Fleeing the extremes

"We, animals, are the most complicated things
in all the known universe."
Richard Dawkins

The economists' propensity of accepting as working hypotheses the assumptions of ideologies already seems natural. In conditions where decisions have either emotional determinants (especially in microeconomics) or political ones (particularly in macroeconomics), the economists have assumed a losing position. Their theories, in order to be successful – which means being friendly towards the leadership – have searched for the explanation around rationality, often in spite of it.

This is why, for instance, the management of companies came to inspire itself from the stories of success in speculation and not coming from economic calculus; just as the government's mission has been reduced to the institutional replication of doctrinarian theses, based on self-sufficient visions or motivated by the interests of political clans.

Economic theory, via economic policies, most often than not has to adopt rhetoric in the place of logic, improvisation of circumstance instead of scientific procedures. The visual interface of the theory, which is the governmental policy, stands in the place of rational argumentation.

The rule of policies is to satisfy ideological or group expectations and not the mechanical regularities of an economic system. There is no other explanation for the procyclical steps taken in the present crisis, for instance, as well as for the fiscal tightening or the restraint in financing public investments. The doctrinaire recipe is more respected than the effect produced by the prescribed medicine.

In a somewhat perverse way we are made to choose among solutions favored for their noneconomic criteria. The key question bears the rational answer which keeps being postponed: why are the state and the market opposed? It's only common sense to admit that we do not have the rational arguments for validating a pure option. Unfortunately the correct attempt of escaping the space of ideological options is seen as an utopia so long as everyone is ready to defend their own ideologically argued truth.

Why should socialist ideology confiscate the plan and capitalist ideology sequester the market? Is there a resulting gain in wealth because the state is ideologically opposed to the market? Does the market require a minimal state anytime anywhere? It's obvious that the answer either preferential or emotional, with no one feeling cold shivers due to the fact that it is totally inadequate for this to happen within a science which pretends not to be based on assumptions. Socialism has compromised planning while capitalism falsifies the market and not the other way around!

The guilty associations are between state, interventionism, government and collectivism on one side, and market, private property, democracy and freedom on the other. They get their just as guilty nuances through other associations, between planning and socialism versus free initiative and capitalism, thereby banning a rational method of management from society or condemning the market as being the regulating mechanism of an ideological construction. The already subliminal interdiction of associating market with planning or government with free initiative configures the dark areas of understanding. The cause resides in the confrontation of ideologies trough which each one follows what it believes to be the truth.

It does not matter, as we can see, the end result for man – wealth and prosperity – whose touch would be more easily felt without the guilty associations between values. What matters is for one of the ideologies to come out victorious, for it to then sacralize its fighting weapons!

What deserves to be revealed is the fact that precisely due to the contamination of Economics with the extensions of ideologies are we able to keep ourselves in mirror-reversed social experiments. In all, the idea of progress finds a fulfillment in ideological experiments, at least in those defined by adversity; plan, evermore plan vs. market, more and more market! Again common sense wants to comprehend until what point to accelerate the advancement and why, at the limit, is there a need for a single dimension? And this besides the human need of knowing whether it is fatal to evolve towards extremes!

Aberrations can be spotted by the naked eye if we come out from under the blinding spot of ideologies. Meaning, as a first aberration, that the state is a poor administrator even though it is an institution made up of each one of us as its subjects and, as a second aberration, that the market is infallible because it treats each of us as objects!

The construction of economic issues starts from either one aberration, or the other. Once again we witness the abandon of logic in the analytical course of Economics. There is one, non-empiric reason for these abandons: the golden background of the theoretical acquisitions of Economics is a non-human surrogate, thought out by a non-biological creature, *homo œconomicus.*

The plead for extension of mechanical behaviors constituted for Economics a channel through which the virus of ideologies predisposed to social experiments could insinuate itself. In a world of efficient mechanics, populated by *homo œconomicus*, any propensity for the extremes is confirmed, because in a world such as this there is a lack of common sense, just measure, doubt and admission of error.

Because they are obsessed with leaps toward the extremes, ideologies achieve in a fake, artificial world and not in a natural one, where leaps are not possible.

Economics still has a chance, though: to build itself *ex-ante* testing procedures for the solutions.

Marin Dinu

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Public Integrity and Performance of Governance. A Comparative Study for South-Eastern Europe

▪

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Abstract. *The studies concerning the impact of corruption on the effectiveness of governance are numerous, valorising profound approaches, based on criteria and standards related to good governance, organizational behaviour.*

The concepts and mechanisms specific for econometrics and statistics provide the quantitative support for qualitative analyses, substantiating public policies, in view to assure effectiveness in performance measurement.

For all South-Eastern European countries, the level of development and social organization determines specific ethical behaviours.

In this context, the current paper aims a comparative economic and social evaluation of the correlations between corruption, performance and economic freedom in South-Eastern European countries, including Romania.

The working hypotheses turn into consideration the following issues:

- *corruption holds national specific character and the statistic, econometric or sociologic analyses reveal that it is stable during the time;*
- *an effective governance leads to increasing the citizens' welfare;*
- *if a country is poor and the economic freedom is reduced than the bureaucratic and political system tends to be more corrupted;*

- *the perspective of accession into the EU has led to the perception concerning the reduction of the corruption level.*

The above hypotheses will be completed and we shall achieve comparative analyses, relevant for the group of South-Eastern European countries.

The above quantitative analyses will use both own results of the researches carried out by the authors and public results of World Bank, Transparency International and Heritage Foundation, as well as results of authorities responsible for national statistics.

The comparative research is achieved on a 10 years period, comprising also the moment of accession into the European Union for some states.

Keywords: public integrity; governance performance; corruption; economic freedom.

■

JEL Codes: H11, H83.
REL Codes: 13C, 13I, 13K.

I. The governance performance

I.1. A systemic framework

The issue of governance performance is more and more present in the field literature. Regarded as a finality of a complex public management process, the governance performance, we refer either to the central, or to the local government, acquires systemic characteristics and, according to their level, the governors establish the feedback that is carried out through new public decisions meant to lead towards a performance improvement.

The concerns for a systemic modelling of the public management can be met both when the issue of the public administration comes out (Pierre, 1995) and, lately, the public management reform (Pollitt and Bouckaert, 2000, pp. 39-134). A brief presentation of some systemic models used in the public management of the local development is also made by Matei (2008). Referring to the performance oriented managerial reforms, Pollitt (1995, 1998) shows that for the public sector "the organisations must redirect in order to focus more on results. These have to take into account the costs, to measure the outputs, to assess the effects and to use all this information in a systemic process of feedback and continuous improvement".

The most relevant and recent point of view respecting the systemic approach of the public sector performance is presented by Bouckaert and Halligan (2008, pp. 11-34). Following a logical sequence of building a complex systemic model of the public sector performance, the mentioned authors described micro, meso and macro models, integrated or individual, that can deliver the proper framework for understanding and study thoroughly the specified concept. The result of this measure is a complex system, with mixed architecture that includes more cycles of intermediary feedback and that integrates "four positions on managing performance: Performance Administration, Management of Performance, Performance Management and Performance Governance" (Ibidem, p. 32). In this context, the governance performance can be seen as a subsystem of the public sector performance or, more, of the managerial performance. Specific to the governance performance is also the fact of being a result of the interaction between public economic systems and that of the public management. Thus, the fundamental concepts as the public intervention, public decision, optimisation, and so on, become adjacent and determinant for the level of the governance performance.

I.2. Present approaches

Bouckaert and Halligan (2008) make an international comparison related to "managing performance". The statistical ratios and/or connections between management the performance, in the context of the public sector, become determinant both for the understanding of the processes of performance's management, and for the governance performance.

The general approach framework of this issue is delivered by the New Public Management (Hood, 1995) or by "reinventing government" (Osborne, Gaebler, 1992).

A broad and generic definition of performance – based public management is taking/allocating responsibility for the performance of the system and being accountable for its results (Osborne, Gaebler, 1992, p. 32).

Hannagan (2008, p. 294), referring to the performance management in an organisation, states that "the term *performance management* means different practices to different managers but usually includes the following elements:

- The organisation has a shared statement of its objectives, or a mission statement or corporate objectives, which it communicates to its employees;
- Individual performance management targets are set which are related to the organisational objectives;
- A regular, formal review is carried out to monitor progress toward the objectives;
- The review process is used to identify training needs, career development and possible rewards;
- The effectiveness of the whole process is evaluated against the overall performance of the organisation".

Important and constant concerns this time with regard to the performance of the public sector can be also found in the UN Public Administration Programme[1], which in the 2005 and 2008 reports presents both the public sector performance (WPSR, 2005), and the issue of the public governance (WPSR, 2008). Thus, WPSR (2005) focuses upon the way in which the human potential will be transformed in order to improve the performance of the public sector. The general context in which the stated issue is approached is characterised, on one hand, by the complexity of the policy making processes and of the public strategies and, on the other hand, by the deterioration of the human resources capacities of accomplishing these functions. The aspects set forth render difficult, for many states, the application of the national objectives and strategies for increasing the governance performance through poverty and corruption reduction, promoting the sustainable human development as it is underlined in the Millennium Development Goals (MDGs).[2]

WPRS (2008) emphasizes the role of the civic engagement in the public governance process. By presenting several case studies, it is being emphasised, in a real manner, the role of the different practices in consolidating the governance capacity through transparency and responsibility. In the context, the relations between the power and the civil society organisations are tackled, as well as the necessity of adopting methodologies and strategies proper for each state's condition for a successful civic engagement in the public governance.

The mentioned technical support is also offered by the analysis made by Willmore (2005).

I.3. The integrity, as a governance principle in the public sector

Along with the UN concerns there are also the ones of the World Bank, which dedicate numerous studies both to the researches regarding the Governance Indices and the Public Sector Governance. The concern of the present paper is situated at the meeting point of the two mentioned topics. Worth to be mentioned, from the point of view of the World Bank, are the governance principles in the public sector, which are referring to:

- Responsibility – according to which the public authority is responsible for the decisions and promotes mechanisms that ensure the application of public management high standards;

- Transparency/openness – that expresses the public authority capacity regarding the roles and responsibilities assumed, as well as the decision-making procedures and the power exercise;
- Integrity – with reference to the public and personal, impartial, ethical action, and in the interest of the public authority;
- Stewardship – imposing the use of each opportunity for developing the public assets;
- Efficiency – ensuring the best use of resources in order to accomplish the organisation's objectives;
- Leadership – applied through a commitment for good governance.(3)

All these principles lead to a public governance approach that would allow obtaining some superior results, in terms of efficiency and with a high performance.(4)

In the view presented in the above papers, the public sector governance includes: "…the set of responsibilities and practices, policies and procedures, exercised by an agency's executive, to provide strategic direction, ensure objectives are achieved, manage risks and use resources responsibly and with accountability".(5) We used this approach of the concept of public sector governance giving the practical approach manner and turning account of the possible connections with the second part of the paper referring to integrity and economic freedom. The State Services Authority (SSA) from Australia addresses the issue in the same manner, accentuating the public integrity among the main pillars of public integrity, assuming the "promotion of high integrity and conduct standards in the public sector".(6) Similar stands took the Association of Chartered Certified Accountants (ACCA), emphasising the fact that "the governance can also cover the behaviour standards, the organisational structures and the processes".(7)

At the same time, OECD states that "good, effective public governance helps to strengthen democracy and human rights, promote economic prosperity and social cohesion, reduce poverty, enhance environmental protection and the sustainable use of natural resources, and deepen confidence in government and public administration".(8) The real issue of public integrity is developed by OECD, in this very moment a global forum is being organised with regard to "building integrity in government".(9)

II. The corruption, integrity and economic freedoms

As it was also shown in the 1st chapter of the present paper there are several indices of the governance performance. We will keep in mind as indices, as Prohnițchi (2003) does too, the Gross Domestic Product (GDP) per inhabitant, as well as the economic freedom (IEF). The mentioned author reaffirms the conclusions of the World Bank or Transparency International, according to which "the poorer the country and the more reduced is the economic freedom, the more corrupt is its bureaucratic and political system". The present study perspective determines us to take into account many organisations' analysis based on the conclusion that the "concern about the negative social and economic impact of corruption has grown rapidly in both emerging and advanced democracies" (Akai et al., 2005).

The conclusion is also supported by the World Bank which identifies the concept "as the single greatest obstacle to economic and social development. It undermines development by distorting the rule of law and weakening the institutional foundation on which economic growth depends".[10] A similar position is that of the International Monetary Fund, which states that "many of the causes of corruption are economic in nature, and are its consequences – poor governance clearly is detrimental to economic activity and welfare".[11]

The development of theoretical and empirical studies has not always been the cause and effect type, between corruption and economic performance.

Worth mentioning here are the comments made by Rose-Ackerman (2009, p. 3) with regard to the conclusions expressed by different specialists and analysts of the corruption issue.

Mauro (1995, 1998) demonstrates that the high corruption levels are associated with low investment levels as part of GDP.

The corruption indices are extremely isolated from the bureaucratic efficiency, as for example the level of bureaucracy and judicious quality. As a consequence, Mauro was incapable of measuring the marginal effect of each of these measures. By putting together the separated indices in a measure of bureaucratic efficiency (on a scale from one to ten): "if Bangladesh, with a score of 4.7 would have improved the integrity and the bureaucratic efficiency at Uruguay's level, 6.8, its investment rate would increase with approximately five percentage points and the annual growth rate of GDP would increase with almost half of a percentage point" (Mauro, 1998). Also, Mauro proves that the extremely corrupted countries tend to under-invest in human capital, spending less on education. Mauro argues that this fact happens because the education delivers less work opportunities for corruption than other types of capital-intensive public expenditures.

Ades and Di Tella (1997) state that an aggressive industrial policy could be motivated, on a certain extent, by the corrupt gains made available by that policy. In such cases, the positive direct effect of the policy could be submitted by its role in the increase of corruption, thus discouraging the investments. Their empirical results demonstrate that, in presence of corruption, the positive influence of the industrial policy is reduced to a half.

Also, for public integrity we end up choosing the corruption perceptions index (TI) computed by Transparency International in the last decade, for the South-Eastern Europe states[12], as well as the KKM index (control of corruption) computed by the World Bank, for the same sample and period, as aggregated and individual governance index. The two used indices express, in different ways, the perception upon the way in which the public power exercise has an impact upon the private sector profit, including both the narrow and the wide corruption form, as well as "capturing" the states by the elites and the personal interests.

II.1. Corruption and governance

One of the fundamental papers presenting the indissoluble link between the corruption and the governance is that of Rose-Ackerman (2005) that eloquently proves how the high level of corruption limits the investment and the economic growth and leads to the government's inefficiency.

For the developing countries, as well as for those being in transition from socialism, the risk is higher. The mentioned author identifies the corruption phenomenon as a complex one of economic[(13)], cultural (Rose-Ackerman, 2005, pp. 89-111, 175) and political nature.

Also, a series of classical papers must be mentioned, having as object the identification of causes and mechanisms of corruption transmission inside a economic and social system, from which we mention: Krueger (1974), Rose-Ackerman (1975), Mauro (1995), Tanzi (1998), etc. In the field literature four categories of factors are identified, which directly influence the corruption in a system: historical factors, social and cultural factors and economic factors. In the political and juridical factors category we include the quality of the political system, the features of the juridical system (Leite, Weidmann, 1999), especially the legislation and the institutions specialised in the fight against corruption, the quality of the democratic system, the features of the electoral system in a country, the features of the administrative system, the degree of administrative decentralisation in a country etc. A series of studies, like those made by La Porta (1999) and Treisman (2000), accentuate the influence of the traditions and historical factors upon the level of corruption in a country and the features of the mechanisms of its development and transmission. The social and cultural factors have a special role in accentuating the corruption features in a country (La Porta (1999), Treisman (2000), Alesina (2003). Equally, the religious factor play an important part in spreading the corruption on a social system level. The economic factors, as well as the openness level of the economy (for example Dreher, 2003, Treisman, 2000, Wei, 2001), the size of the public sector (Tanzi, 1998, Treisman, 2000), the salaries' level in the public sector (van Rijckeghem, Weber, 1997) etc. directly influence the corruption level in a country.

Another important aspect when studying corruption is choosing the most appropriate econometric models for estimating its effects upon some sectors of activities. From the most important research directions that target the estimation of corruption's effects upon the economic and social environment, we mention:

(i) Measuring the corruption effect upon the economic growth (Mauro, 1995, Abed, Davoodi, 2000, Krueger, 1974);

(ii) The corruption's effects upon the development of some sectors of national economies (Tanzi, 1998, Wei, 2001);

(iii) The effects of the decentralisation process upon the level and the mechanisms of corruption transmission in a system (Shah, 2006) etc.;

(iv) The consequences of corruption upon the financing systems of some activity sectors, like the military one, Gupta (2001), the salaries in the public sectors (van Rijckeghem, Weber, 1997).

For the states in South-Eastern Europe, with special reference to Romania, we remark the papers of Andrei, Matei and Rosca (2008), as well as Andrei, Matei, Stancu and Andrei (2009), approaching the effects of corruption in the public administration systems, education or health, formulating econometric models for evaluating performance in the public sector.

II.2. Public integrity systems

The first chapter of the paper approached the relation between integrity and performance of governance. The National Integrity Systems (NIS) represent an important instrument for promoting public integrity.(14)

In Transparency International (TI) conception, the National Integrity Systems (NIS) comprise "key institutions, laws and practices (the 'pillars") that contribute to integrity, transparency and accountability in a society."(15)

The perspectives of the analysis and modelling the corruption phenomena, aimed by our paper, are supported by the country studies that provide both an overview on NIS, the indicators for measuring the subsequent progresses from those countries, as well as a basis of comparisons among states.

The above mentioned country study asserts: "when it functions correctly, NIS fights against corruption as part of a broader fight against the abuse of power, breaking the law and fraud under all its forms".

II.2.1. Stages in developing the National Integrity System in Romania

1990–1998

- The period coincides with the first half of the transition period;
- The main exponents of the national public integrity were the Parliament and Government, that did not elaborate a public policy to promote the public integrity;
- The Judiciary had no capacity to adjust the deficiencies of the other two powers in the state;
- The social perception on the public pillars reveals a high degree of corruption, just in the interior of most of the public integrity pillars;
- The civil society was not concerned with corruption, focusing on ensuring the basic requirements of democracy, rule of law and respect for human rights;
- The international institutions were concerned about the economic and democratic reforms.

1999–2004

- The second stage coincides with the beginning of the negotiations of accession into the European Union;
- The international agencies have expressed their interest towards the Romanian public integrity system (programmes were initiated and political pressures were exerted for reforms);
- The main pillars of integrity – the Executive and Legislative – have realised the seriousness of the national corruption level;
- In 2001, the Government elaborated a National Anticorruption Strategy and the National Anticorruption Prosecutor's Office was set up;
- Other NIS pillars were strengthened, such as Ombudsman or Court of Audit;
- The progresses have determined Romania to become NATO member and closing the negotiations for accession into the European Union;
- The other pillars: Parliament, justice, police have not recorded progresses;
- The civil society was focused on the fight against corruption, adding on the public agenda draft laws, essential for public integrity;
- The public policies designed to ensure the cooperation between pillars were inconsistent, proving a low capacity of implementation and reduced political will.

2005–2007

- The third period coincides with signing the Treaty of Romania Accession into the European Union;

▪ The main political criteria were fulfilled;

▪ Romania should implement effectively EU standards in the area of justice concerning corruption level, competition and control in customs.

2007–present

▪ Getting thorough knowledge about European standards, instruments and practices about strengthening public integrity as indicator of efficient governance.

The stages undergone by Romania in order to develop its own integrity system are present, with certain features in most states analysed in the actual paper.

II.3. Integrity framework

The concerns of various public bodies, institutions and authorities, universities or outstanding specialists have shaped a model for ethics framework in the public sector(16). Adapting this framework to the general topic of public integrity, we obtain a logical causal relation between integrity and performance of governance.

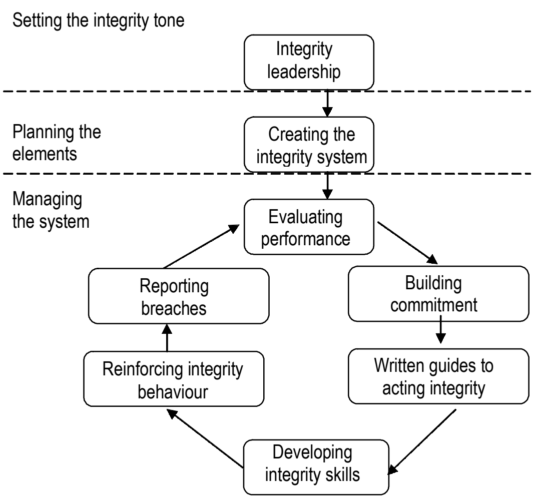

Figure 1. *Integrity framework*

The Integrity Framework comprises in fact three subsystems concerning: integrity leadership, creating the integrity system and managing the integrity system. We add the integrity resource kit, referring to take the integrity challenge, to develop integrity skills and implement the kit.

II.4. Economic freedom

According to the assertions of Heritage Foundation, the economic freedom represents the individual's right to control his/her work and property. In an economically free society, the individuals have the freedom to work, produce, consume and invest in any way, being protected and not constrained by the state. In order to determine the global indicator of economic freedom (IEF), Heritage Foundation uses ten specific indicators, evaluated on fields such as: business, trade, taxation, government size, monetary freedom, investment, finance, right to property, freedom from corruption, labour.

Altman (2007) analyses the impact of economic freedom, including its various components, on the global economic performance of a country. The author states that some specific indicators of IEF are positively correlated to higher levels of GDP per capita, while other indicators are in the opposite situation.

Hall and Lawson (2008, p. 3) conclude concerning Altman's approaches (2007, pp. 1-20): „ Altman's simple correlations add nothing to the on-going and important discussion about the role of economic freedom in contributing to aggregate economic performance".

The specialised literature emphasises connections between the economic freedom and corruption. Graeff and Mehlkop (2003) investigate the impact of various components of the economic freedom on corruption. Also, in this case, the results confirm the fact that certain fields of economic freedom discourage corruption – financial and monetary freedom, freedom of affairs- while others favour corruption –government size. At the same time, Rose-Ackerman (1997) remarks the possibility to increase corruption when obstacles are imposed in free development of economy. Eiras (2003) carries out a complex analysis, referring to ethics, corruption and economic freedom. The conclusions of the author[17] reveal relations between the economic freedom and corruption on the formal and informal economic activities. Informal economy, direct effect of the corruption phenomena will have a higher weight in GDP as long as the economic freedom disappears. „On average, the size of the informal economy in economically unfree and repressed economies is almost three times the size of the informal economy in free economies and almost double the size of the informal economy in mostly free economies".

The following charts are illustrative in the study mentioned, showing "the relationship between economic freedom and the level of corruption in 95 countries around the world. Figure 1 shows a strong correlation between these two factors. As economic freedom vanishes, corruption flourishes. On average, as shown in Figure 2, the level of perceived morality – as a contrast to corruption – in economically free countries is almost four times the level of perceived morality in the public sector in mostly unfree or repressed economies, and almost 60 percent greater than in mostly free economies."

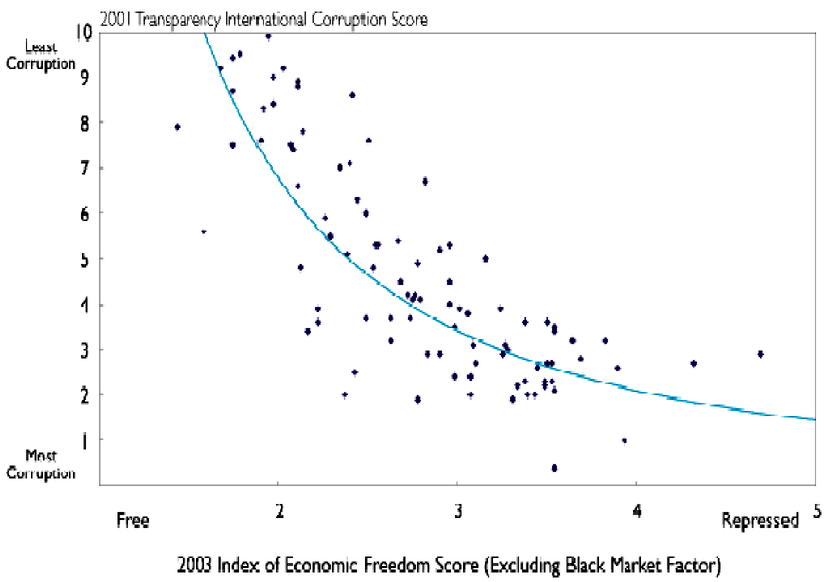

Figure 1. *Economic freedom and corruption*

Sources: Gerald P. O'Driscoll, Jr., Edwin J. Feulner, and Mary Anastasia O'Grady, 2003 *Index of Economic Freedom* (Washington, D.C.: The Heritage Foundation and Dow Jones & Company, Inc., 2003); Transparency International, *The Corruption Perception Index 2001 and 2000*, Berlin, Germany, 2001 and 2000, available at http://www.transparency.org/cpi/2001.htm and http://www.transparency.org/cpi/2000.htm

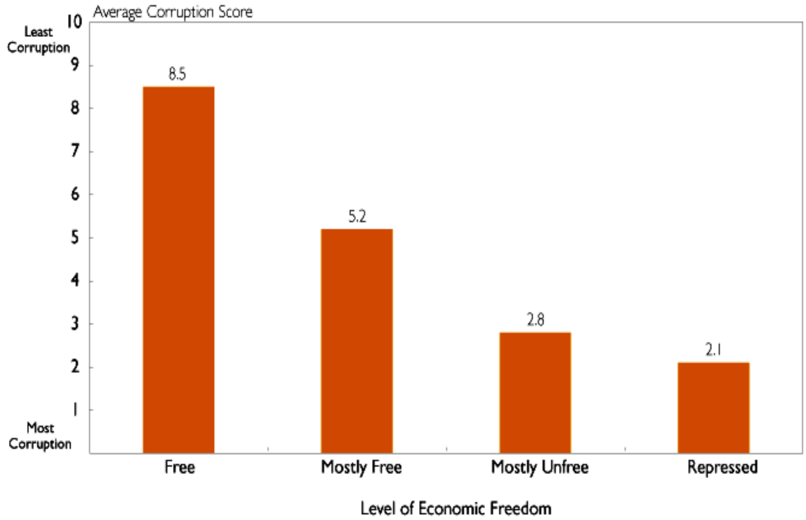

Figure 2. *Economic freedom and corruption*

Sources: Gerald P. O'Driscoll, Jr., Edwin J. Feulner, and Mary Anastasia O'Grady, 2003 Index of Economic Freedom (Washington, D.C.: The Heritage Foundation and Dow Jones & Company, Inc., 2003); Transparency International, The Corruption Perception Index 2001 and 2000, Berlin, Germany, 2001 and 2000, available at http://www.transparency.org/cpi/2001.htm and http://www.transparency.org/cpi/2000.htm

Mushfiq and Dean (2007) achieve similar studies with the study proposed in the current paper, using an econometric model applied in a panel of 60 countries, including the economic freedom as independent variable.

III. An empiric comparative study

The theoretical framework briefly presented in the first two chapters of the paper again substantiates the idea of some mutual determinations between public integrity, corruption and governance performance.

The following empirical study focuses on a sample of 11 states, most of them belonging to the former European communist space and situated at different EU integration levels: an older EU state (GR), 4 states that entered the EU in the last but one wave (2004), (HU, CZ, SK, SL), 2 states that entered EU in the last wave (RO, BG), or others in the process of adhering (HR, TR, MD, UA).

Extending the sample outside the South-Eastern European area also, was determined both by the need to obtain a more relevant comparative study and by the use of some empirical data as comprehensive as possible that can deliver the adequate support necessary for the statistical processing. The states taken into consideration belong to both the former Soviet Union (MD, UA), former Yugoslavia (HR, SI), Balkan area (GR, BG, TR), Central Europe (SK, CZ, HU) and, of course, Romania.

The analysed period is 1998–2008 and the results regarding the used indices belong to the World Bank, Transparency International, Global Integrity or Heritage Foundation.

III.1. Correlating the used indices for public integrity

We stopped both at the index for corruption perception of Transparency International and that of corruption control, annually computed by the World Bank. At the same time, we made a connection with the Global Integrity Index (GI) although, as the very ones who promote it are announcing that their computing methodology[18] is different from that of other governance and corruption specific indices. GI embodies an appreciable quantity of quantitative data delivered by more than 300 indices related to responsibility and governance transparency, as well as different anticorruption mechanisms, benefiting from the expertise of famous analysts and specialists in the complex field of public integrity.

Exactly as their presentation shows, GI does not measure the "corruption disease", but rather it tries to find remedies that the citizens and governments could use in order to fight against it.[19] Considering that it is impossible to accomplish a real corruption measuring[20], GI assesses the corruption's opposite – that is "the access that citizens and businesses have to a country's government, their ability to monitor its behaviour, and their ability to seek redness and advocate for improved governance".[21]

For 2008, the integrity indices have been organised on six big categories and 23 subcategories. The mentioned categories are: Civil Society, Public Information and Media, Elections, Government Accountability, Administration and Civil Service, Oversight and Regulation, Anti-Corruption and Rule of Law (GI, 2008, pp. 5-6).

The analysis preliminary to the results' completion regarding the GI refer not only to the formal aspects – the existence of the legislative framework, procedures, etc. – but also to their assessment and their application through the indices of personnel, budgetary support, political independence, the citizens' access to the most important anticorruption mechanisms. We insisted on a wider presentation of the GI approach model in order to substantiate, as it will be seen, an option of the present study for using the TI corruption perception index as a relevant index, from a statistical point of view, for determining the connections between public integrity and governance performance.

The quantitative data used in the statistical analysis are presented in Appendix 1, for the TI index, Appendix 2, for the control of corruption index of the World Bank (KKM) and Appendix 3, for the Global Integrity Index (GI).

In Table 1 are presented the Pearson linear correlations for the evolutions of the corruption perception index, TI, in the mentioned states.

Pearson linear correlations of the corruption perception index computed by Transparency International

Table 1

	TI_RO	TI_BG	TI_HU	TI_CZ	TI_SK	TI_GR	TI_SI	TI_HR	TI_TR	TI_MD	TI_UA	TI
TI_RO	1	-,169	,457	,931(**)	,787(**)	,518	,741(*)	,297	,848(**)	,419	,428	,906(**)
TI_BG	-,169	1	-,117	-,285	,284	-,817(**)	,161	,312	-,086	-,018	-,065	,116
TI_HU	,457	-,117	1	,465	,271	,366	-,028	,065	,648(*)	,711(*)	,004	,484
TI_CZ	,931(**)	-,285	,465	1	,784(**)	,610(*)	,768(**)	,211	,785(**)	,510	,501	,880(**)
TI_SK	,787(**)	,284	,271	,784(**)	1	,013	,867(**)	,437	,725(*)	,525	,571	,953(**)
TI_GR	,518	-,817(**)	,366	,610(*)	,013	1	,183	-,166	,427	,089	-,002	,235
TI_SI	,741(*)	,161	-,028	,768(**)	,867(**)	,183	1	,229	,528	,125	,731(*)	,808(**)
TI_HR	,297	,312	,065	,211	,437	-,166	,229	1	,491	,113	-,142	,438
TI_TR	,848(**)	-,086	,648(*)	,785(**)	,725(*)	,427	,528	,491	1	,593	,106	,873(**)
TI_MD	,419	-,018	,711(*)	,510	,525	,089	,125	,113	,593	1	,289	,582
TI_UA	,428	-,065	,004	,501	,571	-,002	,731(*)	-,142	,106	,289	1	,484
TI	,906(**)	,116	,484	,880(**)	,953(**)	,235	,808(**)	,438	,873(**)	,582	,484	1

Also, in Table 2 are presented the Pearson linear correlations for the evolutions of the control of corruption indices in the mentioned states. For each of the two tables there were introduced two variables, TI and KKM, representing the mean of the presented indices.

Pearson linear correlations of the control of corruption index computed by the World Bank

Table 2

	KKM_RO	KKM_BG	KKM_HU	KKM_CZ	KKM_SK	KKM_GR	KKM_SI	KKM_HR	KKM_TR	KKM_MD	KKM_UA	KKM
KKM_RO	1	-,460	-,287	,419	-,344	-,022	,628	-,515	,062	,795	-,376	,382
KKM_BG	-,460	1	,822	-,426	,127	,552	-,152	,590	-,149	-,679	,024	,161
KKM_HU	-,287	,822	1	-,116	-,078	,827	,153	,458	-,326	-,505	-,468	,135
KKM_CZ	,419	-,426	-,116	1	-,748	-,093	,688	-,412	-,400	,396	-,668	-,200
KKM_SK	-,344	,127	-,078	-,748	1	,190	-,826	,598	,840	-,410	,746	,401
KKM_GR	-,022	,552	,827	-,093	,190	1	,139	,586	,091	-,258	-,405	,556
KKM_SI	,628	-,152	,153	,688	-,826	,139	1	-,546	-,522	,669	-,802	,122
KKM_HR	-,515	,590	,458	-,412	,598	,586	-,546	1	,365	-,663	,321	,395
KKM_TR	,062	-,149	-,326	-,400	,840	,091	-,522	,365	1	-,046	,670	,628
KKM_MD	,795	-,679	-,505	,396	-,410	-,258	,669	-,663	-,046	1	-,299	,258
KKM_UA	-,376	,024	-,468	-,668	,746	-,405	-,802	,321	,670	-,299	1	,129
KKM	,382	,161	,135	-,200	,401	,556	,122	,395	,628	,258	,129	1

In order to ensure an unitary correlation framework, upon the KKM indices a translation and amotation was performed so to place them in the same interval as the TI. Knowing the fact that the KKM index varies in the (-2.5, 2.5) interval, giving the conditions from above we obtain:

$$y = \frac{1}{2} TI - 2.5 \text{ or } x = 2KKM + 5 \qquad (1)$$

Also, for the G.I. index the following transformation:

$$z = \frac{1}{10} GI \qquad (2)$$

The different assessment methodologies of these indices lead to the impossibility of drawing some common conclusions regarding the evolutions of the corruption phenomena in the analysed states. The support for this statement results also from *Table 3* where there are presented the Pearson linear correlations between the TI and KKM indices. Moreover, the very value of - 0.386 for the correlations of the indices' means reveal negative correlations of the variables. The same conclusion results also from most of the correlations for indices at the level of the analysed states.

Pearson linear correlations of the indices computed by TI and WB

Table 3

	KKM_RO	KKM_BG	KKM_HU	KKM_CZ	KKM_GR	KKM_SI	KKM_HR	KKM_TR	KKM_MD	KKM_UA	KKM	KKM_SK
TI_RO	,463	-,491	-,668	,141	-,552	-,204	-,218	,231	,207	,294	-,129	,043
TI_BG	-,688	,545	,153	-,748(*)	,004	-,895(**)	,621	,365	-,836(**)	,732(*)	-,080	,705
TI_HU	,168	-,499	-,461	,162	-,449	-,183	-,162	-,233	,131	-,015	-,490	-,136
TI_CZ	,606	-,687	-,713(*)	,176	-,556	-,046	-,452	,143	,443	,119	-,169	-,045
TI_SK	,065	-,374	-,682	-,322	-,697	-,580	-,217	,330	-,045	,636	-,315	,352
TI_GR	,732(*)	-,578	-,227	,682	,009	,613	-,350	-,280	,683	-,623	,052	-,532
TI_SI	,169	-,286	-,627	-,311	-,774(*)	-,730	-,685	,179	-,077	,625	-,380	,190
TI_HR	,300	,332	,148	,504	-,114	,411	,043	-,452	-,385	-,267	-,236	-,672
TI_TR	,182	-,467	-,491	,078	-,424	-,288	-,059	-,072	,084	,113	-,375	,005
TI_MD	,100	-,951(**)	-,805(*)	-,016	-,604	-,769(*)	-,517	,266	,443	,365	-,385	,345
TI_UA	,166	-,404	-,660	-,066	-,827(*)	-,083	-,705	,094	,250	,396	-,363	-,064
TI	,169	-,451	-,674	-,103	-,677	-,456	-,225	,174	,015	,445	-,386	,172

As a result, we will proceed to drawing some conclusions relevant for each type of correlations.

So, the analysis of Table 1 result in contradictory evolutions of corruption perception between TI_BG and most of the other states' indices, the strongest being TI_GR (- 0.817), and the lowest TI_MD (- 0.018). For SK, as well as for RO, CZ, TR and MD, except for TI_BG, and for SI, except TI_HU, all the other correlations are positive, the strongest correlations, though not having a high level of significance. In Table 4 are presented, in brief, the types of correlations with the other states.

The synthesis of correlations and significance levels for the evolutions of corruption perception index, TI

Table 4

Index	Positive correlations	Negative correlations	Sig 0.01 level	Sig 0.05 level
TI_RO	9	1	3	1
TI_BG	2	8	1	-
TI_HU	7	3	-	2
TI_CZ	9	1	4	1
TI_SK	70	0	3	1
TI_GR	7	3	1	1
TI_SI	9	1	2	2
TI_HR	8	2	-	-
TI_TR	9	2	1	2
TI_MD	9	1	0	1
TI_UA	7	3	-	1

The previous conclusions are stressed also by the correlations' analysis of the mean index for corruption perception (TI) from which we infer three levels of correlations:

- Weak – TI_BG (0.116) and TI_GR (0.235)
- Medium – TI_HU (0.484), TI_HR (0.438), TI_MD (0.582), TI_VA (0.484)
- Strong – TI_RO (0.906), TI_CZ (0.880), TI_SK (0.953), TI_SI (0.808), TI_TR (0.873).

From analysing Table 2 are obtained the results below the synthesis of the correlations and significance levels is the one presented in Table 5.

Table 5

Index	Positive correlations	Negative correlations	Sig 0.01 level	Sig 0.05 level
KKM_RO	4	6	-	1
KKM_BG	5	5	-	1
KKM_HU	4	6	-	2
KKM_CZ	3	7	-	1
KKM_SK	3	7	1	3
KKM_GR	6	4	-	1
KKM_SI	5	5	-	2
KKM_HR	6	4	-	-
KKM_TR	4	6	1	-
KKM_MD	3	7	-	-
KKM_UA	3	7	-	2

From this synthesis, as well as from Table 2 we observe that drawing certain conclusions is heavier. This is due to the fact, in our opinion, on one hand, to the complexity of the model used by the World Bank to determine the corruption control index, as well as the series of data insufficiently used.

This time we will find a negative correlation too, with the mean control of corruption index (KKM) for KKM_CZ (- 0.2). The other positive correlations with the mentioned index can be considered:

- Weak: KKM_BG (0.161), KKM_HU (0.135), KKM_SI (0.122), KKM_UA (0.129)
- Medium: KKM_RO (0.382), KKM_SK (0.401), KKM_HR (0.395), KKM_MD (0.258)
- Strong: KKM_GR (0.556), KKM_TR (0.628).

From the two analyses appear as obvious the differences or similarities between the processes of corruption perception and control of corruption (see Table 6).

Compatibility of the methodological processes concerning the corruption perception and control of corruption

Table 6

Compatibility		Incompatibility	
Major	Mean	Major	Mean
TR, BG	HR, MD	CZ, GR, SI	HU, UA, RO, SK

For Global Integrity Index, taking into account the available series of data, we cannot achieve correlations for the developments of the above indices in the states under analysis.

However, we calculated a mean index of integrity (GI) and on this basis we calculated the correlations with the other mean indices. The results are not surprising if we take into consideration the calculation "philosophy" of the Global Integrity Index, briefly presented in this paper, the major differences between the legislative and procedural framework of anticorruption mechanisms and concrete public action, in view to change the social perception on this phenomenon in those states.

Pearson linear correlations between mean indices of corruption perception and control of corruption and public integrity

Table 7

Indicator	TI	KKM	GI
TI	1	-0.386	-0.797
KKM		1	0.701
GI			1

All correlations being significant for 0.01 level, we find out a negative correlation between TI and GI and another strong positive correlation between KKM and GI, whose justification derives once again from the calculation methodology.

Therefore, related to the significance of the regression coefficients, it is likely to use TI or KKM or GI index as dependant variable. In fact, a simple regression between the latter 2 indices leads to the relation:

$$KKM = 4.529 + 0.102\ GI + e \qquad (3)$$

with coefficients revealing a corresponding significance level.

The results included in Table 7 emphasise a characteristic element for the states analysed, that could be transposed in the conclusion anticipated concerning social inefficiency for the mechanisms of anticorruption action, even in the conditions of an adequate legislative and procedural framework.

III.2. Correlations of the indicators of governmental performance

As stated, from the indices of governmental performance we took into consideration the Gross Domestic Product per capita (GDP) and the Index of Economic Freedom (IEF).

The qualitative data are presented in *Appendix 5* for GDP and *Appendix 6* for IEF. In statistical processing, we apply log GDP so that the statistic analyses use data of the same order of dimension.

Concerning GDP index, the correlations of the indices for the analysed states are not significant, taking into consideration the ascending evolution of GDP during the period analysed. At the same time, the correlations between IEF and GDP indices are approximately constant for each country, emphasizing either strong positive correlations (BG, HR, HU, RO, SK) but with a significance level almost null or negative correlations or almost null, with a high significance level (for the other states).

The correlations for IEF are more relevant (see Table 8)

Table 8

	IEF_BG	IEF_HR	IEF_CZ	IEF_GR	IEF_HU	IEF_MD	IEF_RO	IEF_SK	IEF_SI	IEF_TR	IEF_UA	IEF
IEF_BG	1	,334	-,515	-,455	,583	,003	,677	,963	,200	-,324	,728	,830
		,315	,105	,160	,060	,993	,022	,000	,556	,330	,011	,002
IEF_HR	,334	1	,171	-,157	,217	,178	,722	,397	,269	,349	,024	,587
	,315		,615	,644	,522	,600	,012	,227	,425	,292	,945	,058
IEF_CZ	-,515	,171	1	,776	,058	-,448	,079	-,405	,450	,782	-,783	-,084
	,105	,615		,005	,867	,167	,818	,216	,165	,004	,004	,807
IEF_GR	-,455	-,157	,776	1	,223	-,583	-,032	-,331	,589	,736	-,507	-,042
	,160	,644	,005		,511	,060	,926	,321	,057	,010	,112	,903
IEF_HU	,583	,217	,058	,223	1	-,093	,662	,587	,243	,372	,255	,767
	,060	,522	,867	,511		,786	,026	,057	,471	,260	,449	,006
IEF_MD	,003	,178	-,448	-,583	-,093	1	-,048	-,079	-,753	-,272	,286	-,095
	,993	,600	,167	,060	,786		,888	,818	,008	,418	,393	,781
IEF_RO	,677	,722(*)	,079	-,032	,662	-,048	1	,780	,491	,396	,202	,938
	,022	,012	,818	,926	,026	,888		,005	,125	,228	,552	,000
IEF_SK	,963	,397	-,405	-,331	,587	-,079	,780	1	,355	-,163	,678	,905
	,000	,227	,216	,321	,057	,818	,005		,284	,632	,022	,000
IEF_SI	,200	,269	,450	,589	,243	-,753	,491	,355	1	,481	-,109	,496
	,556	,425	,165	,057	,471	,008	,125	,284		,134	,751	,120
IEF_TR	-,324	,349	,782	,736	,372	-,272	,396	-,163	,481	1	-,604	,233
	,330	,292	,004	,010	,260	,418	,228	,632	,134		,049	,491
IEF_UA	,728	,024	-,783	-,507	,255	,286	,202	,678	-,109	-,604	1	,457
	,011	,945	,004	,112	,449	,393	,552	,022	,751	,049		,157
IEF	,830	,587	-,084	-,042	,767	-,095	,938	,905	,496	,233	,457	1
	,002	,058	,807	,903	,006	,781	,000	,000	,120	,491	,157	

The analysis on the results in Table 8 emphasise different policies of economic freedom, therefore it is hard to establish the perspective. The synthesis of the developments and significance levels is presented in Table 9.

Synthesis of IEF correlations

Table 9

Index	Positive correla-tions	Negative correla-tions	Sig 0.01 level	Sig 0.05 level
IEF_BG	7	3	1	2
IEF_HR	8	2	-	1
IEF_CZ	6	4	3	-
IEF_GR	4	6	2	-
IEF_HU	9	1	-	1
IEF_MD	3	7	1	-
IEF_RO	8	2	1	3
IEF_SK	6	4	2	1
IEF_SI	8	2	1	-
IEF_TR	6	4	2	1
IEF_UA	6	4	1	2

In Table 9, we emphasise the situation for HU, whose policy of economic freedom positively correlates with most states and at extreme, MD which has negative correlations with most states analysed.

The correlations with a mean index of economic freedom underline evolutions almost independent related to the other states (CZ (- 0.084), GR (- 0.042), MD (- 0.195), weak correlated (TR (0.233)), mean correlated (HR (0.587), SI (0.496) or (UA (0.457)) and strong correlated (BG (0.830), HU (0.767), RO (0.938), SK (0.905)).

III.3. Linear regressions

The analyses reveal that the single interesting regressions in view of the current study are those using TI or GI (or KKM) as dependent variables and IEF and GDP as independent variables. In order to emphasise statistically the influence of the European integration process on public integrity, we introduced an independent variable "dummy", called UE, awarding the following values for each state during the analysed period:

$$UE = \begin{cases} 1, & \text{if the respective state is EU Member State} \\ 0, & \text{in the opposite case} \end{cases}$$

UE variable introduced in the above regressions will underline quantitatively the influence of the integration process on the indices of public integrity.

For TI, we obtain:

$$\underset{(0.219)}{TI = -2.944} + \underset{(0.371)}{0.759\,IEF} + \underset{(0.699)}{0.606\,Log\,GDP} + \varepsilon_1 \quad (4)$$

or

$$\underset{(0.832)}{TI = -1.122} + \underset{(0.485)}{0.654\,IEF} + \underset{(0,877)}{0.287\,Log\,GDP} + \underset{(0.701)}{0.276\,UE} + \varepsilon_3 \quad (5)$$

In both situations, the significance levels of the coefficients are in parentheses.

Unfortunately, lacking comprehensive series of data, for the other regression, the significance levels of the coefficients are null.

Both expressions (4) and (5) help us to determine, approximately, possible influences of the governance indices on public integrity, expressed by means of TI.

As an example, for Romania, the increase by 0.5 of IEF index (in reality by 5, according to formula 2) will lead to an increase by 0.33 of the index concerning perception on corruption, taking into consideration the influence of the European integration process, thus it results an increase by 0.4.

In 2007, the year of Romania's accession in the EU, the increase by 0.6 of the index concerning perception on corruption is due especially to the mentioned event (0.56), according to (5).

GDP growth influences significantly TI index only if it exceeds the annual mean of GDP evolution. Thus, for Romania, an increase by 1500$ of GDP will lead to an increase by 0.0125 of TI index. Consequently, the index of economic freedom will have the most significant influence and UE index will have the most significant influence at the moment of accession of a state in the EU.

IV. Conclusions

The paper presents a new approach for public integrity in view of the influence of the indices concerning GDP and economic freedom. The further developments might take in consideration both enlargement of the area of analysis, comprising more states and longer periods, and introducing new indices for governmental performance.

At the same time, even in the conditions of the current study, other relevant regressions could be determined. For example, if GDP is dependant variable and TI and IEF independent variables, we obtain:

$$Log\,GDP = \underset{(0.020)}{1.139} + \underset{(0.699)}{0.032\,TI} + \underset{(0.002)}{0.467\,IEF} + \varepsilon_3 \quad (6)$$

or introducing UE variable:

$$LogGDP = \underset{(0.037)}{1.994} + \underset{(0.877)}{0.013TI} + \underset{(0.066)}{0.326IEF} + \underset{(0.247)}{0.168UE} + \varepsilon_4 \quad (7)$$

Continuing the judgements, we shall obtain for IEF:

$$IEF = \underset{(0.450)}{-0.781} + \underset{(0.371)}{0.133\,TI} + \underset{(0.002)}{1.53\,Log\,GDP} + \varepsilon_5 \quad (8)$$

$$IEF = 0.432 + 0.110TI + 1.237 \, Log \, GDP + 0.184UE + \varepsilon_6$$
$$(0.843) \quad (0.485) \quad (0.066) \quad (0.530) \qquad (9)$$

All the above regressions reveal a strong dependency between IEF and GDP. For more consistent series of data, the significance level of the coefficients of regression will increase.

Notes

(1) See http://unpan1.un.org/intradoc/groups/public/documents/UN/UNPAN.pdf.

(2) A more detailed presentation of these aspects can be found in the UN Millennium Declaration, http://222.un.org/millenniumgoals/bkgd.shtml.

(3) See ANAO, (2003), "Public Sector Governance", Volumes 1&2: Better Practice Guide, Commonwealth of Australia, Canberra, p. 2.

(4) For details and explanations can be seen also Australia Public Service Commission, (2005), "Foundations of Governance in the Australian Public Service", Commonwealth of Australia, Canberra, http://www.apsc.gov.au/foundations/.

(5) See ANAO and Department of the Prime Minister and Cabinet, (2006), "Implementation of Programme and Policy Initiatives: Making Implementation Matter, Better Practice Guide, Commonwealth of Australia, Canberra, p. 13, http://www.anao.gov.au/uploads/documents/".

(6) According to "Public Sector Standards Commissioner (PSSC), Ethics framework", http://www.ssa.vie.gov.au/.

(7) See http://www.accaglobal.com/.../activities/subjects/publicsector/governance/.

(8) OECD, (2009), "Public Governance and Management", http://www.oecd.org, p. 1.

(9) Details regarding the recent concerns of OECD about promoting governance integrity can be found, for example, in "Building a Clearer World: Tools and Good Practices for Fostering a Culture of Integrity" (2009), Paris, http://www.oecd.publicgovernanceforum.org/, or "OECD Recommendation on Enhancing Integrity in Public Procurement", (2008), http://www.oecd.org/document/...html.

(10) See http://www.worldbank.org/

(11) See http://www.imf.org/external/pubs/ft/issues6/

(12) See http:/www.transparency.org/

(13) See more details in Rose-Ackerman, S., (2005), "Corruption and Government Causes, Consequences and Reform", part I, chapters 1-5, pp. 7-89.

(14) The broad description of the relations between public integrity and corruption concerning the South-Eastern European states is presented in Matei, A., (2008), "Corruption, Transparency and Quality. Comparative Approaches and Judiciary Support; Themis Project "Transformation of the Role of the Judiciary within a European Integrated Context", Bibliothéque de Droit Public Européen, vol LXXXV, Esperia Publications Ltd, London, pp. 127-142.

(15) See "National Integrity System. Country Study. Romania 2005, Transparency International Romania, p. 1.

(16) See "State Services Authority: Supporting Government Serving Victorians – Ethics Framework",http://www.ssa.vic.gov.au/.../Ethics Framework.

(17) Ana Isabel Eiras in Senior Policy Analyst for International Economies in the Center for International Trade and Economies at the Heritage Foundation.

(18) For the data regarding the computing methodology of the integrity index see Camerer, M., (2006), "Measuring Public Integrity", Journal of Democracy

No. 17:1, National Endowment for Democracy and the Johns Hopkins University Press.

(19) See http:/report.globalintegrity.org/globalIndex.cfm.

(20) An idea also supported by authors like Arndt and Oman (2006).

(21) See The Global Integrity Report: 2008, Methodology White Paper, pp. 1, http://globalintegrity.org/documents/Whitepaper2008.pdf.

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Appendix 1

Transparency International Corruption Perceptions Index 1998-2008

Year	Romania (RO)	Bulgaria (BG)	Hungary (HU)	Czech Republic (CZ)	Slovakia (SK)	Greece (GR)	Slovenia (SI)	Croatia (HR)	Turkey (TR)	Moldova (MD)	Ukraine (UA)
1998	3.1	2.9	5.0	4.8	3.9	4.9			3.4		2.8
1999	3.3	3.3	5.2	4.6	3.7	4.9	6.0	2.7	3.6	2.6	2.6
2000	2.9	3.5	5.2	4.3	3.5	4.9	5.5	3.7	3.8	2.6	1.5
2001	2.8	3.9	5.3	3.9	3.7	4.2	5.2	3.9	3.6	3.1	2.1
2002	2.6	4.0	4.9	3.7	3.7	4.2	6.0	3.8	3.2	2.1	2.4
2003	2.8	3.9	4.8	3.9	3.7	4.3	5.9	3.7	3.1	2.4	2.3
2004	2.9	4.1	4.8	4.2	4.0	4.3	6.0	3.5	3.2	2.3	2.2
2005	3.0	4.0	5.0	4.3	4.3	4.3	6.1	3.4	3.5	2.9	2.6
2006	3.1	4.0	5.2	4.8	4.7	4.4	6.4	3.4	3.8	3.2	2.8
2007	3.7	4.1	5.3	5.2	4.9	4.6	6.6	4.1	4.1	2.8	2.7
2008	3.8	3.6	5.1	5.2	5.0	4.7	6.7	4.4	4.6	2.9	2.5

Source: *www.transparency.org*

Appendix 2

World Bank Control of Corruption Index (KKM)

Year	Romania	Bulgaria	Hungary	Czech Republic	Slovakia	Greece	Serbia	Slovenia	Croatia	Turkey	Moldova	Ukraine
1998	-0.11	-0.23	0.74	0.82	0.23	0.68	-1.30	1.7	-0.16	-0.05	-0.26	-0.96
1999												
2000	-0.19	-0.14	0.82	0.69	0.33	0.81	-1.20	0.98	0.11	-0.06	-0.59	-0.97
2001												
2002	-0.24	-0.02	0.84	0.74	0.28	0.72	-0.91	0.97	0.02	-0.14	-0.72	-0.84
2003	-0.22	-0.10	0.82	0.80	0.36	0.77	-0.97	0.92	0.06	0.02	-0.78	-0.85
2004	-0.17	-0.06	0.82	0.70	0.48	0.82	-0.70	0.87	0.11	0.11	-0.62	-0.71
2005	-0.23	-0.19	0.71	0.74	0.44	0.65	-0.86	0.79	0.06	0.08	-0.57	-0.57
2006	-0.21	-0.19	0.76	0.73	0.41	0.68	-0.59	0.79	-0.05	-0.01	-0.65	-0.77
2007	-0.17	-0.14	0.74	0.77	0.35	0.65	-0.57	0.84	0.03	0.00	-0.66	-0.70

Source: *http://www.worldbank.org/*

Appendix 3

Global Integrity Index

Global Integrity Index			
The State	Year		
	2008	2007	2006
Bulgaria	87.0	87.0	80
Croatia			
Czech Republic			
Greece			
Moldova	68.0	60.0	
Romania	80.0	81.0	86.0
Slovakia			
Slovenia			
Turkey	69.0	71.0	
Ukraine		68.0	
Hungary	77.0		

Source: *http://www.report.globalintegrity.org/globalIndex.cfm*

Appendix 4

Year	Romania	Bulgaria	Hungary	Czech Republic	Slovakia	Greece	Slovenia	Croatia	Turkey	Moldova	Ukraine
1998	5.841.958	5477.05	10.550.932	13.745.803	10.690.076	16.746.918	15.565.882	8736.72	8.103.731	1.437.781	2.936.989
1999	5.886.238	5.714.082	11.178.707	14152.22	10.827.393	17.484.193	16.568.128	8.684.596	7.825.376	1.409.092	2.990.677
2000	6.171.507	6199.81	12.052.619	15.007.517	11.217.903	18.587.874	17.602.617	9.487.722	8.149.598	1.472.371	3.316.795
2001	6.710.511	6.653.744	12.871.208	15.816.589	11.867.247	19.822.961	18.547.354	10.018.956	7.739.835	1.603.623	3.739.701
2002	7.204.313	7.120.287	13.702.771	16.405.646	12.639.343	20.904.433	19.551.164	10.747.971	8.226.385	1.762.427	4.038.091
2003	7.769.154	7.684.231	14.625.334	17344.17	13.512.702	22.380.907	20.514.626	11.565.336	8.705.242	1.923.758	4.554.824
2004	8.676.224	8.462.637	15.780.271	18.744.338	14.558.998	23.973.164	21.508.347	12.327.775	9.844.432	2.126.005	5.282.395
2005	9.334.619	9.322.486	16.996.586	20.289.544	15.970.747	25.481.636	22.977.456	13.234.634	11.005.798	2.507.868	5.625.911
2006	10426.16	10.293.976	18250.9	22184.25	17871.13	27.332.603	24.971.021	14.309.071	12.094.915	2.690.524	6.253.454
2007	11.386.509	11.302.483	19.026.503	24.235.511	20.251.125	29.172.089	27.204.876	15.549.453	12.888.286	2900.54	6.941.315
2008	12.285.071	12251.92	19.799.233	25764.79	22.024.495	30.745.408	28.848.256	16.536.688	13.511.161	3.165.931	7531.85

Source: *www.indexmundi.com*

Appendix 5

Economic Freedom Index

Economic freedom is the fundamental right of every human to control his or her own labour and property. In an economically free society, individuals are free to work, produce, consume, and invest in any way they please, with that freedom both protected by the state and unconstrained by the state. In economically free societies, governments allow labour, capital and goods to move freely, and refrain from coercion or constraint of liberty beyond the extent necessary to protect and maintain liberty itself. We measure ten components of economic freedom, assigning a grade in each using a scale from 0 to 100, where 100 represents the maximum freedom. The ten component scores are then averaged to give an overall economic freedom score for each country. The ten components of economic freedom are: Business Freedom | Trade Freedom | Fiscal Freedom | Government Size | Monetary Freedom | Investment Freedom | Financial Freedom | Property Rights | Freedom from Corruption | Labour Freedom.

The State	Score 1998	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption
Bulgaria	45.7	55	49.0	53.5	48.8	25.2	50	50	50	30
Croatia	51.7	55	60.8	68.3	39.5	61.8	50	50	30	50
Czech Republic	68.4	85	77.4	54.7	39.3	75.9	70	90	70	54
Greece	60.6	70	77.8	53.3	52.5	71.4	70	30	70	50
Hungary	56.9	70	61.0	55.7	2.9	63.8	70	70	70	49
Moldova	53.5	70	75.0	57.7	52.7	46.3	50	50	50	30
Montenegro	-	-	-	-	-	-	-	-	-	-
Romania	54.4	55	74.0	43.9	64.3	52.1	70	50	30	50
Serbia	-	-	-	-	-	-	-	-	-	-
Slovakia	57.5	70	73.0	66.4	35.4	72.7	50	50	50	50
Slovenia	60.7	70	59.0	51.8	37.3	68.4	70	70	70	50
Turkey	60.9	70	73.8	58.4	68.5	31.8	70	70	70	35
Ukraine	40.4	55	53.0	64.4	51.0	0.0	50	30	30	30

The State	Score 1999	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption
Bulgaria	46.2	55	46.8	68.0	46.3	0.0	70	50	50	30
Croatia	53.1	55	63.8	68.4	38.4	72.1	50	50	30	50
Czech Republic	69.7	85	79.8	59.2	44.8	76.4	70	90	70	52
Greece	61.0	70	77.8	47.6	55.8	73.9	70	30	70	54
Hungary	59.6	70	63.2	62.6	12.8	66.3	70	70	70	52
Moldova	56.1	70	75.0	58.5	55.1	65.9	50	50	50	30
Montenegro	-	-	-	-	-	-	-	-	-	-
Romania	50.1	55	74.0	45.0	65.1	27.0	70	50	30	34
Serbia	-	-	-	-	-	-	-	-	-	-
Slovakia	54.2	70	73.0	53.0	17.6	74.0	50	50	50	50
Slovenia	61.3	70	59.0	52.4	39.5	70.8	70	70	70	50
Turkey	59.2	70	74.4	57.0	57.1	31.8	70	70	70	32
Ukraine	43.7	55	53.0	63.0	43.0	39.3	50	30	30	30

The State	Score 2000	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption
Bulgaria	47.3	55	49.8	67.9	54.4	0.0	70	50	50	29
Croatia	53.6	55	67.0	68.9	41.9	70.0	50	50	30	50
Czech Republic	68.6	85	72.0	58.1	49.6	75.0	70	90	70	48
Greece	61.0	70	77.8	52.2	54.4	75.5	70	30	70	49
Hungary	64.4	70	76.6	63.9	39.3	69.6	70	70	70	50
Moldova	59.6	70	75.0	55.8	85.5	69.9	50	50	50	30
Montenegro	-	-	-	-	-	-	-	-	-	-
Romania	52.1	55	74.0	58.3	63.3	38.1	70	50	30	30
Serbia	-	-	-	-	-	-	-	-	-	-
Slovakia	53.8	70	71.2	54.8	25.0	73.9	50	50	50	39
Slovenia	58.3	70	73.6	52.9	36.5	71.9	50	50	70	50
Turkey	63.4	70	75.0	67.2	82.7	31.8	70	70	70	34
Ukraine	47.8	55	70.0	62.3	41.9	63.0	50	30	30	28

The State	Score 2001	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption
Bulgaria	51.9	55	57.2	58.1	67.3	26.2	70	50	50	33
Croatia	50.7	55	71.6	66.9	33.7	71.7	50	50	30	27
Czech Republic	70.2	85	72.8	67.5	49.6	81.2	70	90	70	46
Greece	63.4	70	78.0	50.9	54.4	78.3	70	50	70	49
Hungary	65.6	70	77.8	65.7	41.9	73.3	70	70	70	52
Moldova	54.9	55	76.4	54.5	76.5	55.9	50	50	50	26
Montenegro	-	-	-	-	-	-	-	-	-	-
Romania	50.0	55	73.4	57.6	79.7	41.4	50	30	30	33
Serbia	-	-	-	-	-	-	-	-	-	-
Slovakia	58.5	70	80.2	59.3	39.3	70.8	70	50	50	37
Slovenia	61.8	85	67.4	52.8	47.1	73.6	50	50	70	60
Turkey	60.6	70	73.0	66.9	73.0	36.4	70	50	70	36

The State	Score 2002	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption
Bulgaria	57.1	55	60.2	68.3	49.6	75.8	70	50	50	35.0
Croatia	51.1	55	68.8	68.3	25.0	75.7	50	50	30	37.0
Czech Republic	66.5	70	73.0	66.8	33.7	82.2	70	90	70	43.0
Greece	59.1	70	79.6	50.1	54.4	78.7	50	50	50	49.0
Hungary	64.5	70	80.0	65.5	28.0	74.7	70	70	70	52.0
Moldova	57.4	55	76.0	78.2	76.5	54.7	50	50	50	26.0
Montenegro	46.6	40	88.4	89.8	74.8	46.8	10	30	30	10.0
Romania	48.7	55	74.4	64.4	58.9	46.6	50	30	30	29.0
Serbia	46.6	40	88.4	89.8	74.8	46.8	10	30	30	10.0
Slovakia	59.8	70	79.8	61.1	33.7	68.8	70	70	50	35.0
Slovenia	57.8	85	64.2	51.8	41.9	72.0	50	50	50	55.0
Turkey	54.2	55	79.6	65.2	58.9	41.0	50	50	50	38.0
Ukraine	48.2	55	71.0	66.1	58.9	58.2	50	30	30	15.0

The State	Score 2003	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption
Bulgaria	57.0	55	62.4	72.4	56.7	77.5	50	50	50	39.0
Croatia	53.3	55	72.8	77.6	28.6	76.3	50	50	30	39.0
Czech Republic	67.5	70	73.6	67.2	45.6	81.9	70	90	70	39.0
Greece	58.8	70	81.4	57.2	50.3	78.5	50	50	50	42.0
Hungary	63.0	70	76.0	65.6	22.3	70.6	70	70	70	53.0
Moldova	60.0	55	80.4	81.3	78.6	63.4	50	50	50	31.0
Montenegro	43.5	40	68.4	79.8	89.2	34.2	10	30	30	10.0
Romania	50.6	55	60.2	69.1	62.4	50.8	50	50	30	28.0
Serbia	43.5	40	68.4	79.8	89.2	34.2	10	30	30	10.0
Slovakia	59.0	70	72.8	67.5	22.3	71.3	70	70	50	37.0
Slovenia	57.7	85	62.2	53.1	40.6	76.7	50	50	50	52.0
Turkey	51.9	55	73.6	64.6	45.0	42.9	50	50	50	36.0
Ukraine	51.1	55	74.6	67.1	68.1	64.0	30	50	30	21.0

The State	Score 2004	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption
Bulgaria	59.2	55	63.2	81.1	64.5	78.7	50	70	30	40.0
Croatia	53.1	55	65.4	67.3	22.9	79.5	50	70	30	38.0
Czech Republic	67.0	70	73.4	67.0	40.9	84.6	70	90	70	37.0
Greece	59.1	70	79.8	58.4	53.2	78.1	50	50	50	42.0
Hungary	62.7	70	76.0	65.6	20.1	73.7	70	70	70	49.0
Moldova	57.1	55	80.4	81.5	74.2	71.3	30	50	50	21.0
Montenegro	-	-	-	-	-	-	-	-	-	-
Romania	50.0	55	57.6	69.9	74.8	56.8	30	50	30	26.0
Serbia	-	-	-	-	-	-	-	-	-	-
Slovakia	64.6	70	72.8	68.5	42.4	80.8	70	90	50	37.0
Slovenia	59.2	85	65.2	54.4	40.6	77.3	50	50	50	60.0
Turkey	52.8	55	74.2	60.8	56.9	46.1	50	50	50	32.0
Ukraine	53.7	55	74.4	67.5	77.8	74.5	30	50	30	24.0

The State	Score 2005	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption	Labour Freedom
Bulgaria	62.3	55	82.0	80.3	53.4	83.1	50	70	30	39.0	80.3
Croatia	51.9	55	65.4	59.3	26.2	81.4	50	70	30	37.0	44.3
Czech Republic	64.6	70	76.8	68.2	15.1	88.9	70	90	70	39.0	57.7
Greece	59.0	70	80.2	58.0	54.4	78.1	50	50	50	43.0	56.1
Hungary	63.5	70	70.0	67.9	25.6	75.6	70	70	70	48.0	68.2
Moldova	57.4	55	77.2	84.5	68.5	70.0	30	50	50	24.0	64.8
Montenegro	-	-	-	-	-	-	-	-	-	-	-
Romania	52.1	55	70.4	70.1	68.9	62.6	30	50	30	28.0	55.5
Serbia	-	-	-	-	-	-	-	-	-	-	-
Slovakia	66.8	70	72.8	81.9	42.4	78.0	70	90	50	37.0	75.7
Slovenia	59.6	85	81.8	55.6	45.3	79.1	50	50	50	59.0	40.3
Turkey	50.6	55	76.0	65.3	54.4	53.8	50	30	50	31.0	40.7
Ukraine	55.8	55	76.2	83.0	78.6	76.2	30	50	30	23.0	55.8

The State	Score 2006	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption	Labour Freedom
Bulgaria	64.1	70.5	65.8	83.2	49.8	80.7	70	70	30	41	79.8
Croatia	53.6	54.5	78.4	69.6	23.2	81.2	50	70	30	35	44.6
Czech Republic	66.4	57.8	82.4	68.8	36.8	85.9	70	90	70	42	60.3
Greece	60.1	73.2	82.4	61.0	53.9	78.7	50	50	50	43	58.6
Hungary	65.0	70.8	82.4	68.2	27.1	74.3	70	70	70	48	69.5
Moldova	58.0	67.4	79.4	81.9	66.1	68.4	30	50	50	23	63.4
Montenegro	-	-	-	-	-	-	-	-	-	-	-
Romania	58.2	74.6	68.4	87.5	68.9	66.6	50	50	30	29	57.5
Serbia	-	-	-	-	-	-	-	-	-	-	-
Slovakia	69.8	69.3	82.4	89.5	52.5	77.8	70	90	50	40	76.7
Slovenia	61.9	75.1	82.4	64.0	44.3	81.7	70	50	50	60	41.6
Turkey	57.0	66.7	81.0	68.0	68.1	64.7	50	50	50	32	39.1
Ukraine	54.4	43.1	77.2	90.2	75.8	72.9	30	50	30	22	53.2

The State	Score 2007	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption	Labour Freedom
Bulgaria	62.7	70.3	70.8	82.4	57.8	75.8	60	60	30	40	79.8
Croatia	53.4	54.2	87.8	69.9	24.4	79.3	50	60	30	34	44.5
Czech Republic	67.4	61.1	86.6	69.9	47.1	86.3	70	80	70	43	20.0
Greece	58.7	69.7	81.6	62.4	53.4	78.4	50	40	50	43	44.2
Hungary	64.8	70.2	86.6	68.8	26.8	76.6	70	60	70	50	44.0
Moldova	58.7	68.1	79.4	85.6	62.8	68.0	30	50	50	29	61.7
Montenegro	-	-	-	-	-	-	-	-	-	-	64.4
Romania	61.2	73.2	84.0	85.9	71.0	69.7	50	60	30	30	41.5
Serbia	-	-	-	-	-	-	-	-	-	-	84.9
Slovakia	69.6	70.7	86.6	89.5	53.7	76.6	70	80	50	43	32.7
Slovenia	59.6	72.9	86.6	54.6	30.9	78.9	70	50	50	61	97.8
Turkey	57.4	67.4	81.0	69.1	62.4	70.1	50	50	50	35	78.9
Ukraine	51.5	43.6	77.2	83.6	53.2	68.4	30	50	30	26	30.0

The State	Score 2008	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption	Labour Freedom
Bulgaria	63.7	68.4	86.0	82.7	56.0	73.7	60	60	30	40	80.6
Croatia	54.1	58.5	87.6	68.8	28.0	78.8	50	60	30	34	45.5
Czech Republic	68.1	64.2	86.0	71.3	45.6	80.3	70	80	70	48	66.1
Greece	60.6	70.4	81.0	65.6	57.8	78.5	50	50	50	44	58.8
Hungary	67.6	74.4	86.0	70.0	26.5	77.2	80	70	70	52	70.3
Moldova	57.9	69.3	79.2	83.0	56.9	67.6	30	50	50	32	60.7
Montenegro	-	-	-	-	-	-	-	-	-	-	-
Romania	61.7	74.9	86.0	85.6	70.8	72.5	60	50	30	31	56.3
Serbia	-	-	-	-	-	-	-	-	-	-	-
Slovakia	70.0	69.5	86.0	89.4	53.9	76.9	70	80	50	47	77.1
Slovenia	60.2	74.1	86.0	62.4	33.2	79.5	60	50	50	64	42.4
Turkey	59.9	68.3	86.8	77.7	68.3	70.8	50	50	50	38	39.5
Ukraine	51.0	44.4	82.2	79.0	43.0	69.9	30	50	30	28	53.1

The State	Score 2009	Business Freedom	Trade Freedom	Fiscal Freedom	Government Size	Monetary Freedom	Investment Freedom	Financial Freedom	Property Rights	Freedom from Corruption	Labour Freedom
Bulgaria	64.6	73.5	85.8	86.2	58.7	72.8	60.0	60.0	30.0	41.0	78.4
Croatia	55.1	59.9	87.6	68.7	31.iul	79.0	50.0	60.0	30.0	41.0	43.4
Czech Republic	69.4	65.1	85.8	80.2	43.0	79.7	70.0	80.0	70.0	52.0	67.8
Greece	60.8	78.7	80.8	66.5	46.3	78.8	50.0	50.0	50.0	46.0	61.2
Hungary	66.8	77.4	85.8	70.6	19.feb	73.8	80.0	70.0	70.0	53.0	68.4
Moldova	54.9	70.1	81.6	85.3	51.3	67.6	30.0	50.0	40.0	28.0	45.1
Montenegro	58.2	68.7	80.2	89.1	45.3	78.9	40.0	50.0	40.0	33.0	57.2
Romania	63.2	74.9	85.8	87.0	70.0	75.0	60.0	50.0	35.0	37.0	57.1
Serbia	56.6	56.0	78.0	85.9	46.3	65.8	40.0	50.0	40.0	34.0	70.0
Slovakia	69.4	73.4	85.8	84.1	57.4	78.7	70.0	70.0	50.0	49.0	75.4
Slovenia	62.9	84.4	85.8	62.9	38.4	78.6	60.0	50.0	60.0	66.0	42.8
Turkey	61.6	69.9	86.6	73.2	83.4	71.1	50.0	50.0	50.0	41.0	40.3
Ukraine	48.8	40.5	84.0	77.0	39.0	68.1	30.0	40.0	30.0	27.0	52.4

Source: *http://www.heritage.org/Index/Default.aspx*

The Operational Risk – Minimum Capital Requirements

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Abstract. *This paper aims to present how to quantify the minimum capital requirement for operational risk using three approaches proposed by the Basel Committee to identify optimal allocation of capital, given that until recently to this risk has been allocated a minimum attention, considering that it has a low impact on the business of financial institutions.*

Keywords: basic indicator approach; the standardized approach; internal measurement approach; the expected loss; unexpected loss.

▪

JEL Code: G32.
REL Code: 11C.

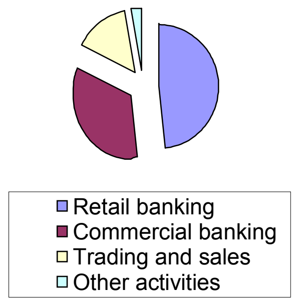
To satisfy the first pillar of the Basel II on the minimum capital required to cover operational risk, a financial institution in Romania, which we will not specify names due to confidentiality, uses an advanced model for measuring operational risk which is aimed at locating potential risks to the goods and/or support activities, in order to estimate the potential impact.

Work undertaken by the credit institution in a group may be classified, as recommended by the Basel Committee, four categories, namely: trading and sales, retail banking, commercial banking and other activities (including the overlapping activities of corporate finance, payment and settlement, agency services), monitor the operations performed on the basis of policy and specific criteria, developed and transformed in internal procedures.

For all business lines of credit institutions used as an indicator showed "gross income"[(1)], deeming it, and according to recommendations by the Basel Committee, a transparent indicator present in the financial statements on annual basis with can be easily accomplished calculations and national and international comparisons, are easily audited and reflecting well sensitivity operational risk.

To determine the capital requirements under the related operational risk based approach it will be applied the factor of 15% on average gross income obtained during three consecutive years.

In case where the standard model for determining the capital requirements is applied the process of allocation of gross income for each business line has to be started and then the average gross income for a period of three years, corresponding to each business line will apply the appropriate risk weight[(2)] to determine the capital requirement.

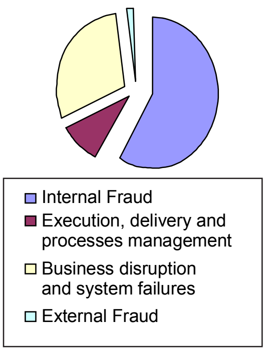


Source: Own processing.

Figure 1. *The capital requirement under the Standard Approach for business line*

As can be seen from Figure 1, when high values for the business line activity in retail banking are obtained reveals the size and intensity of gross income business establishment concerned in that sector, also providing information to the departments concerned about potential losses that may occur and the amount necessary to cover losses related to operational risk on that business line.

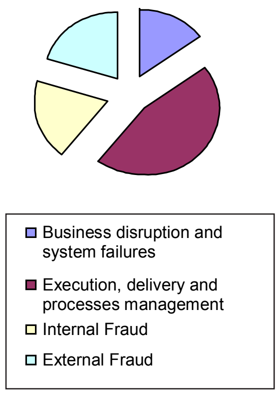
Analyzing Figure 1 we can conclude that the most risky business lines are those of commercial banking and retail, which is due in particular to the errors and transaction processing that may arise in the activities of the bank, explained by errors occurring when customers opened accounts such as the introduction of erroneous data in the system, incomplete documentation, lack of signatures, wrong classification of the client, etc.; errors in the vault, which include: un check client's signature, the issuing of documents for non-exchange rate, etc.; errors occurred when payment: unauthorized payment, late payments, incorrect choice of currency at the time of payment, the transmission delay of payment orders, the same transmission multiple orders, entering incorrect data into the system, the loss of check-ROMs, compensation instruments false debit, etc.; errors occurring in the exchange rate: failure rate regulation, wrong understanding of the sense of exchange, etc.; IT errors: erroneous transfer of data, system downtime, etc.; fraud occurred in lending: the acceptance of incomplete records, falsifying information, the use of identity false, etc.; errors in making the attachment, which can include: delays in the transmission of notices, lock, unlock unauthorized accounts, violation of regulations and rules, etc.; errors in managing complaints, such as retrieving or late reporting by departments authorized transmission of late responses etc. complaints.



Source: Own processing.

Figure 2. *The probability of occurrence of events causing loss*

The most frequent losses, as can be seen from Figure 2, were due to human error, being considered a risk related to human resources in the carrying out unauthorized activities because of negligence or intentional in the form of unreported transactions, unauthorized, unregistered operations, reporting dishonesty positions etc. The second place is occupied by losses due to business disruption and system; this is due to disruption of operations or system crashes and are unavailability risks resulting from hardware or software systems, data quality, problems with computer programs, failure of components, problems related to telecommunications, software, design, implementation and maintenance of the poor "electronic banking", etc. overuse utilities.



Source: Own processing.

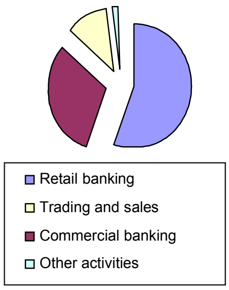
Figure 3. *Operational loss suffered by type of event for the credit institution*

In terms of severity events the conspicuous place is occupied by the events occurring due execution, delivery and processes management which re characterized by events such as erroneous communications, models or systems downtime, poor preservation of databases, errors in the introduction, operation, storage and update data breach terms of powers or lack of documents, losses, damages on the customers, outsourcing process, with controversy, etc., due to partial or total lack of legal documents; erroneous communications, models or systems downtime; loss or damage created due to customer negligence, breach of deadlines, reporting obligations or duties; input errors, operating, storing or updating data, negligence in maintaining databases, etc. failed deliveries.

Next we use an advanced model, the Internal Assessment Approach (IMA), to determine the requirement for operational risk related capital. Thus the first step is to achieve operational risk matrix, in which case the credit institution will be made up of 16 cells, corresponding to four business lines[3] and four events types[4].

Calculation of capital requirement under this approach will be achieved through the following steps:

a) for each business line have resulted in gross revenue, which we will summarize in Figure 4.

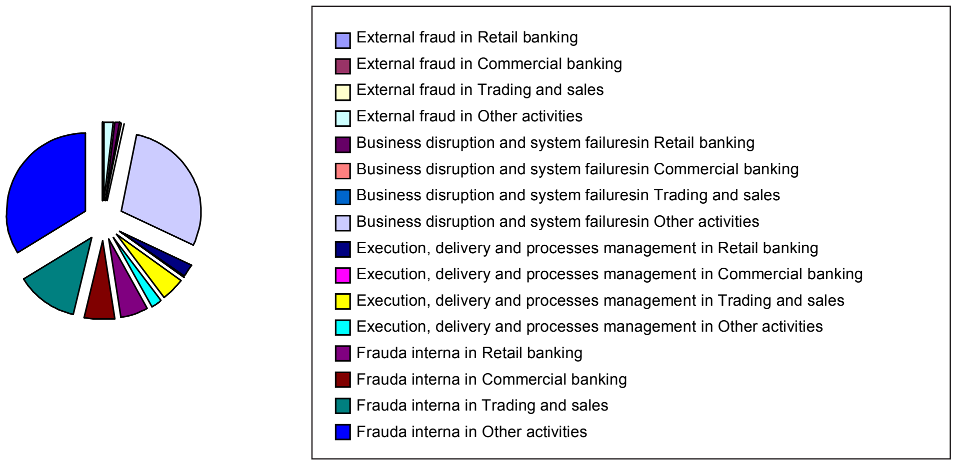


Source: Own processing.

Figure 4. *Average gross income on business line*

b) calculating parameters:

▪ Probability of occurrence of events causing loss (PE - Probability of Loss Event) which is used for internal historical data on the number of transactions concluded by operational losses and the total number of transactions completed on business line



Source: Own processing.

Figure 5. *Probability of occurrence of loss events for each cell of the matrix operational risk*

▪ The proportion of exposure that will record as operational loss (LGE - Loss of Given Event)

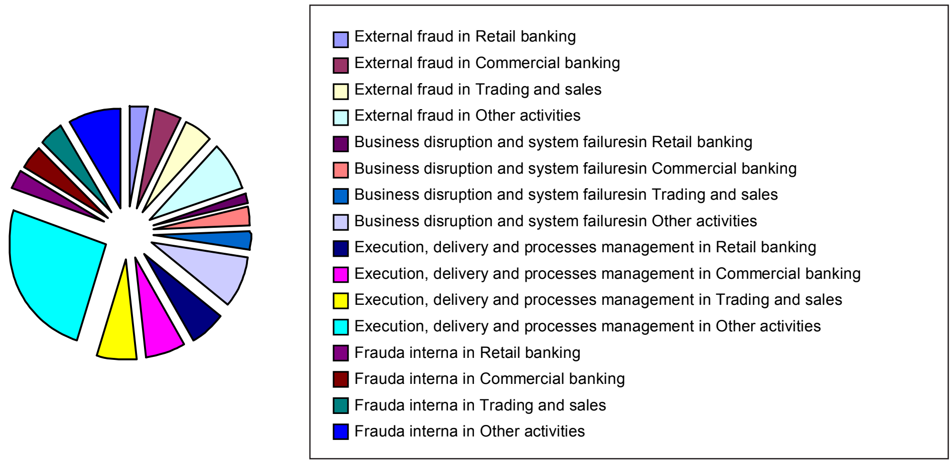


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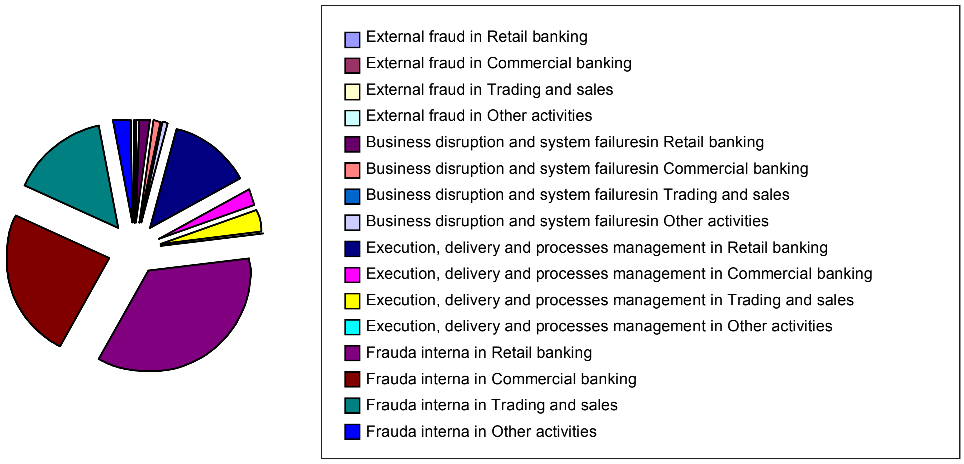
Figure 6. *Proportion of exposure that will record the loss for each operational cell*

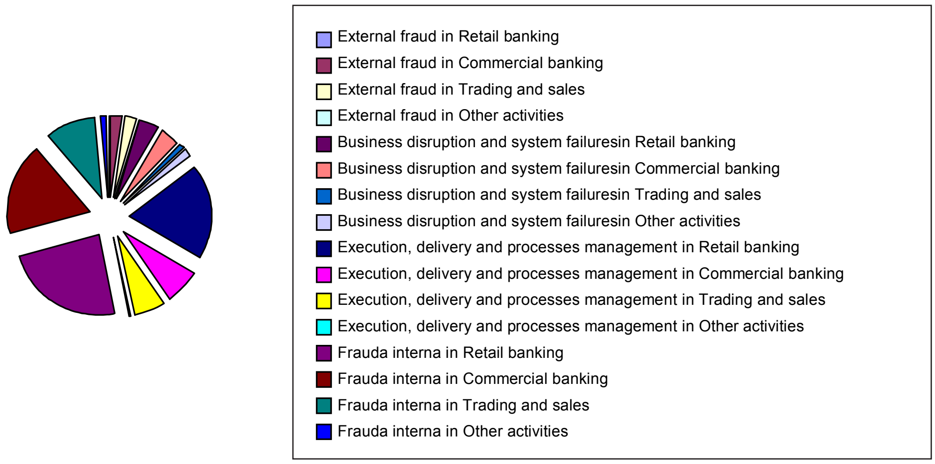
c) Determining the expected loss (EL - Expected Loss) as the product between the parameters determined previously and gross revenue.



Source: Own processing.

Figure 7. *Expected Loss for each cell of the matrix operational risk*

d) Determining the unexpected loss (UL - Unexpected Loss) as a product of the expected loss of the credit institution and the maximum amount of a loss for a period of one year and a confidence threshold of 99.9%. Thus the maximum amount of loss will be calculated for each cell of the matrix operational risk as a ratio between cell multiplier and square root of the number of transactions concluded with operational losses. The multiplier cell has to be estimated using normal distribution, distribution losses, and the corresponding value in the table for a confidence threshold of 99.9%.



Source: Own processing.

Figure 8. *Unexpected loss for each cell of the matrix operational risk*

Capital allocated by the credit institution shall be determined as the sum of expected loss and unexpected loss for each cell of the matrix operational risk, as shown in the following figure:

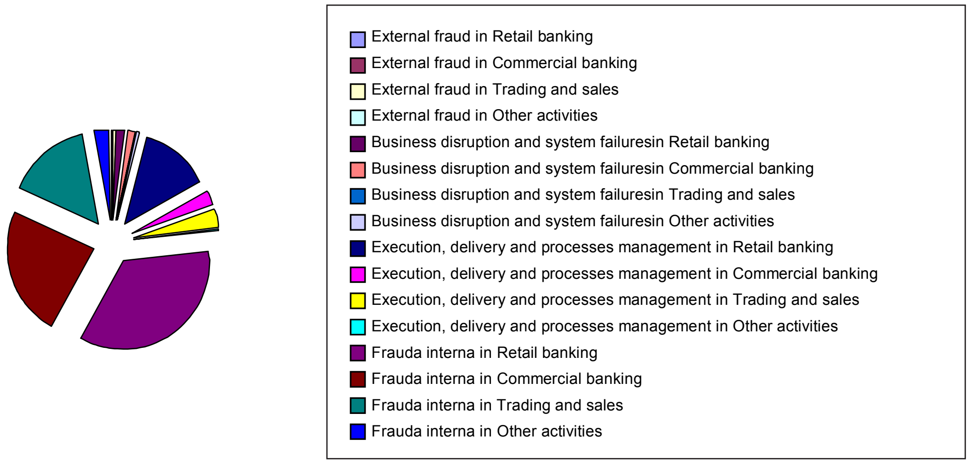


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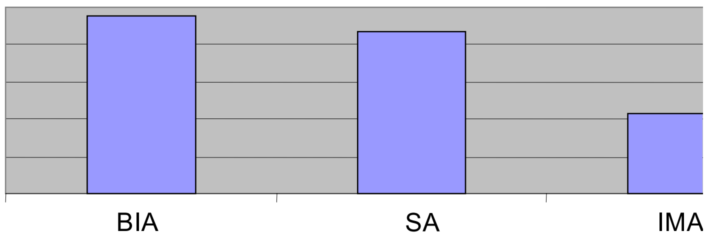
Figure 9. *Capital requirement under Internal Measurement Approach attached to each cell of the matrix operational risk*

e) Finally, to determine capital requirements under the Internal Measurement Approach for the entire institution of credit there will be summed the capital requirements related to each cell of the matrix of operational risk.

Thus, synthesizing the analysis of the

credit institution for consideration, we can see, and in Figure 10, that once the bank uses a method of measuring the more complex operational risk, capital requirement related to this risk is diminishing. Thus the minimum capital is mobilized using Internal Measurement Approach, as it can identify, measure and more effectively manage operational risks being able to discover in which line of activity is a higher operational risk and are the most important risk factors.



Source: Own processing.

Figure 10. *Capital requirement under the three approaches*

Notes

(1) The amount of the profit and loss account of the outcome of interest and similar income from shares and other securities with variable income, the result of commissions, the result of financial operations and other operating income.

(2) Retail banking: 12%; commercial banking 15%; trading and sales and other activities 18%.

(3) Same as for Standardized Approach: retail banking, commercial banking, trading and sales and other activities.

(4) External fraud, internal fraud, business disruption and system failures, execution, delivery and processes anagement.

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Guarantees in Banking Operations with Bank Customers

■

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Abstract. *In a crediting relationship, one of the parties involved – namely the creditor – is exposed to certain risks which impose taking measures to guarantee a debt. If, at the due date, the debtor cannot pay his/her debts and meet the assumed liabilities, the creditor can execute the legally constituted guarantees, on a contract basis, thus covering the debt.*

There are also situations when the state, being directly interested in promoting trade and cooperation with other economies or simply out of the wish to ensure a competitive and safer business environment, gets involved in insurance and guarantee operations. In such situations, the state does not intervene directly; it appeals to banks or to other specialized financial institutions.

Keywords: guarantees; real guarantees; personal guarantees; transfer of debt; risk.

■

JEL Code: J21.
REL Codes: 11C, 11F.

In a crediting relationship, one of the parties involved – namely the creditor – is exposed to certain risks which impose taking measures to guarantee a debt.

If, at the due date, the debtor cannot pay his/her debts and meet the assumed liabilities, the creditor can execute the legally constituted guarantees, on a contract basis, thus covering the debt.

According to their nature, bank guarantees fall into two categories:

a) Real guarantees;

b) Personal guarantees.

Real guarantees are legal means of guaranteeing obligations by affecting one of the debtor's assets so as to ensure the execution of the assumed liability. The asset constituted as guarantee is protected from the pursue of other creditors whose debts are not accompanied by any real or personal guarantees, or whose secured debts have a lower level of priority than the bank, in which case the asset is meant to cover the secured debt of the bank. Real guarantees confer the following rights to the secured creditor:

- The right of preference, on grounds of which, in case of forced execution, the value of the respective asset is to be used to fully satisfy the secured creditor first, and then the claims of other creditors;
- The right of pursue, on grounds of which the creditor is entitled to pursue the asset, irrespective of its owner, in order to cover the secured debt;

In their turn, real guarantees can be classified into two categories, as it follows:

- Personal estate guarantees (pledge) – which may or may not allow the creditor to dispossess the debtor of the asset constituted as guarantee;
- Real estate guarantees (mortgage).

Personal guarantees are legal means of guaranteeing obligations by engaging one or several persons in an accessory contract with the creditor, in order to cover the debt if the debtor himself/herself does not do it.

The personal guarantees regulated by the Romanian laws take to following forms:

- fidejussion (bond), settled by the article 1652 from the Civil Code;
- letters of guarantee issued by banks, financial institutions, insurance companies, administrative authorities (ministries), (inter)national companies which are competent in this field;
- personal guarantees regulated by special laws, which are based on the concept of fidejussion (for example: the guarantee constituted by a third party to cover the eventual damage that might be caused to an economic agent by an administrator, according to the Law no. 22/1969, with all the subsequent modifications).

The transfer of debts, although not falling into the category of real or personal guarantees, as it represents a specific means of transferring obligations, can be constituted to guarantee the credits given by the bank, as well as the afferent interests.

By its result, the transfer of debts ensures, as any other guarantee, the recovery of the bank debts, if it has been constituted under the strict observation of the rules and regulation in force.

As a cautionary measure, depending on each credit applicant's situation, the banks can ask their clients to constitute one or several guarantees (guarantee mix) of the following:

- unconditioned guarantees issued by the Romanian Government;
- bank guarantees;
- bank deposits (collateral cash);
- the contract of insurance in case of non-reimbursement of the credit and the afferent interests (financial risk insurance);
- transfer of debts;
- mortgage;
- the contract of personal estate guarantees (pledge);
- fidejussion (bond);
- corporate guarantees;
- business plans.

In case of clients experiencing difficulties in observing their payment obligations in due time, thus presenting a significant non-reimbursement risk, the bank can ask the borrowers to sign promissory notes which, according to the Law no. 58/1934 on bills of exchange and promissory notes, modified by the Law no. 83/1994, constitute enforceable titles even after being made enforceable and can be put into forced execution without prior formalities.

To be accepted by the bank, the guarantees must meet the following cumulative and mandatory requirements:

- the existence of a distribution market or of potentil buyers for the assets proposed as guarantees;
- the possibility of being rapidly turned into cash;
- the opportunity of being materialized into titles, authentic documents etc.;
- the assets are in a civil circuit, in the possession of the applicant or the guarantor and is not affected by other debts than the ones stemmimg from the creditor bank;
- the assets' owner is capable of bringing them back into guarantee;
- the assets that are bought and put into function prior to the credit application are in good functioning condition;
- the assets bought and still not put into function, as well as the assets which are to be bought and partially covered from credits are new and accompanied by quality and guarantee certificates.

The corporate guarantee is based on the firm engagement of the debtor, under the authentic or private signature, that he/she will circulate through the said bank the total/partial cash-flow resulted from its current activity; in fact, we are dealing with a transfer of debts which does not necessarily require legal procedures. The value accepted by the bank in the case of the corporate guarantee depends on the financial standing of the company, on the turnover circulated through the bank, on the company's reputation in the business environment and it can reach up to 75% of the cash-flow circulated through the bank by the respective company.

The business plan can constitute a guarantee for credits especially in the case of small and medium-size companies, which do not have other forms of guarantees at their disposal. The bank can accept as credit guarantee up to 50% of the cash-flow resulted from the business plan, provided that, according to the plan, the revenues are higher than the expenses.

The guarantee letters issued by other banks, as well as the payment default insurance contracts issued by the insurance-reinsurance companies approved by the creditor bank can be accepted as guarantees for bank credits.

The assets will be insured throughout the whole crediting period, with the risks specific to each category.

The borrower is bound through the credit contract to renew the insurance before the policy for the prior period expires.

The assets will be insured at their real market value, which must be at least equal to the value taken into account when calculating the credit guarantee (the value acknowleged in guarantee) and the damage recovery rights will be transferred to the bank.

The insurance policies will only be accepted within the limits of exposure reported by the insurance-reinsurance companies to the Risk Management Offices.

The credit officers will make sure that the insured value is at least equal to the value of the credit and its afferent interests.

In financial and trade operations with international ramifications, one of the most common guarantee instruments is the bank guarantee letter. It can be used, by defining and adapting its object, both for payments by documentary letters of credit, and for payments by payment bonds. The object of the guarantee is broadly represented by the effort to cover the buyer's obligation to pay the contract price, settled as countervalue for the received goods or services. From this point of view, the guarantee of payment can take the following forms:

1. *Tender Guarantees/Bid Bonds*, which are sollicited by the organizers of international bids as a condition of participation to it. If the Romanian exporter who has been awarded the bid refuses to sign in due time the contract written under the terms of the offer or fails to present the performance bond (if the tender book specifies it and the contract has been concluded), the bid organizer can claim the execution of the guarantee.

2. *Advance Payment Guarantees* are issued to account for the advance payment collected with export, national delivery, work performance or service contracts. This type of guarantee letter is issued when the foreign partners in a Romanian trade want to make the advance payments agreed in an export contract dependent on the full or partial secured advance recovery corresponding to the undelivered goods or the unexecuted works or services as specified in the contract.

3. *Performance Bonds* which mainly stand for a guarantee of the observance of contractual relations between partners in a transaction, from the point of:

- The full delivery of the contracted goods or the performance of works and services;
- The observance of delivery or execution terms for the contracted goods, works or services;
- The provision of quality goods, works and services;
- The setting-up and maintenance within agreed technical and functional

parameters, including during the period of technical guarantee for complex objectives.

4. Payment Guarantees, which have as object covering the customer's obligation to pay the contractual price, settled as a countervalue for the provided goods or services.

5. Maintenance Guarantees, which constitute a version of performance bonds. They often bear the same name, the difference being made only in the text of the guarantee; in this case, it covers the period of technical guarantee. If the commercial contract refers to merchandise deliveries for which the seller covers a period of technical guarantee (6 months, 1 year), this interval is usually covered by performance bonds.

6. Temporary Admission Guarantees, which contain the guarantor bank's pledge to pay for the countervalue of custom taxes and other budgetary debts afferent to the entry of goods, equipment, etc., in the importer's country, if after meeting the contractual obligations (completion of works), the account party does not return them to their country of origin and does not cover the above-mentioned payment obligations in favor of the customs duty unit.

7. Retention Money Guarrantees, which are meant to cover the exporter's contractual obligations (the account party of the bank guarantee) afferent to the period of technical guarantee.

8. Guarantee Limits, within which the bank can issue several types of guarantee letters.

There are also situations when the state, while directly interested in promoting trade and cooperation relations with other economies or simply out of the pure desire to ensure a competitive and more stable business environment, gets involved in insurance and guarantee operations. In such cases, the state does not act directly; it appeals to banks or specialized institutions. In Romania, EXIMBANK provides the following products to Romanian exporters on behalf of the state:

1. The EXIMBANK foreign payment default insurance policy – MARKET RISKS:

Until the end of 2004, EXIMBANK was involved in foreign payment default insurance operations on its own behalf, with COFACE reinsurance. In order to comply with the legal provisions coming from the European Union in this field, according to the *Law no. 440/2004 regarding the modification of the Law no. 96/2000 on the organization and functioning of the Romanian Import-Export Bank and the specific instruments to sustain the international trade*, EXIMBANK is now developping this activity on behalf of the state, while maintaining the reinsurance on the international private market (with COFACE).

This insurance policy covers the debts resulting from export contracts concerning general merchandise, consumer goods and short-term credit service performance, in order to prevent the following categories of market risks included in the definition of market risks which are covered as a result of market mechanisms.

▪ *Political risks*, before and after delivery, connected to commercial risks (risk of war, of civil war, of revolution or rebellion, any general moratory declared by the authorities of the buyer's country or of another country, any measure or decision taken by the authorities of the seller's country, the secured person's country or of another country, any political event or economic depression, legal or administrative measures that prevent or delay the transfer of the amounts paid by the buyer or by his/her guarantor, any other similar action or event);

▪ *Commercial risks*, before and after delivery, caused by the insolvancy of the private buyers or their extended payment default (buyer insolvancy, buyer's extended payment default);

▪ *Payment default* of debts belonging to governmental buyers before and after delivery.

2. The EXIMBANK foreign payment default insurance policy – NON-MARKET RISKS (risks which are not reinsured, other than thise included in the definition of market risks, which are not covered as a result of market mechanisms):

This insurance policy covers the debts resulted from the export contracts regarding general merchandise, consumer goods and short-term credit service performance, against the following categories of non-market risks:

▪ *Political risks*, before and after delivery, connected to commercial risks (risk of war, of civil war, of revolution or rebellion, any general moratory declared by the authorities of the buyer's country or of another country, any measure or decision taken by the authorities of the seller's country, the secured person's country or of another country, any political event or economic depression, legal or administrative measures that prevent or delay the transfer of the amounts paid by the buyer or by his/her guarantor, any other similar action or event);

▪ *Commercial risks*, before and after delivery, caused by the insolvancy of the private buyers or their extended payment default (buyer insolvancy, buyer's extended payment default);

▪ *Payment default* of debts belonging to governmental buyers before and after delivery;

▪ *Force majeure risks:* natural disasters or other similar events, with the exception of those occuring on Romanian territory, which hinder the execution of the export contract.

3. The EXIMBANK medium and long-term insurance policy for export contracts (The insurance policy for construction-assembly works and other export works/ services and the insurance policy for export capital assets). These insurance policies cover export contracts which have in view complex export operations and/or delivery of products with extended fabrication cycle or other export works/services, against the following categoris of risks:

▪ *Political risks*, before and after delivery, connected to commercial risks (risk of war, of civil war, of revolution or rebellion, any general moratory declared by the authorities of the buyer's country or of another country, any measure or decision taken by the authorities of the seller's country, the secured person's country or of another country, any political event or economic depression, legal or administrative measures that prevent or delay the transfer of the amounts paid by the buyer or by his/her guarantor, any other similar action or event);

▪ *Commercial risks*, before and after delivery, caused by the insolvancy of the private buyers or their extended payment default (buyer insolvancy, buyer's extended payment default);

▪ *Force majeure risks:* natural disasters or other similar events, with the exception of those occuring on Romanian territory, which hinder the execution of the export contract;

▪ *Pre-delivery risks:* the risk of unjustified interruption of contract by the buyer and the risk of unjustify refusal of the buyer to take over the contracted goods.

4. *The buyer credit insurance policy:*

This insurance policy covers either a Credit Convention concluded for the buyer credit, granted by the exporter's bank (the Romanian commercial bank) on a medium and long term directly to the importer or to his/her bank, either a buyer credit granted by a Romanian bank and based on an individual export contract or several export contracts. This insurance policy offers coverage for the following categories of risks:

▪ *Political risks*, before and after delivery, connected to commercial risks (risk of war, of civil war, of revolution or rebellion, any general moratory declared by the authorities of the buyer's country or of another country, any measure or decision taken by the authorities of the seller's country, the secured person's country or of another country, any political event or economic depression, legal or administrative measures that prevent or delay the transfer of the amounts paid by the buyer or by his/her guarantor, any other similar action or event);

▪ *Commercial risks*, before and after delivery, caused by the insolvancy of the private buyers or their extended payment default (buyer insolvancy, buyer's extended payment default);

▪ *Force majeure risks:* natural disasters or other similar events, with the exception of those occuring on Romanian territory, which hinder the execution of the export contract.

5. *The insurance policy for Romanian capital investment* has as object the Investment Project/Investment Agreement concluded between the Beneficiary (the Romanian investor) and the Host Country Government (the country where the investment is made) and afferent to the Project Investment to be implemented subsequently. This insurance policy covers the following categories of political risks:

▪ *Transfer risks* (the Host Country Government's actions to prevent the Beneficiary from exchanging Host Country currency into insurance currency or from sending abroad amount representing dividends, profits or other financial benefits resulted from the secured investment);

▪ *Compulsory purchase risks* (the Host Country Government's actions to prevent the Beneficiary from exerting his/her property or control rights over the secured investment, including the right to use the constituted funds or the revenues resulting from the investment);

- *Risks of war and civil rebellion* (the risk of total or partial destruction of the secured investment's physical assets, including the Beneficiary's inability to execute vital operations for the financial performance of the investment, as a result of the above-mentioned events);
- *The risk of breaking/ending the Investment Agreement by the Host Country Government* (the risk that the Host Country Government breaks the contract obligations, provided that the project implementing is carried out to the benefit of the above-mentioned Government, within the framework of an Investment Agreement).

This type of insurance enjoys the option of reinsurance from the Multilateral Investment Guarantee Agency (MIGA), based on the agreement concluded between EXIMBANK and this World Bank institution. The reinsurance is granted by MIGA for each policy signed by EXIMBANK to the benefit of the state, depending on the terms and conditions of execution of the respective investment project.

6. The export production credit insurance policy has as object of insurance a short or medium-term credit contract, concluded between the export-financing bank and the Romanian exporter and meant to secure the good and service range of offers abroad, as well as to finance the work capital. By means of this insurance policy, the financing banks are protected against risks of credit and interest payment default, as a result of the failure to execute or the poor execution of the export contract's obligations – exporter risks.

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Mergers & Acquisitions – a Simulation Model Used in the Negotiation Process

■

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Abstract. *Today, more than ever, an essential element of any corporate growth strategy is growth through mergers and acquisitions. A survey conducted by PricewaterhouseCoopers reveals the fact that mergers and acquisitions are seen not only as instruments to avoid the global economic crisis, but also as an opportunity for firms to either buy their way into new technologies and expand, or to merge and bulk up. Not since the beginning of the 20th century has the economy seen such a massive restructuring. Whole industries are consolidating at a rate and a scale that is off the chart of historical experience.*

In this article we will discuss the MAC, MAE and information disclosure clauses, used in designing an M&A contract agreement. They can represent very important tools in a negotiation and the most beautiful part is that they are equally valuable to the buyer as well as to seller. An interesting analysis could be to look deeper into a cooperative surplus if both the seller ant the buyer will be fully aware of these tools and will use them in a cooperative game strategy, but in this paper we will limit our analysis to investigating them and simulating broad acquisition scenario in which these tools can be used by the buyer to reduce the risks associated with the transaction.

In the next section we will analyze each clause as a separate tool to be used in negotiating a successful acquisition and then we will put them to work. For this, we will construct a reality based scenario for a real life acquisition, which took place in United States, to test the utility of these tools. The case we will analyze ended up in court and created losses for both the buyer and the seller. The purpose of our simulation is to create the incentives for a different outcome, this time a productive efficient one.

We believe that these tools have the great advantage of allocating the endogenous risk to the seller leaving the buyer only with the exogenous risk.

Keywords: M&As; MAC; MAE; information disclosure; scenario simulation.

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JEL Codes: L14, M21, G34.
REL Codes: 11G, 14C, 14K.

1. MAC and MAE clauses

What is a MAC clause? Material Adverse Change (MAC) clauses are most commonly used in acquisitions and project financing transactions. MAC clauses are a common means of allocating the risks presented by adverse business or economic developments occurring between the signing and the closing of an acquisition agreement.

A MAC clause aims to give the buyer the right to terminate the agreement before completion, or to provide a basis for renegotiating the transaction, if events occur that are seriously detrimental to the target assets/company (Gilson, Shwartz, 2005).

Why using a MAC clause? Two hypotheses could account for both the traditional role of MACs and for changes in MAC practice. First, a MAC clause can be used as an offsetting position under the so called *symmetry theory*. The law restricted the ability of parties to make a friendly deal to prevent the target from considering competing bids by agreeing in the acquisition agreement to "no shop" or "no talk" clauses. The result of these economic and legal innovations was to enable the seller always to accept a higher competing bid or to compel a renegotiation of the price; acquisitions require target shareholder approval, whether explicitly by vote or implicitly by tender, and the target shareholders would refuse consent to an initial offer in the face of another buyer's higher bid. If the seller's value at closing time, either to the buyer or to another acquirer, is above the bid price, the seller would either renegotiate the bid price or exit to accept a better offer. If the seller's ex post value were below the bid price, the seller in a contract without a MAC would make the original deal. The buyer thus would bear the full cost of low realizations, but receive only part of the gain (or no gain) from high realizations.

A seller functioning in this economic and legal environment has an incentive to offer a MAC to potential buyers. A broadly drafted MAC would increase a buyer's expected gain from an acquisition, and this would increase the likelihood that the seller would receive bids. Just as the seller would exit if its value turned out to be above the bid price, the buyer now would exit if the seller's value turned out to be below. Transaction costs would keep the seller in the deal if its value turned out to be slightly high and would keep the buyer in the deal if value turned out to be slightly low.

Thus the symmetry theory considers MAC as an offsetting position taken by the buyer. To explain this in financial terms, the MAC clause creates a call option for the buyer that is symmetric to the put option the law gave to the seller by shifting to the target the risk of exogenously caused reductions in the value of the new corporate combination.

The second hypothesis is the *investment theory* (Goetzmann, 1998), which rests upon the ability of a seller, in the post-execution/pre-closing period, to make relation-specific investments that will affect the value of the combined company. These investments fall into three categories. The first category consists in early efforts to facilitate integration, because the acquisition is motivated by the potential for post-closing synergy. As examples of investment, the target company may begin the process of integrating its product line with that of the acquirer by suspending or canceling the development or improvement of products; may freeze investments in capabilities that the acquirer already possesses; may shift its research and development to fit the anticipated post-closing strategic plan; and may discuss with its customers the buyer's capabilities in markets where the buyer has been a competitor. The second investment category comprises efforts by the target company to retain the cohesiveness of its workforce. The announcement of a friendly transaction could lead employees to suspect layoffs or unwanted changes in the work environment. These expectations could cause more mobile, and likely more valuable, employees to become less focused on the target and more focused on their own futures, with the potential of an adverse selection cascade. The third investment category focuses on seller's efforts to preserve the expected profitability of the new enterprise. A target firm's customers and suppliers may reconsider their relations with the target in anticipation of the post-closing situation.

In the absence of the MAC clause, the seller would not make these investments as they have a potential to reduce its stand-alone value if the deal fails to close. The MAC solves these problems in a simple, but nice way. The traditional MAC permits a buyer to exit when a material adverse change or effect would make the deal unprofitable for it. The buyer's exit right encourages the seller to take actions that would protect and possibly enhance the value the new company is expected to have. The set of MAC exceptions, in contrast, encourages the buyer to take actions that would protect the new company against the materialization of risks that neither party could prevent, but that the buyer could best affect. The MAC term thus allocates transaction risks to the party that can most efficiently bear them.

2. Information disclosure clause

The information disclosure clause deals with disclosure of facts and information which the seller knows or should know they are of particular importance to the buyer. In this case, the buyer could walk away from the deal on the ground of deceit. That is, of course, if such a clause of duties of disclosure exists in the agreement contract. This clause of disclosure of information looks very similar with MAC and MAE clauses in a way that both have the same legal effect by allowing the buyer to avoid the contract and also because holding information can produce the same adverse effect on the resulting value of a merger or acquisition.

Another important resemblance concerns the impotence of law in presenting feasible formulas with operational power for courts in dealing with litigations concerning these clauses. Once again the economic analysis could provide more precise criteria and maybe a general principle to be applied by courts when judging these situations. This general principle can also be of great value to lawyers when designing agreement contracts and could even have a strategic importance for managers as information disclosure could give the buyer an important competitive advantage if the deal fails.

Duty of disclosure has two crucial questions to be answered. The first one is: *when there is a pre-contractual duty to disclose information, in other words, when does such a duty exist?* The first problem with this question is that there are significant differences among different European countries with respect to a legal answer to this question. Even the UNIDROIT Principles of International Commercial Contracts(1) is not very helpful in providing a reliable formulation of this clause. It states that a party may avoid the contract in the event of "non-disclosure of circumstances which, according to reasonable commercial standards of fair dealing, the other party should have disclosed." Here, economic analysis comes in and starts with two underlying assumptions: first is the allocative efficiency which states that the buyer offers to buy the target company because he values it more than he values the money and is the other way around with the seller. This is also Pareto efficient since both parties are richer after closing the deal and neither poorer. The second assumption is that informational symmetry should exist between the seller and the buyer so that the buyer would know what he is buying. Accordingly, the duty of disclosure can only apply to facts which are "material" to the other party's decision, and this is what the courts actually hold. What is "material" depends on all the circumstances of the case.

This leads us to the second crucial question: *What are the conditions that must be satisfied in order to permit a party to withhold information he knows to be relevant to the other party?* A first situation is when the contract has a duty of disclosure. In this case there can be no such right to withhold information if a party owes a duty of disclosure. If no disclosure clause exists then the seller should be allowed to withhold information if the information is *productive* and it is *costly to acquire*. The information is "productive" if it advances social welfare, that is, conduces to a better use of the scarce resources of the world. Unless these two conditions are together satisfied, disclosure must be made.

3. Merger simulation model

The scenario

The acquisition analyzed in our scenario is Riggs bank, a Washington D.C.-based bank, purchased by PNC, a Pittsburgh-based bank, for $24.25 per share – about $779 million overall. The deal was supposed to bring the largest Pennsylvanian bank into the underdeveloped branch-banking network of Washington D.C. Riggs saw it as a way of surviving its troubles. In our scenario we will play the role of PNC bank and we will incorporate the tools discussed above in the negotiation process. We will prove that using these tools we can transform a failure, which was the case here, in a success and, thus, instead of wasting money and time in court (this without mentioning the damages done to the reputation of the company) a company can negotiate an agreement that will bring future added value and will maximize the return of its investment (productive efficiency).

What happened in reality?

PNC negotiated a MAC clause to back out of the deal without penalty should a "material adverse change" occur in Riggs' regulatory or financial position. Riggs was accused and proved guilty of money laundering for people like Augusto Pinochet, Teodoro Obiang-Nguema, the dictator of the West African nation of Equatorial Guinea, or two of the hijackers of the 9/11 attacks. Riggs had to pay large amounts of money in fines and faced other lawsuits by the survivors of the attacks and its shareholders.

Believing that it could walk away from the original deal, based on the aforementioned events, PNC offered to purchase Riggs at a reduced price of $19.32 per share, which would remain subject to further reduction if circumstances changed, plus a "contingent security" of as much as $0.83 per share. The new deal offer also requested Riggs to settle at least one lawsuit filed against it and to settle or set aside reserves for several other outstanding lawsuits. Riggs board considered the offer to be unacceptable and filed a lawsuit against PNC for breaching the contract without a serious reason. After three days Riggs and PNC reached an agreement and PNC agreed to pay 20$ per share and Riggs dropped the lawsuit. The final agreement was settled for 652 million USD. Since in this scenario we will consider only PNC we will not make any comments on the difference between the initial 779 million offer and the final sum. Instead, we would say that this negotiation was costly for PNC and that it was accompanied by serious reputation damages as they were not very happy about too much publicity of them acquiring a bank accused of corruption, money laundering and support of the terrorism. Also, as a part of the final agreement, PNC agreed to pay some of the damages Riggs had to pay to its shareholders. It is also obvious that the transaction costs were much higher than initially expected due to a substantial increase in the negotiation costs.

Could things have been done differently?

Let us imagine that, instead of drafting a standard acquisition agreement, PNC would have used the tools presented above. How? First, a simulation model could have been designed to estimate the future profits following the acquisition. This model should have been a Nash-Bertrand-Stackelberg model due to the fact that PNC had the leader position in this cooperative game and Riggs was the follower. Furthermore, PNC knew ex ante that Riggs would follow its actions. The general model used in merger simulations is a Nash-Bertrand model, where firms choose prices non-cooperatively. Thus, this model is not suitable for an acquisition because acquisition is a cooperative game. The Stackelberg component will allow us to incorporate into the model additional assumptions about the firm behavior such as the quantity setting, or the leader and follower game strategy. Such a model will reduce the prediction errors of the Nash-Bertrand model used by Craig Peters (2006) and would give us estimated profits very closed to the post-acquisition real profits.

Secondly, the information disclosure clause tool, which, inserted in the agreement contract, will give Riggs incentives to disclose information about all its trials and its future intentions to plead guilty. Pleading guilty means paying damages and these damages should be taken into account when considering post-acquisition cost of operating. Of course, this information is of obvious importance for refining the model. Since this information is not "productive" and it is costless to obtain it can be very easily disclosed even when they are not the object of the information disclosure clause.

Thirdly, the last tool, MAC and MAE clauses, are of tremendous importance for completing the model and for obtaining the most accurate results from the simulation. We will not use the traditional MAC and MAE clauses which have become almost a standard in designing an agreement contract, but instead we operate some significant changes when inserting them. The first change we intend to operate is to force Riggs to make synergy investments prior to closing the acquisition. These investments are extremely necessary if we take into consideration the fact that Riggs will have to close its international operations which were subject to public opprobrium since the discovering of money laundering operations for ruthless dictators. Another purpose of these synergy investments could be for Riggs to carefully analyze and to integrate its products with PNC's ones. The reason behind this lies in the fact that Riggs was known as the bank of the diplomats and its products were mostly designed to meet specific needs of very specific customers, foreign officials most of them. PNC, on the other hand, is a bank of the working people, with products designed to meet the needs of the working people in Pittsburg. These investments are meant to facilitate products integration. Then, there is a category of investment meant to retain the cohesiveness of the workforce, primarily very valuable employees like the ones from the treasury department, highly skillful risk managers and analysts who are more likely to feel their positions threatened. Third category of synergy investments focuses on preserving the expected profitability of the new enterprise. Behind the obvious importance of this clause there is another very important role in our scenario. This clause is important for simulation purposes as this clause is a warranty of the accuracy of the model since the model relies upon some assumptions connected to the production capacity, production costs and evolution of the prices.

4. Conclusion

To summarize, we have seen that a standard agreement contract is inefficient as it does not offer sufficient protection neither for the buyer and the seller because using the traditional clauses to exit the contract could be very difficult and very costly. Instead, by using the tools presented in this article and by refining them, the buyer could draft a contract that would almost guarantee him the value added he expects from closing the deal. We have used a simple scenario of a real acquisition of a bank, but the model works regardless of the industry or the company being purchased. The only condition for its success is preserving the validity of the initial assumption and this can be done by inserting specific clauses into the contract. If the seller chooses to comply with those clauses then the model is a very accurate simulation tool for estimating the post-acquisition revenues and profits and, hence, for obtaining the added value expected prior to closing the deal. Worse case scenario, if the seller fails to comply to these clauses, then the buyer can costly exit the contract and can easily avoid being sued for damages by the seller or this could serve as a base for diminishing the negotiated acquisition price.

We know that transaction costs are search costs, negotiation costs and enforcement costs. The value of these tools is that they reduce the negotiation costs and they make enforcement costs ridiculously low. And if you are the of an American company we are sure you can appreciate this, as the legal fees in USA are huge even for a company this size.

Ultimately, the entire negotiation process is about risk distribution and by all means we are talking about huge risks. We believe that these tools have the great advantage of allocating the endogenous risk to the seller leaving the buyer only with the exogenous risk. Of course, that too can be reduced by negotiating additional clauses but they are not the object of our paper.

Note

(1) See http://www.unidroit.org/english/principles/contracts/main.htm.

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Aspects Regarding the Development and the Integration of the Corporate Social Responsibility Concept in Firms' Behaviour. Particularities for Small and Medium-sized Enterprises

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Abstract. *Starting from the concept of Corporate Social Responsibility (CSR), the purpose of this article is to highlight some of the particularities, at Small and Medium-sized Enterprises (SMEs) level, regarding: socially responsible behaviour and participation in actions related to CSR; type of CSR strategies adopted by SMEs as compared to larger firms; the motivations, benefits and constraints of the social involvement. The ultimate question refers to the existence, nature and implications of a link between the firm size and the aspects mentioned above. These aspects will be presented according to the conclusions of the previous studies conducted in this area of research, the present paper representing therefore a theoretical synthesis of the existant literature.*

Keywords: corporate social responsibility; socially responsible behaviour; CSR initiatives; firm size; small and medium-sized enterprises.

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JEL Code: M14.
REL Code: 14D.

1. Developments of the concept of corporate social responsibility

The enterprise concept is one of the key concepts of the capitalism, which, according to Schumpeter, represents, essentially, a process of change, of economic progress and the key that starts the engine and makes it work is innovation (McCraw, 2006). In his opinion, the forces that drive and sustain innovation are the entrepreneur, the new enterprise and the entrepreneurial profit (McCraw, 2006). It becomes obvious, therefore, the relationship between enterprise and profit, the maximization of the last one representing, according to the classic view of the enterprise, its main goal, statement so well-known that it needs no references.

In the last decade yet, there has been much talking about the social valences of the enterprise, about its involvement in managing some social problems, involvement that often goes beyond complying with regulations. To designate this social behaviour of the enterprises and their involvement in the social sphere there have been introduced into the common language, terms as: *corporate responsibility, corporate citizenship, social enterprise, responsible enterprise, sustainable development, corporate social performance, triple-bottom line, corporate ethics* and, in some cases, *corporate governance,* all of them pointing to the increase of the role that enterprises are expected to play within society (Castka et al., 2004, Besser, 1999, The CSR Initiative). But further Moir (2001) asks the following legitimate questions: „for what, to whom and who asks firms to be responsible?" Regarding the second question, it is stated that, out of the classic view, an enterprise, an organization, in general, should be responsible to all whom its activity has an impact upon, they being designed by the term *stakeholders,* term that became known by the work of E. Freeman[(1)], and including, alongside shareholders, employees, customers, suppliers, local communities, policy makers and society as a whole (The CSR Initiative, Wikipedia).

The term of corporate social responsibility came into the common usage at the beginning of 1970, leading, during the years 1980 and 1990, to an increasing interest for business ethics, both in academic and business environment (Wikipedia).

At international level, companies and not-for-profit organizations, alongside of governmental organizations have advanced definitions of the CSR concept that reflect their own approach regarding the socially responsible behaviour. According to an exhaustive approach of CSR, it is necessary to understand that all of the enterprise' activities determine effects both within and outside the enterprise, effects that have a triple impact upon the society, namely at social, economic and environmental level[(2)]. *The Corporate Social Initiative,* a multi-disciplinary and multi-stakeholder programme, defines CSR from a strategic perspective, stating that it has to do not only with the way firms utilize their profits, but also the way they obtain those profits (The CSR Initiative). In WBCSD' vision, CSR represents the ongoing commitment of the company to behave in an ethic manner and to contribute to the improving of the economic development, by improving the quality of life for employees and their families as well as of the local communities and society as a whole (WBCSD, 1998). Given the high visibility and the great impact of the provisions and recommendations of the European Commission, it cannot be ignored its vision regarding CSR. Thus, the European Commission views CSR as "a concept by which companies integrate social and environmental concerns into their businesses and interaction with their stakeholders, on a voluntary basis" (European Commission).

A definition concise but consistent which, together with that of the other organizations and programmes mentioned above (WBCSD, The CSR Initiative), reflects the preoccupation of the enterprises to integrate social, economic and environmental aspects alike in their activity and to behave responsible in all these three domains. The CSR has been analysed and explained by the intermediate of different theories (Udayansankar, 2008, Moir, 2001), namely: the firm' stakeholders theory (Udayasankar, 2008, Freeman, 2004, Moir, 2001); the social contracts theory (Moir, 2001) and the legitimacy theory (Udayansankar, 2008, Moir, 2001). Among these, the stakeholder's theory constitutes a key framework for the understanding of the way in which SMEs perceive the CSR (Jenkins, 2006). We will refer to this category of enterprises in the fallowing sections of this paper.

2. Aspects regarding SMEs in the European Union

Within the corporate sector, a segment of particular importance, economically and socially, is that of small and medium-sized enterprises (SMEs). At the EU level, in 2005 (Romania and Bulgaria included), from about 20 millions of active enterprises, the great majority is represented by SMEs, with a weight of 99.8% from total. Although less, their contribution in terms of wealth creation and employment remain important, SMEs offering jobs for 67.1% from the total workforce employed within the non-financial sector and contributing with 57.6% to the generation of the value-added within the same sector (Schmiemann, 2008). In spite of the relevance of these statistic arguments, SMEs face difficulties that the EU and national laws try to correct by providing different advantages to SMEs. In this sense, and in order to avoid distortions in the Single Market, it has been adopted at the EU level a common definition for SMEs (European Commission, 2003). According to this, the category of SMEs include enterprises that employ less than 250 persons and that have an annual turnover which does not exceeds EUR 50 millions and/or an annual balance sheet total that does not exceeds EUR 43 millions. Within the SMEs category, a small enterprise is defined as an enterprise that employs less than 50 persons and that have an annual turnover and/or an annual balance sheet total that does not exceeds EUR 10 millions, and the micro-enterprise is an enterprise that employs less than 10 persons and that have an annual turnover and/or an annual balance sheet total that does not exceeds EUR 2 millions.

3. Involvement of SMEs in CSR field

The research regarding the CSR has received a particular attention in the last decade (Ortiz Avram, Kühne, 2008, Jenkins, 2006, Luetkenhorst, 2004), certain researchers arguing that it has focused and gain its legitimacy on the larger firms case, the undertaking of the CSR being considered as their prerogative, the smaller firms, micro-enterprises included, receiving less attention (Ortiz Avram, Kühne, 2008, Perrini et al., 2007, Castka et al., 2004). But, due to the importance of SMEs, according to the arguments presented earlier, there is a need for further in-depth research regarding the relationship between SMEs and CSR (Russo, Tencati, 2009), the organizational culture, difficulties and perceptions of CSR within SMEs (Murillo, Lozano, 2006), as well as the active and sustained commitment of SMEs in order to implement an CSR agenda (Castka et al., 2004, Jenkins, 2006). The increasing importance of the SMEs sector has lead to the highlighting of their social and environmental impact, as illustrated by the increase of the number of initiatives designed to engage SMEs on CSR agenda (Jenkins, 2006). According to Murillo and Lozano (2006), in the last few years, the public attention and the governmental actions in order to promote the CSR have been pointed particularly toward SMEs, but these lack a deep understanding of what means the CSR language and practices, although Van Auken and Ireland (1982) have been stated, more than a decade ago, that social responsibility applies also to small enterprises but not to the same extent as in case of those considered large.

In the rest of the paper it will be presented some aspects regarding the undertaking of CSR initiatives by enterprises, with a special focus on SMEs.

Entrepreneurship – premise of a socially responsible behaviour

One of the first questions that need to be asked is if entrepreneurship can constitute a premise for undertaking a socially responsible behaviour. The European Commission defines the entrepreneurship as representing "the attitude and the process by which take place the creation and the development of the economic activity by combining risk, creativity and/or innovation, within a new or existing organization" and it has to do with people, their choices and actions regarding the initiation and the managing of a business or with their involvement in the strategic decisions of a firm. Although entrepreneurs are an heterogeneous group, the entrepreneurial behaviour could be characterized by common traits, such as: willingness to undertake risks, taste for independence and self-achievement (Green Paper, 2003). Entrepreneurship is not only a way to stimulate job creation, competitiveness and economic growth but also a possibility for self-development and for dealing with some social issues. As a proof, it is now heard about *social entrepreneurship*, *social enterprise* and *social entrepreneur*, the last one term designing a person who recognises a social issue and uses the entrepreneurial principles in order to organize, create and manage an enterprise to produce social change (Baron, 2005, Wikipedia). Given the fact that, at the SMEs level, lack of awareness and expertise necessary constitute, usually, the principal obstacles for building a business strategy (Perez-Sanchez et al., 2003), recognising the existence of a social problem precedes and conditions the involvement of SMEs in social responsibility initiatives (Lepoutre, Heene, 2006). Although some researchers believe that small firms are more adequate for socially responsible behaviour than large firms, and that they have a so-called "natural propensity" to socially responsible behaviour and that the entrepreneur, as owner-manager of a small firm, is associated with character traits that increase the likelihood of undertaking a socially responsible behaviour, Lepoutre and Heene (2006) state that entrepreneurship in itself does not constitute a guaranty in this sense.

Relationship firm size – corporate social responsibility

Research regarding the existence and the consequences of a relationship between firm size and its participation in the social responsibility sphere has determined lively debates in the last years, one of them contradictory (Russo, Tencati, 2009, Udayansakar, 2008, Perrini et al., 2007, Lepoutre, Heene, 2006). These opposite opinions regarding relationship firms size – CSR is not a classic one, dichotomous, that argue, for example, that the degree of involvement of a firm increases proportionately with its size (direct link). The consequence of this conclusion would be that CSR constitute the exclusive appanage of big firms, as it has been often stated in the literature, due to public visibility, economic power and their links with various interest groups (Ortiz Avram, Kühne, 2008, Perrini et al., 2007, Castka et al., 2004, Van Auken, Ireland, 1982), while the society expects that small firms to undertake limited roles on the social stage, given their low economic power and limited managerial means (Van Auken, Ireland, 1982). Actually, it has been proven that small firms are prepared for responsible behaviour and for undertaking social roles, but that the relationship between firms size and CSR depends upon a number of conditions (Udayasankar, 2008, Perrini et al., 2007, Lepoutre, Heene, 2006), that we will refer to in the following.

Firm visibility, resource access and scale of operations are the attributes that served as a basis for investigating firm size – CSR relationship (Udayasankar, 2008). These attributes are called level attributes, because it is expected that a firm of large dimension to operate on a large scale, to have a high access to resources and, obviously, to beneficiate from a high visibility. At the opposite, according to the general perception, small firms have a low scale of operations, they often face constraints that limit their access to resources (financial, first of all, but also human and material) and they have a low visibility in the public environment. Udayasankar (2008) starts from a set of hypotheses according to which, contrary to the general perception explained above, those three factors can be, each of them, both positively and negatively associated with firm participation in the CSR sphere. The conclusion drawn by Udayasankar is interesting and innovative alike: in terms of visibility, resource access and scale of operations, very small firms and very large firms are equally motivated to involve in CSR initiatives, although their motivations can be different; firms of medium size are least motivated to undertake a socially responsible behaviour. The innovative feature of this conclusion derives from the fact that the author, Udayasankar (2008), proposes also a form for the function that illustrates the relationship between firm size and its social involvement, the function being U-shaped. Eventually, concludes the author, not firm size in itself is important, but those three features of the firm that derive from this (visibility, resource access and scale of operations) and the various configurations found within enterprises, these differences being the ones able to explain the variation in the level of firms participation in CSR (Udayasankar, 2008). A given configuration can offer the stimulus for a firm to engage in CSR or, on the contrary, can justify the lack of stimulus and the non-participation of the firms in this sense.

Firms size and the CSR strategies

If it has been proved that big firms and small firms can be equally motivated to involve in CSR programmes, the next question refer to the existence of any difference between them regarding their manner of involvement and the strategies they use for this purpose. Do small enterprises use the same strategies as the large ones? If the size in itself does not matter, regarding the degree of involvement, does this make any difference in the way of involvement and strategies chosen?

By CSR strategies researchers understand those tools and activities implemented by SMEs and large firms to promote the socially responsible behaviour to internal and external stakeholders (Russo, Tencati, 2009, Perrini et al., 2007). In order to identify the CSR strategies used by firms it has usually used a multi-stakeholder analysis framework, that takes into account the interests of various stakeholder category (employees, owners and financial community; customers; suppliers, financial partners; government; local authorities and public administration; community; environment), affected by firms behaviour, regardless their size (Russo, Tencati, 2009, Perrini et al., 2007). Due to the fact that, according to the general perception, large firms are associated with a high degree of formalism, while the small firms are associated with the character often informal of their organization and management, the hypothesis of the studies regarding the CSR strategies implemented by firms is as follows: there is a positive relationship between the firm dimension and the formal character of the decisions referring to CSR (Russo, Tencati, 2009, Perrini et al., 2007). The general conclusion of these studies, although there a considerable number of gradations worthy of being considered, is that, as it was expected, among large firms prevail the formal strategies, while the decisions made by SMEs in order to integrate the CSR in their behaviour have, especially, an informal character (Russo, Tencati, 2009, Perrini et al., 2007).

SMEs seldom use the language of CSR to characterize their own activities (Russo, Tencati, 2009), they being more adequately characterized by the concept of "tacit CSR" (Perrini et al., 2007). Given the fact that, as it was mentioned above, the framework used for investigating this aspect was a multi-stakeholder analysis, the conclusion regarding the specific strategies adopted by firms of different size is the following: the large firms are more inclined to adopt strategies in domains as the environment management, workforce employment, local communities, controlling and reporting, whilst the SMEs are more willing to promote the socially responsible behaviour along the supply-chain; both categories of firms grant little support for the volunteering within the community (Perrrini et al., 2007). An important role in the decision-making process regarding social and environmental strategies, within the SMEs group, it has been proved to be held by the values of the owner-manager of the enterprise (Murillo, Lozano, 2006).

Motivations, benefits and constraints of involving SMEs in CSR actions

There are opposite opinions as regard to the existence of a social responsibility of the enterprise, some of them extreme, as it is the one that belongs to M. Friedman (1970), arguing that "the only social responsibility of the enterprise is to increase its profit", but also as regard to the forms and the benefits of such an involvement in social actions (Moir, 2001). Regarding the last aspect mentioned, the proponents of the CSR claim that enterprises can benefits on multiple ways, as the result of operating on the basis of a broader perspective and on the long run, as compared with the narrow view of pursuing their own interests, on the short run (Wikipedia), in economic terms inclusively (Murillo, Lozano, 2006). The support that enterprises, especially the small ones, are giving to the local communities where they are operating and their commitment to the community, are positively influencing their success; this is due to the fact that the residents, having different positions, are recognizing and rewarding this support, which confer strategic value to these forms of social involvement (Udayasankar, 2008, Besser, 1999).

The objective to remain well positioned in the market, to improve the corporate image, along with more pragmatic aspects, such as improving the work climate and employees motivation and the competitive differentiation, and not only purely ideological motivations, that derive from moral values, as a result of the pressure exerted by the external stakeholders, especially customers, constitute plausible reasons for actively engaging in CSR (Jenkins, 2006, Murillo, Lozano, 2006). Moreover, SMEs are considering that the

CSR have to be mutually beneficial, in order to have success in a business environment, which implies the fact that enterprises are placed in a framework limited by "the social priority" and "the enlightened self-interest priority" (Jenkins, 2006). It may appear surprising but the best way for stimulating SMEs to undertake the CSR is represented even by educating them as regard to the tangible and intangible benefits of CSR (Jenkins, 2006). The increasing pressure from customers (Perez-Sanchez et al., 2003), the improvement of firm performance by reducing costs and ameliorating efficiency, motivation justified by the fact that SMEs operate within a decisional framework based on market (Williamson et al., 2006), as well as the request of complying with regulations, that supply minimum standards for a great part of the activities embraced by CSR, represent very essential factors for undertaking environmental strategies by the SMEs (Williamson et al., 2006, Perez-Sanchez et al., 2003).

Udayasankar (2008), as it was mentioned in a previous section, has argued that not firm size in itself matters, but the configuration resulting by combining those three level attributes (visibility, resource access and scale of operations). O given configuration for an enterprise, by the view of those attributes, can offer sound incentives for a firm to involve in CSR or, on the contrary, can justify the lack of its social involvement. The same author (Udayasankar, 2008) presents in his study a synthesis of the way in which the different combinations of those level attributes of the firm, visibility (low/high), resource access (low/high) and scale of operations (small/large), lead to a certain level of firm participation in the CSR field (low/moderate/moderately high/high) along with the driving factors in this sense.

In order to have a complete picture it is necessary to consider also the constraints and difficulties that firms must face in their intention of behaving socially responsible. The involvement in CSR not leads only to benefits but implies also facing some difficulties, more evident for small firms rather than for the larger ones (Ortiz Avram, Kühne, 2008, Lepoutre, Heene, 2006), a smaller size of firms, according to one opinion, limiting their possibility to action in a responsible manner (Lepoutre, Heene, 2006). The lack of human and financial resources, that limit the ability of SMEs to engage in CSR activities that do not lead to immediate benefits, together with their reduced power that makes them dependent of the socially responsible behaviour of the owner-manager and the impossibility of discretionary behaviours, represent the difficulties that SMEs must face in undertaking their social role (Ortiz Avram, Kühne, 2008, Lepoutre, Heene, 2006). These barriers act, especially, in the case of those issues of social responsibility that involve external stakeholders or natural environment (Ortiz Avram, Kühne, 2008, Lepoutre, Heene, 2006).

4. Conclusions

The research regarding the relationship between firm size and CSR has enriched considerably in the last few years, but still remain some aspects that necessitate further research. The particular attention granted to this relationship can be judged on background of an increasing interest to SMEs, from governmental organizations and business professionals, but also from academics. Regarding the above-mentioned relationship, the studies conducted have proved that SMEs are able of socially responsible behaviour and that they involved in CSR programmes, but their participation has a different profile comparatively with the large firms, not the size in itself being the one that matters. The particularities are evident at the level of strategies adopted, of benefits, motivations and constraints that limit the socially responsible behaviour of SMEs.

Notes

(1) See Freeman, R., „Strategic management: a stakeholder approach", *Pitman*, 1984, cited in „Corporate Social Responsibility" (Wikipedia).

(2) See Andriof, J.; McIntosh, M., „Perspectives on corporate citizenship*", Greenleaf Publishing*, Sheffield, 2001, cited in Foley and Jayawardhena (2001).

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The Role of Promotion in Milling and Bakery Products Sales

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Abstract. *Irrespective of the avenue chosen for the retail of milling and bakery products, a key role in sales growth is the one played by promotion, information of the future customers as to the characteristics of the products, the execution and sale conditions. Such information process takes place by means of the promotional mix, consisting of a blend of advertising, sales promotion, public relations tools, trademarks, promotional events, and sales forces. The milling and baking industry uses, to certain extent, all the components of the promotional mix. Product promotion is central both to sales growth, as well as to educating, advising and informing consumers as to how they can select quality milling and bakery products.*

Keywords: the milling and baking industry; product promotion; products sales; components of the promotional mix.

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JEL Codes: M31, M37.
REL Codes: 14G, 14K.

Irrespective of the way chosen for the sales of milling and bakery products, a key role in sales growth is the one played by promotion, information of the future customers as to the characteristics of the products, the execution and sales conditions. There is a series of particularities resulting especially from the impact of milling and bakery product consumption on the safety and security of people's lives.

Any modern company relies on a complex marketing communications system. Companies which sell milling and bakery products communicate with the intermediaries, the consumers, and various public institutions. Intermediaries communicate with consumers and public institutions. Consumers communicate amongst themselves orally, and with the public institutions as well. At the same time, each group is reversely connected to all the other groups.

A company's marketing communications programme, known as the promotional mix, is a specific blend of advertising, sales promotion, public relations, trademark use, and sales forces tools, employed to achieve the marketing and advertising goals. For the fiercely competitive industry of milling and baking, each particular element of the promotional mix is of utmost importance.

Companies in the milling and baking sector should not limit their goals to merely providing quality goods. They should seek to inform the consumer of the advantages of their products and to "implant" such advantages in the consumer's mind with surgeon precision. To that end, it is mandatory that businesses properly employ mass promotion tools.

For the purposes hereof *advertising* shall be construed as any form of paid, non-personal way of presenting and promoting ideas, goods or services by means of mass communication channels (the printed media – catalogues, newspapers, magazines; the internet; radio and television stations) and by a clearly identified sponsor. Many of the companies in the milling and baking industry result to advertising in order to transmit messages about themselves, about their products, or about their policy so as to generate reaction amongst a certain audience.

As it is the most intensively used tool when promoting consumer goods, it comes naturally that advertising be the most frequent activity in the promotion of milling and bakery products. Given the nature of the very needs it addresses (first needs, that is), and given that the catalyst of demand for milling and bakery products is the population in the territorial reach of a company, television is one of the main promotion media used. The combination of image, sound and motion generates an indisputable persuasion effect, so much so when taking into consideration the importance of organoleptic properties of milling and bakery products in assessing their quality and, why not, in arousing appetite.

Milling and bakery products' appearance, depicted in vivid colours, is highly significant in influencing market demand. Hence most frequently employed media are the printed press (especially periodicals, in consideration of their reproduction accuracy and colour quality), posters, billboards, catalogues, flyers, brochures, etc.

A growing number of producers in the milling and baking industry chooses to promote and present their products through internet, most of such producers having their own websites – www.boromir.ro, www.velpitar.ro, www.pambac.ro, www.dobrogeagrup.ro, www.titan.ro, www.spicul.ro.

Generally, advertising is emotional at its core, thus exploiting the emotional features and springs of the individual. This kind of advertising is particularly powerful in the case of festive products.

Factual advertising may as well be resulted to, with a focus on, say, the vitamin, mineral, and fibre content of milling and bakery products and their role in the normal development of metabolic processes.

Advertising campaigns make for one of the main leverages of milling and bakery products sale. Sales strategies in the milling and baking industry rely on image campaigns in combination with national strategic campaigns, as well as on promotion point of purchase campaigns customized for sales channels or seasonal sales.

In addition to press layouts, in most cases, players in this market segment result to point of purchase promotions beginning with educating the consumer, placing products on additional positions to the shelf, and cross-promotions with complementary own products.

A communication tool that is more and more frequently used is that of *sales promotion*. Sales promotion resides in short-term incentives granted as a supplement to the very advantages of a certain good or service, with the purpose of boosting sales of that good or service. Sales promotion is that which provides the reasons at the foundation of immediate sale. It is the means to persuade a consumer to buy "now".

Sales promotion targeted at increasing consumer demand for a product is also extensively used in the case of milling and bakery products. As it gives a temporary advantage to the consumer, sales promotion can determine an increase in milling and bakery products sale, at least by drawing consumers of similar goods (i.e., extensively) and to a smaller extent, by increasing the average per capita consumption (i.e., intensively), specifically due to the primary nature of the need which milling and bakery products satisfy.

Most common of all sales promotion techniques when seeking to boost sale of milling and bakery products are price reductions, package sales, promotional contests, promotional gifts, point of purchase advertising, merchandising techniques, etc.

Promotional campaigns for milling and baking products vary according to whether one is looking into modern or traditional trade. In modern trade, promotion is directed to the consumer and relies on point of purchase activities and promotions of the type "buy 1, get 1 free". On the other hand, in traditional trade, promotion takes the shape of trade allowances, price reductions or product promotions. Producers' promotion programmes distinguish between buyer and consumer. At a first stage, women make for the targeted category, as they are the ones usually in charge of shopping for the family; if women are at the same time mothers, they will additionally purchase child products. At a second stage, milling and bakery products address all types of consumers, from children – biscuits and waffles of all kind – to the elderly – especially bulk products.

Public relations are another mass promotion technique. It is a way of establishing good relations with various public bodies and thus benefiting of favourable publicity, creating an appropriate "company image" and preventing or dismissing unfavourable rumours and news.

Public relations help with both product and company promotion. Public relations can generate a powerful impact on the level of public awareness, at a much lesser cost than advertising. Large companies in the milling and baking industry, through their spokes persons, organize press conferences, grant interviews to various publications (e.g., dedicated magazines such as "Piața", "Magazinul Progresiv", „Brutarul", „Food and Drinks Globus", or newspapers such as „Ziarul Financiar"). Other targeted informative activities are organized in order to attract media participation and focus (symposiums, conferences), as well as leisure activities (preferably of informative nature) meant to create sympathy and hence aimed at the emotional or subconscious levels (anniversary celebrations, cocktail parties, trips). However, a more indirect approach is beginning to gain weight, namely a company's association with major events initiated by other organizations (congresses, exhibitions, shows) or a company's involvement with social work (social care, medical research) by means of donations and sponsorships.

Trademark use refers to objectives dictated by the need to single out and differentiate own products and services from those of the competition, depending on the specificity of market segments – determined as they are, amongst others, by the various consumer lifestyles – and oriented towards emphasising psychological advantages and qualities. The trademark functions both as means of identification and communication tool.

As it provides a tangible edge to producers and buyers alike, the trademark plays an important part in the promotion of milling and bakery products. Such a central part comes as a result of the graphic shape and the message communicated, the trademark being thus a means of naming and recognizing a product, as well as an easy manner for the consumer to choose from among a number of similar products which, in the case of milling and bakery, is quite high. The function of facilitating product recognition and, implicitly, purchase is also performed by the package and the label, yet this only stands so long as the shape, the size, the dimension, and perhaps the colour of the package are not changed at short time intervals. The package is essential to the promotion of milling and bakery products; nonetheless, it should always be supported by quality and price. Moreover, the package and the label together work as an irreplaceable, quick and precise product identifier, whereas by way of the informative or promotional message they send out, they definitely influence the purchase decision. Usually, buyers easily recognize the products they regularly purchase by the package and label thereof. A milling or bakery product is characterized not only by means of its nutritional value, but also by such informative elements as make it known and recognizable. In the short run, changing product packaging may result into sales increase.

A more particular product is fresh baked bread. Common rules no longer apply to fresh bread since the greatest number of consumers is not aware of the brand they purchase.

The importance given to ecology, especially in the more developed countries, and the growing ecological approach taken up by more and more companies (including those in the field of milling and baking) lead to the advent of ecological trademarks or symbols. This testifies to a company’s concern with the protection of the environment. The right to apply the eco-symbol on a product is granted to companies to the extent that the products to be so labelled comply with the relevant regulations in force in their country (region).

Alongside the trademark, the eco symbols or the distinctive dress, the informative message contained on the package or the label of milling and baking products is an essential product identifier given the background of increased concerns among consumers with food safety and security.

Participation at exhibitions and sponsorships has at present become part of the *promotional events* widely employed by companies in the milling and baking industry.

The main producers in the milling and baking industry (Dobrogea Grup, Boromir, Vel Pitar, Titan, Pambac) regularly take part in exhibitions (fares and local, regional, national, and international exhibitions - EXPOAGROUTIL, INDAGRA FOOD Bucharest, AGROMALIM Arad, ALIMENTEXPO Bacău, AGROMEXPO Bacău, AGRARIA Constanța, TIMAGRALIM Timișoara, TIBCO, etc). The promotional objectives of such milling and baking companies include the opening of new sales sectors in such geographical areas where the companies are present, establishing a maximum of contact with market agents in the shortest time possible, presentation and testing of new products, launching new products at promotional prices, directing focus of all promotional means to a large number of market agents and a critical mass of potential consumers, being present alongside the competition and gaining insight into competing products and offers, creating a portfolio of immediate or promissory orders, enhancing dialogue with market agents, and raising client awareness (trademark awareness).

Sponsorship, one of the other tools used by large, powerful companies, consists of financial support granted to certain public events (of cultural, athletic, medical, educational nature; theme competitions, etc.) with the purpose of raising mass awareness as to the trademarks under which their products are distributed.

Sales forces refer to that group of company representatives (employees or agents) enjoying multiple competences. As they fulfil a double task – namely, to increase turnover by distributing products outside the traditional trade network, and to prospect and maintain market dialogue – sales forces are part of the promotional toolkit and contribute in a much more tangible manner to the achievement of a company's business objectives. At the same time, this promotional tool is also the most costly one employed for contact and communication building, yet nonetheless highly important and specific to those companies trading industrial products and whose offer addresses a specialized, narrow client base – users and distributors. This being the case, the role of the other promotional tools is far more limited, by comparison to companies in the milling and baking industry. In terms of objectives, sales forces are not limited to the mere act of selling but rather perform a wide array of activities at the same time, such as identifying potential markets, defining the client profile and geographically locating the client, merchandising activities at the level of the distribution network, providing technical and commercial assistance to industrial users and agents, marketing services in relation to product use directions, market prospecting, offer negotiation and deal closing, gathering information from clients or about the competition, and so forth. By performing both prospecting and communication tasks, sales forces have an increased promotional value.

The promotion of both competitiveness and quality of Romanian milling and bakery products must comply with current quality and safety European standards.

In addition to sales increase, product promotion also fulfils an educational function. It is intended to advise and inform consumers on how to make educated, quality, and safe discrimination amongst the milling and bakery products available.

At the national level, the promotional campaigns of companies in the milling and baking industry also seek to build image and maintain notoriety. Creating such solid image calls for consistent work and matching creativity, thus requiring the permanent employment of all communication media available. From this point of view, product display areas function as a powerful image builder. It is such that clients are enabled to discriminate amongst companies even when competing products are highly similar.

A successful company image is that associating the company's identity with the superior quality of the products it offers.

Irrespective of the nature of promotional activities, of the homogeneity or heterogeneity of techniques, of their life span or their effects on sales numbers, companies in the milling and baking industry must never lose sight of the fact that these tools are complementary; an effective market policy aimed to achieve strategic objectives must incorporate available tools in a coherent and operational promotional approach instead of employing them in isolation. At the same time, the effectiveness of using promotional variables within market activities depend to a great extent both on the manner in which they are integrated in the general marketing policy as well as on the way in which the promotional activity is coordinated with the other elements of the promotional mix.

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