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**THE IMPLEMENTATION OF THE COHESION FUND IN HUNGARY FROM  
INSTITUTIONAL ASPECTS BASED ON NATIONAL AND INTERNATIONAL  
EXPERIENCES**

**THESIS**

**ESZTER RÉKA MOGYORÓSY**

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## **PhD Studies**

**name:**           **PhD Studies of Management and Business**

**science:**       **Management and Business**

**head:**           **Dr. István Szűcs**  
university professor, doctor of HAS (economics)  
SZIU, Faculty of Economics and Social Sciences,  
Institution for Economic Research and Methodology

**theme leader:** **Dr. József Popp**  
Deputy General Director  
Research Institute for Agricultural Economics

.....  
Dr. István Szűcs

.....  
Dr. József Popp

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## 1. INTRODUCTION

### 1.1. The importance of the theme

To introduce the significance and importance of the subject, first of all I would like to present some figures. Since 1 May 2004, the support of the Structural and Cohesion Funds are eligible for Hungary, as new member of the European Union. It means that in the first two and a half year, until 2006, Hungary **annually** receives **approximately 650 MEUR** from the Structural Funds and **330 MEUR** from the Cohesion Fund to finance the structural policies.

Among the instruments of the regional policy, the **Cohesion Fund** is one of the most significant. Its aim is to support the poorest member states of the Community in the period of the preparation to join to the Monetary Union. Therefore with the Cohesion Fund, the basic target of the European Union is to support the implementation of timely and expensive infrastructural investments in the area of the environment and transport while the budgetary deficit does not increase and the environmental aspects are taken into consideration.

**From 2007 the annual support for the regional policies is expected to be triple**, while the regulations related to the faster implementation become stricter. It is important to see that the country can live with these opportunities only if it improves the effectiveness of the preparation, the authorization, the public procurement and the implementation, which is impossible without a well-prepared and effectively operating institutional background.

### 1.2. Goals

In my dissertation **I examine the effectiveness of the implementation of the supports Hungary gets from the European Union through the institutional system**. I do that because I am convinced that:

- the successful implementation of the above mentioned amounts is impossible without a well functioning, stable institutional system;
- the institutions, the institutional system influence the economic growth.

As the national institutional system that takes part in the implementation of these supports is extremely divaricate, furthermore it continuously changes, I chosed its most transparent element, the institutional system of the Cohesion Fund, to introduce and analyse the recent implementation system, revealing its deficiencies, weak points, summarizing the experiences and making proposals for further development, which is unavoidable because of the deficiencies and the permanent renewal and on the other hand is very actual now, in the preparation phase of the following programming period of 2007-2013. In the selection of the theme, I mean the examination of the project management from an institutional aspect, the fact that I have been working in the Cohesion Fund Managing Authority in the National Development Office and have been dealing with ISPA and Cohesion Fund related institutional tasks for 5 years, played an important role. I build up my researches on my experiences and ideas with the following **targets**:

- 1) **Gap filling** in the sense that in the recent national and international literature we have only scattered, general information about the importance and effects of the ISPA program and the Cohesion Fund, besides the Structural Funds, but their complex, future oriented analysis is totally missing. Furthermore, nor research examining the effectiveness of the institutional system has been done, we can read about it only in the reports of the auditing bodies.
- 2) **Based on the national and international experiences, analysis and advice** on the necessary institutional developments to use more effectively the opportunities given by the Cohesion Fund taking into consideration the preparation to the 2007-2013 programming period.



## 2. MATERIAL AND METHOD

### 2.1. Synthetization

As I have already mentioned at the targets, both the national and international literature is quite reticent about the implementation, and especially about the examination and analysis of the Cohesion Fund. In my research I collect and synthetize the existing, very fragmented literature and legal background of the Fund, making it complex with the statements of the reports done by national and international bodies. That gives the basis of the study, the frame into which I incorporate the revealed connections, results, conclusions and proposals.

### 2.2. Models for analysing the institutional effectiveness

#### 2.2.1. *Functional analysis*

The aim of the analysis is the establishment, development and the creation of the conditions needed for an effective institutional system. To develop the system first the analysis of its recent tasks are needed. To do that I chosed the method of functional analysis. To the functional analysis I adopted and developed **Duncker's heuristic problem solving method** which contains the following steps:

1. collecting information;
2. analysing the functions;
3. elaborating the alternatives for changes;
4. making final proposal.

The information collection focuses on the background and the establishment of the recent system and is followed by the analysis of the chosen, determining functions and sub systems. As in the study I examine the effectiveness of the whole institutional system when I speak about analysing the functions, I mean analysing the sub-systems. The functions of the institutional system can be grouped in the following categories:

- political functions;
- service functions;
- regulation functions;
- control functions;
- co-ordination functions;
- supporting functions.

The elaboration of the possible alternatives and the final proposals are the results of the analysis, taking into consideration the changes in the legal background and the procedures from 2007.

#### 2.2.2. *The model of the EU to measure the administration capacity*

For the analysis of the effectiveness of the institutional system, in my research I use the study issued by the European Commission: "Key indicators for Candidate Countries to Effectively Manage the Structural Funds", that **measures the administration capacity through the absorption capacity**.

It means that:

struct.+hum.r.+sup.sys. inst. → functionings → administr.cap. → absorp. → performance requirements

in summary, the formula demonstrates the importance of structure, human resources, systems as an input for managing, especially so in relation to the requirements. The ratio between these factors and the requirements determines the actual functioning of the system, or the supply side of administrative capacity that affects the absorption. At the end, absorption capacity only leads to a strong performance of the Cohesion Fund if efficiency and effectiveness are taken fully into account.

### 2.2.3. Model elaborated for the research

In my study I elaborated a third model based on the functional analysis, the model of the European Commission and my own experiences. The model examines the effectiveness of the institutional system through the following points:

- political, regulational, co-ordinational functions, structure  
→ **REGULATIONS, LEGAL BACKGROUND** (internal regulations, rules for procedures, audit trail);
- supporting, service functions, human resources  
→ **HUMAN RESOURCES**
- control function  
→ **CONTROL**
- service, supporting systems and instruments  
→ **RETENTION OF DOCUMENTS, INFORMATION AND PUBLICITY**

## 2.3. Risk analysis

To reveal the hindering elements of the effective function of the institutional system, I chose the method of the risk analysis, which is based on the project cycle management and the Delphi type questionnaire.

### 2.3.1. Theory of project cycle management

I carried out the risk analysis with the help of a questionnaire. I listed the risk factors according to the project cycle and my personal experience. Afterwards, I elaborated the **Capability management Grid of the Cohesion Fund** from the combination of the dimensions of the project cycle and the elements of the management ability.

	Regulations, legal background	Human resources	Control	Supporting sub-systems and tools	Functioning
Management					
Programming					
Implementation					
Monitoring					
Closure					

The grid gives a general frame to examine all the aspects that are important to the effective implementation of the Cohesion Fund, furthermore it gives a good basis to **identify the main indicators**.



### 2.3.2. Questionnaire with Delphi method

The Delphi method is a procedure of multiple round. The questionnaire is restructured several times before it gets its final form. The questions of the first draft are large scaled, formed and answered only by a couple of experts. The second, more detailed questionnaire can be elaborated after that. Finally only those elements remain where all the participants agree.

### 2.3.3. The method of the risk analysis

The identified risks can be prioritized if we make them measurable. To do that we have to define the **scales of the possibility and the effects**. Possibility means that we have to measure, based on the revealed risks and experiences, how big the possibility is that the risk come true, while the scale of the effects shows the effect of the risks. To measure the factors of the possibility and the effects I use the following 5 grade linear scale:

1	1-20%
2	21-40%
3	41-60%
4	61-80%
5	81-100%

Using this scale the possibilities and the effects must be evaluated for all the risk factors. It is followed by the selection of the critical factors with the help of the **risk coefficient**:

$$C=P+2xE$$

Where:

P is the possibility value of the risk factor;

E is the value of the effect on the same scale;

P can be maximum 15 in the 1-5 graded scales.

According to the number we receive for the risk coefficient, the risk can be:

11-15	high
7-10	medium
3-6	low

Finally, based on the risks and the expected changes after 2007, I give proposals for the development of the institutional system.

## 2.4. Study tours abroad

Besides these methods my research was supported by scientific forums, conferences, presentations, study tours, that gave me opportunity to know better both theoretically and practically each problem, to build up profesional relations, personal conversations and helped me to see my own experiences from another aspect I learned a lot especially in Greece where I spent one month in November 2003 studying their institutional system and in Ireland where I had the opportunity to spend one week both in 2003 and 2004.



### 3. RESULTS

#### 3.1. The institutional system of the Cohesion Fund

##### 3.1.1. *The preparation of Hungary for the implementation of the Cohesion Fund*

To understand the recent system it is unavoidable to review the preliminaries, the circumstances of its creation. The ISPA program<sup>1</sup> was the forerunner of the Cohesion Fund both in programming and institutional aspects. Therefore the experiences we got through the implementation of the ISPA have built in the present system, so it transferred its signs and effects. On the one hand the experiences we gained due to the ISPA program can be useful to avoid mistakes in the future, and as from 1 May 2004 all the ISPA projects automatically have become Cohesion Fund projects, on the other, thus the two systems create one unit.

Before introducing the transmission of the ISPA institutional system to the implementation structure of the Cohesion Fund, I would like to mention the tendering and contracting procedures, which in my opinion gave a big impulse to the institutional system before the accession. **The tendering and contracting procedures** were connected with the ex-ante approval of the Commission. But the Council Regulation 1266/1999 made possible to get the extended decentralized implementation system for the ISPA, introducing the **ex-post control** of the Commission at the same time. This required the establishment and management of the adequate institutional structure. To achieve this in co-operation with the Commission in 2001 the gap assessment and the gap filling started in the institutional system to prepare it for the extended decentralized implementation system, the **EDIS** (Extended Decentralized Implementation System). In the ISPA institutional system in the accessing countries the EDIS accreditation did not finish until the accession because the Commission was not satisfied with the preparation of the National Railway Company and the environment sector. In spite of that, with the help of the EDIS process, according to the Commission of the EU, the gap filling assured an adequate basis for the preparation to implement the Cohesion Fund.

The member states have freedom to establish their institutional system, the EU defines only the frames. In the case of the Cohesion Fund, the **Commission Regulation 1386/2002** is the basic document in the regulation of the institutional system. According to this the following institutions must be pointed:

- **Managing Authority (MA)**, which has general responsibility for the management and co-ordination of the Cohesion Fund;
- **Paying Authority (PA)**, which has general responsibility for the financial management;
- **Intermediate Body (IB)**, which functions besides the Managing or Paying Authorities, or fulfil tasks delegated by them into the direction of the Implementing Bodies;
- **Implementing Body (ImpB)** and the beneficiaries are responsible for the implementation of the projects;
- **Monitoring Committee**, which main task is to control the physical and technical implementation of the projects.

##### 3.1.2. *The institutional structure of the former cohesion countries*

Before examining the characteristics of the Hungarian institutional system, I introduce the practice of the former member states, more exactly the cohesion countries. With this in mind, on the one hand, I want to underline that there is no obligatory model given by the EU, but the **institutional system is based on and operates with the national characteristics**. On the other

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<sup>1</sup> Instrument for Structural Policies for Pre-Accession.

hand, thanks to the foreign experts having worked in Hungary during the establishment of the present Hungarian institutional system, their experiences were built in. Furthermore, and I will come back to this later, in the programming period 2007-2013, radical changes of the institutional system are expected, to which examining the practice of the member states can be useful and its useful elements can be adopted to the national practice. By studying the institutional system of the member states, I have the following **statements** and feel important **to the development of the Hungarian system**:

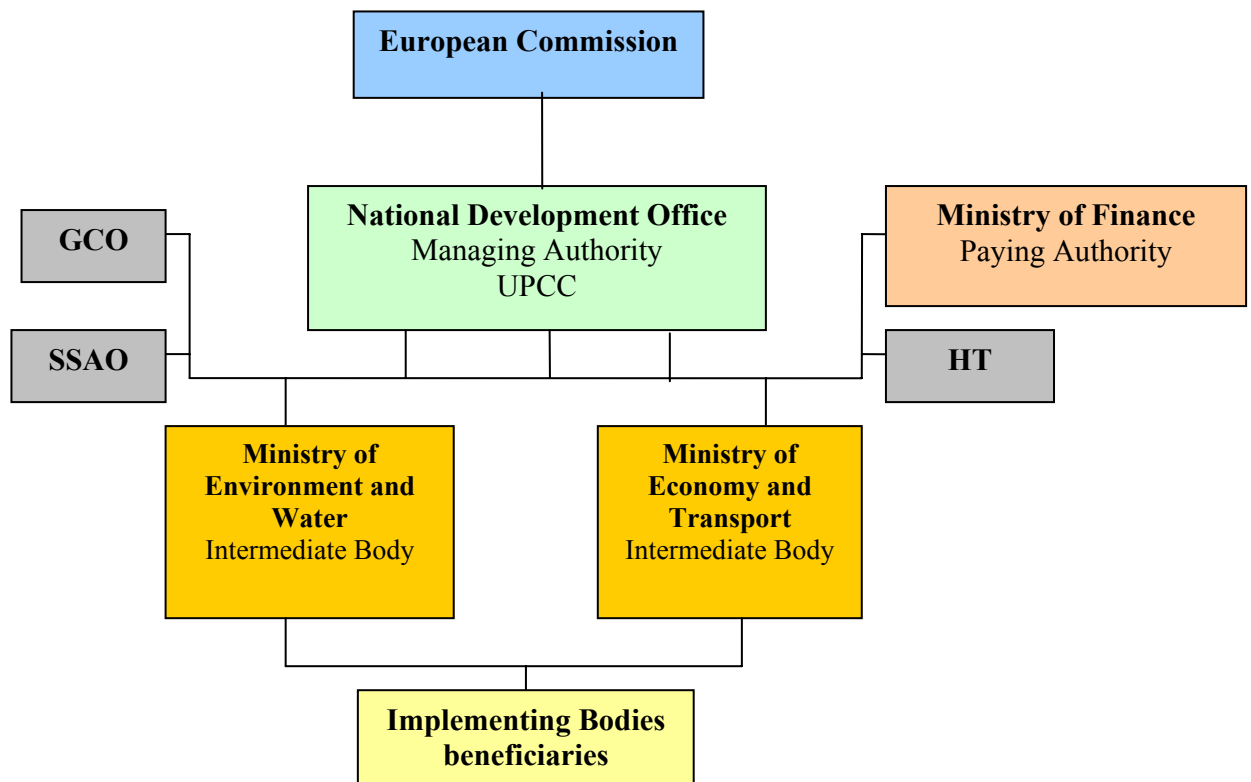
- According to the national characteristics, the institutional structure differs in every country. Hungary should not copy the structure of another member state either, but develop and change the present system.
- The level and type of the regionalisation also differs in every country and the most in Ireland and Spain. The Spanish example is too specific, but I suggest to think over the adaptation of the Irish practice in Hungary, as nowadays the situation here is as chaotic as in Portugal.
- As the Irish example shows, the partnership, the extended consultation is one of the key issues of the successful implementation of the projects. In Hungary this, and I will point it out later several time, is very under-developed at the moment, and we should put more emphasise on it in the future.
- The management of the Cohesion and the Structural Funds can not be separated clearly, which means that the same body is responsible for the implementation of these supports. I feel this a good practice, especially knowing the reforms in the implementation system after 2007. In addition, this is not so far away from the present Hungarian structure either because both the Managing Authority of the Community Support Framework, and the Cohesion Fund Managing Authority operate under the same vice presidency in the National Development Office. But I feel it important to keep separately the co-ordination of the two types of funds, by two departments, or it should be clearly defined in the job descriptions who is responsible for which support.
- The Managing and the Paying Authority can be found in one institution, in the Ministry of Finance in Ireland and Spain. In the case of Hungary because of the national characteristics, I do not think that this practice should work well, therefore I propose to think of it in the present structure and its further development.
- The number of the persons working at the Managing Authorities is minimum 4-7, maximum 12-14. In Hungary at the moment it is 10, which can be an average. In my opinion the effectiveness is not the question of quantity, but quality. Therefore I would put more emphasise on trainings and the assurance of stability and later I shall make my proposals for this issue.

### ***3.1.3. The Hungarian institutional system between 2004-2006***

To measure the effectiveness of the institutional system is not easy and is more complicated in the case of the Cohesion Fund, or of any EU fund in Hungary as the results can be evaluated ex-post, after the programming period, in this case in 2007. In spite of that I try to do that in my dissertation. Its first step is equivalent with the functional analysis, which is collecting information. To do that I review the present system and the functions of the institutions. Its bases are the national and the EU legal requirements.

#### ***Legal background and structure***

The **Gov. Reg. 1/2004** finalised the institutional system responsible for the implementation of the Cohesion Fund in Hungary which is shown by the figure 1.



**Figure 1.**  
**The institutional system of the Cohesion Fund in Hungary 2004-2006**

Afterwards the dissertation introduces detailed the tasks of these bodies.

### ***3.1.4. Changes after 2007 in the Hungarian institutional system***

The **EU does not have obligatory proposal** to establish a body keeping contact with the Commission, but made it clear several times that it is necessary to have such a co-ordinating body. The **Operational Programs (OP) and their number** for the programming period 2007-13 are **determined by the Hungarian Government**, but their approval remains the duty of the Commission. It is an important change that the responsibility of the **Managing Authority** and the Monitoring Committee will be the same, but they will be established only **at OP level**. There will be a new body called **Auditing Authority**, which will control the adequate operation of the managing and audit bodies. In the area of audit the introduction of the theory of proportion is a new element too. It means that if the member state meets the determined requirements, it can establish its own auditing bodies and procedures.

The preparation for the next programming period has the same two dimensions as before the accession: **institutional and regulational**. The institutional tasks are related to the selection and accreditation of the managing authorities and the intermediate bodies. The regulational tasks are first of all the elaboration of the procedures and legal background of the institutional system. It is the government who decides directly about the appointment of the managing authorities, while the selection of the Intermediate Bodies will be done formally by the managing authorities.

### **3.2. New scientific results**

After collecting the tasks of the institutions taking part in the implementation of the Cohesion Fund and reviewing their new tasks in the coming programming period 2007-2013, the next step of the functional analysis is the analysis of the functions, which in my dissertation means the **analysis of the sub-systems** supporting the implementation. The aim of the analysis is

to point out the deficiencies and the weak points. I examine the effectiveness of the institutional system with the model elaborated on the basis of the administration capacity model of the Commission and the functional analysis, with the help of the **Capability management Grid of the Cohesion Fund** and the **risk analysis**.

In the Capability management Grid of the Cohesion Fund, taking into consideration the project cycle, I collected the indicators by which I analyse the sub-systems afterwards:

	<b>Regulations, legal background</b>	<b>Human resources</b>	<b>Control</b>	<b>Supporting sub systems and tools</b>	<b>Functioning</b>
<b>Management</b>	<ul style="list-style-type: none"> <li>- Appointment of Managing Authorities and determining their tasks</li> <li>- Appointment of Paying Authority and determining its tasks</li> <li>- Division of the delegated tasks</li> <li>- Legal background, procedures, audit trail that clearly defines the tasks and responsibilities</li> </ul>	<ul style="list-style-type: none"> <li>- Managing Authorities, Paying Authority have the necessary human resources</li> <li>- Assurance the stability of the institutional system, reducing the fluctuation</li> <li>- Training for the institutions</li> </ul>	Appointment of auditing bodies	<ul style="list-style-type: none"> <li>- Frames for the retention of documents according to the EU rules</li> <li>- Assurance of transparency and publicity</li> </ul>	<ul style="list-style-type: none"> <li>- Transparent operation with well defined tasks and responsibilities</li> <li>- Modern public sector</li> </ul>
<b>Programming</b>	Elaboration of guidelines. Manuals for programming	<ul style="list-style-type: none"> <li>- Having the capacity for programming</li> <li>- Clear job descriptions</li> </ul>	N.A.	<ul style="list-style-type: none"> <li>- Partnership, consultation</li> <li>- Acceptance of the project</li> </ul>	Well prepared projects
<b>Implementation</b>	<ul style="list-style-type: none"> <li>- Appointment of Intermediate Bodies, beneficiaries</li> <li>- Co-operation among the institutions</li> <li>- Manuals, guidelines for implementation</li> </ul>	<ul style="list-style-type: none"> <li>- Intermediate Bodies, beneficiaries have the human capacity</li> <li>- Assurance stability</li> <li>- Assurance promotion</li> </ul>	<ul style="list-style-type: none"> <li>- Elaborated control methods</li> <li>- Audit plans</li> <li>- Assurance of proficiency to carry out audit</li> </ul>	<ul style="list-style-type: none"> <li>- Retention of documents according to the EU rules</li> <li>- co-operation with the public, civil associations</li> <li>- Publicity according to the EU rules</li> </ul>	Absorption of the Cohesion Fund
<b>Monitoring</b>	Appointment of responsibilities in the area of monitoring and evaluation	Experts	Treatment of irregularities	<ul style="list-style-type: none"> <li>- documentation, traceability</li> <li>- Publicity according to the EU rules</li> </ul>	Well functioning monitoring and control system
<b>Closure</b>	Clearly defined tasks for the participants in the closure	Experts	<ul style="list-style-type: none"> <li>- Experts</li> <li>- Guideline for the closure</li> </ul>	<ul style="list-style-type: none"> <li>- documentation, traceability</li> <li>- according to the EU rules</li> </ul>	Transfer the last part of the support

### **3.2.1. Regulations, legal background**

There is no doubt that in the last years the institutional regulation has been improved, but there are still some unregulated areas. Besides this it makes the examination even more difficult that the quality of the international regulations of the institutions and their adequacy to the legal requirements are different similarly to their application in the practice.

### *The anomalies of the legal background*

As for the appointment of the institutions in the period 2004-2006, the Gov. Reg. 1/2004 did it. The **TNM-GKM-FMM-FVM-PM common regulation 14/2004** completes it, defining more details of the tasks. But in the last three years it has become clear that it has not covered everything. I feel especially problematic the paragraphs related to the public procurement, which are on the one hand rough, and do not define clearly the tasks and the responsibilities, on the other. In my view the regulation is needed to be precise in several points because it **does not regulate unanimously the delegated tasks and/or does not define the responsible body**. In my opinion it is very dangerous, as it is shown in the practice too, and in many cases leads to lack of responsibility for accounting the decline or slip on someone else the responsibility.

Regarding the **public procurement**, I feel it an especially sensitive area. In spite of that the **Hungarian law** was approved in the summer 2004, it has been modified several times, which also means that it **needs to be** improved as for the effectiveness of the projects.

In my opinion the **legal regulation is still not** complete. It was already seen with the ISPA program, but **the financial system of the project preparation and the financial background of the social consultation and the information of the public are still not regulated**. I will come back to this point in the chapter about information and publicity.

**There is no legal obligation about the human resources**, only the Gov. Reg. 193/2003 specifies the educational requirements for the internal auditors. In my view it is enough and I have not found any regulations related to the human resources in the other member states either, but I feel important the analysis and the regulation of the capacity and the educational requirements of the human resources.

Finally I find it quite scarce that in spite of that the start of the new programming period is really close, there are no regulations prepared about the operation of the institutional system.

### *Internal regulations*

My study tours in the member states convinced me that with adequate, well elaborated, clearly defined tasks and responsibilities of the internal regulations, the legal background can be effectively substituted, furthermore the long process of the approval of the regulation can be avoided. Analysing the system I found that the highest level of the implementation system (MA, PA, IB) possesses these internal regulations and guidelines. As I have already mentioned, I put great emphasis on the EDIS process in the development of the institutional system, in the frame of which the institutions elaborated their internal regulations and **manuals**. Though I think that this process is absolutely positive, I do not see its results like that. To explain this I would like to mention that there is no obligation regarding the format of the manuals and according to the Gov. Reg. 360/2004, the Managing Authority can oblige the Intermediate Bodies to elaborate these manuals, but can not define their content, only can make proposals about it. This has led to the fact that, because of the lack of consultations, the manuals of the Intermediate Bodies are differently detailed. As for the manuals of the Implementing Bodies, the picture is even more colourful. Their structure, quality does not show any connection, furthermore the Hungarocontrol and the National Motorway Company, as well as the beneficiaries (environmental sector) do not have this kind of document. I consider it a serious deficiency already now, but it is risky especially after 2007, when the ministries will be the managing authorities and the responsibility level of the beneficiaries also increases in the implementation of the fund, which can be delivered only by well elaborated manuals.

The Managing Authority and the Ministry of Finance have elaborated several guidelines for the Intermediate Bodies and the beneficiaries. In spite of that we have to see that these **guidelines very often had to be prepared quickly, when in a certain area the problems already arose**.

### *Audit trail*

According to the **Regulation 2064/97/EC** an audit trail has to be worked out in the member states about the management and control systems. In spite of that in Hungary before July 2003 there was no obligation for the National Fund to do that. In addition, neither the EU, nor the Hungarian regulations defined which bodies and tasks should be regulated in the audit trail. During the EDIS accreditation all the relevant body elaborated its own audit trail. The **audit trail containing the whole institutional system and project cycle** was elaborated in spring 2004, in the frame of harmonized working groups, with the participation of the representatives of the relevant bodies and with the co-ordination of the Managing Authority. I see the **importance of this audit trail** in that it:

- harmonizes the manuals of the institutions taking part in the implementation of the Cohesion Fund in Hungary;
- describes the processes of the implementation of the Cohesion Fund in Hungary;
- reveals the unregulated areas in the implementation of the Cohesion Fund;
- creates a common knowledge;
- can be used directly, its language is easy to understand.

### *3.2.2. Human resources*

The report of the Supreme State Audit Office issued in 2004 about the implementation of the ISPA environmental projects also points out that the Hungarian institutional system of the ISPA program, following the continuously changing legal background and institutional concepts, operated in a **continuous transformation**. In my opinion this statement is relevant for the Cohesion Fund too. It is strange that the Hungarian society and the leadership of the institutions consider this a normal phenomenon, while **the continuous restructuring obviously threatens the stability of the system, which leads to the backwardness of the desired effectiveness**.

During the implementation several problem is erected in the **lack of** the necessary technical professional preparedness and **experience and** the lack of the **human resources**. In spite of the fact that recently there has been a significant increase in the staff at the institutions, we can not forget about the **high rate of fluctuation** either. The staff are usually young, the average age is around 30, and - in spite of the adequate educational background - miss the practical experience. On the other hand we have to see that this is the first generation that has EU-related education and speaks languages. What I see really problematic in this area is as follows:

- **There is no adequate financial background** to assure the required capacity;
- The leadership often **does not apply new persons where it would be really needed** (e.g. institution building, communication);
- The **public sector does not offer the required promotions and financial background** to the young staff in the long run.

### *3.2.3. Control system*

The aim of the control is to give a clear, detailed description until the level of the project manager about the financial and informational processes of the Cohesion Fund, about their documentary background and control system. The control system was created also in the era of the EDIS accreditation. In the frame of that independent internal audit units were established, too. Some tasks were regulated by the Gov. Reg. 255/2000, but the whole system was not covered by it. The control system needed to the implementation of the Cohesion Fund was regulated by the Gov. Reg. 233/2003. To harmonize the audit levels and to improve the co-ordination, the Gov. Reg. 360/2004 reregulated the control structures and the control tasks of the institutions.

Because of the different internal regulations, however, **the „four eye” principle and the control built in the implementation** with its documentary background **still do not exist**.



It was a good initiative that the control of the ISPA projects was regulated in the Co-operation Agreement signed by the Implementing Agency and the beneficiary, but the ISPA/Cohesion Fund audit bodies prepared and approved their audit manuals in different times.

The Gov. Reg. 80/2003 about the preparation, implementation and control of the pre-accession funds of the EU does not specify those beneficiaries who are not budgetary institutions (National Railway Company, National Motorway Company), therefore in their case these management and control regulations are not obligatory.

**The regulation background of the audit reports is defective and contradictory.** According to the Gov. Reg. 360/2004 it is the responsibility of the Managing Authority to forward the audit reports to the Paying Authority. But the regulation does not contain such an obligation for the Implementing Bodies and the beneficiaries. Furthermore I object that the regulation does not make it obligatory to send automatically the audit reports to the main audit body, the GCO.

Between **2000 and 2004 the half of the audits were system audit**, especially in connection with the EDIS accreditation and the audit of the managing and control systems of the Cohesion Fund. The **audits did not focus on the processes of the technical preparation** (project, TD preparation). Between 2004 and 2006, besides the system audit several **project audits** were carried out, but **without any harmonisation**. I mean that in many cases it occurred and has still occurred that **an institution or a project was or has been audited by different audit bodies at the same time**. In the one hand it means unnecessary burden for the project managers who are not able to deal with their every day work in this period, and, on the other, it does not make sense to audit the same project when it would be more useful to audit more.

Furthermore, and the DG Regio audit carried out in 2005 (see more details later) confirms my feeling, I see problematic the **quality of the site visits**. I mean that they are not done with the necessary frequency and generally the quality of the reports is far away from that desired. Behind this I think the reason is on the one hand the lack of the human capacity, and, on the other that the tasks are not precisely regulated in this area.

#### ***3.2.4. Further supporting systems***

##### ***Retention of documents***

There are serious deficiencies in the area of retention of documents too. During the implementation of the ISPA program, the Implementing Agencies did not regulate at all the documentation of the project proposals submitted by the beneficiaries, which is really worrying as after 3 years of the project closure and in the frame of that the Commission can check any kind of document related to the project implementation. In the case of the Cohesion Fund the Council Regulation 1164/1994/EC contains the general regulations, the managing and control regulations 1386/2002/EC, the Commission Regulation 16/2003/EC contains the regulations of the eligibility, while the requirements related to the managing and control systems are regulated by the Commission Regulation 2355/2002/EC. But I would like to mention that the EU regulation is not adequate either, because the relevant regulations determine the necessity of the retention of documents in the case of the projects supported by them, but do not give further detail about its methodology.

As for the national regulations, the **Gov. Reg. 255/2000** provides for the budgetary and accountancy settlements of the ISPA projects from the beginning of the implementation, but does not specify the specialties of the accountancy of the ISPA projects and **does not harmonize the retention obligation of the institutions taking part in the implementation**. According to the above mentioned government regulation, it is the task of the relevant body to establish its accountancy procedures in line with the national regulation, taking into account the EU

requirements. Because of the lack of the harmonisation of the retention system in the different institutions, the deficiencies of the data-basis and the unregulated areas, the reliability of the data and the transparency exist only partly.

Besides, the **Gov. Reg. 360/2004** deals with the necessity of the establishment of the retention system, but does not determine obligatory, undefined procedures and does not determine precisely the necessary system, the method of the treatment and the retention of the documents. In compliance with the Council Regulation 1386/2002/EC, the Government Regulation declares that the bodies taking part in the implementation of the Cohesion Fund are obliged to keep the project documents for three years after their closure by the European Commission.

According to the draft general regulation for the period 2007-2013, it remains the responsibility of the Managing Authority to assure the disposal and retention of the document as well as its description in the audit trail.

### ***Information and publicity***

In spite of the improving legal background of the area information and publicity, its use **in the practice is still not adequate**, while the information activity is needed to the successful project preparation and implementation. The connections among the actors in the vertical level of the economic processes are usually regulated by laws, while the initiation of the horizontal partnership (because of the different type and huge number of the actors and the local characteristics) can be assured only partly by legal regulations. The conscious, well prepared information dissemination is an **essential condition to gain the support**, as, because of the ignorance of the local population, in the lack of a good communication campaign, the projects can fail. Therefore the aim of the PR activity is to **gain the goodwill and the acceptance of the local people and dispel their fears**.

In spite of that, in the case of ISPA and of the Cohesion Fund, the Regulation 1267/1999/EC and the Regulation 621/2004/EC, respectively, declare that the beneficiary country has to assure the adequate publicity of the program and that the potential beneficiaries and the professional associations get information about certain measures, neither in the case of ISPA, nor in the case of the Cohesion Fund, the regulations contained obligations about the information of the potential beneficiaries and the necessary publicity activity and social consultation before the submission of the application. Because of the lack of the publicity activity and social consultation during the selection of the project proposals and the elaboration of the projects, **the principle of partnership was not realised**, the representatives of the regional and local associations were involved only in some cases. Because of the lack of appraisal, the social acceptance, besides the risk of getting the support for choosing a new site and preparing the new documentations, cause **delay**. In my opinion and the practice of the last years it does not make sense to submit project applications before getting the acceptance of the local population.

It is also a problem that **the cost of the project preparation can be financed only by national sources**, because the support of the Cohesion Fund and ISPA can/could be used only after the project approval in Brussels. Therefore this former information and the referendum have to be financed by the municipalities which lack the financial sources.

It shows also the importance of the information and publicity that during the audits of the project implementation the EU puts a great emphasis on the realization of the information and publicity requirements. One of this instrument is the control of the adequacy of the **billboards and commemorative plaques** that have to be erected on the project site. The mistake means irregularity and can lead to pay back several millions of euro.

In certain elements the **regulations** for the Cohesion Fund are not so strict as for the ISPA, but exactly, the different regulations make the requirements confusing for the institutional actors. It makes the situation even darker as there is no person appointed at the European Commission to be responsible for the communication, who should give advice when a question arises. And besides that, it is obvious that the political elite likes using the EU support as a tool to their popularity and therefore the Community requirements fall into the background.

With the aim that the institutional actors see and understand better their obligations, the **Cohesion Fund Communication Working Group** has been operating since February 2004. Its members are the representatives of the CSF Managing Authority, the IBs and the ImpBs. The themes of the sessions are the horizontal questions related to the communication (e.g. visual identity, legal background). But the effectiveness of the working group lags behind because at the institutions there are no experts appointed to deal with communication, the members change continuously and participate in an ad hoc way, furthermore the leaders do not take part in the work, therefore most of the initiations are not carried out.

From the draft regulation for the programming period 2007-2013, it can be seen clearly that in the future the Commission would like to put more emphasis on information and publicity.

### ***3.2.5. Risk analysis in the institution system of the Cohesion Fund***

To the effective operation we have to know those **internal and external risks** that can influence the project implementation. **The basis of the risk analysis is the project cycle** (project preparation, project implementation, monitoring, project closure, institution building tasks<sup>2</sup>), because in my opinion the risk factors can be most easily identified this way, furthermore it contains the whole preparation and implementation process. In certain project cycle elements, in the one hand, based on my personal experiences, and on the other hand based on the requirements of the regulations and the legal background, I define further groups, which are:

- Regulational background;
- Financial background;
- Human resources;
- Implementation;
- Publicity.

In the case of the implementation, I add the public procurement, which I consider as a key element in the aspect of the timely implementation and financial issues of the project. And as for the examination of the successful institution building, I completed this with the revealing of the deficiencies of the leadership and management.

I asked the colleagues of the Managing Authority to fill in the questionnaire because in the present institutional system of the Cohesion Fund, I identified this unit as the main risk-holder and risk-manager at the same time.

To measure the effect of the risk, I added a new scale e.g. in the case of the project preparation 1 is the effect of the risk if there is a maximum 2 months delay comparing to the planned date. To define the possibility of the risk between 1 and 5 was the duty of the colleagues. Based on the possibility and the effect I calculated the risk coefficient, by which it was possible to identify its seriousness level. Because of its longitude I present only the high risks in the table.

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<sup>2</sup> In the Capability management Grid of the Cohesion it is equivalent with the “management”.

**Table 1: High risk factors in the implementation of the Cohesion Fund**

**Risk values:**

Low		Medium		High	
3	5	6	10	11	15
					<b>Risk coefficient</b>
<b>Project preparation</b>					
Workflows are not harmonized or not adequately regulated					11
The Assistance Contracts are signed with delay					11
The budget is not enough for the preparation at the beneficiary level					11
Lack of quantity and/or quality capacity					11
Lack of up-to-date and precise technical planning					11
Non logical project structure					11
Delay or lack in authorization					12
Delay in the TD preparation					12
Possible protestation of the population and civil associations					12
<b>Project implementation</b>					
Liquidity problem					11
Delay in public procurement procedures					12
The public procurement procedure is attacked					11
Delay in planning, the missing permissions are not on disposal or take long time to get them					12
The co-operation between the IB, the beneficiary and the engineer is problematic					11
The financial settling is not adequate and reliable					11
The eligibility of the costs is not checked adequately					11
<b>Monitoring</b>					
Lack of the control of publicity requirements					11
<b>Project closure</b>					
The GCO does not give the final declaration					12
Lack of commemorative plaque					11
<b>Operation and development of the institutional system, trainings</b>					-

According to the risk analysis it is clearly identifiable that:

- In the future, a special emphasis should be put on the control of the adequate process of the project preparation, because the highest risk factors can be found in this group. Among them **I underline the lack of the harmonization and adequate regulation of workflows, the lack of capacity and the possible protestation of the population and civil associations**. To solve the other risk factors I consider basically a task of programming and, only indirectly, the institution development.
- In the group of the implementation, the financial, public procurement and eligibility problems got the highest points. From an institutional aspect more attention should be paid to and regulate the **problematic co-operation between the IB, the beneficiary and the engineer**.

- As for the groups of monitoring and project closure, the risk is related to the publicity. In the one hand there are problems with its control, on the other hand with the fulfilment of the requirements.

In addition, from the aspect of my study, I would like to underline that the **human resources** as well as the **existence of the necessary regulations, manuals** got **medium risk** in every project cycle group.

#### ***Risk factors revealed by the European Union audits in 2005***

Besides the above elaborated risk analysis, I feel important to introduce the main statements, related to the institutional system, of the audits carried out by the Commission in Hungary in 2005. The visit between **11 and 15 April** focused on the adequacy of the whole institutional regulation, while the audit between **26 and 30 September** controlled the practice and regulatory background of the public procurements in the environment sector.

Though there were some minor deficiencies, the reports found the system adequate, but **the human capacity at the Intermediate Bodies got a high risk number**. Besides the report of the audit in April pointed out the **weakness of the site visits and the progress reports**.



## 4. CONCLUSIONS, PROPOSALS

### 4.1. Elaboration of regulation and the legal background

The regulations and the legal background give the basis of the operation of the institutional system. As I have already pointed out, first the recent legal background is fragmented, second it has deficiencies, third, in many cases, it does not harmonize the requirements for the Structural and the Cohesion Fund, even though from 2007 these two types of support become one. In my opinion they should be solved by a **unified government regulation**, which would extend to the institutional, financial implementation and audit areas. To elaborate this, firstly the revision of the recent legal background is needed if it helps the effective implementation of the projects. The Gov. Regulations 217/1998, 360/2004, 1/2004, 54/2005, 55/2005 and the common regulation 14/2004 TNM-GKM-FMM-FVM-PM should be unified.

We can not wait with the **appointment of the institutional system after 2007**, to see which detailed tasks should be regulated by the above mentioned, unified regulation.

During my research I also pointed out the problems related to the **public procurement** law. They should be treated, **the law must be revised** and if possible, make it simpler, user-friendly, practical manuals should be elaborated to make it better understood and hold trainings about it.

Of course besides the elaboration of the legal background, the elaboration of the **Procedure Manuals, audit trails, and guidelines** for those who take part in the implementation in the changing system is unavoidable. The manuals have to reflect the transformation of the institutional system and the new tasks. I would say that they should be preventive, I mean we should try to study how to foresee and regulate certain processes before and not after. I feel especially important to close the debate, started several years ago, on the necessity of working out Procedure Manuals for the Implementing Bodies and the beneficiaries. In my opinion the answer, especially as we know the forthcoming changes after 2007, is obvious. I consider the present system unsustainable, where only the Assistance Contract defines the tasks of the beneficiary level. In the case if there are no changes into this direction, I would suggest to think over to make them obligatory to be elaborated by legal regulation.

Besides the elaboration, refreshment of the institutions **audit trails**, I would propose its elaboration **for the whole institutional system**, too. I suggest it because in the one hand it proved to be useful in the present programming period and, on the other,, because for those who participated in the working groups it was a kind of learning process and with this method the definition of the tasks and responsibilities was based on consensus, therefore its acceptance and observance was greater.

### 4.2. Development of human resources

**The changing regulations result in the development of the human resources too**, because on the one hand, in many cases several planned reforms have not been done due to the lack of human capacity, and, on the other, Hungary can effectively use the increased support in the programming period 2007-2013, if it poses the necessary human basis. Taking into consideration the dangerous effect in the timely, quality and regular project implementation, I feel extremely urgent to elaborate a **resource plan** to assure the successful start of the projects after 2007.

During the implementation of the ISPA program the inadequacy of the human resources, the high rate of fluctuation and the lack of stability caused several problems. Therefore in the future

we have to meet the EU requirements regarding the **institutional stability**. To cancel the revealed deficiencies and to have professionally well prepared human basis behind the recent and the future implementation of the Cohesion Fund, I consider the **following tasks** related to structure development and human resources unavoidable:

- With interview and questionnaire, reveal the relationship between certain units, and identify the problematic areas;
- Analyse and reveal the functional relationship of certain institutions (at present: NDO, MoEW, MoET, MF, PA, UPCC, other professional units in the ministries, European Commission, National Railway Company, National Motorway Company, UKIG, Hungarocontrol);
- Reveal, evaluate, examine the effective connection of the human resources in the working flows.

On this basis the **Human Resources Strategy** can be elaborated with the aim to assure in quantity and quality the necessary human resources for the regular and effective implementation of the Cohesion Fund project. Therefore it contains:

- Proposal for the introduction of effective work flows;
- Identifying the goals of the institution and the decision points to reach it with the human resources necessity;
- Strategy for trainings;
- Proposal for planning the internal-external human resources;
- Proposal for the improvement the effectiveness the relations between the institutions.

Because of their measure, complexity, number and severity of regulations, the implementation of the Cohesion Fund projects require several experts with different educational background. In the following, without touching all the important points, I collected those areas that I consider especially important:

- Public procurement expert;
- Monitoring expert;
- Different engineers;
- Financial expert;
- Quality control expert;
- PR and communication expert;
- Legal expert;
- Internal auditor;
- Expert of risk management;
- Project manager, etc.

From the list, but not lagging behind the others, I would like to draw the attention to the importance of the **expert dealing with horizontal issues**. As I have already mentioned at the stage of revealing the problems, in general the leadership does not take care about this “background activity”, that, in my view, is very important for the successful implementation and operation. From the above list these experts can be the quality control and the PR and communication experts. In the institution, the task of the quality control expert is to work out certain regulations, e.g. Procedure manual, audit trail, manual for retention documents, etc.). These can guarantee the adequate operation and regulate and make clear the tasks and responsibilities of the staff. Its task can, and actually does extend, of course, outside of the institution as we have seen the Managing Authority elaborates manuals and guidelines for the whole institutional system, while the Intermediate Bodies help the work of the Implementing Bodies and the beneficiaries in the same way. In my opinion to deal with these tasks at least a full-time person is needed, but at the moment at the institutions there is nobody appointed to do this work, therefore the project managers try to deal with this besides their every day work, which leads to hurry and bad quality. Several institutions try to solve this problem by the way that



outsource these tasks. In spite of that it seems to be very comfortable, I personally would not suggest this, because:

- It is an unnecessary financial burden for the institution;
- An external company is not able to perform this or it takes a long time for it to understand the processes needed to be regulated and this study time is helped again by the project managers.

The statements written above are equivalent in the case of the PR and communication expert. At the moment there is no person appointed to do this task at the institutions.

I would place more emphasis on trainings and study of the colleagues. To achieve this, firstly the mentality of the leadership should change, as it is their responsibility to decide on the kind of training needed for the staff, and beside this they should make it possible that the colleagues participate in the training. In the selection of the trainings the legal regulations can help to define the tasks of the institutions, and on the other hand it is needed to analyse what kind of educational background, practice, language knowledge is needed to fulfil certain task.

Finally I would like to go back to the problem of the **stability**. In some cases to keep the staff is more important than their application. The good staff guarantee effective operation. To have it, good atmosphere in the working place and the minimal fluctuation are needed. In my point of view it is a big mistake of the public sector that in Hungary it is not attractive being civil servant. It is not attractive financially in the long run, the promotions are too bureaucratic and in many cases politically influenced. In the public sector the salaries are fixed, regulated by law, therefore in this area there is not so much to do, but besides the salaries other types of financial incomes, premiums should be given (e.g. supplementary wages, premiums, rewards). Beside the trainings, study tours can motivate too. I am convinced that with the adequate combination of these tools, the fluctuation would decrease, the experience would remain in the institutional system and the lack of capacity would diminish too.

#### 4.3. Development of the control system

The reliability of the control system is especially important for the EU. In addition to that, of course, it is also our interest that this area operates adequately because strong and effective internal and external control systems are needed to deal with the possible risks. Besides the treatment with the deficiencies of the present system, we have to take into consideration that in the programming period 2007-2013, the EU is planning reforms in the regulations about the control systems and one of them is the **increase of the national independence**. To sum up it can be said that **different type of audits will be needed**. For the programming period 2007-2013 we have to count with new funds and control areas, furthermore certain institutions have different ideas about their audit methods in the future. In my opinion it is not a problem, though it would be important that the present institutional system adapt the control requirements and not reverse. The European Union does not want to define the number of the Audit Authorities in the member states (it can be appointed by OPs, or there can be established a central one). But if the policy decides about appointing several audit authorities, then one, co-ordinating body should be appointed too.

Until that it would be important to develop the national control system along the following lines:

- To **harmonize the audits**, avoid the duplications, to develop a cost effective internal control system:
  - The PIFC (Public Internal Financial Control) Interdepartmental Committee should offer an adequate, wide platform for the consultation of the annual audit plans;
  - The audit reports should be registered in a common data base at the disposal for the audit bodies;

- The audit bodies should try to minimize the discharge of the audited body, the same information, documentation should be enough to submit only once to the auditors;
- The action plans and their implementation should be at the disposal of all the relevant bodies;
- Training possibilities;
- Elaborating guidelines about the treatment of irregularities and project closure;
- In consultation with the EU Commission elaboration of new accreditation criteria, establishment of an effective institutional system, appointment of audit bodies.

I have already mentioned at the problem revealing phase that besides this high level of control, the practice of the **site visits** and the **control built in the process** should be developed. To achieve this the revision and correction of the actual used reports and check lists is unavoidable on the basis of the national and member state experiences, and taking into consideration the recommendations of the EU.

I only would like to mention that to achieve that the control system function adequately, its legal regulation is needed too, which can be done by the modification of the recent Gov. Reg. 360/2004, or by the proposed unified regulation.

#### **4.4. Development of the supporting systems**

##### *Retention of documents*

According to the problem revealing, the harmonization of the retention system of the different institutions and the assurance of transparency can not wait. To achieve that, besides the **legal regulation of the requirements**, I consider important to carry out the following tasks:

- **Examination of the present retention system** related to the Cohesion Fund in the institutions;
- On the basis of this analysis, **elaboration of manual** taking into account the national and EU legal background and the characteristics of the certain institutions;
- The manual should contain **audit trail**.

Besides the elaboration of manuals maybe this is the area where the human actors play an especially important role. I mean that the manuals should build in the thinking of the colleagues, to make it part of the every day work, routine. This can be helped by **training** for the staff about the retention system, but supposly its practical use needs a longer time.

Finally, but not in the last line, I would like to draw the attention to the fact that the adequate retention system has a financial side too, the **necessary equipments** have to be bought. And the assure its financial necessity is the responsibility of the leadership.

##### *Tasks related to information and publicity*

I feel the tasks related to information and publicity an especially important area and this is not only because of the EU requirements, but as I have already mentioned, the adequate support, acceptance of the project is one of the key elements of the successful implementation and this can be achieved by informing the population and listening to their opinions. To achieve that the development possibilities and targets, including the period after 2007, be well known and accepted, I would suggest to think over the following ideas:

- The development areas should be clear and should be communicated;
- The expected changes after 2007 should be clear and should be communicated;
- Tasks and responsibilities in the area of communication should be clear (e.g. by modifying regulations, elaboration guideline);
- The publicity of the approved projects should be assured (e.g. website);

- The project selection criteria should be objective and therefore easily communicated, defended;
- The population should be informed adequately about the support possibilities, their connections, it should be made clear e.g. by manual, guideline how and where can take part of it, or a data base should be created on the Internet where all the national and EU support systems can be seen;
- The social consultation should be assured, the green and civil associations should be involved in the preparation and implementation processes e.g. there should be regular partnership conferences, interactive websites;
- In the site visits the control of the PR activities should be emphasized better, especially the billboards and the commemorative plaques;
- The leaders should put more emphasis on the tasks related to publicity, should support the work of the Cohesion Fund Communication Working Group and appoint responsible person for the communication.

Finally I would like to mention the problems arising in the field of information and consultation during the **project preparation**. As I have written at the problem revealing, it would be important to assure financial sources to support the communication activities in this project phase. To solve this problem in the short run I would suggest that **the Managing Authority should assure this amount of money for the Intermediate Bodies**. And beside this the municipalities should live with the opportunity offered by the **municipality law**, that offers the initiation of **local referendum** about the certain project.



## 5. SUMMARY

The first part of the dissertation introduces the regional policy of the European Union, emphasising the importance of the Cohesion Fund. The history of the cohesion policy, the introduction and evaluation of the Funds and the overview of the reforms expected after 2007 point out the role of these supports in the growth of national economies in the Member States.

From 2007, besides the simplification of the programming system, Hungary has to be prepared to deal with increased amount of support, changed and expanded supported areas and greater national independence. However the country can live with these opportunities only in the case if it knows and adequately prioritizes its facilities and needs and is able to enforce its well defined interests. To achieve a good result in the absorption, the establishment of a stable and effective institutional background and the development of the current system are unavoidable. The national **preparation for the period 2007-2013** has two dimensions: **programming**, which means the elaboration of strategic documents, and paralel with it the establishment and reform of the **institutional system** that supports and helps the implementation. The study puts the emphasis on this second component, analyses it and gives advice with the aim of increasing the efficiency.

As the **Hungarian institutional system is extremely divaricate and has been changing continuously** since the change of the regime, and the high rate of fluctuation is a permanent phenomenon, the study examines one piece of the institutional system. This piece is the Cohesion Fund, the most stable institutional system, therefore further conclusions and suggestions are based on its analysis. The dissertation examines the institutional system along three lines:

1. Background of the establishment of the current system;
2. The operation of the current system;
3. Suggestions for the development of the institutional system.

Finally I would like to end my dissertation with the though that the **development of the institutional system is a continous, endless task**, which is based on its flexibility and renewal ability. Because of the changes of the internal and external environment, its situation can not be static. To be able to accomodate and deal with the moving challenges, it is important having an institution above the whole institutional system, which main task is the co-ordination, the elaboration of the legal background, the definition clearly the tasks and responsibilities for the actors in the institutional system. In spite of that the study concentrates on the analysis of the Cohesion Fund, I consider the conclusions and proposals useful for the successful and effective implementation of any kind of national, EU, international supports.



## 6. PUBLICATIONS

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