds directed to create a better business environment, a reliable and innovative one.

Economic and financial crisis increases the difficulties faced by SMEs because, on the one hand, funds are more difficult to find and, on the other hand, crisis brings a dramatic drop in demand for goods and services. In general, SMEs are more vulnerable in times of crisis, for a multitude of reasons. Being already small, their dimensions can hardly be reduced and, at the same time, their financial structure is less solid and often supports the countercoup of difficulties faced by large enterprises.

Economic recovery of Romania is conditional on SME access to finance. Improving access to finance for SMEs plays an important role in promoting entrepreneurship and intensifying competition in the Member States of the European Union (EU), the projects financed from European non-refundable funds have represented and represent means of achieving these strategic objects.

SMEs Role in Economy

SMEs contribution to economic and social wellbeing of a nation is widely recognized. Professor Peter Drucker (1999) said that "small businesses represent the main catalyst for the economic growth".

SMEs play a crucial role in the economic life of a country in that they create new jobs that contribute to a significant share of the labour market supply. Their relatively small size makes them to be flexible and innovative in terms of satisfying the requests, the needs of consumers becoming more sophisticated. By their large number, they contribute to the stimulation of competition, being real barriers in the constitution of monopolies. SMEs contribute to the smooth functioning of large enterprises for providing various services or producing different parts, manufacture products and provide services in terms of efficiency.

SMEs are important to all world countries, especially to those with developing economy facing acute employment and income distribution per capita.

Proponents of the economic model centred on small and medium enterprises bring the following arguments (Beck *et.al*, 2005):

- SMEs ability to enhance competition and develop entrepreneurship. A high level of competition helps maintain or even reduce prices with immediate effect on purchasing power. Stimulate competition and entrepreneurship development requires the availability of sufficient financial resources, so that, supporting SMEs by facilitating access to finance is the main tool in ensuring economic growth.
- A significant contribution of SMEs to increase the occupation level of the workforce. Creation of jobs within SMEs implies much more reduced costs than for large enterprises. As these small businesses grow harmoniously, they need a more increasing work force. From this perspective, SME financing thus leads to reducing poverty and ensuring prerequisites for economic growth.
- Productive flexibility of SMEs. Flexibility means the SMEs ability to produce more sophisticated goods, which are varied and innovative compared to large enterprises; having rigid production cycles, these ones offer goods that often do not correspond to the needs, permanently in change, of the customers. SMEs ability to seize the market opportunities and adapt quickly to its changes has been intensively studied, existing in this regard, a lot of works to demonstrate that flexibility of the enterprises on size categories varies inversely with the size of the enterprise.

At European level, but without limitation thereto, SMEs are considered as being key factors in economic development, employment, social integration and innovation. Flexibility and adaptability, defining features for SMEs sector, are essential for overcoming periods of crisis, being extremely relevant for the current period of economic recession.

Having as central point recognition of the essential role of SMEs in economic development, European Union has adopted in 2008 the initiative *Small Business Act* that includes a number of measures aiming at creating a favourable environment for development of SMEs and enabling potentiation of entrepreneurial energies at European level. Accent on entrepreneurship and SMEs role is reassumed in Europe Strategy 2020, which aims at opening a single market for small entrepreneurs. In the case of our country, the public policy recognizes the importance of the SMEs, existing various support tools, both, directly, by national and European funds and, indirectly, by creating a legislative environment favourable to these.

However, the actual policy in the SMEs sector is a mix of contrasting aspects, given that large amounts are invested annually in relation to Romania's GDP, but that there is no consensus regarding the effectiveness or results.

Access to sufficient and adequate capital to grow and develop is, as it has been underlined before, one of the main obstacles facing most of the SMEs. Many governments and financial institutions have tried to approach the issues related to ensuring the financing of SMEs by developing projects to support the small entrepreneurs. This is also the case of our country that, since entering in EU, has supported the creation of packages of financial instruments (guarantee funds, loan products, etc.) oriented to facilitate the SMEs access to finance, in line with the best

European practices. Initiatives in this field, carried out until now, have sought to strengthen the capacity of financial intermediaries (microfinance institutions, banks, venture capital funds etc.) to support at national and regional level the investments undertaken by the private sector.

Issues on Accessing and Implementing the External Non- Refundable Grants within SMEs

Many countries, as is the case of Romania, have sought to reduce barriers to SME financing by developing programs to support small business. Our country, since joining the European Union, has supported creation of packages of financial instruments designed to facilitate SMEs access to finance, in line with best European practices. In addition, the EU membership status entitles our country to benefit of transfers oriented to facilitate access to knowledge and innovation, education and preparation in the business area, creation of a clear and predictable business environment. The financial support granted through the external post-accession non-refundable grants includes (UGIR, 2006):

- Structural and Cohesion Funds (European Fund of Economic Development, European Social Fund, Cohesion Fund);
- Complementary Funds (European Agricultural Fund for Rural Development and European Fund for Fishery).

The palette of activities eligible for funding is generous, the European Union allocating funds for energy projects and its efficient use, promoting those programs aimed at alternative “friendly” energy sources with the environment. Thus, SMEs are encouraged to develop partnerships with institutions of research and innovation in order to create innovative products and services based on advanced technologies; tourist activities, to highlight the natural beauty of the rural environment and not only, the investments for intangible and tangible fixed assets, the regional development by stimulating investment and creating new jobs in SMEs sector are, among many others, eligible activities to finance.

Procurement of financing of European non-refundable funds is not always simple, there are lots of aspects that SMEs applicant is required to consider when seeking financing of such funds, aspects aiming at both the applications for funding and the implementation of projects approved for financing, thus:

- Filling a funding application, forms for an application are not always easy for SMEs that do not have specialized staff for facing such assignments. A project is eligible for financing given that after the evaluation process achieves a score of at least 60 points. This score does not guarantee the approval of financing. In terms of a large number of projects, whose aggregate values exceed the amount approved for financing, allocation is done in the descending order of the score achieved. Hence the importance that it has the component of filling and preparation of the documentation related to the application for funding, the target of each applicant being that of obtaining a score as close to the maximum in order to increase the chances of funding of the project. Any document omitted or incomplete can lead to elimination of competition. In order to avoid such situations many SMEs rely on the services provided by consultancy companies specialized in the field of accessing European non-refundable funds.
- Ensuring co-financing that the applicant must contribute to for the financing of the project, co-financing that may reach up in some cases up to 50% of the total project budget; The applicant who wants to access European non-refundable grants, must prove that it has the financial resources to support the project, the settlement of the costs incurred within the project being made subsequently, based on reimbursement requests, requests that are accompanied by supporting documents that certify expenses. During 2007- 2013, there have been plenty situations in which the period between the application for payment by the beneficiary and reimbursement of expenses exceeded one year.

- In the implementation phase of the projects approved for financing, the beneficiary of a financing contract has to organise separate accounts to enable the identification of the operations related to projects financed from European funds, independent of any accounting process of the applicant. The beneficiary, also, has to develop internal procedures to ensure the implementation of European and national legislation and, last but not least, to provide all accounting information required to control or verification by the experts of the European Commission;
- The accounting for transactions made from European non-refundable funds involves creating analytic accounts for the joint accounts of intangible and tangible fixed assets, for transactions regarding stocks, suppliers, salaries etc., as well as use of specific accounts to highlight the reimbursement requests and collection of reimbursements.

Obligation of separate accounts, as previously stated in the preceding paragraph, is necessary to justify at any time that the funds have been used exclusively for achieving the objects of the project financed from European funds, as they have been described in the funding application and in accordance with the approved expenditure in the project budget.

- Another important aspect raised by the use of European funds by the SMEs, beneficiaries of financing, represents the procurement of goods, services and works for achieving the objectives contained in the financing contract.

Although SMEs are not contracting authorities under the provisions of the Public Procurement Law 98/2016, they must follow certain rules for all the acquisitions made within the project, respectively the persons involved in the SMEs procedures of public procurement have the obligation to ensure a transparent non-discriminatory process, providing access to all tenderers presenting a valid offer, so efficient use of funds to be made.

Lately, there have been taken measures regarding the elimination of artificial constraints imposed by the acquisitions made by beneficiaries in the private sector (that is applicable to SMEs), within the projects implemented by European funds. Currently, it is applied a simplified procedure that takes into consideration certain thresholds and value ranges (over EUR 30,000 for goods, EUR 30,000- 200,000 for services and EUR 100,000- 5,000,000 for works) related to procurement of goods, services and works from which beneficiaries in the private sector must publish a notice in a section dedicated on the website of the Ministry of European Funds (MEF). Beneficiaries in the private sector have the possibility to choose the most competitive offer, reasoning their decision by drawing- up a supporting note.

- SMEs, beneficiaries of European non-refundable funds have the obligation to organise internal control of their management in order to ensure the financers with respect to observing the European and national legislation in the field of using these funds, but, also, as a measure of internal management aimed at reducing risks of making illegible expenses.

Most financing contracts entered into by the beneficiaries (SMEs and other types of entities) stipulate auditing the expenditures of the project budget, an operation that is performed either by active auditors enrolled in the panel of Chamber of Auditors in Romania or authorised audit companies.

Auditing is done usually, before submitting the application by the applicant of the reimbursement request for the expenses incurred, the process ending with the preparation of the audit report. In this document, the auditor shows on the structure of the approved budget the eligible expenses incurred and their value, including the expenses that considers as being not-eligible, if this is required. The audit report is an important document that is submitted, in original, in the same time with the submission of the reimbursement request of the expenses.

Audit services are eligible expenses and are included in the project budget at outsourced expenses, since the design phase. Subsequently, these services are, depending on the value stipulated in the budget, the subject of direct acquisitions or by selection of the offers submitted as a result of publication the notice on the website of MEF.

During implementation and after its conclusion, the expenses incurred in the framework of projects financed from European funds go through several stages of assessment and verification made by experts employed by the Ministry of European Funds (MEF), the experts of the Court of Auditors and the European Commission. The role of these verifications is to ensure the use of funds in accordance with the objectives set in the financing contract and observance of legal provisions on spending national and European funds

The period of the years 2007-2014, meant for central public administration authorities, both for SMEs and other applicants, beneficiaries of European funds accumulating new experiences on the management of these resources funding, experiences that today represent the basis of the initiation of measures that MEF wants to undertake to facilitate access to European financing for the period 2014-2020.

These measures focus on the following aspects:

- Improving the financing contract and partnership agreement which ensure rights and responsibilities equally to all concerned, the applicant and partners in achieving the objectives of the financing contract**;**
- An improved electronic system that allows submission of requests for reimbursement exclusively by electronic means;
- In order to reduce bureaucracy and the risk of errors in justifying expenditure, MEF will encourage the use of the option for simplified costs (beneficiaries will not send supporting documents in hardcopy only in electronic format);
- To ensure an integrated approach and a coherent implementation of European funds. MEF aims at correlation financing granted under operational programs to facilitate an integrated approach to interventions supported and to meet both identified needs and development strategies at national, sectoral, regional and local level, avoiding disparate investments.

The measures planned to be implemented to facilitate access to European funds in the next period are beneficial to all categories of applicants and especially for SMEs, which will have the possibility of buying financing sources with lower costs. Easier access will stimulate interest in participating in the competition for obtaining European non-refundable grants.

Raising The Rate Of Absorption Of Irredeemable European Funds, Essential Condition of Economic Development

The absorption of European funds, as close to the maximum allocated by the EU, represents an issue of national concern. These funds are amounts of additional money in the Romanian economy and their impact on the economic development is significant, if we take into account that the GNP of Romania is approx. €140 billion. The annual absorption of an amount of € 3-4 billion from the European funds can generate a plus for the economic growth. Since Romania has approx. 1% of GNP contribution to the EU budget, a low degree of absorption may lead us to the situation of being net contributors, as it happened during the first years of integration (Romania is not an exception in this respect, other countries that were newly integrated in the EU experienced the same low level of absorption of the allocated European funds). It is of real importance to be aware of the fact that these amounts money are not lent, it is free of charge, but the EU keeps an eye on how they are spent. It is inconceivable for this money to be used for other purposes than it has been allocated, and those who do not observe the norms are obliged to give it back.

During 2007-2013 the European Union allocated Romania € 19.2 billion (amount included in National Strategic Framework of Reference subdivided into seven Operational Programs) comprising structural and cohesion European funds. The Statistics of the European Union, mentioned in the Fiscal Council Report, state that Romania registered in March 2012 17.3% average rate of absorption, occupying the final position, after Slovakia, with 27.8% and Bulgaria, with 24.0%.

The degree of absorption didn't improve during the next years either. In 2015, in its report on financial stability, the Romanian National Bank stated that our country, with 35.6% rate of absorption in July 2014, 51.30$ for the same period in 2015, continued to have one of the lowest rate of absorption in the EU (Romanian National Bank – Report on financial stability, 2015). According to the Ministry of European Funds balance of accounts, out of €19.20 billion representing structural and cohesion funds allocated by the EU for 2007- 2013, Romania required €12.06 billion and acquired €10.73 billion, the rest of €1.33 billion representing the difference to be acquired from EU, approx. € 7 billion could not be absorbed.

The EU Regulation nr.1297/2013 of the European Parliament and of the EU Council permitted Romania to access European funds in the 2007-2013 program. The funds allocated for Romania for 2014-2020 amount to €30.7 billion. As a result of the experience acquired during 2007-2013, the Ministry of European Funds, responsible for the management of these funds, proposed a series of measures meant to accelerate the rate of absorption. We mention some of these measures:

- Simplifying and making more efficient the process of programs and projects implementation;
- Simplifying the procedures of submitting projects (reducing the number of documents and standardizing them, reducing the time of getting authorizations and notices) ;
- Reforming the sector of public acquisitions, from a legal standing, institutionally and including the corresponding procedures (standardized documentation, reducing the number of documents required from the economic operators);
- Attaining a rate of 80% of fund absorption.

Conclusions

Accessing EU funds represent an important source of funding for SMEs, on which they must call whenever they are available to access. These resources are safer and cheaper than other types of financing, the most important criterion that SMEs should have in view is that the activities of the company concerned to represent the subject of EU funding is to be eligible;

Implementation of projects financed from European funds requires compliance with European, national and legal regulations, whose violation leads to declaring the used funds, partly or wholly, as ineligible. To reduce the risk of invalidation of expenses incurred in European fund the SMEs management needs to organize their internal control systems so that these procedures be observed.

The experience of more than 8 years acquired in accessing and implementing European non-refundable funds in our country has resulted in a wide-ranging measures taken by the public policies to facilitate greater interest of the beneficiaries, SMEs or other types of entities eligible, to submit projects for accessing funds, increasing the rate of absorption of EU funds and transforming these resources as a genuine vector for economic growth.

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