

Journal of Turība University

# Acta Prosperitatis



7

ISSN 1691-6077

**Journal of Turība University**

# **Acta Prosperitatis**

**No. 7**

**ISSN 1691-6077**



Rīga 2016

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Publisher Turība University, Ltd.

Head of Publishing House **Daiga Rugāja**

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# CONTENT

Introduction .....	4
THE DOMINO EFFECT IN RISK AND CRISIS COMMUNICATION IN THE CONTEXT OF ITS LEGAL ASPECTS .....	7
<i>Derkevica-Pilskunga Jolanta</i>	
IMPROVEMENT OF NOTIONAL DEFINED CONTRIBUTIONS OLD-AGE PENSION SCHEME FOR ENSURING PENSION SUSTAINABILITY .....	24
<i>Dundure Ināra</i>	
MULTICULTURALISM IN THE WORLDWIDE MIGRATION CONDITIONS .....	42
<i>Gražulis Vladimiras</i>	
EVALUATION OF NON-FINANCIAL SOCIAL ASSISTANCE TO FAMILIES IN CHILD DAY CARE CENTERS: SITUATION ANALYSIS IN LITHUANIA .....	59
<i>Gražulis Vladimiras, Čižikienė Janina</i>	
INFRASTRUCTURE FUNDING FOR SUSTAINABLE DEVELOPMENT OF RAILWAY TRANSPORT IN LATVIA .....	75
<i>Jurušs Māris, Landmane Līva, Ivanova Anastasija</i>	
COMPARISON OF THE RETAIL EFFICIENCY INDICATORS IN THE BALTIC STATES .....	89
<i>Liniņa Iveta</i>	
INTELLECTUAL CAPITAL AS A FACTOR OF ECONOMIC DEVELOPMENT OF UKRAINE.....	104
<i>Masлак Olga, Grishko Natalya, Hlazunova Olha, Masлак Maria</i>	
INTERCULTURAL COMPETENCE IN MULTICULTURAL ORGANIZATIONS .....	119
<i>Namatēvs Ivars, Turlais Viktors, Dubkēvičs Lotārs</i>	
INNOVATIONS IN PUBLIC PROCUREMENT .....	132
<i>Skrastiņa Una, Gaile Džeina</i>	
SOURCES OF ADMINISTRATIVE LAW IN LITHUANIA AND LATVIA .....	153
<i>Urmonas Algimantas, Načisčionis Jānis</i>	
Kopsavilkums .....	171

## INTRODUCTION

**Aldis Baumanis**, Dr. paed.

Editor-in-Chief of the Journal of Turība University

*Acta Prosperitatis*, No. 7

To win in marketplace, organizations must move faster entering new markets, being more competitive and accessible to clients, launching new, innovative ideas, and offering better prices. It means we all live in a complex world to be dictated by many changing patterns in business environment. Business environment builds on the proposition that is not necessarily in equilibrium. Organizations, firms, consumers constantly change their strategies, tactics and actions in response to the developing set of contingency, openness to change and indeterminacy.

Current circumstances affect conditions that determines what might come next. Business is a system whose building blocks are constantly updating their behaviour based on the present situation. The priorities of scientific and business research are changing along with the development of national politics and economy. Now it is shifting towards seeing these changes as a series of denoting actions – to innovate, to be effective and productive,

Readers of this volume of *Acta Prosperitatis* can get acquainted with the authors' views regarding the key elements of today's business environment, i.e. regulatory requirements, change management, the importance of culture, as well as business process modelling and value creation for organizations.

**Jolanta Derkeviča-Pilskunga** in her article "The Domino Effect in Risk and Crisis Communication of its Legal Aspects" examines the problems of effective communication when companies have come to downturn of their business activities. Accurate and timely communication in which all units of the business entity take part together, alongside a sound risk management mitigation process, can be used to decrease the influence of negative factors. Special attention has been paid to the evaluation of domino effect on the business factors that can exercise influence on Latvian small-sized companies.

"Improvement of Notational Defined Contributions Old-age Pensions Scheme for Ensuring Pension Sustainability" is a research conducted by **Ināra Dundure**. The author assesses global notational defended contributions (NDC) old-age pension schemes in Europe, as well as the criteria of sustainability. Based on the measures taken, improved and sustainable old-age pension scheme has been developed and offered.

Globalization and worldwide contacts between organizations, companies and individuals have given rise to the need to be able to manage migration flows in a successful way. **Vladimiras Gražulis** in his paper "Multiculturalism in the Worldwide Migration Conditions" presents the trends of interculturalism development in the world of today. The paper presents approaches of foreign and Lithuanian scholars and international organizations (UN, UNESCO, etc.) to the phenomenon of interculturalism and trends of its expression in contemporary society, and analyses the results of an empirical study of 2015 with about 1100 participants.

The paper "Evaluation of Non-Financial Social Assistance to Families in Child Day Care Centers: Situation Analysis in Lithuania" by two authors **Vladimiras Gražulis** and **Janina Čižikienė** shows how non-financial social assistance can help the disadvantaged families and their children, and in child day care centers. The paper demonstrates the necessity of improving the process of providing non-financial assistance in child day care centers. The results of the research also reveal the possibilities of organizing and improving the process of providing non-financial assistance in child day care centers in Lithuania.

Railway has a significant role in transportation industry. **Māris Jurušs, Līva Landmane** and **Anastasija Ivanova** in their paper "Infrastructure Funding for Sustainable Development of Railway Transport in Latvia" analyse the current trends in the railway transport and logistics sector in accordance with the EU development strategy "Europe 2020" – to make carriage by railway more competitive than road transport. The authors suggest redistribution of the revenue from excise duty on diesel used in rail transport to finance the maintenance and development of railroad infrastructure.

Efficiency and productivity are the major drivers of competitive economy, including retail industry. **Iveta Liniņa** in her article "Comparison of the Retail Efficiency Indicators in the Baltic States" uncovers and compares efficiency indicators among the Baltic states. The main conclusion of her research is that to ensure competitiveness the retail businesses have to carry out their operations as efficiently as possible and evaluate the flow of investment.

Social phenomena have an essential role in the economic development of any country. The paper "Intellectual Capital as a Factor of Economic Development of Ukraine" by **Olga Maslak, Natalya Grishko, Olha Hlazunova** and **Maria Maslak** analyses intellectual capital. The basic components of development and improvement of the effectiveness of realization of the intellectual capital as a factor of decreasing the effects of economic crisis and speeding up the future development of Ukraine have been studied. The main factors of *formation and development of intellectual capital* of Ukraine are strengthening of innovation, investment activities, and formation of stable legal system to support them.

**Ivars Namatēvs, Viktors Turlais** and **Lotārs Dubkēvičs** in their paper "Intercultural Competence in Multicultural Organizations" present the results of the empirical study relating to business process modelling paradigm. The authors of their scientific paper propose a new model of evaluation of the intercultural competence level among companies which are located in different countries. The objective of their research is to provide a deeper insight into the problem to assist other researchers of the intercultural competence evaluation by reflecting differences between cultures and finding ways towards efficient collaboration and diverse business environment.

Innovation and creativity still, and, presumably, will play, an important role in many industries and businesses. The paper "Innovations in Public Procurement" by **Una Skrastiņa** and **Džeina Gaile** within the scope of innovation inspects political and legal documents, especially, the new Public Procurement Law of Latvia. The authors suggest that not only a new regulation is needed, but also a clear understanding how to introduce knowledge and know-how. Twisting together technical and legal aspects could drive innovation and help to achieve the established goals of organizations.

The administrative law plays an important role in the legal environment of any country. **Algimantas Urmonas** and **Jānis Načisčionis** in their article “Sources of Administrative Law in Lithuania and Latvia” present a historically comparative analysis of the development of administrative law in Lithuania and Latvia. The paper conveys the opinion that there are differences in constitutional regulation in Lithuania and Latvia for the hierarchy of legal acts; thus, in the Constitution of the Republic of Latvia there is no legal norm on legal acts as it is done in Article 7 of the Constitution of the Republic of Lithuania.

As editor-in-chief, I would like to express hope that the present volume 7 of the *Acta Prosperitatis* will be received and read by the community of business researchers and managers, as a result enabling better organizational and business management decisions.

## THE DOMINO EFFECT IN RISK AND CRISIS COMMUNICATION IN THE CONTEXT OF ITS LEGAL ASPECTS

Jolanta Derkevica-Pilskunga, Mg.soc., Latvia

### ***Abstract***

*The aim of this article is to explore to what extent communication as a business factor influences risks and crises in Latvian businesses in the context of the domino effect and legal aspects*

*In this article, a pilot research poll was to determine the views of companies in Latvia. 70 small companies with fewer than 10 employees were involved, and 50 answers were received from them. The author of the article posed questions to get the necessary information, as inquiry method ranks among the most popular research methods. Inquiry methods are basically used to research information in which the data carrier is a human being. The author used both unstructured and structured answer options. Structured questions were mostly dichotomous with ready answers and answers on a scale. The author used dichotomous answers. 93 of the 100 questionnaires were completed.*

*A domino effect has speed and time distance and force, as well as communication in terms of quicker speed, closer time, and more power force, and, according to Nelms (1992), it consists of four causes – the root cause, latent causes, human causes and physical causes, with latent causes very often provoking crises as they are based on a spokesperson's lies in a manner that could influence the company's reputation (Jolanta Derkevica-Pilskunga, 2016). According to Schmitt-Geiger (2013), "litigation public relations are used in all kinds of legal disputes". It means that companies facing crisis should comply with the law. That is why focus on law in communication is important but it cannot be a chaos. In risk and crisis communication some frames are necessary, and there is a need for a general legislative system for any company when it comes to risk and crisis situations to avoid harm to human lives and other resources. This could be a law related to risk and crisis communication. The target of the law must be to avoid the domino effect or chain that influences other companies, audiences and states in crisis situations.*

**Keywords** – risk and crisis communication, domino effect, legal aspects



## **Introduction**

The legal aspects of communication related to the risk and crisis management of Latvian organisations have not been studied since 1990 in Latvia. There have been studies regarding labour risks, natural disaster risks, communication risks among public and different institutions in Latvia, but there have been no studies done on the legal aspects of communication related to risk and crisis management. Almost any risk is part of everyday life. These could be safety, technology, operational etc. risks. Many different types of risks and crises can be encountered by businesses. Some have a minimal impact and can be managed easily, while others may create threats against the organisation's existence in the long term. Both could cause a domino effect and concern stakeholders. An understanding of the principles and processes of effective risk communication management helps business owners take the necessary decisions to ensure the best possible outcome for their businesses. Communication is a concept that is difficult to place in a normative framework, although there are such frameworks. The concept of "legal aspects" in the field of communication is complicated because there has never been a serious crisis in this regard in Latvia. There are, however, gaps in Latvian norms, which means that Latvian organisations are learning to manage risks and crises now.

According to Schmitt-Geiger (2013), "litigation public relations are used in all kinds of legal disputes. For companies, it may become relevant in corporate law disputes such as product liability suits, capital market lawsuits, insolvency proceedings and employment law disputes". The situation in Latvia is similar. Companies facing crises in the field of PR comply with law, and if the focus is on board members, criminal and civil proceedings are also important.

The domino effect is a phenomenon that can expand the crisis. For example, one accident may cause another one. The domino effect, benchmarking, reputation and ethics are concepts connected to risk and crisis management processes and communication therein. Communication is a process that can cause the domino effect and result in a permanent crisis. The domino effect is a process in which one event triggers a chain of similar events (similar to one falling domino that causes the whole row to fall). A hazardous event or negative news about one member of society causes pressure on the reputation of other, similar members of society. A crisis involves the perception of an unpredictable event that threatens the important expectancies of stakeholders and can have a serious impact on the relevant organisation's performance and generate negative outcomes. The outcome of a crisis can be a scandal and there have been such scandals in Latvia. Communication represents a liaison between various elements. Crises are unpredictable, but not always unexpected. Wise organisations know that they will eventually face a crisis, but they do not know when that will happen. Crises appear suddenly and with an element of surprise and unpredictability. Crisis situations can appear in companies with what is known as the speed of the domino effect. This refers to a situation in which one accident causes another one. In most cases, the speed is very fast and hard to control. Bad communication can influence the speed and, accordingly, the reputation of the company. Are company managers aware of this? The pilot study conducted by the author of this article (Derkevica-Pilskunga, 2008) suggests that the reputation of a company can worsen if bad

messages are hidden from employees. The pilot research done led the author to explore the topic in greater depth. An important issue is how Latvian legislation influences the risk and crisis processes and the way in which these are managed.

### **Methods of research**

In the present article, a pilot research poll was to determine the views of companies in Latvia. 70 small companies with fewer than 10 employees were involved, and 50 answers were received from them. There were three questions – does communication influence the reputation of your company?, Have you noticed the “domino effect” in the case of a permanent crisis at your company and can your company’s reputation worsen if only staff members are aware of a bad message? A survey that involved an interview of 100 company directors identified opinions about risks and their legal aspects in Latvia. The companies had suffered risks or even crises. The author posed questions to get the necessary information, and the inquiry method used ranks among the most popular research methods. Inquiry methods are mainly applied to research information in which the data carrier is a human being. This helps to find information about reasons, interests, plans, emotions, relationship structures, family life, etc. The aim of this inquiry was to collect information about risks and crises, as experienced by companies. The process involved three parts. First, there were contact questions to increase the interest of respondents in the inquiry process. These questions were easy and understandable. Next came the most complicated questions to clarify the thoughts of the individual, followed by the most easily formulated questions. The author suggested both unstructured and structured answer options. Structured questions were mostly dichotomous with ready answers and answers on a scale. The author used dichotomous answers. 93 of the 100 questionnaires were completed.

To examine deeper aspects of risk and crisis communication laws and practices, the author interviewed directors of bankrupt companies, as well as directors of companies that had undergone crises in Latvia. The interview involved a set of questions and a dialogue so as to gain in-depth information about the issue. The interview method is a popular research method and is used to research more in-depth information.

## **1. The domino effect in risk and crisis communication**

Risks and crises are very closely related to the domino effect, which means that any crisis situation can spread. Firstly, it is important to eliminate the phenomenon, and that is true at this time in Latvia, too. A crisis at one company can influence other companies. The present article describes and analyses the domino effect in risk and crisis communication in detail. The purpose of the article is to analyse the essence of domino effect theories, to discuss the pilot project "Influence of the Domino Effect" and the results obtained, as well as the judicial aspects of risks and crises insofar as they affect companies.

One could say – a chain of cause and consequences here, one that is indefinite and without any initial point. When it comes to the domino effect, a domino is a small, rectangular block. If you line up many dominoes and then push the first one, they will all fall down, one after another, with the first domino knocking down the second one, the second one knocking down the third one, the third one knocking down the fourth one, and so on. If one of the dominoes in the line falls independently and without the help of others, then the domino effect is not observed. The whole line, then, would be in a perpendicular state. The main point here is that there must be the King of Cause, because otherwise nothing will happen. If this aspect is compared to communication in companies, then it can be concluded that the communication of bad management and the domino effect can cause a permanent crisis. In this situation, dominoes would be in the internal or the external environment of the company. For instance, a pharmaceutical company may find unhealthy substances in vitamins before the drugs are sold.

### **1.1. The essentials of the domino effect theories**

From a historical point of view, the domino effect theory is related to the foreign policy between the 1950s and 1980s. Promoted at times by the government of the United States, it posited that if one country in a region fell under the influence of Communism, then the surrounding countries would follow in a domino effect. The domino effect suggests that a change, albeit a small one, will cause a similar change nearby that will then cause another, similar change and so on in a linear sequence, the analogy being a falling row of dominoes. The theory was used by successive US administrations during the Cold War to justify the need for American intervention around the world. Referring to Communism in Indochina, US President Dwight D. Eisenhower formulated the theory in words during a news conference on April 7, 1954: "Finally, you have broader considerations that might follow what you would call the 'falling domino' principle. You have a row of dominoes set up. You knock over the first one, and what will happen to the last one is the certainty that it will go over very quickly. So you could have a beginning of a disintegration that would have the most profound influences." (Stacey, 2003)

The domino effect is found in many different instances. More often the major accidents have resulted in substantial harm to human lives and other resources have involved the domino effect. This can happen in various ways, though an essential aspect is always the issue of whether it involves a single factory or progresses from one factory, where the accident occurred, to others. In line with

this criterion, Reniers (2010) identified two categories of domino effects – internal domino and external domino. Internal (single-company) domino effects mean that the escalation of an accident occurs within the boundaries of a chemical plant. In external (multi-company) domino effects, one or more secondary accidents occur outside the boundaries of the factory where the primary event occurred. External domino effects often have more severe consequences than internal domino effects do, as the affected area is larger, and more equipment is involved (Darbra, Palacios, 2010). A number of domino effect definitions have been proposed. Reniers (2010) has listed 13, some of which are very concise (e. g., “an event at one unit that causes a further event at another unit”, while others are more complex. Most of these definitions contain the following three concepts:

- 1) A “primary event” such as a fire or explosion in a specific unit;
- 2) The propagation of the accident to one or more units or plants in which “secondary” accidents are triggered as the result of the primary event;
- 3) An “escalation” effect, which leads to a general increase in consequences, with secondary accidents being more severe than the primary one.

Among the various definitions of the domino effect that have been proposed, the one by Delvosalle (1996) covers these three aspects and seems suitable for the present survey: “A cascade of events in which the consequences of a previous accident are increased, both spatially and temporally, by the following ones, thus leading to a major accident.” This is the definition used by the author as a framework for the selection of accidents. The domino effect is a highly important phenomenon in the processing industries and was specifically addressed in the first version of the Seveso Directive (European Council Directive 82/501/EEC), in subsequent versions of the directive, in Directive 96/82/EC, and in Directive 2003/105/EC. These stipulated that domino effect hazards must be assessed both within and outside of industrial installations. The Seveso Directive obliges the member states to ensure that operators have policies in place to prevent major accidents. The subsequent version of the directive speaks to control major accident hazards involving dangerous substances. This amended and subsequently repealed the previous directive. The Directive 2003/105/EC, in its turn, is about the control of major-accident hazards involving directive substances. The domino effect is an important aspect of risk analysis, as knowledge of the main hazards and features of this phenomenon can be used to identify additional safety measures such as the minimum safe distance between certain types of equipment.

Several authors have analysed aspects of domino accidents. Bagster and Pitblado (1991), and Khan and Abassi (2001) analysed their frequency and likelihood. Cozzani and Salzano (2004) studied the contribution of a blast wave as a primary event and proposed threshold values for process equipment and models for various categories of equipment. Antonioni, et. al. (2009) developed a methodology for the quantitative assessment of the contribution of domino effects towards overall risks in an extended industrial area. Reniers, et. al. (2005) analysed the efficiency of current risk analysis tools in preventing external domino accidents. The same authors also proposed a technical framework to integrate three risk analysis methodologies to prevent external domino accidents. Cozzani, et. al. (2007) emphasised the importance of combining inherent safety criteria with conventional protection of an active and passive nature. It is important to filter in risk and crisis

management or risk or crisis with the domino or non-domino effect. If this involves the domino effect, then there is a need for a different management and communication plan. If an accident occurs and, as a result of this, another accident (secondary event) occurs temporally or spatially, then the scenario is considered to be a domino effect.

If an accident or risk involves the domino effect, then it is necessary to calculate the real distance and the effect distance. These numerical values represent the relative level of importance of the pairs of installations with respect to the danger of inducing or continuing domino effects. The measurement of distance is important in decision-making in the area of safety management. It means that risk and crisis communication plans for companies must include real domino effect data, connecting these data with real decisions. This is easier for decision-makers, because human beings have biologically programmed feelings. According to Wills (2001), feelings act as instincts and explain most of the behaviour of human beings and other species of animals. Crisis situations often involve chaos, and decisions are taken in a big hurry and mostly on the basis of instinct. These instinctive decisions usually are not good for a company in question, because they are not based on theory and could have bad effects in future. That is why planning the risk and communication is needed.

The domino effect can occur in risk and crisis management of a company's internal and external environment and have three phases – an event, its propagation, and its escalation. Effect speed and time distance are important in all of these phases. According to Nelms (1992), the domino effect theory has four causes – the root cause, latent causes, human causes, and physical causes. Very often lawyers cause commotion in crisis situations because of delayed communication in the crisis or pre-crisis phase. This results in a loss of corporate reputation. When lawyers tell the truth, the domino effect very often influences the reputation. During the pre-crisis phase, it is very important to analyse root causes, because that helps to avoid the domino effect.

Bad or unplanned communication will mean that this information pervades the internal environment of an organisation, thus causing stress and rumours. Rumours appear when information is not disseminated in a sufficiently precise and transparent manner. The “dominoes” in the organisation will be the formative elements of the internal environment – aims, staff, structure, corporate culture and technologies.

Bad communication can influence each of these elements in relation to the domino effect. The information is spread more extensively in the directly and indirectly influenced environment of a company, which means that directly influencing factors reach suppliers, consumers and competitors, influence the mass media, and lead to changes in normative acts. This practice in several countries suggests that normative acts are sometimes based on facts which have malevolent influences on society.

In Latvia in autumn 2009, for instance, the Tele2 mobile phone company organised a fake meteor crash in the area of Mazsalaca, as the marketing and commercial director of the company, Jānis Spogis, has testified. Many rescue services were involved in the investigation of the “meteor,” and that cost a lot of money. In response to this, the government passed a series of legislative amendments. The

company gambled its reputation by deliberately misleading people, and there were no sanctions against it, because the law did not speak to such processes. The company instead attracted attention and increased its client numbers. The case was a deliberate promotion campaign. Yes, there were communication with society, but the domino effect very quickly distributed the information, and the reputation of the company was exposed to risks. Legal regulations are a traffic circle, but they will be amended. The management of reputation risk, moreover, is divided into components such as crisis and situation management, as well as social responsibility. In most cases, a crisis is seen as the biggest threat to the reputation of a company, and many companies are prepared for crisis management. Companies are often prepared for crises, but they are not ready to encounter the reputation hazards or the elements thereof. Corporate reputation expert Andrew Griffin has argued that “crisis situations that are faced by companies are more easily managed than those that are created by the companies themselves.” In this case, Tele2 probably did not realise that the fake meteor could cause a permanent crisis in terms of creating reputational risks in relation to the speed of the domino effect.

During the 2008 crisis of the Parex Bank, which the Latvian government took over, the domino effect involved the mass withdrawal of people’s savings. The government initially spoke of an investment of LVL 200 million, though a few days later it was clear that more money would be needed. People who discussed the “anchor” of stabilisation asserted that this would only be the beginning, and they predicted that the government would have to invest a billion or even two billion lats to rescue the bank. The government was responsible for analysing provisions related to the bank’s takeover. Banks that are based in Scandinavia have announced government guarantees, but the natural avalanche of cash withdrawal would lead to a sad situation. Any bank faces a crisis if depositors band together in withdrawing their savings. In the case of the Parex Bank, it could be concluded that rumours and communication had an effect on indirectly influencing the company’s external relations in the sense of international relations, the country’s economic situation, sociocultural relationships, government policies, science and technologies.

Among challenges that are posed by the risk of accidents, the most vexing one is the prevention of secondary or “knock-on” accidents, i. e. , one accident creating grounds for another. Forecasting and preventing a stand-alone incident is in and of itself fraught with great complexity and uncertainty; any attempt to deal with the probability of “knock-on” accidents and their consequences must content with even greater complexity. This is perhaps why much less work has been done in terms of studying the “domino effect” that is caused by knock-on accidents, as compared to stand-alone ones (Abdolhamidzadeh, 2010).

## **1.2. Avoiding the domino effect in the post-crisis phase**

Many financial crises in the world have been followed by the domino effect. Post-crisis management and communication is necessary to avoid this strategic post-crisis. According to Faganel (2011), the financial crisis in the United States in 2007 was followed by a domino effect that caused global loss of ethical values when pursuing monetary health. Individual citizens who had heard preachers saying that it is alright to spend money and to be indebted were suddenly faced with

disillusionment and sobering. Clear actions are very important to avoid the domino effect's "alarm management".

According to Nelms (1992), the domino effect theory consists of four causes – the root cause, latent, human and physical causes. The author of the present article has referred to "physical, human and latent causes" on several occasions. The domino theory helps to explain these three levels of causes. The physical cause of the failed shaft is "fatigue." It also suggests that someone did not align the shaft properly (the human cause), which results in fatigue failure. Finally it is argued that the person did not think that he had time to align the shaft properly – the latent cause (Nelms, 1992). Latent causes in terms of crisis communication usually address attitudes, assumptions and beliefs, or the way in which our businesses that contribute toward the human cause. Nelms describes latent causes as generic and argues that they are "carried around" inside of people's heads. They affect many or all actions, not just the one that caused that particular failure. Lawyers very frequently create latent causes, e. g., being too late in terms of communication during the crisis or pre-crisis phase. When layers relate to truth, the domino effect very often influences reputation. During the post-crisis phase, analysis of the root causes is very important, because this helps to avoid the domino effect.

### 1.3. Results of the research "The Influence of the Domino Effect"

Figure 1 shows that 32 of 50 respondents said that communication does influence the reputation of their companies, 13 denied this, and five did not have an answer. Thus the research project shows that communication does have an influence on reputation.

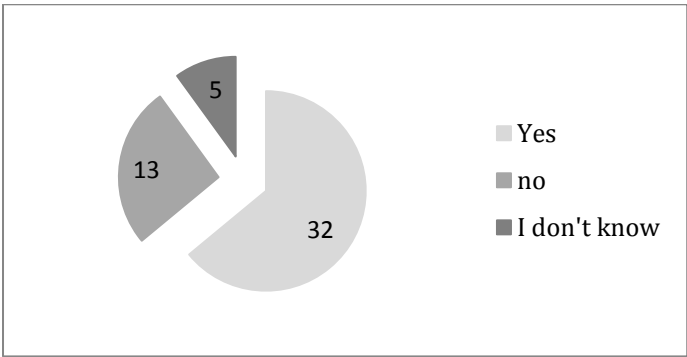


Figure 1. Does communication influence the reputation of the company?  
(Jolanta Derkevica-Pilskunga, 2016)

Figure 2, in its turn, shows that 35 entrepreneurs are unaware of whether they have noticed the "domino effect" during a permanent crisis at their companies. Ten respondents said that they don't believe that it has been noticed, while five said that it has been noticed.

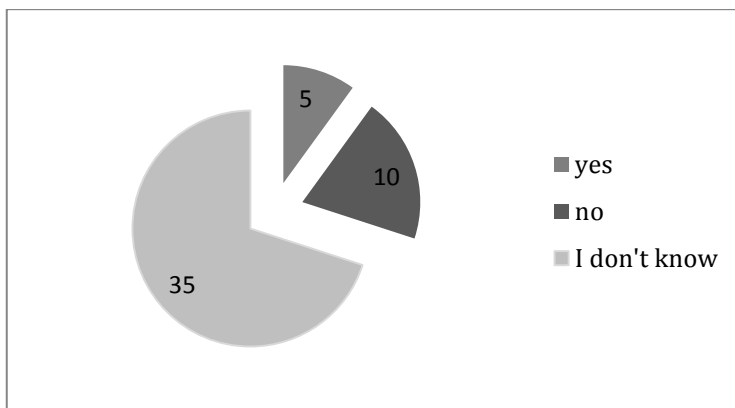


Figure 2. Have you noticed the “domino effect” in the case of a permanent crisis at your company? (Jolanta Derkevica-Pilskunga, 2016)

Figure 3 shows that 29 entrepreneurs believe that the reputation of their company can worsen because the relatives of employees can deliver information to the mass media, consumers, suppliers and competitors. Another 13 believe that the reputation can worsen because employees themselves can deliver such information, while eight argue that it cannot, because employees do not do so. This means that the large majority of respondents – 42 – agree that reputation can worsen because of the activities of employees and/or their relatives.

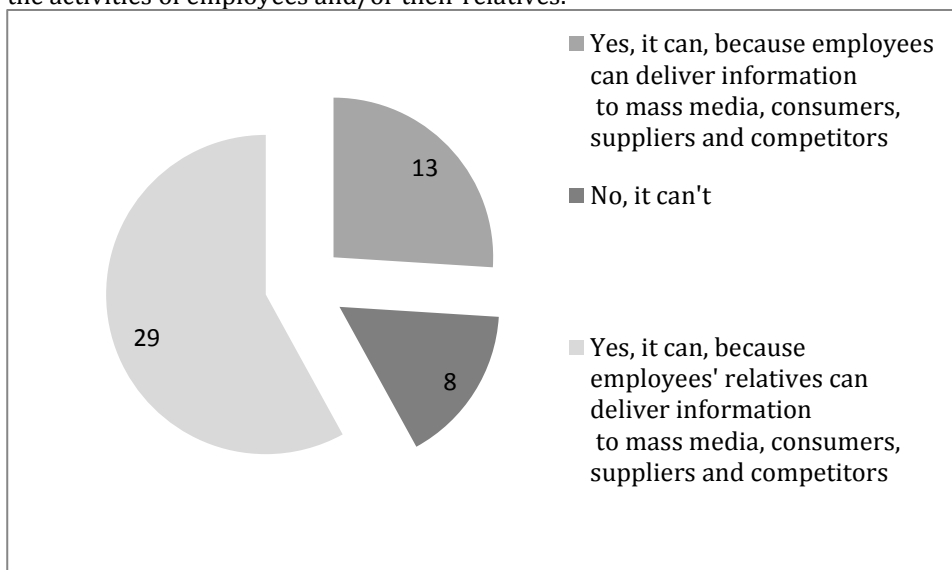


Figure 3. Can your company's reputation worsen if only staff members are aware of a bad message? (Jolanta Derkevica-Pilskunga, 2016)



This pilot research helped the author to identify the standpoint and knowledge of companies about communication that can influence their enterprises. The main conclusion from the pilot research is that reputation can be influenced in risk and crisis processes. Indeed, a company's reputation can be destroyed in a matter of mere seconds. A mishandled response, inappropriate act, labour dispute, product tampering, or poorly timed reorganisation can instantly tarnish a sterling reputation that has been built up thanks to stellar performance and hard work. A well-managed and reputation-conscious company, however, does not have to be defenceless when faced with a damaged reputation.

### 1.4. Results – Legal aspects of risk and crisis communication in Latvia

The results show that 64 of the responding companies were five years old or younger, 17 were between 6 and 10 years old, 10 were between 11 and 20 years old, and two were more than 21 years old (Figure 4). Companies in Latvia tend to be rather young because the country regained its independence only in 1990.

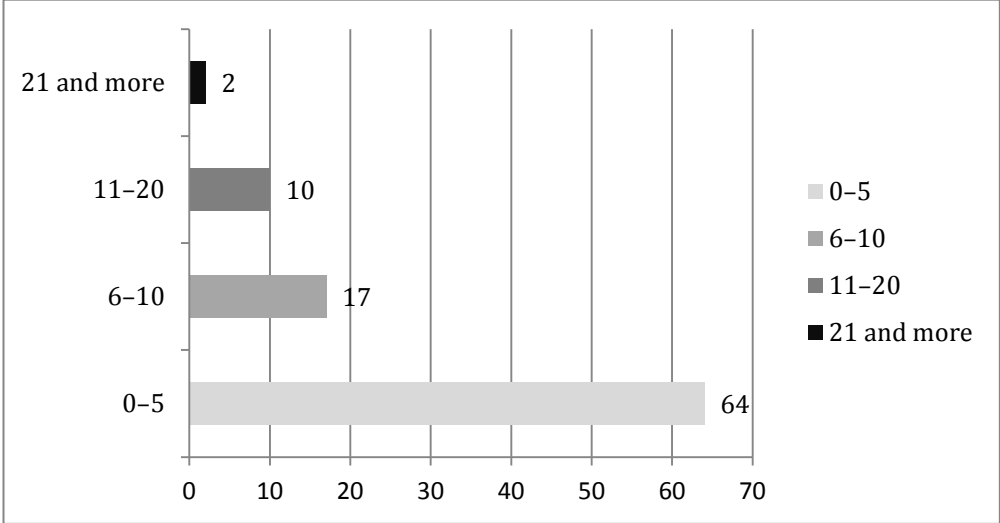
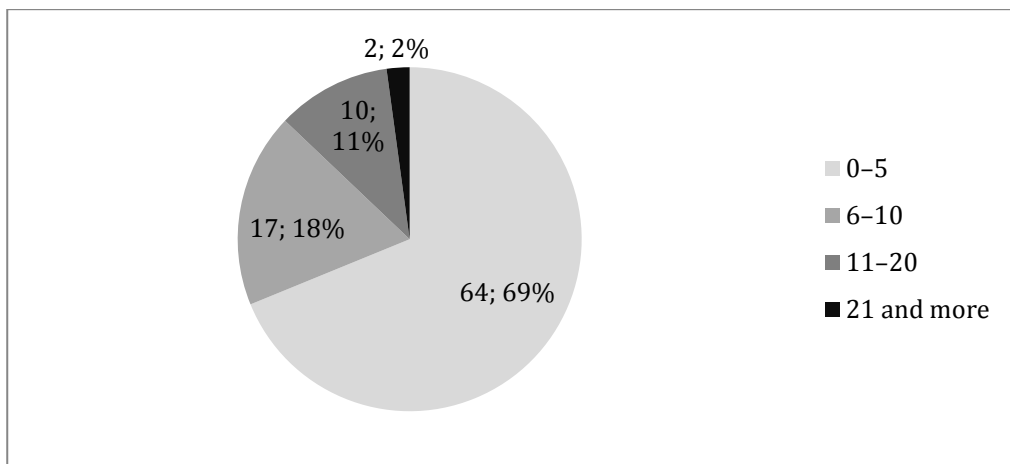


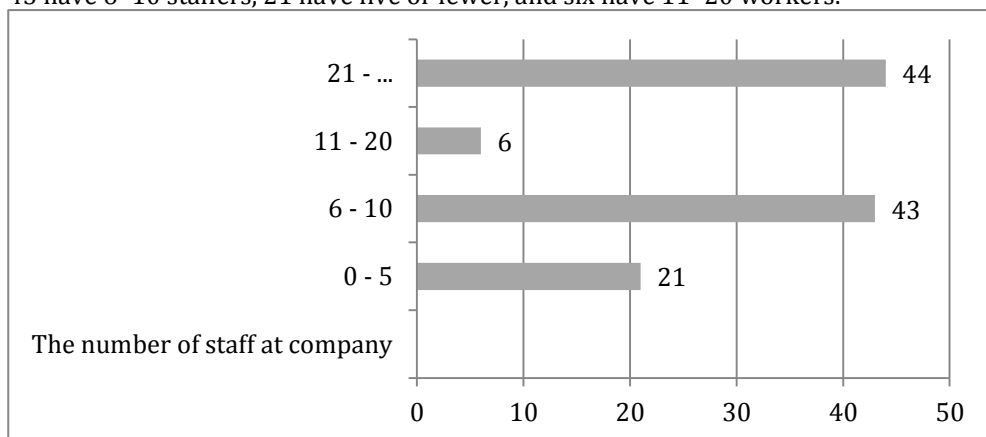
Figure 4. The age of responding companies (Derkevica–Pīlskunga, 2016)

Figure 5 shows the distribution of companies by age, with most being five years old or less (64.69%), 17.18% being 6–10 years old, 11% being 11–20 years old, and 2.2% being 21 or over. The companies all were from the manufacturing and service sectors.



*Figure 5. The age of responding companies (percentage)*  
(Derkevica-Pilskunga, 2016)

Figure 6 shows that 44 of the responding companies have 21 or more employees, 43 have 6–10 staffers, 21 have five or fewer, and six have 11–20 workers.



*Figure 6. The number of staff at responding companies*  
(Derkevica-Pilskunga, 2016)

In terms of percentages, 39% of responding companies had more than 21 employees, 38% had 6–10, 18% and five or fewer, and 5% had 11–20 staffers.

The research data show that the largest number of companies (91) reported financial risks, 78 had experienced commercial risks 68 had undergone legal and regulatory problems, while 62 had faced reputation risks. 59 companies had problems with service delivery, 47 with internal organisation, 43 with projects, 12 with equipment, 9 with strategic technologies, 6 with security, 5 with stakeholder management and 2 with other issues.

Eddie Bensilum from Regester Larkin focuses on corporate reputation and crisis management as a crisis management consultant as part of a corporate communication module. The first point raised by Eddie is that “as public relations practitioners, we need to educate clients on the difference between an issue and a crisis.” She argues that the difference can be understood on the basis of five parameters such as speed, surfacing, scrutiny, structure and stance. A crisis erupts quickly and suddenly, and demands intense scrutiny, while an issue develops gradually and generates sporadic interest on the part of an audience. An organisation’s structure needs to be rigid during a crisis, but, on the other hand, it should be fluid in the case of an issue. The stance should be reactive in a crisis situation, whereas in the case of an issue, an organisation should be proactive. Although this fundamental difference should be kept in mind by public relations practitioners before they formulate crisis communication plans, they must first understand the relationship between the two. (Kapoor, 2010) By this, the author means that crises and issues are not two entirely different entities; they share a deep relationship instead. One can say that if an issue is not managed in a timely manner, it can turn into a crisis.

## **2. The influence of legislation on the risk and crisis communication in companies under the domino effect**

The legal aspects of risk and crisis communication influence companies in terms of all risk management elements that are the organisation’s strategic objectives, including risk assessment (risk analysis, risk identification, risk description, risk estimation), risk evaluation, risk reporting, threats and opportunities, decisions, risk treatment, risk reporting and monitoring. These elements cover modification and a formal audit (Rowe, 2004). The domino process can occur at all stages of management.

The similarities among elements of the risk management process are apparent as organisations attempt to codify and standardise industrial practices in terms of risk management. Various researchers have written about common elements. For instance, Ross and Bodapati (2006) describe the process of controlling risk as involving the steps of risk identification, risk evaluation, selection of management alternatives, implementation of the appropriate strategies, and monitoring of the results thereof. Kallman and Maric (2004) examined various models of risk management, and the purpose of their work was to propose a new risk management paradigm that incorporates many of the components of earlier works. The proposed risk management model assessment tool involves four major categories (or steps), as well as eleven subcategories. The ideal and practical categories of the risk management programme include programme development, which, from the perspective of the domino effect, includes strategic and tactical planning in the long and short term. This includes organisational needs, staffing, the chain of command, adequate personnel, policy development and written policies.

The chemicals industry is interesting in terms of the deeper aspects of a domino effect. As of yet, there is no universally accepted definition of the concept of a domino effect when it comes to accidents in that industry. Most scientists in Asia, North America use the term to describe situations in which a containment accident

in a process unit triggers one or more losses of containment accidents in one or more other process units. At times, the “victim” unit or units become the cause of new accidents, and sometimes the chain continues even further. The first knock-on event is referred to as the “first level” or “first order” domino effect, while events occurring at second or further stages in the chain are referred to as second level/order, or a higher level/order domino effect. In the European Union, the term “domino effect” is sometimes used in a more restricted sense, and only in situations in which the loss of a confinement accident in one establishment causes the loss of a confinement accident in another establishment. This interpretation is based on the so-called “Seveso II Directive”, which calls competent authorities to use information that is received from compliant operators, identifying establishments or groups of establishments in which the likelihood, possibility and consequences of a major accident can increase because of the location and proximity of the establishments, also thinking about their inventories of hazardous substances Chemical Accidents (Seveso III). Authors who use this definition only use the concept of the “domino effect” when an industrial accident has occurred due to the impact of an accident in another industry that is adjacent or nearby. The term “internal domino effect” is to distinguish among several accidents at a single establishment from those occurring in more than one establishment.

One of the earliest definitions of a domino effect was proposed by Lees (2005, 1980), and it is rather “liberal”. According to Lees, a domino effect is a factor that takes account of the hazards that can occur if the leakage of a hazardous material can lead to an escalation in the incident, e. g., a small leak that catches fire and damages a larger pipe or vessel, thus leading to the subsequent spillage of a large amount of hazardous materials.

The American Institute of Chemical Engineers Centre for Chemical Process Safety (AIChE-CCPS) also has a very liberal definition, arguing that a domino effect relates to an incident that begins in one item and can affect nearby ones (e. g. , vessels carrying hazardous materials) with thermal, blast or fragment impact (CCPS, 2000). By this definition, all knock-on effects, even including those that occur within a single process unit, would fall under the umbrella term “domino effect”. Between the extremes of the restrictive Seveso II definition and the liberal definitions of Lees and AIChE-CCPS are “middle-of-the-road” definitions such as the one proposed by Bagster and Pitblado (1991). They define a “domino effect” in terms of knock-on accidents involving two distinct process units (which may or may not be a part of the same establishment). Given this diversity of interpretations of the term “domino effect” in the context of process industry accidents, it may be interesting to review the origins of the term as such. It comes from the game of dominoes, which are small, flat blocks, often of wood, marked on one side with two groups of dots that represent numbers (Crowther, 1996). If dominoes are arranged so that each falling domino hits the one that is next to it, and if the domino at the front of the row is caused to fall, then that can lead to a chain of collapsing dominoes, with every falling one toppling the next one. On the basis of this analogy, the term “domino effect” is used to describe an event, usually an unpleasant one, which causes other, similar events to happen. The term is frequently used by economists and political scientists to describe the impact of actions that have the propensity to cause crisis situations or do cause one crisis

after another. The importance of studying chains of accidents stems from the fact that such serial, knock-on or cascading events are not only fairly common, but also cause much greater damage than one-off accidents. This means that there is little relevance as to whether the units involved in such a chain of accidents happen to belong to the same establishment or different ones. Indeed, even within the EU, the concept of the domino effect is often used in a more generalised sense than that which is reflected in the Seveso II Directive. It has been called a phenomenon that occurs inside and outside industrial sites (Cozzani et. al., 2005), one in which a primary event propagates nearby equipment in terms of triggering one or more secondary events, a phenomenon involving a cascade of accidents in which the consequences of one accident are increased by the following ones in spatial and temporal terms (Reniers, Dullaert and Karel, 2009), and a physical effect caused by a primary event that may trigger secondary events in other process units. Bahman Abdolhamidzadeh (2010) has analysed the definitions and theories of a domino effect and argued that in the present study, the term has been used in the sense in which it is commonly used outside of the EU and often even within the EU, referring to knock-on accidents in which one process unit jeopardises another. The effect is characterised by the following sequence:

- The primary accidental scenario, which initiates the domino sequence of accidents;
- The propagation of the primary event due to an “escalation vector” that is generated by the physical effects of the primary scenario and results in the damage of at least one secondary piece of equipment;
- One or more secondary events (e. g., a fire, an explosion and toxic dispersion) involving the damaged pieces of equipment (the number of secondary events usually being the same as the number of damaged pieces of equipment).

As the author has argued in the past, European legislation related to domino accidents is enshrined in Article 8 of Directive 96/82/EG, 9 December 1996. This article obliges Seveso upper-tier companies to exchange information with adjacent plants to prevent domino accident, but it does not force them to co-operate with one another. The chemicals industry has much freedom when it comes to complying with the data exchange requirement. From a social and economic point of view, preventing domino accidents deserves more attention and co-operation among companies, and this should be strongly stimulated by the EU. The problem is that there is a fierce competition among most chemicals companies, and most have their own and specific approach towards safety. This hampers co-operation (Reniersa, 2005).

In the present article the author has described and analysed the domino effect in a legally correct approach towards risks and crisis communication in the context of management. The author has analysed the essence of domino effect theories, the results of the pilot research of the influence of the domino effect, and the effects of risk and crisis-related judicial aspects on companies.

## **Conclusions**

A domino effect has speed and time distance and force, as well as communication in terms of quicker speed, closer time, and more power force and according to Nelms (1992), it consists of four causes – the root cause, latent causes, human causes and physical causes, with latent causes very often causing crises in that as they are based on a spokesperson's lies in a manner that could influence the company's reputation (Derkevica-Pilskunga, 2016). According to several authors (Bagster and Pitblado (1991), Khan and Abassi (2001), Cozzani and Salzano (2004) which have analysed aspects of domino accidents, it is clear that a domino effect can appear in a company's internal and external environment, with external effects often having more severe consequences than internal ones, because the affected area is larger, and more equipment is involved; that is why companies must strive to avoid a domino effect by including this aspect in risk and crisis communication plans. Domino effect could be prevented. According to Reiners (2005), it must be started with the analysis of the efficiency of the current risk. Not always companies are aware of the need of risk analysis because what is not compulsory very often does not apply to a person or company. There is a necessity of a legislative system in this field. According to the research done by Jolanta Derkevica-Pilskunga (2016), companies mostly report financial and commercial risks. And the largest part of respondents say that risks are related to legal and regulatory problems.

According to Schmitt-Geiger (2013), "litigation public relations are used in all kinds of legal disputes". It means that companies facing crisis should comply with the law. That is why focus on law in communication is important but it cannot be a chaos. According to Wills (2000), in chaos human feelings act as instincts and crisis situations often involve chaos, decisions are taken in a hurry and chaos. In risk and crisis communication there are necessary some frames and there is a need for a general legislative system for any company when it comes to risk and crisis situations to avoid harm to human lives and other resources. This could be a law related to risk and crisis communication. The target of the law must be to avoid the domino effect or chain that influences other companies, audiences and states in crisis situations. Communication law and clear guidelines of risk assessment is suggested for the policy makers in Latvia. Latvia must adopt a risk and crisis communication law, because it would be more understandable and concentrate all necessary activities such as risk and crisis plans, responsible individuals and their training, dark sites, information about the risk, etc. The law must make it obligatory for all companies to prepare risk and crisis communication plans.

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## Author's bibliography notes



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# IMPROVEMENT OF NOTIONAL DEFINED CONTRIBUTIONS OLD-AGE PENSION SCHEME FOR ENSURING PENSION SUSTAINABILITY

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## ***Abstract***

*The aim of the present article is to improve the notional defined contributions (NDC) old-age pension scheme in order to build sustainability of old-age pension system. To reach the target, the following research tasks have been defined: on the basis of the scientific literature, to analyse and characterize old-age pension systems and schemes common in Europe and other countries, as well as their types and sustainability criteria; by improving NDC old-age pension scheme, to develop a sustainable old-age pension scheme based on Latvian and global NDC old-age pension scheme experience and to assess, whether the developed old-age pension scheme prototype provides sustainability.*

**Keywords:** pension system, sustainable, NDC, solidarity.

## **Introduction**

Despite the fact that in the early 90s of the 20th century in many countries around the world, including Latvia, pension system reform was implemented and a three-level old-age pension system based on the principles of capital accrual was established, which at that time was considered as one of the most progressive and modern pension systems in the world, in recent years there is a lot of debate about its ability to ensure sustainability, fairness and solidarity.

The sustainability of a pension system is based on the fiscal and financial balance between the revenue and liabilities. Dutch Professor of Economics Asghar Zaidi defines financial sustainability as the government's long-term ability to meet its financial obligations with respect to the existing and future spending and liabilities (Zaidi, 2010, 3).

For ensuring the adequacy of pensions, pension indexation is widely used, because it is a tool to prevent pensioner poverty and ensure proper level of substitutability. Professor Margaret Borella and academician Elsa Fornero from Turin University indicate that it is important to establish a proper and fair relationship between contributions and benefits, since sufficiency of income is the fundamental objective of a pension system (Borella and Fornero, 2009).

International researches on the financial sustainability and social sustainability of pension systems or pension adequacy of the European and OECD pension systems show that a financially sustainable pension system does not necessarily ensure adequacy of pensions. Comparing pension system financial sustainability and income adequacy, the financial sustainability of the pension system of Latvia is ranking the ninth among the EU and OECD countries, but in respect of retirement

income adequacy level takes only the 29th position, which in total indicates low level of pension income and high level of poverty risk (Allianz Global Investors, 2014, 2015). So, the topical issue is how to achieve the balance between the contributions and the amount of pension within the pension capital accumulation phase and pension payoff period.

The author of the present article has studied and analysed the old-age pension systems, which function on the basis of defined benefit (DB) old-age pension schemes, defined contribution (DC) old-age pension schemes, point-based (PS) old-age pension schemes and notional defined contributions (NDC) old-age pension schemes, as well as the reforms implemented in order to ensure sustainability on the basis of the experience and sustainability figures of Germany (PS), the Netherlands (DB), Chile (DC), as well as Sweden and Latvia (NDC). The research of the author shows that none of the above mentioned schemes has succeeded in fully ensuring economic, social and political sustainability, as well as level of pay substitutability and pension value preservation during the pensioner's lifetime.

Thereby, the author has set the goal to develop an old-age pension scheme, which addresses the old-age pension instability causes on the basis of the principles of the NDC old-age pension scheme. The author improves the NDC old-age pension scheme so as to ensure the balance of annual contributions and costs, as well as compliance with the intergenerational solidarity principle.

The proposed NDC pension scheme improved by the author provides for the introduction of uniform index that is linked to the cyclical nature of the economy – if the economy grows, the index increases, while in case of the economic recession the index decreases. The author's formula provides that the pension funds and the pensions are indexed annually by using a uniform index, thus ensuring equal treatment of contributors and pension recipients. In the uniform index calculation formula, the author introduces the indicator alpha ( $\alpha$ ), which characterizes the demographic changes. The use of the uniform code allows the pensioners to maintain a reasonable level of their standard of living after retirement. Unlike the current practice, when the level of pay substitution is determined in relation to the salary at the time of retirement, the author of the article offers to attribute the pay substitutability as against the national median income.

For achieving the stated goal and objective the following research tasks were set:

- On the basis of the scientific literature, to do research on and characterize the most common old-age pension systems in the European, as well as in other countries, their types and sustainability criteria.
- To improve NDC old-age pension scheme and to develop a sustainable old-age pension scheme based on the experience of the pension scheme of Latvia, as well as the NDC old-age pension schemes of other countries.
- To assess, whether the proposed old-age pension scheme ensures pension sustainability.

The following research methods were used: monographic method, graphical method and analysis of statistical dynamics series method.

## **1. The types and characterisation of old-age pension systems**

State old-age pension policy has its roots in the late 19<sup>th</sup> century, when countries started to develop compulsory social insurance against such social risks as age and incapacity for work. The first two pension schemes were created, which have long been the two main models in forming pension policy: the German working life income-based scheme (1889) and the universal, the means test based Danish scheme (1891). Such a difference indicates distinction in purposes: in the case of Germany – the need for a lifetime income stability, but in the case of Denmark – the need to prevent poverty in old age. These two objectives were forming the basis of pension systems for a number of years, and while in some countries there is still political rhetoric in favour of one specific purpose, nowadays the majority of pension schemes are targeted to implementation of both these purposes (Barr and Diamond, 2006). There are other types of pension system classification: (i) the means of pension payment: defined benefit / defined contribution; (ii) the type of funding: funded / unfunded; (iii) the degree of actuarial fairness: actuarial / nonactuarial (Lindbeck and Persson, 2001, 75–76).

The aim of the pension system is to create an opportunity for the individual and the society as a whole to maintain the usual level of consumption when, after reaching a certain age, an individual is no longer able or willing to be economically active and productive. So the state pension system must be able to assess and effectively manage two types of risks – those involving individuals and those affecting society as a whole. The pension system is (i) a mechanism for consumption smoothing and (ii) an insurance agent (Barr and Diamond, 2006).

Retirement was fully institutionalized in the late 20<sup>th</sup> century. This was facilitated by the economic boom of the 1950–1960. The situation began to change in the middle of the 70s of the 20<sup>th</sup> century – the economic growth rates decreased and the aging of the population became more pronounced. The economy began to move away from Keynesianism towards a new supply-based policy, which takes into account productivity, international competitiveness and stronger public finances (Taylor-Gooby and Daguerre, 2002). Thus pension reform became a topical issue – the problem was how to make the current pension scheme financially sustainable, while maintaining its effectiveness.

In implementation of the pension reform, the multi-level pension system initiated by the World Bank must be noted. In the 90s of the 20<sup>th</sup> century, the World Bank study “Averting the Old Age Crisis: Policies to protect the Old and Promote Growth” (World Bank, 1994) influenced the choice of the Central and Eastern European countries in remodelling their pension systems and making the choice in favour of a multi-level scheme, including the introduction of funded pension systems in Latvian. Multi-level pension system consists of various programs or schemes, which have their own approaches, financing, benefit calculation and administration rules that provide information about the role of the various institutional spheres – the state, market, civil society and the social partners (Natali, 2008, 2011).

## **2. Common objectives and sustainability criteria of old-age pension system**

The common objectives and sustainability criteria of the pension systems are on the agenda of scientists and experts from all over the world. Pension experts Holzmann, Hinz and Dorfman give the following definition of sustainability of a pension system: “One can consider a system sustainable if it is financially justified and may be maintained in the foreseeable future, with a wide range of reasonable assumptions” (Holzmann, Hinz and Dorfman, 2008, 8). These experts suggest that the primary objective of any pension system is to ensure an adequate, effective, sustainable and robust old-age pension, at the same time continuing the search of enhancement options of the general public welfare that are specifically suitable to a particular country. British Professor of Economics Asghar Zaidi claims that the term “sustainability” acquires a different meaning in different contexts but in the context of pension systems it is essential to come to a clearly defined, measurable statement that emphasizes the common goals and values of any pension system (Zaidi, 2010, 2012).

As indicated by the European Commission in its White Paper “An Agenda for Adequate, Safe and Sustainable Pensions”, the approach regarding the sustainability of a pension system is focused only on the three pension purposes – (i) pensions should be adequate, (ii) sustainable and (iii) secure (White Paper, 2012). Whereas economist and Professor Donghyun Park confirms that a well-designed sustainable pension system can be described as follows: a broad-based both in terms of coverage and the range of risks covered; sustainable in relation to financial stability; stable enough to withstand macro-economic and other shocks; available from personal, business, financial and macroeconomic perspective; provides a reasonable level of retirement income; provides a safety net for the elderly (Park, 2009, 5). This list suggests a multiple set of goals that should be met by each pension system. Yet these priorities may vary, depending on the political, economic and social changes in the society. The approach of the author is based on the view that the pension system can be considered sustainable if it is adequate, accessible, fair, predictable and stable.

### **2.1. The political, financial and social sustainability of an old-age pension system**

For ensuring sustainability of a pension system, political stability is essential. For political sustainability of a pension system a continuous support at all levels, starting from the government, the administration and the society in a broader sense, that is, the pensioners' associations, trade unions, business representatives and non-governmental organizations, is necessary (Barr, 2002).

Ensuring fairness of a pension system is an important aspect, too. Enhanced linking of contribution with the future pension amount justifies itself, because it results in achievement of a much fairer pension system with the right incentives to make contributions and work (De Graaf, Maier and Frericks, 2007).

## **2.2. The financial sustainability of a pension system**

Professor A. Zaidi defines financial sustainability as the government's long-term ability to meet its financial obligations with respect to existing and future expenses and losses (Zaidi, 2010, 3). Pension costs represent a large portion of public expenditure and are an essential current as well as long-term cost item. The financial sustainability of the pension system depends not only on the amount of contributions and public pension expenditure; it is influenced by: (i) the type of the pension scheme that forms the basis of the pension system, that is, Pay-As-You-Go, DB, NDC, PS or DC scheme; (ii) what are the principles of capitalization or valorisation defined for the particular scheme; and (iii) what are the pension indexation rules.

Valorisation of pensions or indexation of pension capital plays the balancing role in financial situation of a pension system (D'Addio and Whitehouse, 2012). In state and private pension schemes, social security contributions are generally determined by the national legislation providing the level of contributions. If the level of contributions is not indexed, the individual makes smaller contributions in the long run which have an impact on pension funds (Whitehouse, 2010; Piggott and Sane, 2009).

## **2.3. Social sustainability**

In pension schemes, the right balance between fiscal and social viability is the basis for its economic stability. Financial sustainability and adequacy of pension systems are not conflicting, separately existing targets, but the two sides of the same coin – the true financial sustainability cannot be ensured, if pension adequacy is not provided at the same time (Barr and Diamond, 2006). An important condition for ensuring social sustainability is indexation of old-age pension, which provides old-age pension adequacy.

## **2.4. Indexation of old-age pension**

Old-age pension indexation is a tool for poverty alleviation or ensuring adequate level of substitution. Indexation should be performed in accordance with a specific country's pension system and its objectives. Conditions for indexation of pension at payment period: pensions are not indexed at all or are indexed on the basis of price changes or according to the average annual wage increase in the state (European Commission, 2015a, 59). Pension indexation provides retention of pensions' long-term value and helps to avoid periodic political debate.

## **2.5. Adequacy of old-age pension**

Sufficient or adequate pension system gives benefits that are sufficient to prevent old-age poverty in the country-specific absolute level within all levels of the population, in addition providing a secure means for aligning the life consumption of the majority of the population (Holzmann, Hinz and Dorfman, 2008, 81). Professor of Turin University Margaret Borella and academician Elsa Fornero

indicate that it is important to establish an adequate and fair link between contributions and benefits because sufficiency of the income level is the fundamental objective of a pension system (Borella and Fornero, 2009).

The studies of the Alliance Global Investors on the financial sustainability (Allianz Global Investors, 2014) and social sustainability of the European and OECD member states' pension systems – pension adequacy – (Allianz Global Investors, 2015) show that having a financially sustainable pension system does not mean that it also provides pension adequacy.

### **3. The types and characterisation of old-age pension schemes**

State pension systems are usually organized by the state, namely, the country with the applicable legislation sets the procedure for contribution collection and payoff and is responsible both for the collection of the contributions and making the pension payments. This system in most countries is a must. There are two types of state old-age pensions (often state old-age pension consists of them both): (i) flat-rate old-age pension, where every pensioner is provided with a uniform pension regardless of the former earnings; and (ii) earnings related old-age pension, where every pensioner is provided with a pension based on work-life income (Natali, 2008). In the EU member states, for poverty eradication or for ensuring the rights to means of subsistence, various types of pension payment operating on diverse principles and having different sources of funding are applied: resource tested, basic, minimum (Holzmann, 2012, 9).

Income-based state pension scheme is divided into three broad categories: public DB old-age pension scheme, PS old-age scheme and NDC old-age pension scheme. Private pension scheme is a defined contribution pension scheme, which, according to the classification of the London Pension Institute and Yermo (2002), the Senior Advisor of the OECD, in relation to the type of management of the funds collected by the pension system, is referred to as the “funded” pension scheme and 3<sup>rd</sup> pillar pension that consists of voluntary privately managed pension plans.

The design and operation of any of the above mentioned old-age pension schemes, regardless of their forms of governance (public or private), the state regulates by implementing legislative framework within the delegated capacity and carries out executive function. The state establishes state institutions and delegates to them the management, control and monitoring of the pensions.

#### **3.1. DB old-age pension scheme**

In a defined benefit scheme the amount of pension is determined as percentage of the earnings and professional employment. A worker receives a previously defined old-age pension and does not assume the longevity and investment risks. For DB schemes no legal regulation exists, which would require indexation of the contributions made in the preceding years, yet on practice, indexation is applied on the basis of the agreements concluded with social partners. During the period of

declining economy, the majority of pension plan managers have chosen to link indexation of savings to the performance of pension funds.

As the Dutch researchers D. Broeders and E. H. M. Ponds admit (Broeders un Ponds, 2012), Dutch pension funds require structural changes. The following should be taken into account: increase in life expectancy of population, decline in the financial market interest rates, reduction of the capital market rate of return. Geographical changes in the financial markets, market contraction and lack of stability should be also kept in mind.

Based on the author's study of the Dutch pension system and the changes that were brought about by the system reform, the author found out that the DB old-age pension scheme fails to ensure sustainability and financial stability of the pension system, and it is not protected against financial and economic shocks.

### **3.2. PS old-age scheme**

The author analyses the sustainability of the old-age pension point scheme by using the German old-age pension system as an example. This system is income based and similar to the NDC scheme. Here, the average annual payroll contributions earn one pension point. In proportion to the level of income – low or high, the contributions accrue less or more pensions points accordingly; every contribution is presumed to be of equal value, in this way the principle of equity is observed. The contribution scheme ensures a fixed level of the future pension. To ensure the PS pension system stability, countries are reforming their pension systems. For example, the German pension system has been incorporated into the pension system stabilizing factor (Borsch-Supan and Wilke, 2004): pension point value is tied to the increase in gross wages; sustainability factor, which measures the number of standardized contributors change towards a standardized number of pensioners; a new pension indexation formula has been introduced by incorporating sustainability factor; increased retirement age.

### **3.3. NDC old-age pension scheme**

The foundations of the NDC old-age pension scheme were laid in Sweden in 1994. In Latvia, the NDC reform was formulated and provided a legal basis on the 1<sup>st</sup> of January, 1996 (Holzmann and Palmer, 2003).

In a notional account old-age pension scheme, individual accounts are established for every contributor, in which all information about the contributions is recorded. Content of the accounts is credited with an interest; the amount of interest is specified on an annual basis. At retirement, the value of an individual's notional accumulated wealth is converted into an annuity based on the formula and the rules for measuring life expectancy. Social insurance contributions made by the workers in a current year are used to pay old-age pensions to existing retirees. Pensions are awarded as a life-annuity, and the annuity value is calculated on the basis of the individual account balance and an individual's birth cohort life expectancy at retirement (Holzmann, et. al., 2013).

A direct link between contributions and pensions ensures fairness (equity) and creates motivation to work. It is important that future pensioners should assume higher responsibility throughout their lives because the lifetime earnings and the taxes paid form the basis for the future pension.

The economic crisis that began in 2008 triggered public discussions on pension reform in Latvia, Italy, Poland and Sweden and highlighted the drawbacks of NDC pension scheme. Wage indexation of pensions, which is technically feasible within the NDC framework, was not carried out in Latvia, Poland and Italy.

According to the research of the author, in order to ensure sustainability of NDC pension scheme the following should be taken into consideration:

- When reforming pension system, the costs of transition from the old to the new system should be identified and financed.
- An explicit stabilising mechanism must be adopted to ensure correct application of the cohort remaining (future) life expectancy ratio by preventing political intervention.
- Gender related issues must be identified and formulated to achieve equivalent pensions for women.
- NDC lacks the mechanism, which would ensure redistribution of earnings of highly paid workers to support the financially disadvantaged citizens. The government may grant pension entitlements that are not based on insurance contributions and an individual's earnings; it is necessary to determine the principle, according to which the minimum pension level is set.
- Rules (which currently do not exist) that regulate distribution of rights between spouses must be adopted.
- The duty of the policy makers and pension service providers is to provide a clear and comprehensive information about the principles of operation of NDC schemes.

### 3.4. DC old-age pension scheme

The defined contribution old-age pension scheme or the *funded pension* scheme, as termed by London Pension Institute and Yermo (2002) with reference to the mechanism used for managing the pension system financing or the way of managing the funds collected by the pension system, is the pension scheme, where a pension benefit depends on definite contributions in pension funds, the professional competence of the fund managers and return on investment. A worker should assume the longevity and investment risks. Old-age pensions are financed from the social insurance contributions in private pension funds. Accumulated contributions and resulting return on investment at retirement are normally converted into pension annuities.

Having reviewed the process and the results of Chilean pension reform and knowing the scholarly opinions, the author concludes that transition to the funded pension schemes does not mean that macroeconomic performance of a country will automatically improve (Gill, Packard and Yermo, 2005) due to high financial expenditures and new risks associated with the management of the funded pension schemes (Shelton, 2012). Instead, the government should develop a



regulatory legal base to supervise the activity of pension funds, adopt a control mechanism to ensure protection of savings of the pension plan participants, and specify the permissible level of pension fund management fees and commissions (Melguizo, et. al., 2009), as well as introduce a mechanism to ensure a minimum pension that is payable from the state budget.

By summarising and analysing the principles of operation of the DB old-age pension schemes, DC old-age pension schemes, PS old-age schemes and NDC pension schemes, the author sees that pension systems have a number of goals, which cannot be achieved in full and in equal measure. The author agrees to the opinion expressed by the scientists Nicholas Barr and Peter Diamond (Barr and Diamond, 2009) that the best one pension system simply does not exist.

The pension system reforms are a reflection of the government's political choice; they are based on the fiscal capacity of the national social budget, they fail to take into account the current negative developments in the economy and demography, all of which does not ensure sustainability of the old-age pension system.

## **4. Problem solutions and proposals for ensuring a sustainable old-age pension system**

When analysing the old-age pension schemes and the pension reforms implemented worldwide, as well as the objectives reached by NDC pension schemes, the research of the author indicates that although these reforms seek to promote sustainability, none of the pension schemes solves the political, social, demographic and economic risks.

### **4.1. Solidarity old-age pension scheme through development of NDC pension scheme**

Based on NDC structure and the principles of solidarity, equity and voluntariness and the above mentioned provisions, the author of the article proposes to introduce changes in the pension calculation methodology for ensuring financial, political and social sustainability of NDC old-age pension scheme. To achieve that:

- Pension calculation formula should be based on the solidarity principle;
- Eligibility conditions should be transparent, and the adjustment mechanisms need to be specified in advance;
- A defined (and stipulated by the law) process should be in place, which leads to a more secure and foreseeable outcome.

The basic elements of the proposed pension scheme are similar to those of the Swedish and Latvian NDC pension scheme; however, the proposed solution allows to prevent all currently known external or internal factors causing instability of the old-age pension system. In the formation of the formulae, the author chooses several description principles:

- small letters define an individual pensioner or an individual contributor;
- capital letters define the figure country wise;
- small indexes define the year or the ordinal number;

- superscripted indexes are not meant for summing up or multiplying, these are applied for value characterisation purpose only.

Further description refers solely to the old-age pension accrued within the NDC pension scheme.

In a consecutive year with the index  $k$ , a payroll tax payer  $i$  makes a pension contribution representing a definite percentage of the amount of payroll tax.

$$S_{ik} = Lw_{ik} \quad (1)$$

*(created by the author)*

Where

$S_{ik}$  – a contribution made by a contributor  $i$  in a year  $k$ ;  
 $w_{ik}$  – taxable income (wage) of a contributor  $i$  in a year  $k$ ;  
 $L$  – the contribution rate applied to taxable income directed to old-age pension (in Latvia's case – the rate  $L=20\%$  is applied to those, who do not participate in the creation of the funded pension).

The total amount of social insurance contributions (the sum of all contributions made by all tax payers during that year) will be  $S_k$ . Unlike other NDC pension scheme, the new pension scheme ensures balance of the contributions and pension outlays. In contrast to other NDC pension schemes here we introduced the equilibrium (balance) of contributions and payoffs.

$$P_k = Sw_k \quad (2)$$

*(created by the author)*

Where

$P_k$  is the amount of pension in the  $k$ -th year, which consists of individual pensioners' old-age pensions. Unlike the generally accepted payment procedure, Formula (2) shows that the sum of the pension in payment is a fluctuating value – depending on the aggregate amount of contributions and the change in the number of pensioners the social insurance contributions are changed causing the amount of the pension payable in a consecutive year change as well.

## **4.2. Solidarity does work if the natural increase or decrease of population and the difference in the pension level are taken into account**

In the proposed model, similar to other NDC schemes, each individual social security contributor  $i$  accumulates pension capital over the years, by increasing the pension wealth with every contribution  $S_{ik}$  made by an individual, while the previously made contribution is being indexed.

## **4.3. The universal annual index**

The author introduces the uniform index  $I_k$ , which is applied both at the pension capital accumulation phase and for indexation of the previously awarded old-age pension. Uniform index  $I_k$  is calculated by Formula 3:

$$S = \frac{S_k}{S_{k-1}} (1 - \alpha_k) \quad (3)$$

*(created by the author)*

Where

$S_k$  – the sum of social insurance contributions in  $k$  year;

$S_{k-1}$  – the sum of social insurance contributions in the preceding year  $(k-1)$ .

The value  $\alpha_k$  is determined by taking into account the change in the number of pensioners in a year  $k$ , i.e., pensions unpaid to deceased pensioners in a certain year and pensions in payment to new pensioners in the same year are taken into consideration.

Although the value of  $\alpha_k$  is small, still, it does reflect demographic change small, still, it does reflect demographic change. Value of  $\alpha_k$  is calculated by Formula 4:

$$\alpha_k = 1 - \frac{1 - \frac{\Delta P_k}{2S_k}}{1 - \frac{\Delta P_{k-1}}{2S_{k-1}}} \quad (4)$$

*(created by the author)*

Where

$S_k$  – the sum of social insurance contributions in  $k$  year;

$S_{k-1}$  – the sum of social insurance contributions in the preceding year  $(k-1)$ ;

$\Delta P_k$  – shows the difference in the pension level in year  $k$  during one year;

$\Delta P_{k-1}$  – shows the difference in the pension level in year  $(k-1)$  during one year;

Pension capital of an individual taxpayer  $i$  over the years is accumulated on the basis of the following formula:

$$k_{i,k+1} = I_{k+1} k_{ik} + S_{ik} \quad (5)$$

*(created by the author)*

Where

$k_{i,k+1}$  – the pension capital of  $i$ -th pensioner in the forecasted year  $(k+1)$ ;

$I_{k+1}$  – a uniform index forecasted for a year  $k$ ;

$k_{ik}$  – an individual  $i$  pensioner's pension capital in a year  $k$ ;

$S_{ik}$  – an individual  $i$  payer's contribution in a year  $k$ .

In the year of retirement  $D$  the earned pension benefit is calculated by the formula, which is identical to the already existing pension calculation formula (6) that is characteristic of Swedish NDC model and is applied in Latvia (according to Article 12 of the "Law on State Pensions").

$$P_{iD} = \frac{K_{iD}}{G_i} \quad (6)$$

Where

$p_{iD}$  – a pensioner's  $i$  pension in the year  $D$  of retirement;  $k_{iD}$  – a pensioner's  $i$  accumulated pension capital in the year  $D$  of retirement;  $G_i$  – the average life expectancy (life span) correspondent to the age of a pensioner  $i$  in the year of retirement, gender differences not being considered. Every year on January 1, when allocating or recalculating old-age pensions, the State Social Insurance Agency applies new values of  $G$  according to the data of the CSB on the life

expectancy for the particular age. For instance, if one retires at the age of 63, one's life expectancy shall be 17,82 years, but if at the age of 65, the life expectancy shall be 16,45 years.

#### 4.4. Old-age pension indexation

Pension indexation is the tool that is used for prevention of pensioners' poverty, ensures preservation of pension long-term value and helps to avoid periodic political debate. Price indexation maintains pension purchasing power, however, usually it is lower compared to wage indexation. This is the reason why in case of pension indexation the replacement rates in the year of retirement only partially explain the adequacy of the pension system, because they do not set off a relative decrease in the pensioners' standard of living. In Latvia, indexation of pensions is turned into a political issue. For the period from 2009 till 2012 indexation of pensions was frozen. Having assessed historical pension increase over years, which was the result of indexation, the author concludes that the rate of increase was insignificant and only partially sets off the impact of inflation on pensioners and does not prevent the poverty risk.

#### 4.5. Indexation of the awarded pensions

The author proposes to carry out further annual indexation of pensions by the formula on the basis of the forecasted earnings and expenditures and apply the uniform index  $I_k$ . If any forecast error occurs, it can be technically carried forward to the next year computations to make sure the error over time is not overinflated.

$$p_{i,k+1} = I_{k+1} p_{i,k} \quad (7)$$

Where

$p_{i,k+1}$  – a pensioner's  $i$  pension in the  $k+1$  year (forecasted);

$I_{k+1}$  – universal index in the  $k+1$  year;

$p_{i,k}$  – a pensioner's  $i$  pension in a  $k$  year.

The most serious risk inherent in the proposed pension scheme is associated with political stability. In the proposed pension scheme each pensioner receives pension benefit that is based on inter-generational solidarity principle. Such resource generation method has been already probe-tested by developed countries for a century at least and does not raise any serious public antagonism.

The amount of pension, in its turn, is proportional to the life investment. Those who contributed large amounts just for a number of years and those who have been making small contributions for many years receive pensions that are equal in size. It follows from the above described pension scheme that every year contribution to the pension capital is proportional to the relative wage (taxable income) earned by a  $i$  taxpayer in a  $k$  year:

#### 4.6. Relative wage $r_{ik}$ (taxable income)

Relative wage  $r_{ik}$  (taxable income) of a taxpayer  $i$  in a  $k$  year is calculated by the following formula:

$$r_{ik} = \frac{w_{ik}}{W_k} \quad (8)$$

*(created by the author)*

Where

$r_{ik}$  - relative wage (taxable income) of a taxpayer  $i$  in a  $k$  year;

$w_{ik}$  - taxable income (wage) of a  $i$  taxpayer in a  $k$  year;

$W_k$  - the sum of all social tax payers' wages in a  $k$  year.

#### 4.7. Pension capital adjustment is a one-off measure, applied only at the moment of calculation of the pension amount and influences the size of an individual's old-age pension for the rest of that individual's life

The accumulated pension capital calculation formula – Formula 9, applied to a certain  $i$  payer till a certain  $k$  year, expressed through relative wage, is:

$$k_{iD} = L \overline{W}_D \left( r_{iD} + M_D \sum_{j=1}^{D-1} \frac{r_{ij}}{M_j} \prod_{m=j+1}^D 1 - \alpha \right) \quad (9)$$

*(created by the author)*

Where

$k_{iD}$  – a pensioner's  $i$  accumulated pension capital in the year  $D$  of retirement;

$L$  – social security rate on taxable income directed to old-age pensions;

$\overline{W}_D$  – the average wage in the year of retirement  $D$ ;

$r_{iD}$  – relative accumulated contribution by a payer  $i$  in the year  $D$  of retirement;

$M_D$  – number of payers of social tax in the year  $D$ ;

$r_{ij}$  – relative amount of accumulated contributions by a certain payer  $i$  till the year  $j$  of retirement;

$M_j$  – number of payers of social tax;

$(1-\alpha_m)$  – the value that characterises the change in the number of pensioners.

#### 4.8. Wage replacement rate

Wage replacement rate for a pensioner  $i$  in the year of retirement is calculated by the following formula created by the author:

$$R_{iD} = \frac{L D r_{iD}}{G_{iD}} \quad (10)$$

*(created by the author)*

Where

$R_{iD}$  – wage replacement rate for a pensioner  $i$  in the year of retirement  $D$ ;  
 $L$  – social security rate on taxable income directed to old-age pensions;  $D$  – length of service (working career) (number of social tax payment years);  
 $G_{iD}$  – average life expectancy of a pensioner  $i$  in the year  $D$  of retirement;  
 $r_{iD}$  – relative accumulated contribution by a payer  $i$  in the year of retirement.  
The formula for calculation of the wage replacement rate for a certain  $i$  pensioner in the year of retirement (10) shows the commitment of an individual contributor to assume responsibility for his or her old days.

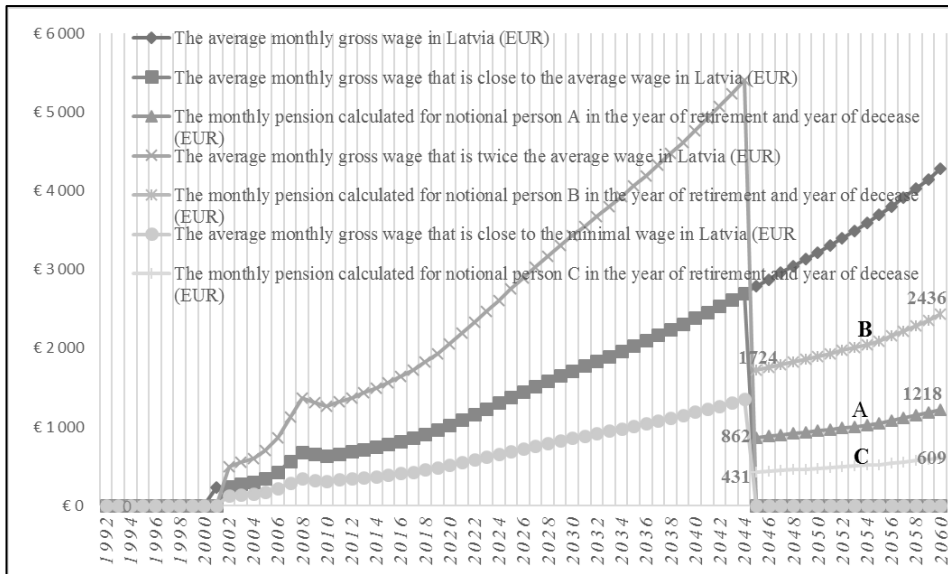
## **5. Simulation of the improved Notional Defined Contributions old-age pension scheme**

To show the sustainability of the NDC pension scheme as improved by the author (the functioning of the formulae created by the author), the author of the article carried out simulation of the improved NDC pension scheme. For the simulation the author chose a future pensioner from Latvia under the following conditions:

- 1) Social taxpayer from 2002 (that is, entering working life) and retires on December 31, 2044, at the age of 65;
- 2) Ongoing work experience for 43 years;
- 3) Not entitled to any additional allowances for children or other bonuses and additional payments;
- 4) Not participating in the 2nd pension level;
- 5) Social insurance contributions of 20% are directed to the NDC pension scheme;
- 6) Within his/her whole working life has received:
  - The average insurance contribution wage – notional person A;
  - Twice the average insurance contribution wage – notional person B;
  - The minimum insurance contribution wage – notional person C.

For simulation of the possible results and calculation methodology the author of the article uses the statistical data of the Latvian CSB (2015), the Social Security Insurance Agency (2015) and EUROSTAT (2015) and the data collected by the EC Report “The 2015 Ageing Report. Economic and budgetary projections for the 28 EU Member States” (European Commission, 2015a, 337). The report contains data about years 2013 and 2015 and the forecasts for years 2020, 2030, 2040, 2050, and 2060.

For simulation the author has used the following formulae: (1); (3); (4); (6); (7); (8); (9) and (10). The calculation results of the pensions of all three notional persons A, B, and C, that have been calculated according to the person's income during life, both in retirement and death year, are graphically displayed in Figure 1.



**Figure 1. Comparison of the pensions of notional persons A, B and C depending on the average gross wage per month in Latvia during lifetime (EUR) in 2044, the year of retirement, and in 2060, the year of decease**

*Source: as calculated and created by the author*

The simulation results show:

- 1) The direct impact of wage on the amount of pension in 2044, the year of retirement, and in 2060, the year of decease. If the lifetime income has been close to the minimum wage, then pension at retirement shall be EUR 431, which according to the author's calculations is two times lower than the sum of the pension of the middle-income pensioner and four times lower than that of the pensioner with income that is twice the average income in the country.
- 2) The application effect of the uniform index on the amount of pension in 2060, the year of decease. Given that pensions are indexed according to the formula (drawn up by the author and pensions are indexed to the relative wages, pensions in the year of decease increase according to the wage increase in the country.

## Conclusions

1. For preventing the old-age pension instability risks, a modified NDC pension scheme can be proposed, which provides consistent adherence to the cross-generational solidarity principle and allows pensioners to preserve a reasonable comfortable standard of living during retirement.
2. The key distinctive feature of the proposed modified NDC old-age pension scheme is that annual indexation of the pension capital and pension is done by applying a uniform index, thus ensuring equal treatment of the contributors and receivers of pension benefits.

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# MULTICULTURALISM IN THE WORLDWIDE MIGRATION CONDITIONS

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## *Abstract*

*In today's world politicians, scientists, the media and the general population of numerous countries show much more interest in the topic of interculturalism<sup>1</sup>. One of the reasons thereof is globalization of the world and an increase in international migration flows. In Lithuania this topic has been researched quite sporadically, and usually focuses on only some issues related to interculturalism. The article presents approaches of foreign and Lithuanian scholars and international organizations (UN, UNESCO, etc.) to the phenomenon of interculturalism and trends of its expression in contemporary society, and analyses the results of an empirical study of 2015 with about 1100 participants. On the basis of the collected data the article presents evaluation of the trends of interculturalism development and its characteristic 'weak points'.*

**Keywords:** globalization, migration, multiculturalism.

## Introduction

The growing flows of international migration, especially unregulated migration (illegals, refugees, etc., UNESCO, 2013), indicate that politicians and the society in general need to look for cooperation possibilities with newcomers, accept challenges of becoming aware of less known cultures, their prevalent ethical norms, communication styles, value attitudes, and help the legally residing foreigners integrate into the new society. The perception of current intercultural differences of various ethnic groups and countries they live in has been formed by efforts of several generations of scholars, in particular by Florence R. Kluckhohn and Fred L. Strodbeck (1961), Andre Laurent (1983), Geert J. Hofstede (1980, 1988, 1991), Fons Trompenaars (1994), Charles Hampden-Turner (1991), Farid Elashmawi and Philip R. Harris (1993), Christopher A. Bartlett and Sumantra Ghoshal (1998), Manuel London and Valerie I. Sessa (1999), Nancy J. Adler (2002)<sup>2</sup>.

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<sup>1</sup> In legal, scientific, historic and other types of literature the concept of interculturalism is most commonly used alongside such concept as multiculturalism, so this article relies on the traditional use of these concepts.

<sup>2</sup> In general, the term 'multiculturalism', which describes ethno-culturalism, racial and religious diversity, emerged in 1970-ies in Canada and was formally institutionalized in 1971 in response to the prevailing policy of 'assimilation' of arriving foreigners. On the other hand, manifestations of multiculturalism can be traced back to early human civilizations. E.g., such cities as the capital of Syria, Damascus (which is older than seven thousand years), or the capital of ancient Persia (present Iran), Persepolis (518 BC), due to their geographic location historically were centres of several cultures, and, alongside ancient Egypt, Greek civilization and the culture of the Roman empire have left deep traces in the emergence of multicultural societies.

For instance, G. J. Hofstede (1980) claims that to understand people means to understand their origin, which reveals their present and future behaviour.

It is predicted that in the near historical perspective, the number of culturally monogamous countries will be continually decreasing, whereas being in a multicultural environment will be usual, thus those coming to a foreign country and seeking to settle there, experience a certain kind of pressure to comply with the existing laws and codes of conduct, to get acquainted with cultural traditions of the new country, and to master the official language to a certain level. Various studies show that such collision of different cultures leads to confusion, often provokes conflict situations, miscommunication, and gives rise to stereotypes, thus with time it has been realized that the newly-arrived and other ethnic groups, which have already been formed, should be treated with conscious awareness and sensitivity when it comes to their attitudes and values; meanwhile public openness and flexibility in respect to the new developments should be promoted (Adams, 1995; Adler, 2002).

Professionals acknowledge that specific features of intercultural communication both at a national level and the level of an individual community should be perceived not as an obstacle, threat, and the like, but as an advantage and an opportunity to take advantage of strengths of other cultures; thus countries should declare public tolerance, awareness of multiculturalism development, aspiration to gain the necessary intercultural competence, etc. on their policy agenda (Adams, 1995; London and Sessa, 1999; Adler, 2002; Deardorff, 2006).

Recently researches on interculturalism have expanded significantly: they address a range of related aspects, including efficiency of intercultural training (Graf, 2004), choosing a proper management style in different cultures (Jacobs, 2005), leadership in a multicultural environment, developing awareness, knowledge and skills (Connerley, Pedersen, 2005), intercultural communication, its efficiency and models (Liu and Lee, 2008), cross-cultural team building and operational efficiency (Lloyd and Hartel, 2009; Oerlemans and Peeters, 2010), etc. Scientific sources place more focus on preferred characteristics of a global manager (Hurn, 1999; Stanek 2000; Collard, 2007; Bird et. al., 2009) with a particular emphasis on his ability to manage cultural diversity.

In Lithuania research on cultural diversity and multiculturalism is a relatively new scientific direction. Giedrius Jucevičius (2001) examined cultural characteristics of Lithuanian organizations in the European context, Valdas Pruskus (2012) discussed the topics of multicultural communication and management, Aušra Repečkienė et. al. (2011) focused on cultural diversity management, Vladimiras Gražulis is interested in conditions for intercultural competence development (2015).

The article analyses the approach of foreign and Lithuanian scholars and international organizations (UNESCO, UN) to the expression of multiculturalism, discusses the results of the quantitative study performed by the author in Lithuania, which involved 1,067 respondents (about 73% are women, 70% work in the public sector and live in cities, 85% have a higher degree, 79% are under 50 years old), who, on the basis thereof, formulates recommendations on the conditions for development of this process. The structure and scope of the respondents' demographic characteristics help to reveal the situation of expression of interculturalism in Lithuania.

Expression of multiculturalism is discussed in the article within the scope of systemic analysis of scientific works related to the topic (Adams,1995; London and Sessa,1999; Adler, 2002; Pruskus, 2011, 2012; Connerley and Pedersen, 2005; Keršienė and Savanevičienė, 2005; Deardorff, 2006, 2009; Oerlemans and Peeters, 2010; Petkevičiūtė 2005, 2012) and can be described as an intersection of two dimensions: global migration processes and an individual's approach to multiculturalism, as well as his or her experience (competence) to act in the conditions of cultural diversity. Hypothetically it can be stated that when an individual supports interculturalism as a phenomenon, he or she welcomes representatives of other cultural groups and is able to learn, work and live together with them. On the other hand, a negative attitude to multiculturalism could be attributed to weaknesses of the national policy and negative precedents in its daily practice.

## **1. Multiculturalism in the globalized world**

The UNESCO report of 2009 on the issue of multiculturalism highlighted the fact that due to the ongoing globalization the world is shrinking, there is a need for different cultures<sup>3</sup> to develop a closer relationship than ever before (Intercultural Competences, UNESCO, 2013, p. 7). At present it is acknowledged that one of the key factors characterizing the process of globalization is the ever increasing flow of international migration, which results in noticeable intermingling of different cultures with their values, customs, and religious beliefs. According to the UN data the volume of international migration for the purpose of work, reuniting families, studies, purchasing property, fleeing from persecution, etc. in Europe from 1990 to 2015 increased by 1.55 times and reached more than 76 million people, i.e. every seventh resident of Europe is an immigrant, meanwhile, migration within the European countries amounted to almost 40 million of people (International migrant stock 2015, UN)<sup>4</sup>.

The number of foreigners crossing the borders for tourist motives is growing rapidly and during the last decade has reached hundreds of millions per year. Due to this 1 out of 11 workplaces in the world are established in the tourism sector (Tourism Highlights. UNWTO. 2015). At the same time, the increase in the number of tourists places additional requirements on employees of this sector to be able to work in a multicultural environment. Similarly, the development of multiculturalism is affected by the recent situation in the European member states with the increasing flows of refugees from the Middle East and some African countries (e.g., Eritrea, Sudan), due to which the global migration crisis has become an issue for discussion.

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<sup>3</sup> Darla K. Deardorff (2006) defines 'culture' as values, beliefs and norms characteristic of a group of humans and therefore culture shapes the procedure for people to communicate and act, that is, the way they interact with others.

<sup>4</sup> An increase in migration rate is observed in Lithuania as well, e.g., in 2010 more than 5 thousands of immigrants came to Lithuania, whereas in 2014 this number increased by 4.7 times and exceeded 24.3 thousand people (Population and social statistics. International Migrations, 2015).

For a few past decades the ever expanding cross-border migration, especially unregulated (illegal, refugees, etc., UNESCO, 2013), has become a serious challenge for receiving countries, including such issues as how to achieve effective cooperation with the newly-arrived, how to respond to new challenges of coming into contact with little-known cultural and religious traditions, rules of etiquette, and communication style, and how to help integrate foreigners, who have legally come to the country, into the new society.

Multicultural environment has become part of daily life; thus the clash of different cultures often leads to various conflict situations, miscommunication, and gives rise to opposing stereotypes; however, a positive attitude towards expression of tolerance for other cultures and showing understanding and sensitivity, including openness and flexibility to the relevant changes, bring a number of benefits to receiving countries (Adams, 1995; Adler, 2002). In this case, receiving countries have to deal with the phenomenon of the culture of peace. It is obvious that in order to develop the culture of peace we should focus on human rights issues, which are viewed as a relevant topic for anyone interested in intercultural dialogue, because the culture of peace, first of all, is conflict prevention, education for tolerance, mutual respect and dialogue (UNESCO, 2011a).

Current processes of societal development are likely to expand any national cultural boundaries, increase the pace of social transformation and, as an overall result, cultural diversity and intercultural communication become a fact of modern life. Intercultural skills of lots of individuals are expressed through their ability to discuss such complicated and important issues as values, beliefs and attitudes among the multicultural group members in a way which would not cause conflict. Table 1 presents the attitude of D. L. Adams, De Merode, M. London, V. I. Sessa, N. J. Adler, D. K. Deardorff et. al. to interculturalism.

Table 1

**Diverse definitions of intercultural competence**

Authors/ sources	Description of interculturalism
Diane L. Adams (1995). <i>Health issues for women of color: A cultural diversity perspective</i> . Thousand Oaks: SAGE Publications.	Knowledge of another ethnic group's cultural characteristic features, history, values, belief system and the ability to adequately deal with its members; conscious understanding and sensitivity to another ethnic group, including openness and flexibility towards the relevant changes when it comes to other attitudes and values
De Merode (1997), cited in Mary L. Connerley, Paul B. Pedersen. 2005. <i>Leadership in a Diverse and Multicultural Environment- Developing Awareness, Knowledge, Skills</i> , SAGE Publications, p. 72. <a href="http://www.sagepub.com/sites/default/files/upm-binaries/4965_Connerley_I_Proof_3_Chapter_5.pdf">http://www.sagepub.com/sites/default/files/upm-binaries/4965_Connerley_I_Proof_3_Chapter_5.pdf</a>	The ability to motivate the creation of intercultural teams, the ability to lead intercultural negotiations, the ability to select personnel and evaluate employees in different cultural environments, awareness of how to build good relations between different cultural groups

Manuel London, Valerie I. Sessa (1999). <i>Selection of international executives: An introduction and annotated bibliography</i> . Monograph. Greensboro, NC: Center for Creative Leadership.	The ability to positively evaluate other cultures, awareness of cultural differences, empathy for other cultures, recognition of cultural differences, liberalism, sharing cultural differences with other
Nancy J. Adler (2002), cited in Mary L. Connerley, Paul B. Pedersen. 2005. <i>Leadership in a Diverse and Multicultural Environment– Developing Awareness, Knowledge, Skills</i> , SAGE Publications, p. 72. <a href="http://www.sagepub.com/sites/default/files/upm-binaries/4965_Connerley_I_Proof_3_Chapter_5.pdf">http://www.sagepub.com/sites/default/files/upm-binaries/4965_Connerley_I_Proof_3_Chapter_5.pdf</a>	The ability to facilitate cultural sensitivity, the ability to solve intercultural problems synergistically, the ability to negotiate in the diverse cultural environment
Darla K. Deardorff (2006), <i>Journal of Studies in International Education</i> , Fall 10, pp. 241–266 and <i>The SAGE Handbook of Intercultural Competence</i> , 2009 (Thousand Oaks: Sage).	Effective and appropriate behaviour when communicating in an intercultural environment, where ‘effective’ and ‘appropriate’ behaviour and the consequences of the effectiveness of communication assessed by another person; behavioural suitability directly related to cultural sensitivity and regarded as the cultural norm for this person.
Multiculturalism. Published 2010 in Stanford Encyclopedia of Philosophy. <a href="http://plato.stanford.edu/entries/multiculturalism/">http://plato.stanford.edu/entries/multiculturalism/</a>	A body of thought in political philosophy about the proper way to respond to cultural and religious diversity, which recognizes that mere toleration of group differences is not enough; there must be legally enacted norms of such a group of people, on an equal footing as the rights of local people.
Conceptual and Operational Framework Intercultural Competences. Published in 2013 by UNESCO, p.12. <a href="http://unesdoc.unesco.org/images/0021/002197/219768e.pdf">http://unesdoc.unesco.org/images/0021/002197/219768e.pdf</a>	Merger of two or more different cultural groups that interact or affect each other. .... and when all the group relations develop into a subculture or cooperating cultures
Cultural Competence and Spirituality in Community Building / Cultural Competence in a Multicultural World ... / <a href="http://ctb.ku.edu/en/table-of-contents/culture/cultural-competence/culturally-competent-organizations/main">http://ctb.ku.edu/en/table-of-contents/culture/cultural-competence/culturally-competent-organizations/main</a>	The interaction of two or more entities (individual people, a group) who represent different cultures, orientations, attitudes of life, customs, etc., or organizations, which declare the objectives and missions oriented to people from different cultures.

Compiled by the author, source: V. Gražulis. *Current Issues of Development of Multicultural Competence in Conditions of Global Migration Process (Situation in Lithuania)* in journal *HRM&E*, 1/2016, volume X, p. 65.

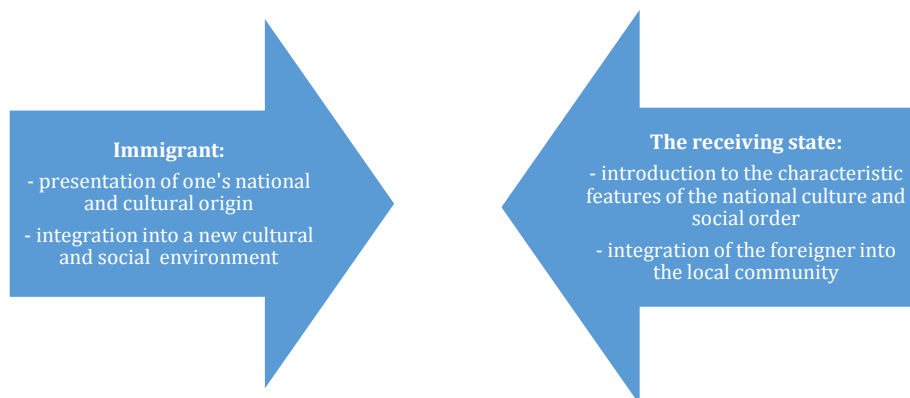
The systemic analysis of information presented in Table 1 allows to claim that multiculturalism and personal multicultural competence are characterised by:

- awareness of cultural features of an ethnic group, its history, values, the belief system, tolerant attitude towards people from a different culture,
- a conscious understanding and sensitivity to another ethnic group, which includes openness, flexibility and empathy for people from other cultures,
- the ability to motivate to work in an intercultural environment,
- awareness of how to build good relations between different cultural groups,
- the ability to solve intercultural problems synergistically.

D. K. Deardoff (2009) notes that proficiency in a foreign language as such does not describe a person as having intercultural competence, because proficiency in a foreign language is not the only indicator of evaluation of interculturalism. Moreover, interculturalism cannot be viewed as a personal characteristic feature, thus its development requires a person to constantly excel (Hoopes, 1997; Fantini, 2000; Byram, 2012). It can be suggested that communication with people of other cultures provides possibilities to develop individual skills of interculturalism, however, due to the ever emerging challenges (human rights violations, the consequences of war, unemployment, etc.), as A. Fantini (2000) notes, the process of skill formation and development often lasts for a lifetime. Inability to accept new challenges is often seen in impeded interculturalism development, which are expressed through a person's preconception or absolutely unreasoned prejudices against foreigners. U. Liebschand and N. Petkevičiūtė (2005) refer to preconception or unreasoned prejudices as an irrational feeling of dislike or even hatred, based on direct experience or lack of knowledge about the object. A similar position is also supported by A. C. Krizan, P. Merrier, J. Logan and K. Williams (2008), who agree that lack of knowledge about cultural diversity and inability to understand other cultures give rise to stereotypes, as very often individuals rely on a simplified principle – 'they' are not like 'us'. The above mentioned specialists in the area of multiculturalism believe that it is important not only to acquire knowledge in the process of formal education and, thus, form positive attitudes towards foreign nationals, but also to constantly develop the acquired skills in practice.

Interculturalism can be defined as a two-way process (Figure 1), where awareness and sensitivity to another ethnic and social group should be assessed by applying features of multiculturalism (interculturalism). The focus of scientific researches is on the issue of effective cooperation of people, determined by the necessity to be able to communicate with each other in foreign languages, the need to be aware of other cultures, to know the history of different countries and the like.





*Figure 1. The process of cognition and change of multiculturalism.*  
(Compiled by the author)

## 2. Methods

The study consists of two blocks of diagnostic research, distinguishing criteria selected on the basis of scientific works of other researchers (Adams, 1995; London and Sessa, 1999; Adler, 2002; Pruskus, 2003; Connerley, Pedersen, 2005; Keršienė & Savanevičienė, 2005; Deardorff, 2006; Oerlemans and Peeters, 2010; Petkevičiūtė 2010, 2011). The first block helps to establish the importance of the content of intercultural competence: knowledge, attitudes, skills and cultural awareness. The second block helps to reveal the respondents' ability to act under conditions of cultural diversity.

The article analyzes the approach of foreign and Lithuanian scholars and international organizations (UNESCO, UN) to the expression of multiculturalism, discusses the results of the quantitative study performed by the author in Lithuania, which involved 1,067 respondents (about 73% are women, 70% work in the public sector and live in cities, 85% have a higher degree, 79% are under 50 years old), who, on the basis thereof, formulates recommendations on the conditions for development of this process. The structure and scope of the respondents' demographic characteristics help to reveal the situation of expression of interculturalism in Lithuania.

The results are generalized by means of SPSS package version 16.0. Percentage frequencies were calculated; the analysis of statistical significance was checked by calculating the difference between two average scores of diagnostic groups. To assess the statistical significance of differences in distribution of responses in different groups of respondents Pearson Correlation and t-test, with  $p \leq 0.05$ , was applied. The measured coefficient of internal consistency of the scale Cronbach  $\alpha$  was 0.886.

### **3. The research.**

## **Conditions for the development of multiculturalism in the legal environment of Lithuania**

In spite of the fact that Lithuania, which has historical experience of living at peace for several centuries with Polish, Jewish, Russian, Belarusian, Tatar and other ethnic communities, traditionally is attributed to relatively homogenous European countries, which are characterised by permanence of ethnic composition and small scale immigration. For example, in 2015, 3.7 thousand foreigners arrived in Lithuania as immigrants, mostly from Latvia, Germany, Poland, Ukraine, Russia, and Belarus (Who is coming to Lithuania? 2015). 407 individuals came to Lithuania from Asian and African countries (ibid). In 2015 m. Lithuania granted refugee status to 17 asylum seekers; in total from 1997 refugee status has been granted to 217 individuals. The most common applicants for asylum in Lithuania are citizens of Ukraine, Russia, Georgia, Belarus, Azerbaijan, Afghanistan and Iraq (Asylum in Lithuania, 2016). As is apparent, most of the immigrants and applicants for refugee status arrive from countries which have had historical and intercultural links with Lithuania for more than 50 years (proficiency in the Russian language, joint education programs, joint festivals and contests, sport events, similar conditions for access to the world outside the Soviet borders and so on). Intercultural differences are manifested mainly in literature, art and folklore traditions of each ethnic community, thus in this case the development of Lithuanian multicultural diversity remains quite limited.

It is generally recognized that a nation's cultural isolation often lies in the nation's national features, e.g., domination of peasant (rural) monoculturalism or urban culture characterized by a wider range of interculturalism. Until the mid 20th century peasant culture with monocultural perception of the world is considered to be the Lithuanian national feature. On the other hand, 50 years of the isolated environment of the Soviet regime had a rather negative impact on shaping public attitudes towards foreigners or less known cultures.

Small-scale multicultural diversity and experience of the historical peripetia of the Lithuanian community have hardly contributed to promotion of the need for development of multiculturalism and have hindered a more comprehensive discourse of this phenomenon. A vivid example hereto is the guidelines for cultural policy change of the Republic of Lithuania (Resolution of the Government of the Republic of Lithuania No. XI-977, 30 June, 2010), which do perceive culture as a resource and recognize that international economic relations should not be ignored, however, do not mention the intercultural dimension associated with internationality. Presumably, there is a serious reason for the Lithuanian migration policy guidelines (Resolution of the Government of the Republic of Lithuania No Nr. 29, cl. 11.8, 22 January, 2014) to acknowledge that public opinion is characterized by traditionally dominant cultural isolation, which is considered to be one of the major barriers to the development of multiculturalism. Circumstances of a similar type form rather negative than positive public opinion about foreigners coming to Lithuania. The comparison of the results of public surveys of 2010–2013 reveals that intercultural differences are perceived more as a barrier, thus the number of

those who support the argument that immigrants bring benefits to the state and society, is decreasing, while the number of those who oppose the argument is increasing (*ibid*). Such findings reasonably prove that Lithuania has so far taken the first steps towards perception and management of cultural diversity.

After the restoration of Independence in 1990, the residence of foreigners lawfully present in the territory of Lithuania has been regulated under provisions of the Republic of Lithuania law on the legal status of aliens, which enables them to integrate into political, social, economic and cultural life of Lithuania (the Republic of Lithuania law on the legal status of aliens, cl. 107). After Seimas ratified the 1951 Convention Relating to the Status of Refugees and passed a corresponding law (27 July, 1997), foreigners were given the right to apply for refugee status in Lithuania, be granted asylum and integrate into the local society. At the start of the year 1998, the Procedure for social integration of refugees in Lithuania came into force<sup>5</sup> (Resolution of the Government of the Republic of Lithuania No. 239, 26 February, 1998), which provides for a wide range of integration measures – from assistance in finding housing, organization of education and employment to provision of social welfare and health services. In addition, the Procedure emphasizes formation of favourable public opinion about the importance of arriving foreigners, through close cooperation of state and municipal authorities with the media and NGOs. The aforementioned acts constitute sufficient preconditions for the increase of the Lithuanian public interest in global developments, the latest features of migration processes and cultural diversity of the arriving foreigners.

So, at least two decades ago Lithuania declared that the process of integration of a foreigner is not only his/her responsibility, but also the responsibility of public authorities which have to create additional possibilities to enjoy the universally recognized human rights. Best practice of other countries shows that consistent implementation of integration measures allows to view this process not only as some kind of expenditure, but also as a kind of investment that can contribute to improvement of the social and economic situation in the state.

Ministry of Social Security and Labour, which is responsible for coordination of the policy of integration of foreigners in Lithuania (Resolution of the Government of the Republic of Lithuania No. 446, 22 May, 2014), at the end of 2014 approved the action plan for implementation of the policy on integration of foreigners for 2015–2017 (Order of the Ministry of Social Security and Labour Nr. A1-683, 31 December, 2014), which sets forth three major objectives:

- to integrate third country nationals into the society;
- to make the society more tolerant towards foreigners;
- to improve cooperation between the authorities in the area of integration of foreigners.

As can be seen, even after nearly several decades since the regulation of the legal status of foreigners was adopted, the action plan still identifies such problematic issues as social tolerance and the existing gaps in cooperation between

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<sup>5</sup> Social integration, in the broadest sense, is the process by which the state guarantees the means of providing equal possibilities to foreigners, who have been granted asylum, to support themselves and to participate in the society in the future, as well as to its other members.

institutions. There are many reasons for this, for example, so far there has been no clear distinction between the functions of the state/municipalities and NGOs in the process of refugee integration; there are serious problems in co-operation and co-ordination of these activities; the process of teaching the Lithuanian language is not appropriately ensured and, as a result, employment issues are not dealt with (Conference proceedings 'Refugees in Lithuania – experience and perspectives of integration', Mykolas Romeris University, 7 December, 2015), which hinders the development of multiculturalism of the society.

## 4. Trends of the development of multiculturalism in Lithuania – the focus on the possibilities

### 4.1. General trends of the development of multiculturalism

The research, conducted by the author of this article in 2015, which involved almost 1,100 respondents, aimed to evaluate the significance of factors which determine the development of multiculturalism and cover such questions as *Frequency of communication of Lithuanians and representatives of other cultures* (Table 2 and 3), *How multiculturalism is developed*, *Relevance of features of cultural differences* (Table 4), *Which countries people communicate most often* (Table 5), etc.

Table 2

#### Frequency of communication of Lithuanians and representatives of other cultures

Frequency of communication, %			
Several times in the quarter	Once in the quarter	Once every six months	Never
50	10	20	20

Source: compiled by the author on the basis of the results of the research in 2015

As we can see, every second respondent (50%) evaluates his/her relations with foreigners as permanent, however, every tenth respondent communicates with foreigners not more than once in the quarter (10%), while four out of ten respondents communicate with foreigners only once every six months or have no such experience at all. According to the data of the Department of Statistics of Lithuania, in 2014 less than half of employees in small municipalities communicated with foreigners 1–2 times per year, while 50% to 75% of employees had no contact with foreigners at all (Table 3).

Table 3

**Frequency of communication of employees from Lithuanian small municipalities and representatives of other cultures**

Municipality	Frequency of communication with foreign nationals (%)		
	More than once in half a year	On average once a year	Never
Kazlų Rūda	25	0	75
Kalvarija	20	20	60
Kupiškis district	20	40	40
Birštonas	20	40	40
Zarasai district	0	50	50
Skuodas district	0	25	75

*Source: Data of the Lithuanian Department of Statistics in 2014.*

The research of 2015 showed that there are problems with the development of multiculturalism in the working environment. The majority of Lithuanians communicate with foreigners without leaving Lithuania (52%), almost every third respondent (28%) goes abroad only once in a few years, and only one in five goes to other countries from several to a dozen times a year. In most cases this is higher-level officials. only every fourth participant in the study had possibility to gain experience of multiculturalism, for example, through participation in various experiential trainings and workshops or going on business trips or internships abroad. Nearly 50% of the respondents are not interested in this topic at all; others have learnt about multiculturalism while communicating with their colleagues.

Infrequent communication, or complete absence thereof, does not allow the people of Lithuania to reduce isolation and gain the required level of intercultural competence. Besides, the low frequency of communication with foreigners forms Lithuanians' attitudes to cultural differences, which is worth a serious scientific discussion. The study conducted by the author in 2013 (Table 4), which involved 200 respondents, shows that the attitude of the Lithuanian society to the need to develop interculturalism is quite diverse and varies in the range from 'very important' to 'not important/not relevant.'

Table 4

**Relevance of features of cultural differences, percent**

<b>Features of cultural differences</b>	<b>Important</b>	<b>Neither important nor unimportant</b>	<b>Not important</b>
Race	30.0	30.5	39.5
Nationality	42.6	30.9	26.6
Language	54.7	27.9	17.4
Religion	12.5	54.8	32.7
Sex	16.5	34.6	48.9
Sexual orientation	36.4	30.5	33.2

*Source: V. Grazulis, I. Kojelyte. Multiculturalism trends in modern Lithuania: problems and perspectives. In Megatrend Review, Megatrend University, Belgrade, 2014, p. 77–90.*

On the other hand, although a person's race and gender are not the essential features for Lithuanians in communication with foreigners, it is the person's nationality, the language of communication and sexual orientation that are still important factors which hinder the development of multicultural skills not only of a particular Lithuanian, but also of a foreigner residing in Lithuania. Besides, this study shows that the language barrier, different temperament and differently perceived informal styles of communication, misperception of a foreign culture and, more generally, lack of interest in foreigners as such are all significant reasons to cause intolerance outbreaks, thus, even though every second Lithuanian does not object to foreigners from non-EU countries to live in the neighborhood, an equal number of respondents do not want this neighborhood to be too close.

According to the research, more than half of the Lithuanian people (51.9%) communicate with people from a familiar cultural environment: East Europe (Russia, Ukraine, Belarus), Baltic States (Latvia and Estonia) and Middle Europe (Poland, Czechia, Slovakia, Hungary) (Table 5.).

Table 5

**People from which countries do you communicate most often with?**

<b>Destinations</b>	<b>Percent</b>
East Europe (Russia, Ukraine, Belarus)	19.7
Baltic states (Latvia, Estonia)	16.4
Middle Europe (Poland, Czechia, Hungary, Slovakia)	15.8
West Europe (France, Germany, Spain, Great Britain)	12.4
North Europe (Denmark, Norway, Sweden, Finland)	11.0
South Europe (Italy, Greece and other)	6.6
North America (Canada, USA)	3.8
Far East (China, South Korea, Japan, Philippines)	2.4
Australia, New Zealand, Indonesia	1.2
Iran, Iraq, Syria, Israel, Egypt, Qatar, Lebanon, Libya, Sudan, Nigeria, Brazil, Argentina, Columbia, Venezuela and other	10.7

*Source: compiled by the author on the basis of the results of the research in 2015*

In the last decade there has been a significant increase in communication with the West (France, Germany, Spain), North and South European countries and at present has become a major phenomenon in the development of interculturalism for three out of ten respondents going abroad. Although the pace of development of multiculturalism can hardly be considered as sufficient, the knowledge of Lithuanians about the geography of the regions of the world, which for the last several decades have been considered 'taboo' (North America, Far East and other 18.1%), is expanding significantly. At the same time, the increase in communication between the people from Lithuania and foreigners while leaving abroad, promotes the development of practical skills of multiculturalism, which, alongside communication in Lithuania, can be regarded as a positive feature in reducing isolation of the society.

As shown, the need to acquire and develop intercultural competence in the Lithuanian society is quite varied and evaluated from a 'very important' to 'not important / not relevant'. The study showed that more than half of the respondents (51.9%) most frequently communicate with people from Eastern Europe (Russia, Ukraine, Belarus), Baltic states (Latvia and Estonia) and Middle Europe (Poland, Czech Republic, Slovakia, Hungary). In the last decade there has been a significant increase in trips to the West (France, Germany, Spain), North and South European countries and at the moment trips have become an important intercultural phenomenon for four out of ten respondents who go abroad.

## **4.2. Evaluation of expression of multicultural competence**

The respondents of the study were asked to evaluate the importance of their education and the acquired intercultural competence elements (Table 6). The respondents had to provide answers to the following blocks of questions on such intercultural competence elements as:

- knowledge of the etiquette,
- knowledge about how to behave in public abroad,
- knowledge about business etiquette,
- general knowledge about the country's cultural and political situation,
- the ability to explain to a foreigner the important holidays, cultural peculiarities, etc.,
- understanding how foreigners interact with each other,
- knowledge about the most usual reasons of problems with foreigners.

Self-evaluation of the respondents according to the intercultural competence elements reveal statistically significant ( $p < 0.01$ ) differences in average values (t-criteria) according to most competence elements in the public and private sectors, the highest being as follows:

- how they perceive the relations between young and older persons ( $t = 4.36$ ,  $M = 3.25$  and  $2.87$ ),
- how they tend to tackle their problems ( $t = 5.00$ ,  $M = 3.14$  and  $2.71$ ),
- what peculiarities of their communication and negotiation there are ( $t = 5.41$ ,  $M = 3.19$  and  $2.72$ ),
- what method of expression of emotions is acceptable ( $t = 4.85$ ,  $M = 3.19$  and  $2.76$ ),
- how they understand religious variety ( $t = 4.04$ ,  $M = 4.05$  and  $3.66$ ),

- communication to a foreigner is not stressful for me or does not raise distrust in myself ( $t=4.84$ ,  $M = 3.82$  and  $3.38$ ),
- I know how to behave in unexpected and new situations that emerged due to cultural diversity ( $t=4.26$ ,  $M = 3.45$  and  $3.09$ ),
- I am flexible when I communicate with foreign nationals ( $t=4.91$ ,  $M = 3.85$  and  $3.41$ ),
- I observe and understand what I learned during communication with foreign nationals ( $t=4.33$ ,  $M = 3.82$  and  $3.44$ ).

According to other intercultural competence elements there were no statistically significant differences found. Differences in average values of self-evaluation of most of other competence elements are less perceptible; however, the obtained results show that the private sector pays more attention to the development of intercultural competence than the public sector (in the private sector the evaluation is higher than in the public sector).

## Conclusions

1. A person's interculturalism is defined as a two-way process, where awareness of and sensitivity to other ethnic groups should be assessed through multicultural competence characteristics. Communication of the Lithuanian people with other nationals is constantly expanding, which requires to pay special attention to the analysis of issues of multiculturalism.
2. The attitude of Lithuanians to the need to develop interculturalism in the society is quite diverse and varies from 'very important' to 'not important/not relevant.' Besides, older people, compared to the young generation, have a more reserved attitude towards communication with other nationals.
3. The respondents' self-evaluation of intercultural competence elements reliably suggests that special attention should be paid to such elements as *how they perceive the relations between young and older persons, how they tend to tackle their problems, what are the peculiarities of their communication and negotiation, what method of expression of emotions is acceptable, how they understand religious variety, communication with a foreigner is not stressful for me or does not raise distrust in myself, I know how to behave in unexpected and new situations that emerged due to cultural variety, I'm flexible when I communicate to foreign nationals, I observe and understand what I learned during communication with foreign nationals*. It was also noticed that the development of intercultural competence in Lithuania gets more attention in the private sector than in the public sector.

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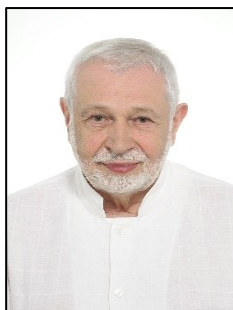
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## EVALUATION OF NON-FINANCIAL SOCIAL ASSISTANCE TO FAMILIES IN CHILD DAY CARE CENTERS: SITUATION ANALYSIS IN LITHUANIA

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### ***Abstract***

*The article focuses on the peculiarities of providing non-financial social assistance to social risk families in child day care centers. The research provides an analysis of the aspects of providing social assistance to disadvantaged families and their children, and it also discusses the possibilities of providing non-financial social assistance in child day care centers. The aim of the article is to identify the effectiveness of non-financial social assistance and to define its influence on social risk families and children of such families. The research, firstly, reveals the difficulties that the providers of non-financial social assistance and employees of child day care centers face in fulfilling their duties, and, secondly, specifies how non-financial social assistance provided in child day care centers affects disadvantaged families on reducing their social exclusion. The results of the research also reveal the possibilities of organizing and improving the process of providing non-financial assistance in child day care centers.*

**Keywords:** child day care center, non-financial social assistance, social risk families.

### **Introduction**

Lithuania's National Strategy "Lietuva 2030" calls for strengthening the family institution by establishing a family-friendly environment. The latter strategy encourages expanding the system of complex services and infrastructures for families, establishing favorable conditions for implementing the proactive function of families, and forming a positive public attitude towards the family institution. Moreover, the strategy foresees an obligation for the state, firstly, to protect the family institution as an important value of the society as a whole, secondly, to implement an effective family policy that would duly protect and support the family institution, and would ensure adequate conditions for raising and educating children. Article 38 of the Constitution of the Republic of Lithuania specifies the following: "The family shall be the basis of society and the State. Family, motherhood, fatherhood, and childhood shall be under the protection and care of the State." However, some families are not able to adapt to the rapidly changing economic conditions or to solve its problems independently and to care about their children's future properly. Therefore it is necessary to provide social assistance to families which encounter social exclusion and are marginalized not

only by means of satisfying the immediate needs which arise while being at social risk, but by ensuring adequate family welfare. The National Social Policy of the Republic of Lithuania prescribes providing financial and non-financial assistance; nevertheless, marginalized families still face many challenges, the gross family income is low, and hence these families face an increased risk of social exclusion. It must be noted, that it is crucial to help overcome social isolation and to ensure that such families and their children would receive adequate support that would ensure their welfare. Wolf (2012) points out that the social risk families must have more opportunities for socialization. One of the institutional forms of assistance to children from disadvantaged families is child day care centers, which provide comprehensive assistance to problem families and their children.

The effectiveness of social assistance and support for families was analyzed by scholars Lazutka, Guogis (2008), Krankalis, Dumskytė (2012), Žalimienė (2015), Žalimienė, Dunajevus (2015), Čižikienė, Virbalienė (2016). Currie, Gahvari (2008) analyzed the structure of social assistance, and Palme et. al. (2009) researched the effects of social assistance and social services to distinguished groups of service and assistance recipients, *etc.* Activities and organizational aspects of child day care centers were studied by such scholars as: Sipovič (2007); Masiliauskienė, Griškutė (2010); Bartkutė, Čižikienė (2012), Buzaitytė-Kašalynienė, Liaudginaitė-Zamalienė (2012); Gudžinskienė, Railienė (2012); Jančauskytė, Širiakovienė, Plaušnaitienė (2013); Vaitiekienė (2013), Gudžinskienė, Raudeliūnaitė, Uscila (2016). However, research results on non-monetary social support to problematic families of children in day care centers are lacking.

The aim of the article is to overview the peculiarities of providing non-financial social assistance to families in child day care centers and to assess the factors which affect the organizing of support to social risk families. The object of the research is non-financial social assistance to disadvantaged families in child day care centers. The methods of the research are the following: analysis of scientific literature, structured qualitative interview, analysis of gathered data and content, generalization.

## **1. Aspects of providing social assistance to social risk families**

The National Social Policy of the Republic of Lithuania encompasses means of assisting families in educating children, providing families with accommodation, providing a wide range of other social and health services (The National Family Policy Conception, 2008). The total social security costs for assisting families in order to reduce their social exclusion fall into the following categories: covering the costs of raising a child (family welfare, child benefits, child birth benefits); assistance with reconciling family-based and employment commitments (maternity/paternity benefits, child day care); special assistance to certain (the most vulnerable) types of families (benefits for multi-child (large) families, social services for families and children, custody and care benefits, covering costs of children catering).

The aim of social assistance is to reduce the poverty level of socially vulnerable persons and families, to compensate their loss of income, to ensure adequate

assistance and to reduce social exclusion (Information report “Social assistance to families and children” issued by the Ministry of Social Security and Labor of the Republic of Lithuania, 2015). Social assistance may be provided in a financial and non-financial manner; however, there is no consensus on which is the most effective form of assistance to the family. Comparing the changes in the levels of financial and non-financial assistance provided in Lithuania, it is estimated that during 1996–2013 the number of financial assistance cases increased 4,7 times, whereas non-financial support cases increased 4 times. From the perspective of an earner, financial social assistance provides greater personal autonomy, whereas non-financial assistance is perceived as help in a form of services (Žalimiene, Dunajevs, 2015). When analyzing the structure of costs of social security in Lithuania Žalimiene (2015) notes that financial assistance accounted for three-quarters of the total cost of support, whilst non-financial assistance tends to decrease and accounts for only about a quarter of all family support costs.

Providing assistance to social risk families in Lithuania is relevant and often leads to discussions about the feasibility and effectiveness of the social security system. A social risk family is a family raising one or more children under the age of 18 and where at least one of the parents abuses alcohol, drugs, psychotropic or toxic substances, is addicted to gambling, unable or unwilling to take proper care of the children due to lack of social skills, uses psychological, physical or sexual abuse against the children, uses state granted benefits contrary to the family’s interests subsequently endangering the children’s physical, mental, spiritual, moral development and security (The Law on Social Services of the Republic of Lithuania, 2006). The following principles and concepts are applied while working with social risk families: family responsibility; emphasizing that the family itself is responsible for the well-being of its members, whereas the additional assistance is provided in order to enable the family to take care of their children independently and properly; involvement and inclusion of the local community in creating a favorable social environment, while satisfying the common needs of living in the neighborhood, and, namely, for this reason the municipality strengthens and mobilizes communities; the principle of subsidiarity according to which the issues occurring in social risk families and providing assistance to such families are dealt with at the most effective level, *i.e.* at the community or municipality level, whereas assistance of a greater level is organized and provided only in cases when the community level assistance to the family is no longer sufficient; the principle of family individualization and assistance differentiation, understanding that every family and its need for social assistance is different; the principle of cooperation and mutual trust which suggests that social assistance and social services are provided, and the joint work with families is organized following the notion that the family itself can and must be responsible for the well-being of its members, whilst the community, community-based and other non-governmental organizations (NGOs), and other providers of social assistance and services may offer support to the family, and the municipality may concentrate the efforts of community-based organizations, non-governmental organizations and other social assistance and service providers, organize their joint work in order to enable families to solve their problems and to avoid social exclusion by all possible means

(Description of the Procedure of Join Work with Families approved by the order of 7 July, 2016, No. A1-362/V-936/V-464/1V-495).

It must be noted that social families encounter various problems, including but not restricted to the following: one or both of the parents have harmful habits and addictions, one or both of the parents threaten or employ physical punishments as the main means of discipline; one or both of the parents use the child as property; one or both of the parents do not satisfy the vital needs of the child or threaten to do so; one or both of the parents employ strong authoritarian control as means of education; the family fanatically follows certain movements or stereotypes; one or both of the parents implicitly requires the child's obedience (Methodical recommendations on Working with social risk families, 2003). Given the vast variety of challenges arising in social risk families, social assistance must be provided only after the particular case of the family is assessed in order to properly help the family to effectively solve its problems and to meet the needs of the family best.

Even though since 2007–2015 a decline of the number of social risk families and children growing up in them is observed (see Table 1), institutions that implement social security policies must continue searching for means and solutions for providing effective support to social risk families in order for the number of them to drop significantly.

*Table 1*

**Families at social risk and children growing in these families 2007–2015**

Year	2007	2008	2009	2010	2011	2012	2013	2014	2015
Social risk families	11 958	11 350	11 121	10 904	10 608	10 389	10 230	9 908	9 892
Children growing in social risk families	27 881	25 483	24 222	23 335	22 073	21 303	20 964	19 663	19 527

*Source: Data of the Lithuanian Department of Statistics*

One of the possible means of providing social assistance to social risk families is ensuring that their children can attend child day care centers. A child day care center (hereinafter – Day Care Center, Center) is an establishment or its subdivision that provides day care, activities through the day, recreational and other services for children in order to normalize their relation with the social environment (Catalogue of Social Services, 2006). The Centers provide an opportunity for the children to engage in useful and interesting activities. These centers also help the children with changing and aligning their values, adapting to the society, distracting the children from harmful effects of the streets. Moreover, child day care centers establish the necessary conditions for doing homework, preparing for classes and offer advice and counselling of experts in various fields (*e.g.* psychologists, social pedagogues). The first Day Care Centers in Lithuania were established in 1994 by the initiatives of various NGOs. The processes of establishing Day Care Centers started to intensify with the adoption of the National Program for Child Day Care Centers of Non-Governmental Organizations for 2002–2004 which

provided an opportunity for the project promoters to receive state funding, whereas the municipalities undertook to ensure the availability of social services in their territories by procuring social services following the public procurement procedure prescribed by law (National Program for Child Day Care Centers of Non-Governmental Organizations for 2002–2004). Being aware of the importance of social services to social risk families and their children, in 2002 the Ministry of Social Security and Labor of the Republic of Lithuania opened calls for public tenders of funded projects in order to provide social day care services for disadvantaged families and children. This measure was intended to ensure the continuity of the operations and development of child day care centers and to ensure the stability of the project promoters, especially NGOs (which make up about 85 per cent of all project promoters). Following the Child Welfare Program for 2013–2018, each year the Ministry of Social Security and Labor initiates a public tender for supporting projects of child day care centers. In 2015 the financing for the implementation of the aforementioned measure was increased by more than 2,65 million euro, contracts with 166 organizations were extended, and 49 organizations were funded in public tenders additionally (amounting to a total of 215 child day care centers), where social day care services were provided to 6274 children. The services provided in child day care centers act as preventive measures for ensuring that children from disadvantaged social risk families receive the required support together ensuring the integration process and that the family obtains assistance it requires to function. In 2015 there were 252 active Centers with 6730 children from social risk families attending them (see Table 2). It is evident that since 2014 there is a tendency of decline of the number of children receiving social services in child day care centers. Therefore, the amount of children attending child day care centers out of the total amount of children living in social risk families (34,5 per cent) shows that child day care centers satisfy only a third of the total need for social services. It is to be noted, that the majority of child day care centers are located in only a few regions of Lithuania (Kaunas, Vilnius and Marijampole city districts). However, currently twelve municipalities have at least one child day care center per municipality. In some instances only children living in cities can attend local day care centers since some elderships do not have day care centers, thus in these cases children are not provided with the required social care (according to a research conducted in 2015).

*Table 2*

**Children who receive social assistance in day care centers**

Year	2006	2007	2008	2009	2010	2011	2013	2014	2015
Children at social risk	7186	9245	6766	6764	8387	8013	8700	10600	6730

*Source: Report of the Lithuanian Department of Statistics on Social services, 2015*

In order to ensure the continuity of the National Child Welfare Strategy and its implementation measures under the plan for 2005–2012, and the National Strategy on the Child Guardianship (Care) System and its Reorganization and the



subsequent implementation measures under the plan for 2007–2012, the Ministry of Social Security and Labor confirmed the Child Welfare Program for 2013–2018 (hereinafter – the Program). The aim of the Program is to take into account the child's interests and needs, to create conditions for the child to grow in the biological family, to develop preventive and comprehensive services for children and families and to ensure accessibility of these services. Moreover, for children deprived of parental care, the Program aims to ensure adequate guardianship (care) or adoption conditions, in line with the best interests of the child and the child's need to grow up in a family environment or in an environment close to the family. The Program also aims at properly preparing the child for an independent life in the family and society. Furthermore, the Program seeks to improve the well-being of children and youth, who are in the risk group. Taking the current situation into account, the Program seeks to develop the establishment of child day care centers and open youth centers, to renovate existing child day care centers and youth centers, and to establish new centers. In summary, it may be stated that social services provided in child day care centers act as preventative means for ensuring that children from disadvantaged social risk families could avoid being separated from their biologic families and getting into foster homes. Therefore, given the importance of child day care centers, institutions must identify the reasons of families becoming of social risk, and they must also provide resources for the continuous development of child day care centers, ensuring that all persons and families at need are provided with social assistance.

## **2. Non-financial social assistance in child day care centers**

Having assessed the activities of child day care centers (2015), it may be stated that the social assistance provided in the centers contributes to reducing social exclusion of social risk families, establishes a safe environment for children, protects children from violence and abuse, reduces the influence of risk factors, prevents children from engaging in crime, drug addictions, and alcoholism. Day Care Centers also provide targeted activities for children from disadvantaged backgrounds and encourage children to develop and nurture their social skills. Sipovic (2007) distinguishes the following services as the main services provided in child day care centers: counseling, providing information, mediation and legal representation, providing socio-cultural services, assistance with developing social and communication skills, catering, training of job skills, behavioral correction, counseling and support in developing basic daily skills, computer literacy classes. The services of providing information and counseling are of particular importance as the parents are informed about the services provided for their children and the progress of such assistance. Moreover, these services allow the parents to analyze the situation of the family and to seek solutions for their issues together with specialists. Some of the day care centers offer mediation and legal representation services to families at need. Such services encompass legal counseling, assistance, help with solving legal, health, household difficulties, document and tax management, *etc.* Day Care Centers also organize various socio-cultural events for the whole family, as well as provide psychological counseling to parents.

Child day care centers aim to meet the needs of a specific client group (Sipovič, 2007). According to Masiliauskienė and Griškutė (2010), these organizations provide complex assistance with the purpose to organize proper child employment and after-class activities, to develop and foster the children’s abilities to resist social risk factors. Day care centers aim to foster and support the children’s motivation for learning, to organize leisure activities, and to protect children from abuse and loitering in the streets. Day care centers also aim at making the children from disadvantaged backgrounds feel like full members of the society and at increasing their self-esteem. Kvedaravičiūtė (2007) identified the classification of social services provided by non-governmental organizations to children from disadvantaged backgrounds (see Table 3).

*Table 3*

**Social services for children on the street**

<b>Social services</b>	<b>Activities</b>
Organizing leisure and recreational activities	Games, outings, trips, movies, sports, amateur activities
Family counseling	Individual and group sessions, situational analysis, expert counseling
Modelling behavior	Professional counseling, art therapy
Prevention programs	Integration into school and society, prevention against bad habits and addiction
Education	Homework preparation, developing social and personal hygiene skills

*Source: Kvedaravičiūtė, (2007)*

The report of the “Study on the Evaluation and Possibilities of Feasibility of the Activities and Social Services provided in Child Day Care Centers” (2015) indicates that child day care centers work with target groups which are attributed to the social risk category following various parameters (income, education, lifestyle, etc.). The activities of day care centers contribute to a crucial task of the social policy which is to tackle the “poverty circle” that includes a share of children from disadvantaged families. The assessment of the services provided in child day care centers suggests that the variety of such services is sufficiently diverse: the centers organize educational activities, homework preparation, leisure time activities, catering, and work with parents of the children who attend the Centers. The report of the study carried out by 2015 and the relevant survey of the parents indicate that comparing to the efforts of other organizations, child day care centers have become one of the main sources of support for social risk families.

## **Methods**

The aim of the research is to determine the opinion of the representatives of Day Care Centers and parents of disadvantaged families on providing non-financial social assistance to families in child day care centers, also the opinion of the

respondents regarding the situation, conditions, prerequisites and possibilities of providing such assistance.

The problem of the research is that when providing non-financial assistance it is crucial to precisely identify the possible difficulties of organizing the assistance and to offer the appropriate complex non-financial assistance to the family and children.

The tasks of the empirical research are the following: 1) to carry out an assessment of the opinions of executives and employees of Day Care Centers in order to determine the issues of providing non-financial social assistance; 2) propose ways to improve providing non-financial social assistance to social risk families and disadvantaged children in child day care centers.

The empirical research was conducted by applying the qualitative research method of analyzing the opinion of the respondents via a structured interview form of survey (Bitinas et. al., 2008). By applying the criterial selection principle two groups of respondents were distinguished: five non-financial social assistance providers (executives of child day care centers, who have been working with families at social risk for more than five years, and who directly interact with recipients of the assistance and provide non-financial social assistance to disadvantaged families) and five parents whose children attend child day care centers and receive non-financial social support.

The study was carried out in September–October, 2016 by applying the method of formal structured interview, *i.e.* an interview consisting of pre-formulated questions that all of the respondents were asked in the same order. The method of formal interview was chosen in order to assess the opinion of the respondents regarding the current situation. The evaluation of the research data reveals the approach and key issues regarding receiving and providing non-financial assistance in child day care centers. The predefined interview included interconnected questions for the respondents to answer. The following are the problematic questions of the interview: *How do you rate the importance of providing non-financial social assistance to families in order to solve their social issues? What changes in the family did you notice after your children started attending the child day care center and the family started receiving non-financial social support? Could you please describe the prospects of providing non-financial social assistance in child day care centers?*

It must be noted that the respondents agreed to participate in the study after they were informed about the ethics of the research: the course of research, data discretion and confidentiality, and that the data will be presented in a way that is not possible to identify a particular informant or Day Care Center. It should be noted, and the limitations of this study. The study was conducted in Vilnius county and it may not fully reflect the general situation of all Lithuanian children in Day Care Centers. In order to obtain accurate and reliable information necessary to carry out more detailed quantitative analysis.

## Results

During the interview the employees of child day care centers were asked to identify the difficulties that social risk families face. The respondents emphasized the following: *"the parents suffer from bad habits or addictions"*, *"there are acts of violence in the family"*, *"the parents are addicted to alcohol"*, *"the families face financial deprivation"*, *"the parents fail to satisfy even the basic needs of the family"*, *"the children do not have the possibility to prepare homework"*, *"the children do not get help at home, there is a lack of connection and communication with the parents"*, *"poor living conditions"*, *"the parents lack social skills"*, *"the children do not feel safe at home"*, *"the parents do not care about the child's needs"*, *"the parents lack parenting skills"*, *"the parents lack interest in the child's issues"*. The following problems of social risk families were identified: alcoholism and other addictions, acts of violence at home, financial deprivation, and lack of social and parenting skills. In summary, it can be said that children from disadvantaged families often face lack of parental attention, as they also experience the consequences of alcoholism and addiction of the parents, in most cases poverty prevails in the families, and also situations of violence outbreaks in the families were mentioned. The answers of the respondents reveal that the employees of child day care centers are well informed about the problems and difficulties occurring in social risk families. During the interview the employees noted that they not only have to help the children, but also need to pay a significant amount of attention to the rest members of the family and the family as a whole. Moreover, it is crucial to identify the challenges and difficulties that the children face in school. The employees of child day care centers pointed out the following problems: *"the children experience bullying because of their poverty"*, *"bullying"*, *"bullying is a huge issue in schools"*, *"the children are bullied because of their family situation"*, *"the have learning difficulties due to neglect"*, *"they are unable to learn because they have learning gaps"*, *"they have learning and behavioral difficulties"*, *"they have lost desire to learn"*, *"they experience learning difficulties"*. All of the respondents identified the issue of bullying in schools: *"the children face bullying because of their family situation and that their parents abuse alcohol"*, *"the parents cannot afford buying new things for children"*, *"the children do not have the possibility to go to events or field trips with the class"*. Interestingly, the respondents identified poverty and the situation of the family as one of the main causes of bullying because the children do not have the things that the majority of their peers have. Furthermore, the respondents identified and pointed out the problems associated with the behavior and communication of the children in school: *"conflicts with peers"*, *"skipping classes is our problem"*, *"the parents are indifferent to the problems of their children"*, *"there is an increase of emotional abuse"*, *"physical abuse of other students"*, *"conflicts with teachers"*, *"smoking tobacco, alcohol consumption and exposure to toxic substances"*. The respondents notice that children who lack social and communication skills often misbehave and get into conflicts with their peers and teachers, they also tend to solve their issues using violence. Moreover, such children usually befriend peers from a similar disadvantaged background and then subsequently find themselves in social exclusion. The respondents also note that the aforementioned reasons determine the behavior of the child: *"the children*

*experience difficulties communicating”, “the children have low self-esteem”, “they are unable to manage their emotions”.*

The respondents listed the following ways of how social assistance provided in child day care centers helps solving issues of social risk families and disadvantaged children: *“personal attention to the child”, “individual attention to the whole family”, “developing social skills”, “preventative events and activities”, “means and methods of solving problems and conflict”, “personal consultations provided for the children and parents”, “catering”, “psychological counseling”, “developing personal hygiene skills”, “providing essential facilities, equipment and supplies”, “assistance with coping with the authorities”, “consultations on various issues”.* The employees of child day care centers found that families often ask for help when there is a need to mediate issues with various authorities regarding the family's social issues. The study showed, that complex social services offered in child day care centers help social risk families with solving their problems and provides an opportunity to reduce social exclusion of the families. It may be stated that individual care and attention, group activities and sessions, proper and adequate non-financial social assistance provided in child day care centers shall be effective when there will be reciprocal communication and cooperation with the child and family and this shall subsequently reduce the number of social risk families.

Cooperation between the employees of child day care centers and with the parents of disadvantaged families, their confidence in the latter employees are all very important factors in the successful integration process: *“it is crucial that the parents trust the center and its employees”, “it is essential to establish a contact with the parents”, “it is difficult to invite parents to participate in group sessions and activities, but after some time they attend the activities willingly”, “the mother told her story”, “the parents ask for advice on various issues”, “we are glad when the family puts in effort and endeavors”.* The respondents state that non-financial social assistance is highly important to disadvantaged families and to the children of these families as it helps in solving their problems, integrating them into the community, finding like-minded people, generally getting support and assistance, expressing their concerns and learning to deal with them in a safe manner.

The respondents emphasized the shift in the behavior of the children and family due to the social services provided in the centers: *“the life of the family changed”, “they gradually became capable of assessing and comprehending their behavior and actions”, “the psychological condition of the family members improved”, “the behavior of the children improved, they became more polite”, “they gained self-confidence”, “the child's approach to school changed”, “they stopped cursing and using foul language”, “they gradually learned how to reach an agreement”, “they learned how to express their emotions”, “they became able to help a friend with homework”, “the children's grades improved”, “they became more confident”, “they managed to share personal stories, feelings and experiences in personal consultations”, “families started participating in groups sessions and events”, “the parents helped when we were tidying up the environment of the center”, “the parents became more interested and involved in their children's lives”.* It may be said that receiving non-financial social assistance has a great influence on the communication of the family members. Moreover, positive changes in the behavior of the children and the life of the family are evident. The families manage to take into account the advice provided by the specialists; they approve individual and

group work, understand the positive effects of the assistance not only to the well-being of their children, but also to the family as a whole.

With regard to the prospects of providing non-financial social services to children and their families, the employees of child day care centers states the following: *"it is important to accept the child, to know and understand the child's problems", "the child must be able to talk to me", "it is crucial that the child and the family members would feel and endorse their personal value", "to make the child happy", "when the child will trust the employees and specialists of the center, it will become easier to work with them, however this takes time", "it is crucial to get to know the child", "we discuss the assistance plan with the families individually", "we establish personal future goals, even though sometimes they are very small...", "the children must feel safe and they must trust the employees", "we must discover the strengths of the child", "development of personal virtues is important", "if the families feel sincere support, it is likely that the family will endeavor on its own", "to help the family by all means", "the family must comprehend its responsibility for the issue".* The study shows that it is important to initiate and maintain a personal connection and relationship between the child (children) and parents. Whether the social assistance will be accepted, whether the right system of values will be fostered, whether the required skills and a sense of responsibility will be developed, and whether future goals shall be accomplished depends solely on the abilities and competences of the employees of child day care centers.

The qualitative study was also aimed at revealing the views of the parents regarding their social issues and non-financial social assistance. The respondents identify the following problems: *"my husband becomes very aggressive when he is drunk", "I used to abuse alcohol", "we argue about old mistakes", "my husband tends to be very angry", "disagreements with my husband interfere with our lives", "I do not know how to get along with him", "the children are furious about the divorce", "we fight and quarrel because my husband prefers the company of his friends", "they do not communicate a lot, both the father and the son are interested only in themselves", "I cannot express my opinion", "perhaps these are my communication problems".* It may be stated that most of the disagreements in social risk families arise due to alcohol abuse, subsequently resulting in outbreaks of violence, whereas children suffer experiencing such behavior in the family. The respondents emphasize the issues that occur in the communication between children and parents. It may be assumed, that alcohol consumption by the parents, violence, constant disagreements between the parents, communication flaws and gaps are the main causes of families becoming of social risk.

The study was aimed at examining what the parents know about the issues that their children face in school. The respondents listed the following: *"my child is only interested in hanging around with some sort of friends", "he told me he was going to school but apparently he did not show up", "my child always gets into conflicts with everyone in the class, the teachers say that he is a roughneck and bully", "he spends the whole day outdoors and does not want to do his homework at all", "my child was having problems with homework, but I do not understand any of it so I cannot help", "my child could not work individually", "he does not do his homework or forgets to bring important supplies to school", "forgets what was for homework", "he has troubles learning and writing", "he has difficulties reading", "math is too hard for my*

girl", "he does not know how to behave with his classmates", "he has troubles concentrating, he only wants to run off somewhere", "I cannot help him, I do not have the time". The respondents noticed, that their children fail to concentrate, have issues reading, writing and doing mathematics, moreover, the children are unable to do their homework independently. The answers of the respondents show that children raised in social risk families do not obtain sufficient support and help with their homework. All of the respondents pointed out that they do not have the capacity and (or) time to help their children with their homework. It may be assumed, that the children are neglected and left on their own in learning matters and must answer for their performance in school. Such behavior of the parents forces children to feel tension, which manifests in reluctance to go to school, unacceptable behavior in school, etc.

Part of the questionnaire included queries regarding the changes that the children experienced because of the social services provided in child day care centers and how in general did this assistance benefit the children. The answers varied as follows: "started doing homework at home", "the child is eager to interact, tell what he did in the child day care center", "there are obvious improvements in the child's behavior", "communication with the child changed dramatically to the better", "the child can now clearly express his opinion", "she found true friends in the child day care center", "now she has her own opinion", "he willingly interacts with other children", "he is no longer rejected in class, because now he has interesting stories to tell", "he is no longer afraid to invite friends home", "he understands that education is necessary", "he feels responsible, checks whether everything is done and prepared for school", "there are not as many of complaints from the teachers as before". All of the respondents identified positive changes in the lives of children who attend child day care centers. According to the respondents, children try to do their homework independently, they interact more with their parents and tend to share their experiences more often. Such evident changes in the children's lives gladden their parents, the respondents begin to comprehend the subsequent changes in their own lives as the risks reduce, there is more positivity in the family and the communication between the family members improves.

The study indicates that children who attend child day care centers have a better sense of their value and more self-esteem as they learn to express their opinion with more confidence, manage to choose suitable friends, children advance in school and education, the children generally show better results and demonstrate better behavior. All of the respondents rated the non-financial social assistance provided in child day care centers positively, emphasizing the contribution of the employees of the centers. The respondents answered accordingly: "we get help here", "the child day care center offers significant support to our family", "we started to communicate better in the family", "our child likes coming here and I am calm", "I feel welcome and awaited in the day center", "the child has more confidence in himself", "the child experienced dramatic changes, he already has friends in school", "my son relies on himself", "she manages to smile", "my daughter does not feel so constrained anymore", "the boy started to express emotions", "the children had the possibility to see the sea, when we did not have opportunity to travel", "he is now able to realize himself", "the employees understand us and listen to us".

Summarizing the opinions of the representatives of child day care centers and parents regarding social issues occurring in families, it is evident that the parent's

issues with alcoholism (alcohol abuse) and violence outbreaks were distinguished as one of the most relevant problems of social risk families. It may be stated that children who are raised in social risk families experience the consequences of alcoholism of their parents, the children also face neglect, abuse, violence, tension in the family, communication difficulties and are bullied in school. It was determined that parents have a positive approach to the effort of the employees of child day care centers and appreciate the positive interaction, personal development and emphasize the importance of the social non-financial assistance provided in child day care centers.

## **Conclusions**

Providing non-financial social assistance in child day care centers is based on the principle of cooperation by assessing and comprehending the particular case of each family individually, identifying the occurring issues, involving the parents and specialists into the process of providing social assistance. The study reveals that children who are raised in social risk families experience alcoholism and alcohol abuse of their parents, violence and neglect at home. Furthermore, these children encounter bullying and tension in school, they have difficulties communicating with their peers and teachers, and they also experience difficulties learning. All of the aforementioned factors subsequently lead to behavioral disorders and reluctance to go to school. The following social issues may be distinguished: children lack communication and conflict management skills, violence and misbehavior is justified, the children have low self-esteem, they do not feel safe at home and school.

It was found that integrated and complex social services provided in child day care centers help the families and their children to overcome and solve their social issues with the following means: counseling services; cooperating and interacting directly with the parents and children; organizing individual and groups sessions with the family members; providing expert consultations and case analysis; addressing the basic needs of the family and its members; developing crucial skills; providing activities and keeping the children busy throughout the day; assisting the children in the learning process; creating conditions for appropriate communication among children. The research shows that non-financial social assistance provided in child day care centers is effective, purposeful, and necessary, even more, the services fulfill the expectations and needs of the children and parents. Following the results of the research it may be stated that good personal relations between the employees of the center and the parents and children help the families in achieving positive changes in their behavior, whereas the social services provided in the day care centers contribute to the social cohesion of the society and reduces the social exclusion of social risk families and disadvantage children.



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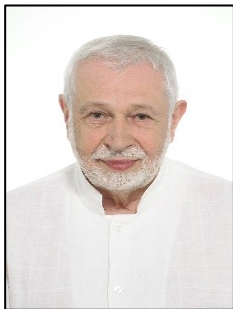
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## INFRASTRUCTURE FUNDING FOR SUSTAINABLE DEVELOPMENT OF RAILWAY TRANSPORT IN LATVIA

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### ***Abstract***

*Transportation and storage industry in Latvia generates a rough 10% of national GDP and therefore has a significant impact on the economy. Overall, more than 70 thousand people are employed in the transit and logistics sector. Underlying railway sector contributes more than EUR 100 million in taxes each year. For specific goods and destinations railway transport is a more sustainable, environmentally effective and economically efficient transport mode in comparison to the road transport and therefore should be promoted, which is in line with one of the transport policy priorities of the EU development strategy 'Europe 2020' – to make carriage by rail more competitive than road transportation. To help implementation of this strategy, the railway sector is in need of governmental help, either in form of state aid or alternatively revision of national excise duty policy on fuel used in railway transportation. One example is to redistribute the revenue from excise duty on diesel used in rail transport to finance maintenance and development of railway infrastructure.*

**Keywords:** railway transport, excise duty, investments, infrastructure

### **Introduction**

Rail transport is one of the most efficient transport modes for carriage of large volume freight over long distances. European transport policy aims to create a high efficiency network of the European transport with the main central railway lines, to develop internal market sector of rail transport, make it more efficient and more relevant to customers' needs, which leads to increased rail transport (COM 2012).

Railway transport sector in Latvia experiences a decades long slowdown. Arguably the latest geopolitical standings imply a further drop of international transit freight flows; however, internally one of the main reasons behind the decline is outdated rail infrastructure and rolling stock. Deterioration of infrastructure has occurred in the light of insufficient infrastructure funding which is provided solely by railway operators in Latvia.

A new network access charging scheme has revived the issue of reverting excise tax duty on petroleum products paid by railway operators to help funding the rail network maintenance. A solution eligible to persisting straits: tight national budget, no excise duty relief for railway transport, no public funding for railway infrastructure, excise duty collected from railway industry allocated to competing road transport sector.

The purpose of this research is to provide insight into the rail transport development in Latvia, to determine the main obstacles hindering its progress and provide a ready solution to the complex situation. The objectives of the research are to determine the multitude of loss of the railway transport market share, to investigate the main technical features of railway network, to evaluate funding sufficiency of the infrastructure manager and economic burden it imposes on railway operators, to review the new infrastructure access charging model and valuable experiences in other countries.

The study was based on comprehension of the causation behind the railway transport slowdown, examination of the applicable rules and strategic planning documents and the actual practice with particular attention to the issues of public infrastructure access charge impact on railway operators and insufficient network maintenance and development funding. In order to determine the possible practical solutions to the problem, the research is based on the findings from the economic and statistical analysis, using the graphical, descriptive and other methods.

### 1. Drift away from railway transport

The Transport White Paper published by the European Commission states that 30% of road freight over a distance of 300 km by 2030 should be transferred to rail or water transport and by 2050 this amount needs to be at least 50%. By 2050 the majority of medium- distance passenger transport should be carried by rail (COM 2011).

Contrary to the EU policy, a dramatic fall of railway transport employment is observed in Latvia. The percentage of freight transported by rail has reduced by 20% since 1998. Long lasting trend in Latvia shown in Figure 1 illustrates preferential use of road transport instead.

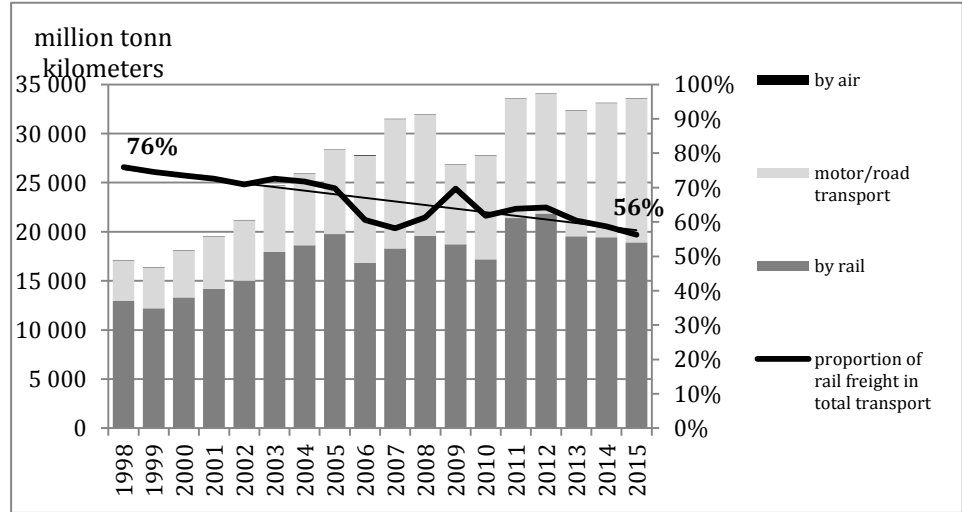
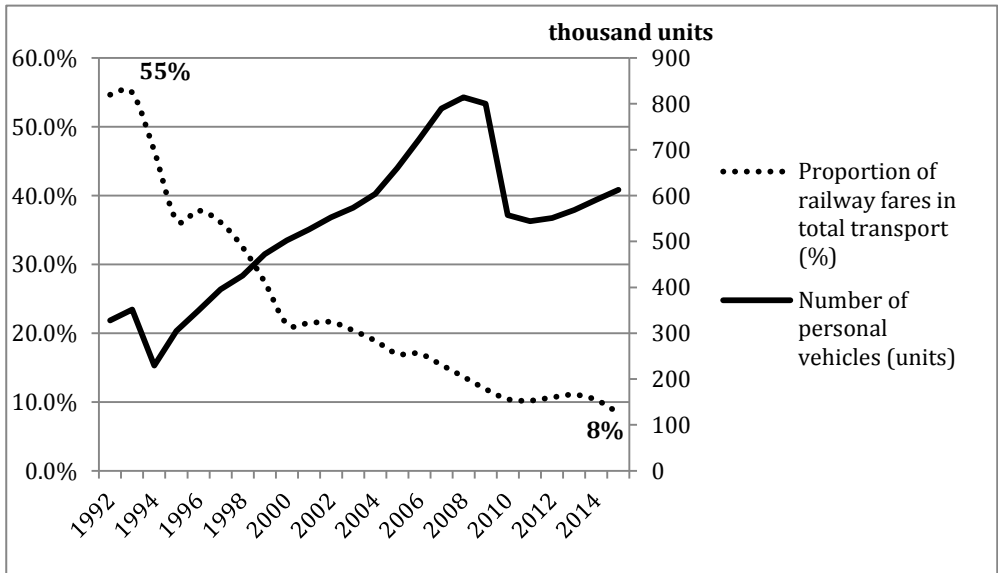


Figure 1. The dynamics of freight turnover in Latvia by main modes of transport (mln tonn – km) and percentage of rail transport (%)

Source: Central Statistical Bureau, 2016

The basic use of the railway transport in Latvia is carriage of transit cargos to the main Latvian seaports. Fossil fuel product exports from Russia and Belarus in the amount of 45.44 million tons last year form 80–82% in total freight volume carried by rail (Central Statistical Bureau 2016). The main competitor for transit cargos is Lithuanian port Klaipėda, yet fundamentally all Baltic states face a direct and hardly diversifiable threat of losing all Russian and potentially Belarussian freight flows, since the strategic and politically motivated decision being enforced of channeling fossil exports through the own ports in Russia.

The number of passengers travelling by rail has shown a major fall as well during the last two decades (see Figure 2).



**Figure 2. Comparison of passenger transport preferences in Latvia, units of personal vehicles vs. percentage of rail transport (%)**

*Source: Central Statistical Bureau, 2016*

In 1993 55% of all passenger kilometers in Latvia had been transported by rail, whereas in 2015 only 8.4% of the total made it by rail (Central Statistical Bureau 2016). The main reason behind such a dive is the rapid growth of private vehicle usage during the years 1993–2008, which outperformed the outdated railway infrastructure and rolling stock. Hardship to increase the percentage of railway passengers lies within the thin population outside Riga, which roughly holds about a half of all inhabitants in Latvia, as well as the fact that railway lines lack connection to other main railway lines and interoperability with other transport modes. For comparison, the Swiss travel system comprises 27'000 kilometers of rail, road and waterway routes nationwide, the densest public transport network in the world, with coordinated connections linking more than 150 public transport services and travel tickets which cover the entire country (Swiss Travel System). In Latvia, as chairman of the national passenger carrier puts it, there is a potential for the rail transport to become the main mode of transport in specific regions and

specific groups of passengers, e.g. in the suburbs of Riga for transportation of workforce or seasonal lines from Riga to Jūrmala, a popular recreation place in summer (A.Lubāns). It is furthermore stated in the law that for major long distance passenger flows covering long distances the priority transport mode should be railway (The Law on Public Transport).

## **2. Main technical parameters of railway infrastructure**

Latvian public rail infrastructure is geographically lined across the state connecting East border of the State with the largest seaports Riga, Ventspils and Liepāja (East-West freight transit corridor). The network also includes the principal railway line across the State from North to South connecting Estonia, Lithuania, Russia and Belarus. The overall length of the rail network is 1'827 kilometers of which 257 km (14%) are electrified lines. All tracks bear 1'520-millimeter gauge, maximum axle load is 25 tons. The railway infrastructure in Latvia is eligible for carriage both freight and passengers. The current capacity use of rail infrastructure is 70% for freight trains and 30% for passenger trains (Statistics of Latvijas dzelzceļš, 2015).

Due to insufficient funding deterioration of railway infrastructure is evident, and in order to retain the current infrastructure capacity and quality, minimum 181.2 kilometers of the tracks require capital repairs before 2020. The number of electricity supply lines and contacts have been long outdated and require repair, many buildings require replacement of outdated heating systems. Railway infrastructure development projects aim towards expansion of Daugavpils marshalling yard (EUR 39.8 million), development of Daugavpils train arrival station and its access driveways (EUR 45.8 million), modernisation of Riga railway junction (EUR 19.6 million), modernisation of platforms, transport security and information systems for passenger transportation (EUR 24.2 million), modernisation of train traffic planning system (EUR 21.3 million). Government considers electrification of mainline railways to Riga and Ventspils seaports totaling EUR 1.5 billion of which EUR 347 million is granted by European Cohesion fund. (The Ministry of Transport 2016).

Construction of the new high-speed Rail Baltica infrastructure linking Tallinn, Riga, Kaunas, Warsaw and Berlin face various hardships from the very beginning since the project was put on the drawing board in 1994. Delays much stem from hassle among the Baltic states on various items, yet the fundamental problematics associated with the new European standard 1'435-mm gauge infrastructure is the train speed. In particular, the technical condition of 200 km part from Lithuanian-Poland border to Białystok often drops to around 30 km/h. The Polish government however has promised to upgrade the section to 160 km/h, still below the projected 240 km/h, which undermines the high-speediness of the whole project. (Niitra, The Economist). Clearly the feasibility to cover the Tallinn-Warsaw distance under reasonable 7 hours is uncertain.

### **3. Infrastructure funding and access charge wedge**

In Latvia all capital and current rail network expenditures are financed by users of the network (rail operators) and no public funding is provided for maintenance and modernization of the network. Generally, infrastructure maintenance expenses in Latvia, which form a relatively fixed amount per year, to this day is collected from rail operators in the form of access charge, being inelastic to changes in the cargo flows. In shrinking freight market such access charging model creates significant pressure upon operators' ability to provide competitive carriage tariffs. The authors have investigated that infrastructure access charge forms up to 41–43% wedge in total transportation tariff for several dry bulk cargos in longer destinations (e.g. coal products to Ventspils). Market dictates tariff limits well below full cost levels, barely covering operator's variable costs. Else, because infrastructure access charge is tagged to the distance a train covers, those operators providing carriage services within shorter distances, such as to Riga, are less handicapped. This is one of the main reasons why freight flow shift from Ventspils port to Riga is observed.

In order to maintain national rail infrastructure at least of its current capacity and condition and prevent further deterioration, state aid is indispensable. Besides technically outdated infrastructure, Latvian infrastructure manager JSC Latvijas dzelzceļš faces a serious financial pressure. Gross yield of the company was negative in 2013 (-1.0%), which improved slightly in 2014 reaching 3.1% and reported negative again in 2015 (-4.65%) (Latvian Railways in 2016). The Ministry of Transport has estimated that by current freight volume flowing through rail infrastructure (48–50 million tons per year), infrastructure manager's funding is EUR 20–25 million shy (The Ministry of Transport 2016).

Secondly, financial statements of the JSC "Latvian Railway" show increased insolvency risk due to highly leveraged capital structure. Infrastructure manager reports EUR 840.4 million in long-term assets in 2015 financed by EUR 267.6 million equity and EUR 498.4 million long term debt, and the gap of EUR 74.4 million is financed by short term liabilities. Considering that the debt to equity ratio of infrastructure manager has reached 2.13 in 2015, additional liabilities if available may incur insolvency risk. At infrastructure manager's best projection availability of external capital will exhaust by 2020 unless state aid is provided for funding of the public infrastructure.

### **4. New policy framework for infrastructure funding**

Requirement of the Single European railway area, which Latvia joined earlier this year, is that a multiannual agreement is settled between infrastructure manager and the Ministry of Transport covering various important aspects such as provision of economic equilibrium for network maintenance, provision of funding for low intensity used lines, funding (also European funding) for new large infrastructure projects, funding for maintenance of public services facilities (passenger carriage), funding for state security facilities, funding for state



regulative institutions in railway sector and funding for heritage railways (p.10<sup>2</sup> Railway Law).

New approach to infrastructure access pricing is established in the Railway Law (p.11, 11<sup>1</sup> and 10<sup>2</sup>) splitting current comprehensive access charge into charge for minimum access package and charge imposed for track access within service facilities, as under EC Directive 2012/34/EU. Starting January 1, 2018 the state will be obliged to provide funding for the spread between infrastructure maintenance full cost expenditures and collected revenue from access charge, where the latter is determined in accordance with directly incurred costs principle. The law thereto allows several sources of funding to secure financial stability of the infrastructure manager: revenue from minimum access services, revenue from state land lease under the public railway infrastructure, net income from state owned service facilities and other commercial operations, state aid for granting financial equilibrium of the infrastructure manager and funding for investment projects, other private non-refundable sources.

## **5. Review of literature and practice in other countries**

Retardation of railway transport development is observed elsewhere in Europe, showing average decline from 10% to 6% market share in passenger kilometers and from 20% to 8% market share in freight ton kilometers over the last 30 years. In the last two decades the European Commission has been very active in restructuring the European rail sector addressing the problem in Commission White Paper of 30 July 1996 "A strategy for revitalizing the Community's railways", Commission White Paper of 28 March 2011 "Roadmap to a Single European Transport Area – Towards a competitive and resource", railway legislation packages and other policy framework documents aimed to improve transport systems in Europe.

Besides legislative provisions, the European Commission has played a major role in the development of high speed rail passenger services in Europe through grants to develop the trans-European network, although most European funding has in fact come from regional and cohesion funds or through the European Investment Bank (Nash, 2010). European Commission (2014) estimates for European countries €34.5 billion investments in 2012 for the whole rail network (including high-speed). Concerning the conventional networks, these investments cover maintenance (29%), enhancement (36%) and renewal (35%) of the infrastructure. In most of the European countries, public funds represent the main source for infrastructure investment while access charges finance the majority of operations and maintenance costs (Laurino et. al., 2015). Also Dehornoy (2011) provides evidence to this statement in a study on public contributions to European rail systems: German government transfers were €4.2 bn in 2010 and fund most of infrastructure investments, including 80% of renewal investments and all development investments, while access charges were enough to finance operations and maintenance (€1.5 bn) and a share of renewal investments (€0.5 bn). British Network Rail in 2009 received £3.9 bn in direct grants, but only £2.0 bn in track access charges; the direct subsidies from the Department of Transport constitute most of Network Rail revenue. The infrastructure is almost entirely financed by the State budget in Sweden – €1.6 bn in 2009 and only marginally by access charges

(~ €0.05 bn). Major infrastructure investments in Switzerland are funded by a special Public Transport Fund, whose resources are direct affected taxes: levy on commercial trucks (65%), oil tax (25%) and sales tax (10%).

At governments disposal there are a number of options to choose from in determining the level of public aid for railway transport and techniques of its implementation. Examples include fixed regional public expenditure shares are used in Belgium to allocate federal investment funds to railway projects (Proost & Zaporozhets 2013). This study confirms the relative efficiency of such an approach to Belgian rail investments. Perkins (2005) describes experiences in 2001 in Switzerland, where implementation of road Heavy Vehicle Fee (HVF) raised approximately €450 million, of which two thirds were earmarked for rail investments, mainly for two long tunnels through the Alps designed to substantially increase rail freight productivity and make rail competitive with road freight; also some revenues went to high speed passenger rail investments. Similarly, in Italy, upgrading of the rail line leading to the Brenner alpine pass into Austria is being financed with revenues from the toll motorway serving the same route.

Public authorities (usually central Governments) subsidies appear to be the most important form of public funding used across Europe (NERA, 2004). This support can be either a generic subsidy to the infrastructure manager or it can be targeted towards specific investments programs, many countries have both (Dehornoy, 2011). In some countries, grants for investments as per ton kilometer are available if the railway system attracts new customers that would otherwise use the road transport. This may be the option for for rail only, or combined road-rail transport operations, and the support is provided in the interests of protecting the environment (Perkins, 2005).

The country-specific research reveals a large amount of different approaches to the funding of infrastructure network. Some countries place fuel and other excise taxes with general revenues and fund roads from general revenues, including Australia, England, Germany and Italy. Several of the countries appear to rely on private roads, concessions or private-public partnerships as means to fund some of their road infrastructure, including Canada, China, France, Israel, and South Africa (May, 2014). Most of the countries have tolling systems to obtain part of their revenue for financing roads (Andersson, 2012; Raux et. al., 2007). In the case of Japan and France, tolls are linked with the weight of the vehicle and distance traveled (May, 2014; Raux et. al., 2007).

By international comparison, Swedish rail infrastructure charges are low – nearly ten times as high in Germany and France (Ljungberg, 2013). In addition, the infrastructure charges' share of the costs of rail transport in 2011 is on average only 5% for passenger transport and 6% for freight transport in Sweden, while the corresponding figures in Europe are on average between 10% and 30%, and considerably higher in certain cases (Matthews et. al., 2009). Sweden is trying to compensate industry for the peripheral location of the country and hence higher transport costs through low rail infrastructure charges and limited taxation on heavy goods vehicles. There is also an intention, for environmental reasons among else, to shift freight transport from road to rail or at least maintain the existing rail freight transport (Ljungberg, 2013). Many authors pointed out the importance of environmental factors, for instance, Dziuba (2015) claimed that offering tax a

refund in its construction can function as an incentive encouraging to choose railway as the means of transport which results in lower environmental burden.

Charges vary among the countries for plenty of reasons and can only partly be explained by actual differences in the infrastructure, which result in varied costs for wear and tear. However, it is obvious that the difference in infrastructure charges applied is also related to the extent to which governments are willing to allocate resources to directly finance the infrastructure in order to make good, but especially cheap, rail transport possible (Ljungberg, 2013). Nash, Nilsson and Link (2013) suggests that the German approach has led to a relief of taxpayers' burden for railway financing – government transfers have almost remained constant in real terms, in contrast to other countries such as the UK and Sweden.

Roads and railways in Sweden are mainly financed with national government taxes. Andersson and Söderberg (2012) propose a new regional order for the infrastructure policy in Sweden: government expenses for roads and railways should be decentralized to regions along with the real estate taxes to finance them. Instead of financing 50–75% of the costs for transportation projects with national taxes, as now is the case, the regional authorities are supposed to determine their own tax rates according to their different needs to cover expenditures for their infrastructure.

Also Denmark recently launched a regional reform that has given new large regions the responsibility for parts of the infrastructure network (Andersson, 2012). The development of the railway infrastructure in regions can be one of the main factors creating the conditions for social and economic development of the region (Buslowska, 2015). The most salient conclusion of Cohen and Kamga's research (2013) is that public grants, loans and credit guarantees that greatly minimize financial risk are required to attract private sector participation in financing high costs railway projects. In both Britain and Sweden public financial support for the rail industry has grown enormously, particularly in terms of spending on infrastructure renewal and enhancement; public support has grown significantly less in Germany, but the growth there has been mainly in subsidies rather than investment (Nash et. al., 2013).

According to Council directive 2003/96/EC the member states can apply total or partial exemptions or tax reduction on energy products used for the carriage of goods and passengers by rail. Several member states apply partial or total exemption of the excise tax on diesel used in rail transport (see Table 1). However, excise duty on fuel used by railway transport is paid in full amount in Latvia.

Table 1

**The excise tax on diesel used in rail transport**

Country	EUR/1000 l	Country	EUR/1000 l
Belgium	0	Luxembourg	0
Denmark	60.99	Portugal	90.11
France	128.3	Slovenia	253.66
Estonia	110.95	Finland	214
Italy	185.22	Spain	0
Ireland	108.28	Hungary	0
Latvia	341	Sweden	0

Source: TAXUD, 2016

## 6. Infrastructure funding solution for tight national budget

National budgetary deficit in 2015 is EUR 306.2 million or 1.3% of GDP (Central Statistical Bureau 2016), which allows to assume political reluctance to provide urgently needed funding for railway infrastructure. The authors therefore sought solutions to the problem which would have no impact on the national budget and offer a fair remedy helping promotion of rail transport.

As mentioned before, in Latvia only a small proportion of railway lines is electrified for the use of passenger transportation, whereas all freight carriage by rail is performed using diesel traction. Full rate excise duty (EUR 341 per 1'000 liters) is imposed in Latvia for diesel fuel which operators use in railway carriage. No reduced taxation or tax exemption is provided in national legislation, although provided so under Council Directive 2003/96/EC and is observed in practice in number of Member states. Since any tax reduction would put additional constraint to the national budget, authors revive suggestion to redistribute excise duty collected from rail operators and reverting it back to the railway transport system, infrastructure in particular. Such settlement has been discussed in 2012 and suggested to government by The Latvian Port, Transit and Logistics Council in support of professional associations in the industry, however no results had been achieved.

The excise duty imposed on diesel is nested in the carriage tariff. The authors have estimated that subject to physical properties of the goods transported, power and fuel efficiency of the traction vehicle used, the carrying capacity and elevation of the rail track, etc. parameters, the excise duty forms 8–12% wedge in total carriage tariff (see Table 2).

*Table 2*

**Excise duty wedge in rail carriage tariff**

<b>Carriage route (Eastern borders to seaports)</b>	<b>Transit freight volume</b>	<b>Excise duty cost, EUR/t</b>	<b>Total excise duty p.a., EUR</b>
Indra/Kārsava/Zilupe–Ventspils	15 mln. t	0.72 EUR/t	EUR 10.8 mln.
Indra/Kārsava/Zilupe–Liepāja	3 mln. t	0.72 EUR/t	EUR 2.16 mln.
Indra/Kārsava/Zilupe–Rīga	30 mln. t	0.46 EUR/t	EUR 13.8 mln.
<b>TOTAL</b>	<b>48 mln. t</b>		<b>EUR 26.76 mln.</b>

*Source: Estimations by authors*

According to the calculations, Latvian railway transport sector provides in excess of EUR 26 million per year to the national budget in the form of excise duty contributions. This amount is sufficient to cover the EUR 20–25 million infrastructure funding deficit mentioned earlier.

In 2015 total revenue from excise tax collections imposed on petroleum products amounted EUR 428.3 million (SRS 2016) being used for various public necessities. Ironically, Motorway Law allows up to 80% of the total excise duty revenues from

petroleum products for motorway maintenance funding (p.12(4)), including contributions provided by railway transport, which authors find unjustified.

## **Discussions**

Though redistribution of excise duty would have no impact on aggregate national budget, the authors recognize the effect it would have on national motorways maintenance budgets. Discussions within the railway industry therefore are on the proportion of reinvested excise duty which varies through 10–100%. Plain estimates show that 80% of EUR 428.3 million provides EUR 342.7 million for motorway maintenance, and EUR 26 million to be reverted to the rail transport sector is sensible.

The new approach to infrastructure access pricing has untwisted vast discussions in the railway industry, since the impact that access charge has to the carriage tariff. The authors suggest discussion over redistribution model of excise tax which is linked to distance a diesel train covers carrying the goods. This would balance competitive disadvantages of remote seaports such as Ventspils and Liepāja, a problem which exists in the industry.

## **Conclusions**

Motivation to promote railway transport is evident – carriage by rail is more sustainable, environmentally effective and economically efficient in comparison to road transport. Several EU Member states apply partial or general exemption of the excise duty on diesel used in rail transport. At governments disposal there are number of options to choose from in determining the level of public aid for railway transport and techniques of its implementation.

Latvian railway operators fully cover all the rail network construction and maintenance costs. Railway operators in Latvia also contribute full rate excise duty to the General State Budget. Latvian government does not take part in co-financing of railway infrastructure maintenance and renewal, although the state is obliged to ensure that network funding and infrastructure expenditures are coordinated and that rail transport is able to compete with other modes of transport.

Considering the financial aspect of the infrastructure manager performance, clearly JSC “Latvian Railway” struggle to balance the incurred costs with the proceeds without the co-financing of EU funds. Due to the lack of sufficient government support, comparing with other EU countries, and consequently higher railway charges, the competitiveness of railway in Latvia has reduced; thereby there is risk that freight transit flow will shift away from Latvia. Therefore, state aid in form of excise duty relief on diesel used in carriage of goods and passengers by rail in Latvia or financial support is required. One form to do it is to redistribute revenue from excise tax on diesel used for rail transport back to railway system as funding for the infrastructure maintenance and development needs.

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## COMPARISON OF THE RETAIL EFFICIENCY INDICATORS IN THE BALTIC STATES

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### *Abstract*

*Retail industry (NACE G47) has a significant place in the national economy of all countries. Like for all kinds of companies, the operation of retail businesses is based on gaining profits by satisfying consumer needs. To reach this aim and to ensure competitiveness, the retail businesses have to carry out their operations in as efficient way as possible, i.e. to reach the results with less investment. The goal of the present research is to compare the efficiency indicators of retail operations in all three Baltic States and to approximate the directions for improvement.*

**Keywords:** retail, operations efficiency, shadow economy

### Introduction

Private consumption is one of the cornerstones of economic growth and, therefore, retail can be perceived as a country's economic growth indicator. Since restoration of independence, the retail in Latvia and in all Baltic States has developed with changeable success. For several years it used to be one of the largest contributors to the domestic product growth. It was largely due to the trend on behalf of the countries to organise the industry. The retail transferred from trading squares sports halls and sheds to stores and supermarkets. Yet, during the global economic crisis (from 2008 to 2009) the retail was one of the sectors of national economy to experience the largest fall. When the economic situation started to stabilize in the country, the retail sector also started to recover and since 2011 its development follows the general development trend of the national economy. The retail sector mainly depends directly on the internal situation; nevertheless it is indirectly influenced also by the external environment factors that have negative impact on consumer behaviour and motivate savings, thus hindering total consumption.

The **goal** of the present research is to compare the efficiency indicators of retail operations in all three Baltic states and to approximate the directions for improvement.

To reach the goal the following **objectives** were established:

- to describe the subject matter and development of the retail;
- to analyze the indicators describing retail efficiency;
- to evaluate the shadow economy in the retail sector.

**Research limitations:** to establish the efficiency in the retail of the Baltic States, the following indicators were evaluated: net turnover, added value, number of employees, labour costs, working hours within a particular period.

**Research methods:** the applied research methods included monograph or descriptive method, as well as gathering, grouping and comparison of secondary data, the graphic processing and description of data applying MS Excel, to gain understanding on the situation in the retail sector in the Baltic States.

The **methodological basis** of the research is the works of foreign (R. Best, F. Kotler etc.) and Latvian scientists, contemporary authors, and publications in periodicals.

**Research period:** The research is mainly based on the data for the period from 2005 to 2014.

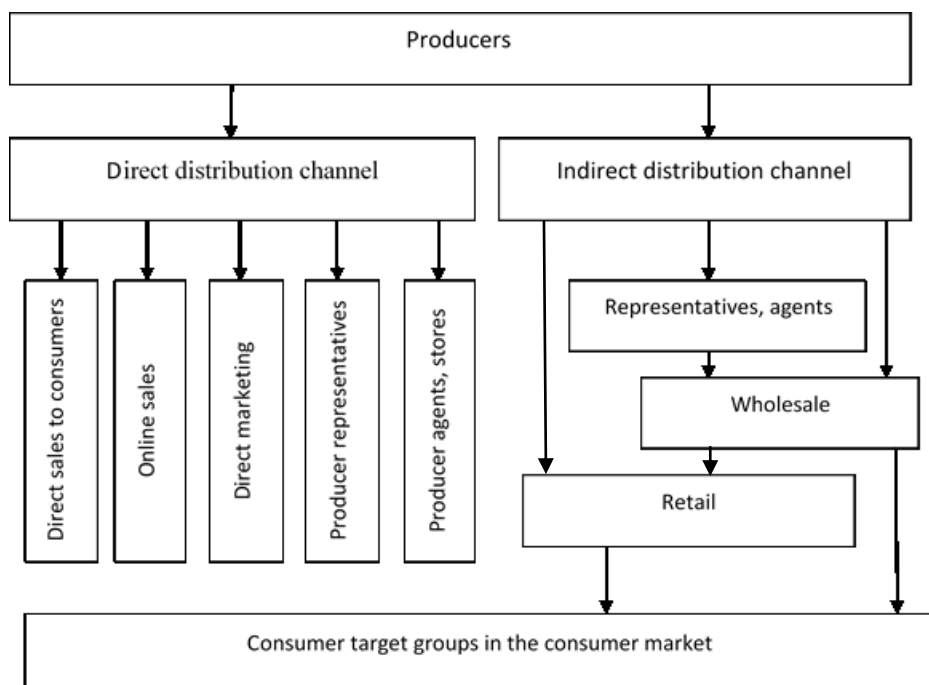
## **1. Retail: subject matter and development trends**

Essentially, the product distribution function can be carried out by the producer himself forming direct relationships with consumer, which guarantees the control over distribution process. Yet this approach is not always applicable as it is more convenient to use intermediaries. The producer does not always have sufficient resources and/or experience for the organization of the direct channel without intermediaries. In such cases the producer uses an indirect channel which contains one or several intermediaries. Thanks to the specialization of the operations, wide contacts, experience and advanced qualification, the intermediaries are able to provide both producers and consumers with the larger extent and higher quality services than they would be able to gain on their own. To optimize expenses, sell products to different target groups and ensure the necessary service quality, producers sometimes use a combination (a mix) of direct and indirect channels.

The indirect product distribution channels include at least one intermediary who may gain property rights to products, as well as organize and control their distribution and sales (see Figure 1).

As it can be seen, the retailer as an intermediary within the product distribution channel may have contacts with and product supply from the producer directly and/or from the wholesaler and/or from another intermediary as 'retail is any activity of selling goods and services directly to consumers in or outside shops for their personal non-commercial needs' (Praude, 2011, 111–162; Kotler, Keller, 2006, 605–642).

The regulations number 312 of the Cabinet of Ministers of the Republic of Latvia defines the retail as the sales of goods for individual household consumption or use. The use of a product is one of the forms of consumption. Firstly, services are traded in the same way as goods. Secondly, it should be highlighted that the sales take place within and outside shops.



*Figure 1. Alternative distribution channel types in the consumer market*  
(Best, 2005, 431; Doyle, Stern, 2006, 401–432)

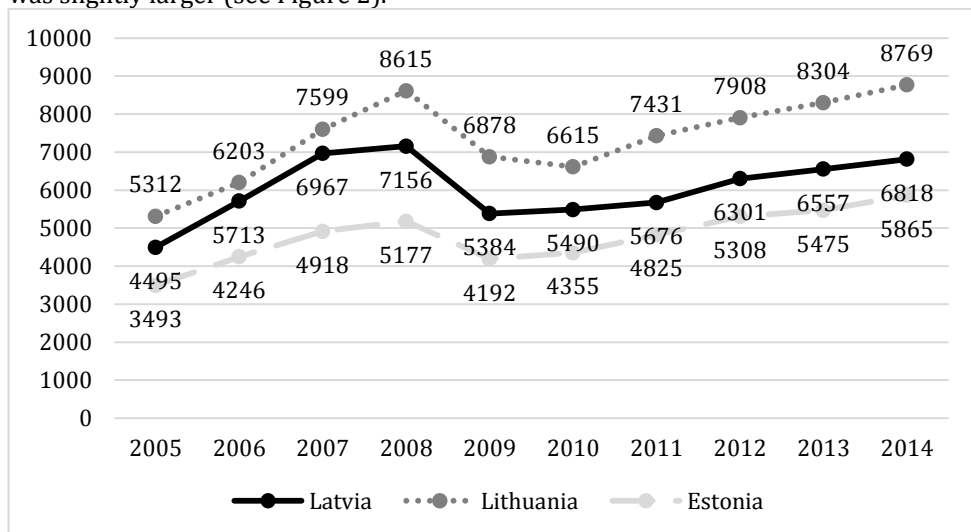
Retailer as a participant within the distribution channel of goods undertakes the following functions (Praude, 2011, 111–162; Kotler, Keller, 2006, 605–642; Best, 2005, 431; Krūmiņa, 2007, 223–238):

- prevents the imbalance between demand and supply;
- carries out the management of the stocks of goods;
- promotes the efficiency of product logistics;
- forms the assortment of goods in accordance with the needs of consumers;
- establishes contacts and arranges negotiations with product suppliers;
- serves the consumers by selling them goods and services;
- carries out marketing activities (research, communication etc.);
- undertakes risks, to ensure perfect operation of product distribution channels.

The fulfilment of the above mentioned functions increases the value of both products and consumption. There are different indicators substantiating the role of the retail sector in the development of the national economy: the weight in the growth domestic product (GDP): added production (PP): added value (PV).

To gain a better understanding on the retail situation in all Baltic States there were compared data for the period from 2005 to 2014. The turnover in current prices in all Baltic States has fluctuated very similarly. Until 2008 there was an increase in turnover in all Baltic States. Contrary to other Baltic States, this rise was smaller in Latvia. Then, in 2009, all three Baltic States experienced a fall followed by recovery starting in 2010, except for Lithuania where the fall continued. Still, starting with

2011, all three Baltic States experienced turnover growth until 2014. While the turnover growth was very similar in all Baltic States, in Lithuania the growth rate was slightly larger (see Figure 2).



**Figure 2. Retail turnover in 2005–2014 in the Baltic States (millions, EUR, current prices)**

Sources: [www.csb.gov.lv](http://www.csb.gov.lv), [www.osp.stst.gov.lt](http://www.osp.stst.gov.lt), [www.stat.ee](http://www.stat.ee)

Lithuania and Estonia surpassed the figures of 2008 already in 2014 (see. Figure 2), but Latvia has not yet even reached the level of 2007. This means that in order to achieve at least the level of 2008, the planning of development strategy regarding Latvian retail businesses should also give priority to the internal reserves, incl. management, marketing, and relationship management with customers.

The various aspects of retail analysis allow for the following conclusions:

- 1) Retail trade, similarly to any other industry, is subject to economic cycles, but the decline phase affects the functioning of this sector to a larger extent than other sectors because it is dependent on both the current supply by producers and the consumer demand;
- 2) Despite the growth rate fluctuations, the overall retail trade in the Baltic States is characterized by relatively high growth rates reflected turnover growth in the researched period of time;
- 3) As noted by several authors (A. Krūmiņa; V. Praude), the retail development is affected by the following external factors:
  - rapid growth of domestic consumption;
  - favorable credit conditions for retail businesses;
  - increase in mortgage lending, which contributes to an increase in demand for consumer products;
  - inflow of investment in sectors with rapid movement of capital;

- the development of new technology commercial equipment, software, and communication (Krūmiņa, 2007; Praude, 2011).
- 4) among the internal development factors of the retail there should be noted:
- increase in retail concentration levels;
  - active development of retail networks, shopping centres, online trade.

Retail-related macroeconomic indicators also include output value. It is the 'output produced or services rendered, including changes in stocks of own produced fixed assets and intangible assets, except for the goods and services purchased for the resale' (Latvian Statistical Yearbook 2013, 297). The production value and development trends of the Baltic States are reflected in Figure 3.

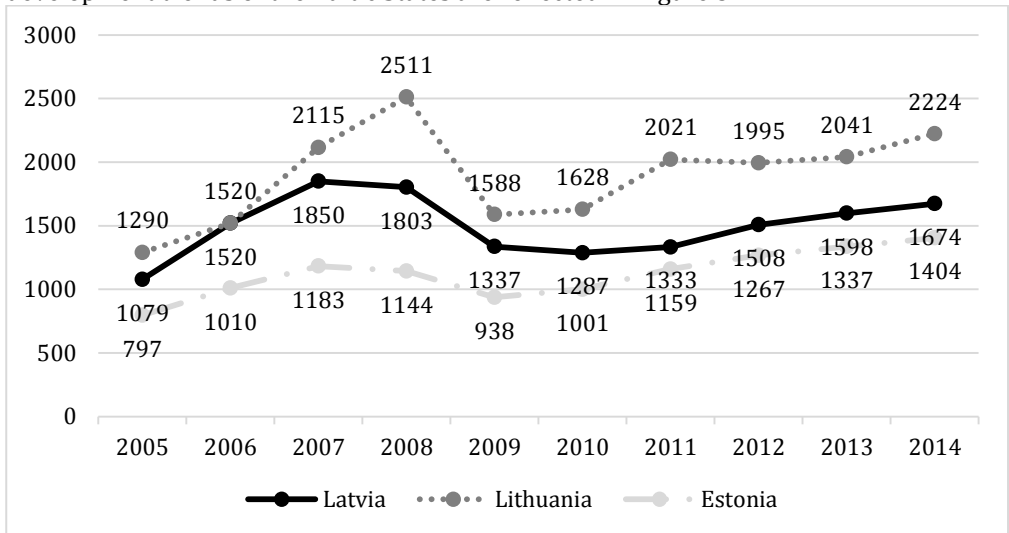


Figure 3. Production value in retail 2005–2013 in the Baltic States (millions, EUR) (based on Latvian Statistics Yearbook, 2013, 297)

Assessing the value of the production in the Baltic States for the given period of time, it can be concluded that:

- During the period from 2005 to 2008, Lithuania experienced a rapid development with a dramatic fall (by 37%) in 2009, followed by an increase until 2011 and with a relatively stable development from 2012 to 2014. However, even in 2014, the figure still had not reached the level of 2008.
- After the rapid development from 2005 to 2007, Latvia saw a drop starting in 2008, and the recovery started only in 2011. As well, even in 2014 it had not reached the level of 2007.
- Estonia also experienced a decline in the production value during the crisis period, but it was not as significant as in Lithuania and Latvia. Consequently, in 2012, it had already exceeded the pre-crisis level of 2007.
- Despite the different production value volumes (explained by the differences in the number of inhabitants and, respectively, the turnover in the Baltic States), the country data show similar trends in indicators as depicted in the graph in Figure 3.

The importance of the role of trade within distribution channels and within the economy as a whole is essentially stressed by all leading researchers and marketing specialists (P. Kotler; K. L. Keller; G. Armstrong; V. Wong; I. Saunders; R. Best; P. Doyle; P. Stern; N. Capon).

The macroeconomic indicator analysis also shows that the Latvian retail industry still misses all opportunities in the exercise of intermediary functions within the goods distribution channels and promoting consumer needs. Certainly, part of the efficiency in function execution is dependent on national economic regulation; applying such economic regulation instruments as taxes, resource utilization rates, financial assistance, investment stimulation, interest rates, etc., government organizations can actively participate in the process of creation and operation of any distribution channels. Performing intermediary functions between producers and consumers, retail acts as separate sector made up of several different companies that use the material, financial, human and information resources to meet the needs of consumers.

To a greater or lesser extent, retail affects all inhabitants of the country. People use retail services to acquire things necessary for life. According to the estimates, about 77% of household consumption expenditure in 2014 was to some extent related to the sale of products in retail (the researcher's calculations according to CSP, 2014).

## **2. Retail efficiency analysis**

Retail business efficiency, as in any other sector, is characterized by the results achieved in relation to the applied resources or costs. One of the performance result indicators is the turnover (A), while the other is the added value (PV) – 'production value, minus the value of the goods and services used in the production. The added value of the product shows the increase in the market value created during operating activities' (Ekonomikas skaidrojošā vārdnīca, 2000).

The main retail-related resources and costs include the number of employees or labour force (P), the personnel or labour costs (PI), and the labour hours used (NS). It should be clarified that the labour costs include 'the total remuneration, in cash or in kind, by the employer to an employee in return for work. Personnel costs also include employer social security costs' (Latvian Statistical Yearbook, 2013, 297).

Thus, in order to determine the efficiency of the retail business, there should be calculated the turnover and the added value in relation to the number of staff, labour costs, and hours worked within a specified time period. The efficiency measurement system is visually depicted in Table 1, where the matrix highlights six indicators.

Table 1

## The retail efficiency indicators

Indicators	No of employees (P)	Labour costs (PI)	Worked hours (NS)
Net turnover (A)	$\frac{A}{P}$ (4.)	$\frac{A}{PI}$ (6.)	$\frac{A}{NS}$ (8.)
Added value (PV)	$\frac{PV}{P}$ (5.)	$\frac{PV}{PI}$ (7.)	$\frac{PV}{NS}$ (9.)

The analysis of the A/P ratio provides information on the effectiveness of the retail staff working in the Baltic States, namely – the average net sales per employee during the period 2005 – 2014 (see Figure 4).

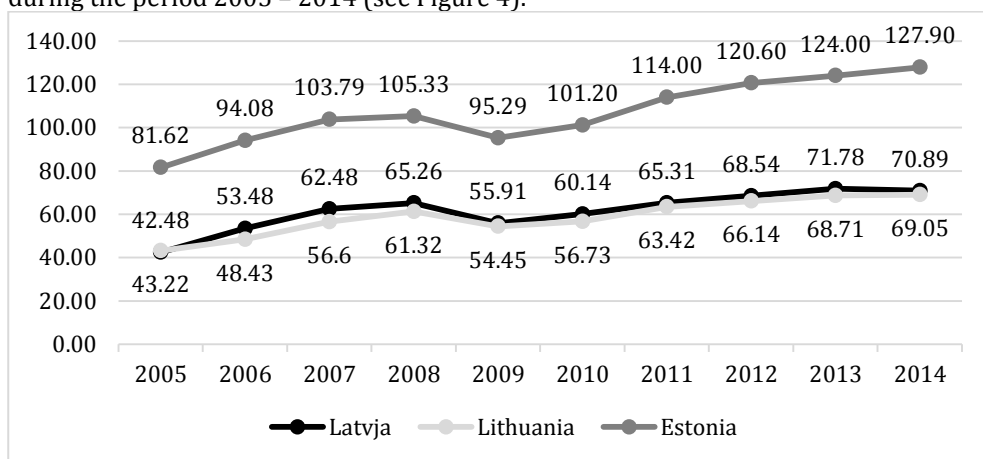


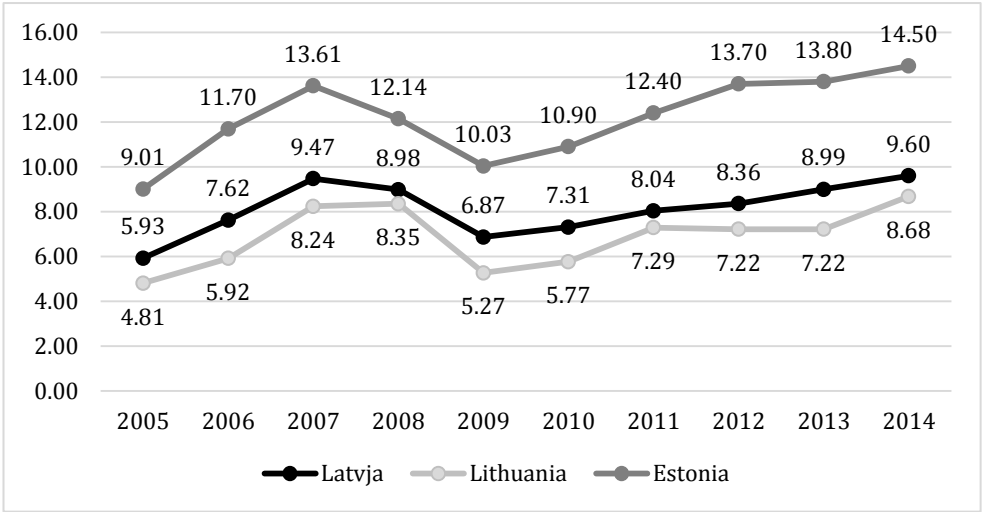
Figure 4. Net turnover in relation to the number of employees in retail in the Baltic States, 2005–2014 (thousands, EUR)

(data sources: [www.csb.gov.lv](http://www.csb.gov.lv), [www.osp.stst.gov.lt](http://www.osp.stst.gov.lt), [www.stat.ee](http://www.stat.ee))

As can be seen, according to the A/P ratio, the unquestionable leader among the Baltic countries is Estonia. In addition, the difference between the Estonian and Latvian A/P indices in the surveyed period only increased from 38.40 thousand EUR in 2005 to 57.01 thousand EUR in 2014. It should be noted that the Latvian A/P ratio is only slightly higher than the rate of Lithuania, and the difference gradually declined from 5.5 thousand EUR in 2005 to 1.84 thousand EUR in 2014. This means that the Latvian retail business still has a lot of untapped internal resources for increasing business efficiency. As for the trends, a similar situation can be observed in all Baltic States: the A/P growth before the crisis, the fall during the crisis and the recovery after the crisis (with Estonian growth rates being higher) (see Figure 4).

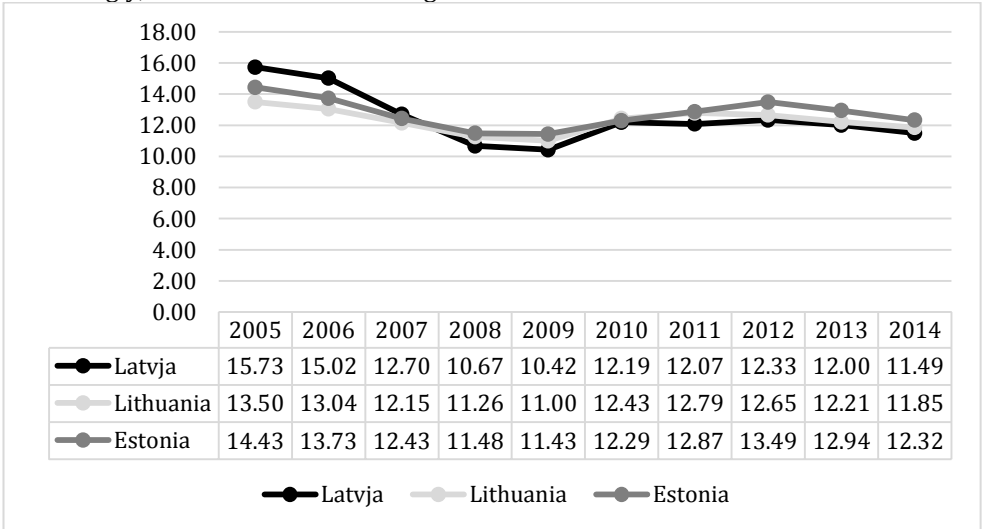
The PV/P ratio does not change, but only confirms the data trends depicted in Figure 4. The only difference – according to the PV/P ratio, the Latvian retail advantages are more substantial than by the A/P ratio (see Figure 5).





**Figure 5. Added value in relation to the employee number in the retail sector in the Baltic States, 2005–2014 (thousands, EUR)**  
(data sources: [www.csb.gov.lv](http://www.csb.gov.lv), [www.osp.stst.gov.lt](http://www.osp.stst.gov.lt), [www.stat.ee](http://www.stat.ee))

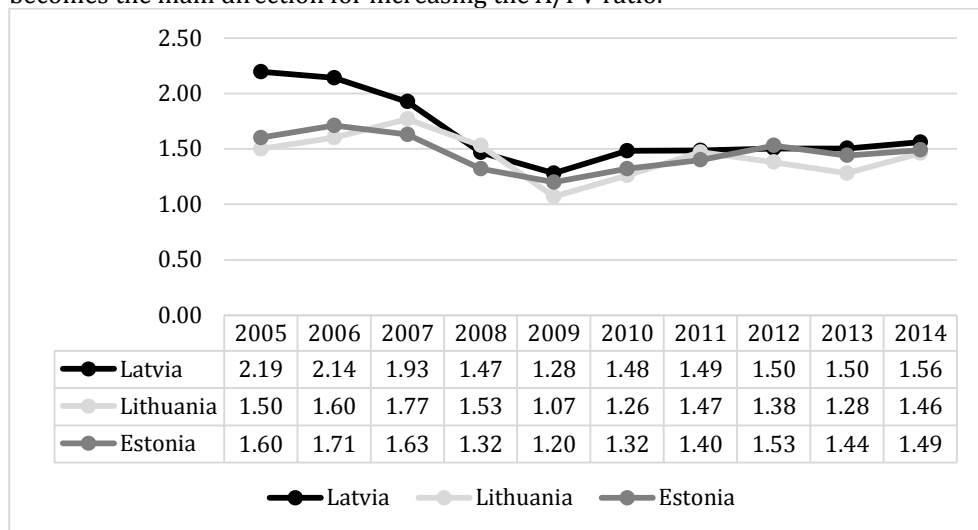
A/P ratio indicates the return on labour costs (salaries, social security costs, etc.). Accordingly, the data are shown in Figure 6.



**Figure 6. Net turnover in relation to the labour costs in the retail sector in the Baltic States, 2005–2014 (EUR)**  
(data sources: [www.csb.gov.lv](http://www.csb.gov.lv), [www.osp.stst.gov.lt](http://www.osp.stst.gov.lt), [www.stat.ee](http://www.stat.ee))

As shown, the A/PI data for the Baltic States are very similar. During the period 2005 – 2007, Latvian retail was even at the forefront, but during the crisis and post-crisis period it remained behind Lithuanian and Estonian retail. In addition,

the difference between Latvian and Lithuanian retail is very small (only € 0.36 in 2014). To improve the A/PI ratio, it is appropriate first to focus on the increase of the turnover (A) per labour costs (PI). It is doubtful whether it would be justified to reduce the PI, because, for example, gross wages and salaries per hour worked in Latvian trade (€ 3.83) are significantly lagging behind the Latvian average costs (€ 4.54) (Darbaspēka izmaksas 2014.gadā, 2015, 10). The reduction in labour costs, and even their stabilization, can lead to a reduction in service quality. Thus, the increase in turnover while serving consumer needs and forming loyalty becomes the main direction for increasing the A/PV ratio.

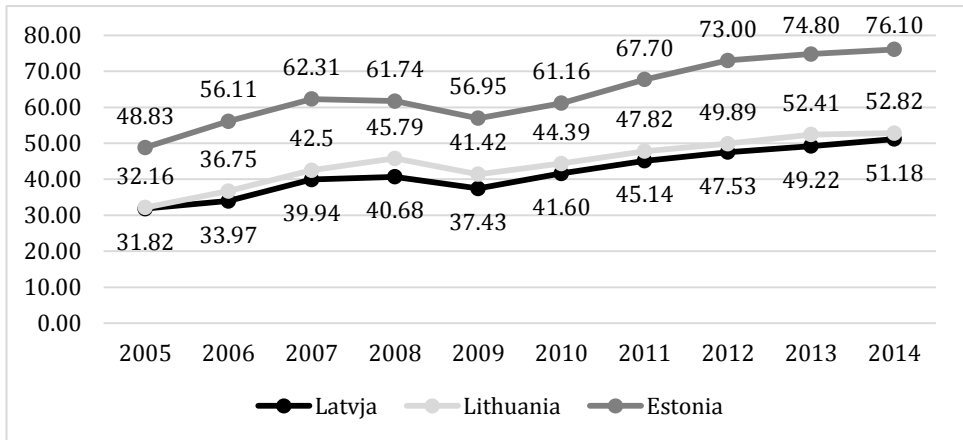


**Figure 7. Added value in relation to the labour costs in the retail sector in the Baltic States, 2005–2014 (EUR)**

(data sources: [www.csb.gov.lv](http://www.csb.gov.lv), [www.osp.stst.gov.lt](http://www.osp.stst.gov.lt), [www.stat.ee](http://www.stat.ee))

When analysing the return on personnel costs by added value (PV), it can be concluded that the Latvian retail sector has practically been at the forefront among the Baltic countries throughout all the researched period of time (with the exception for the year 2012). Nevertheless, the difference is small (only 0.06 euro between the Latvian and Estonian PV/PI indicators in 2013) (see Figure 7). In essence, it is a good achievement, as the added value, as it has been established, shows the growth in the product market value, created directly by operating activities. Thus, the PV indicates the quality of services in retail. In order to maintain the leading position and to approach the PV/PI levels of the more developed western EU countries, all internal resources should be used, including consumer relationship management. The opportunities in this area are indicated by 2005 data, where the PV/PI in Latvia was 2.19 euros, which is about 46% above the level of 2013.

The next performance indicator is the turnover per hours worked (A/NS), which indicates the staff returns per each physical hour worked (see Figure 8).

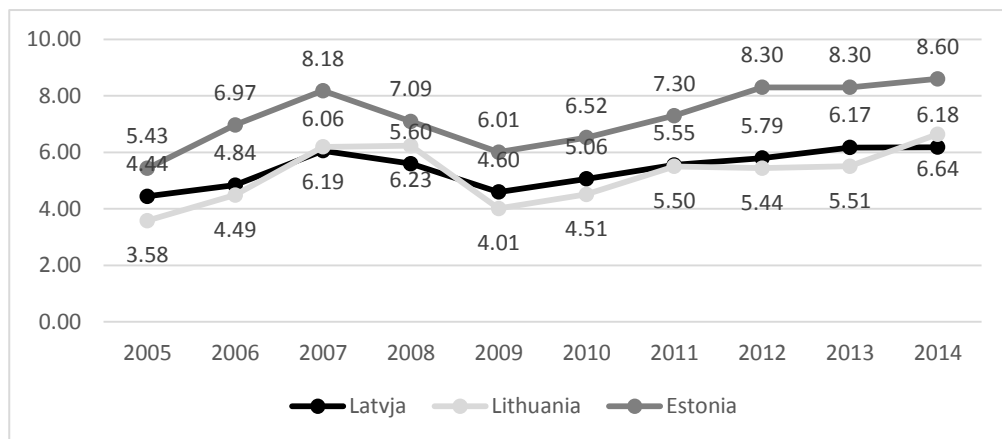


**Figure 8. Net turnover in relation to the hours worked in the retail sector in the Baltic States, 2005-2014 (EUR)**

(data sources: [www.csb.gov.lv](http://www.csb.gov.lv), [www.osp.stst.gov.lt](http://www.osp.stst.gov.lt), [www.stat.ee](http://www.stat.ee))

Unlike the A/PI ratio, where Latvia had the 1st place, according to the A/NS indicator Estonia is at the forefront, while Lithuanian retail ranks 2nd, leaving Latvia only in the 3rd place. It should be noted that the PI is a measure of the value that reflects the remuneration for hours worked, but the NS – a physical indicator, regardless of salary and other costs. Thanks to the relatively low remuneration per hours worked, Latvian retail ranks the 1st by the A/PI index, but the low A/NS indicator shows that there has not been reached the necessary turnover rate per each hour worked. In addition, the difference between the Latvian and Estonian results increased each year. (See Figure 8.)

The Estonian retail sector has also an undoubted advantage according to the PV/NS indicator (see Figure 9). Although the Latvian retail has been slightly ahead of Lithuania all years, it lost the 2nd place among the Baltic States in 2014. It should be concluded that businesses have to look for internal reserves to reach the Estonian level. The Estonian and Latvian retail sectors already managed to achieve a high PN/NS pre-crisis levels in 2012 and 2013 respectively. As for the development trend, all the Baltic States look similar (with some minor exceptions in 2007 and 2011) (see Figure 9).



*Figure 9. Added value in relation to hours worked in the retail sector in the Baltic States, 2005–2013 (EUR)*

(data sources: [www.csb.gov.lv](http://www.csb.gov.lv), [www.osp.stst.gov.lt](http://www.osp.stst.gov.lt), [www.stat.ee](http://www.stat.ee))

The analysis of the Baltic retail efficiency indicators is summarized in Table 2, which shows the rankings of each country for each indicator (designations from Table 1).

*Table 2*

**Retail efficiency indicator rankings (place taken) for the Baltic States**

(by the author, according to the data of Figures 4–8)

No.	Indicator	Latvia		Lithuania		Estonia	
		2005	2014	2005	2014	2005	2014
11	A/P	2	2	3	3	1	1
22	PV/P	2	2	3	3	1	1
33	A/PI	1	1	3	3	2	2
44	PV/PI	1	1	3	3	2	2
55	A/NS	3	3	2	2	1	1
66	PV/NS	2	3	3	2	1	1
<b>Sum of rankings</b>		<b>11</b>	<b>12</b>	<b>17</b>	<b>16</b>	<b>8</b>	<b>8</b>

The sum of rankings (see Table 2) provides a general idea of the efficiency indicators. The smallest sum (meaning the highest efficiency) is for the Estonian retail (8), the Latvian retail is in the second place (12), while the Lithuanian retail takes the third place (16). On the one hand, Latvia can be proud of being ahead of Lithuania, but on the other hand, there should be focus on the best results. In this regard, it should be noted that there was no positive change in 2014 if compared with 2005. Latvian retail companies still have much work to do in order to increase sales, optimize labour costs and make more efficient use of the hours worked.

### **3. The shadow economy in the retail sector**

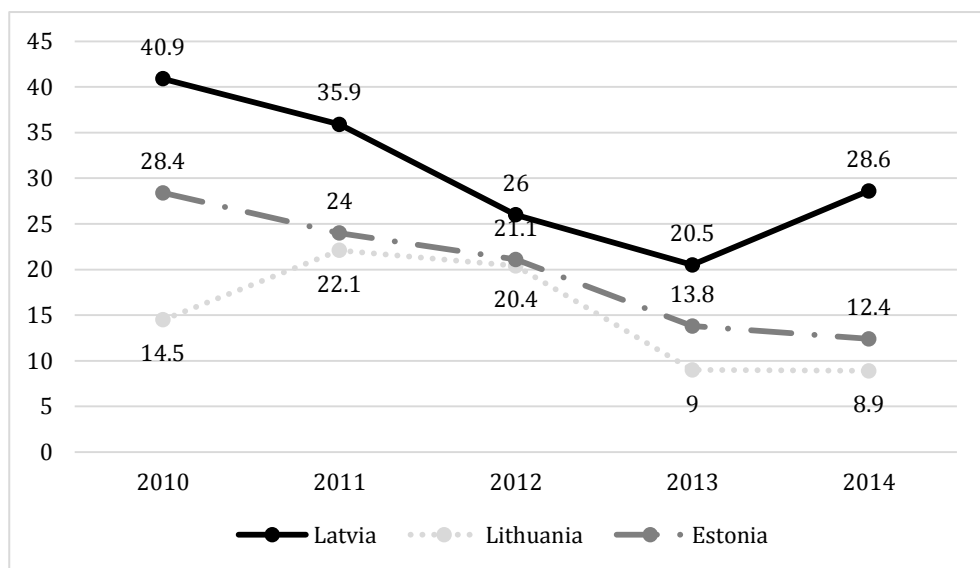
Unfortunately, many companies choose unfair and/or illegal practices instead of increasing the efficiency to achieve their business goals. This is shown by research on the so-called Shadow Economy Index (SEI), which is calculated as a percentage of GDP.

According to the studies by authors T.Putniņa and A.Sauka, the main driving factors of the shadow economy is tax evasion and the 'envelope' wages. The former head of the Latvian State Revenue Service (SRS) I.Pētersone in the 1st half-year report (2015) on the situation in the retail trade mentions the facts that 1540 thematic inspections were made and in 63% of cases there have been detected a variety of violations – 72% of which were related to the use of Electronic Cash Registers (ESAs). Irregularities were found mostly in the trade of food and alcohol, clothing, baby goods and toys, as well as automobile parts. I.Pētersone also indicates that SRS identified the types of fraud through manipulation of ESAs:

- Grand Total value deletion;
- Lack of sequentially increasing numbering of receipts;
- Non-entrance of the information in the control tape (control tape recording at the time of the transaction is stationary);
- Unjustified money issuance for the returned goods;
- Unjustified transaction cancellation at the time of registration;
- Unjustified deletion of the registered transactions;
- Use of data-adjustment programs (such as the Zapper or the Phantom-Ware);
- Unjustified issue of receipt copies (30% of all registered transactions);
- Issue of pre-receipts without issuing the fiscal receipt;
- Use of two cash registers with the same chassis numbers and other required properties, although only one cash has been registered with the SRS (Pētersone, 2015).

As an example, I.Pētersone refers to a case of May 2015, when the SRS found that the clothing store company used electronic cash registers with changed program functionality providing a revenue reduction of about 1271.6 thousand euros. This situation distorts competition in the retail trade and fair commercial practices (Sauka, 2015).

To review this point of view, the author analyzed the data of the given researchers on the shadow economy in the retail sector in the Baltic States (see Figure 10).



**Figure 10. Shadow economy in the retail sector in the Baltic States 2010–2014 (% of GDP)**

(according to the data by Putniņš, Sauka, 2015, 23–24)

As can be seen, among the Baltic States in the field of shadow economy in retail industry the leader is Latvia. If from 2010 to 2013 there was a positive trend – the SEI index declined by 20.4 percentage points, in 2014 this indicator increased by 8.1 percentage points. It should be noted that for the Estonian retail trade, which shows the highest efficiency (see Table 2), this index was only 12.4% in 2014. In addition, for Estonia and Lithuania the SEI indices are constantly declining. This means that companies can achieve their goals on the basis of legitimate and transparent business practices, incl. in the field of consumer relationship management etc.

On the one hand, it is possible to agree with A.Sauka that the SEI can be reduced by adjusting the tax system and public support to honest entrepreneurs, but on the other hand, the author believes that such methods will not suffice. Unless the companies themselves ascertain that effective management techniques and marketing can be used to increase market share, sales, revenue, profit, and as a result – wages and social benefits, they will continue to use practices inappropriate for normal and fair business. Thus, the termination of the shadow economy (or at least its reduction to the level of Estonia and Lithuania) in retail trade primarily depends on the companies' internal factors, namely – on the activities and corporate social responsibility of owners, managers, specialists, and other employees.

## Conclusions and recommendations

1. The analysis of the retail sector of the Baltic States allows concluding that retail, as any other industry, is subject to economic cycles, but the decline phase of the additional vulnerability affects the functioning of this sector more than other sectors because it is dependent on both the current supply by

producers and the consumer demand, despite the growth rate fluctuations. However, in current circumstances, Latvia does not experience the sharp growth in the retail trade, which was observed in 2005 – 2008. This means that in order to achieve at least the level of 2008, the retail businesses while planning their development strategies should focus on internal reserves, including management, marketing, and customer relationship management.

2. The analysis of the retail sector in the Baltic States regarding the business aspects (efficiency indicators) (see Figures 4–9) shows that the Estonian retail sector has the highest efficiency, the second place taken by Latvia, but the third place – by Lithuania. However, in this regard, Latvian retail sector in 2014, if compared with 2005, does not show any positive changes. Taking into account the positive experience of Estonia, the relevant associations, incl. the Baltic Trade associations, should organize events (conferences, seminars, forums) to share this experience with other retail businesses.
3. Unfortunately, many companies are choosing unfair and/or illegal practices instead of increasing their efficiency to achieve their business goals. It should be noted that for the Estonian retail trade, which shows the highest efficiency (see Table 2), the shadow economy index was only 12.4% of GDP in 2014. In addition, the neighbour countries keep constantly decreasing their SEI indices. This means that companies can achieve their goals on the basis of legitimate and transparent business practices. Therefore the Latvian state institutions need to develop measures to reduce the shadow economy and to ensure fair competition. As the shadow economy is also due to the tax evasion by using modified software cash registers, the author recommends that the responsibility for such acts is also partly put on software providers, not only on the retail businesses. In order to reduce the shadow economy in the retail sector, the trade associations of the Baltic States, within their capabilities, have to develop internal rules of fair competition and to ensure compliance.

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## INTELLECTUAL CAPITAL AS A FACTOR OF ECONOMIC DEVELOPMENT OF UKRAINE

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### ***Abstract***

*The purpose of this article is to study intellectual capital as an important factor in implementing an innovative model of the development of national economy. **Background.** Many scientists studied this issue, however, given its relevance and width, it is appropriate to further research in this area. The issues of effective realization of intellectual capital as a key resource for competitiveness improvement and development of the national economy are becoming particularly relevant in terms of intensification of integration processes. **Methods.** To achieve this goal a system of empirical and fundamental methods of scientific knowledge has been used in the study, among them: analysis and synthesis, induction and deduction methods, the method of comparison and graphical method. **Results.** The crucial role of human capital as a high-performance power of modern society and the most promising component of improving the competitiveness and economic development has been defined. Ukraine's positions in the world rankings by different criteria of implementation of human capital have been analyzed in this article. The general trends of development of the higher education, the training of highly qualified personnel, and the funding of the chosen educational direction have been determined. The features of scientific and technical activities, the level of availability of labor and financial resources have been investigated. **Conclusions.** The basic components of development and improvement of the effectiveness of realization of the intellectual capital as a factor of decreasing the effects of economic crisis and speeding up the future development of Ukraine have been stated, namely: strengthening innovation and investment activities, attracting the foreign and public investment in the processes of formation and development of intellectual capital, meeting the challenges of the optimization of financing scientific and technical activities, increasing the level of social protection in the country; and the formation of a stable regulatory system to support innovation and investment.*

**Keywords:** intellectual capital, human capital, scientific and technical activities, higher education, research intensity of GDP, social guarantees.

## Introduction

The nature of the modern global economy defined by rapid growth of intellectualization of labor and means of production allows to create new high-quality competitive products with high value added fate (Chalfin, Oren, Hillis, Jelveh, Luca, Ludwig, Mullainathan, 2016).

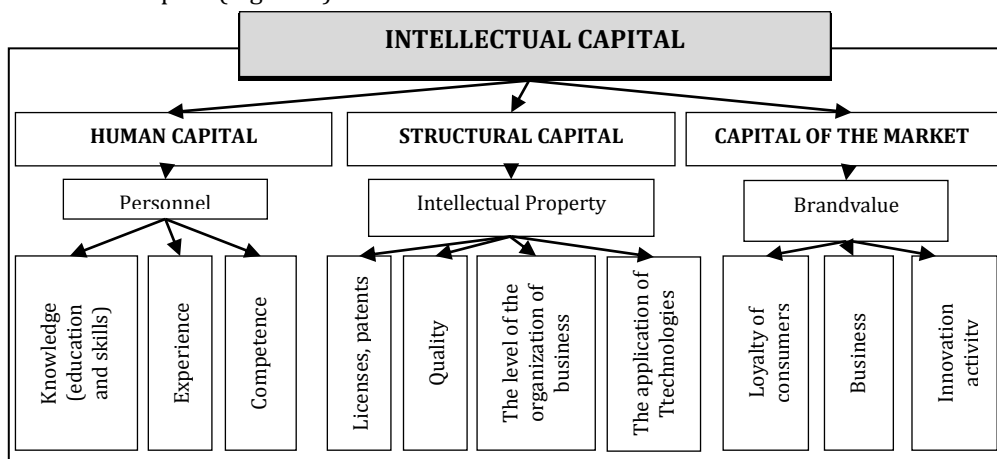
Intellectual capital is the basis of wealth, a key resource for the development of economic systems. Today it is the national economy's ability to create and effectively, increasingly use intellectual capital as a factor which determines the economic strength of the nation and its welfare.

## Methods

To achieve this goal a system of empirical and fundamental methods of scientific knowledge has been used in the study, among them: analysis and synthesis, induction and deduction methods, the method of comparison and graphical method.

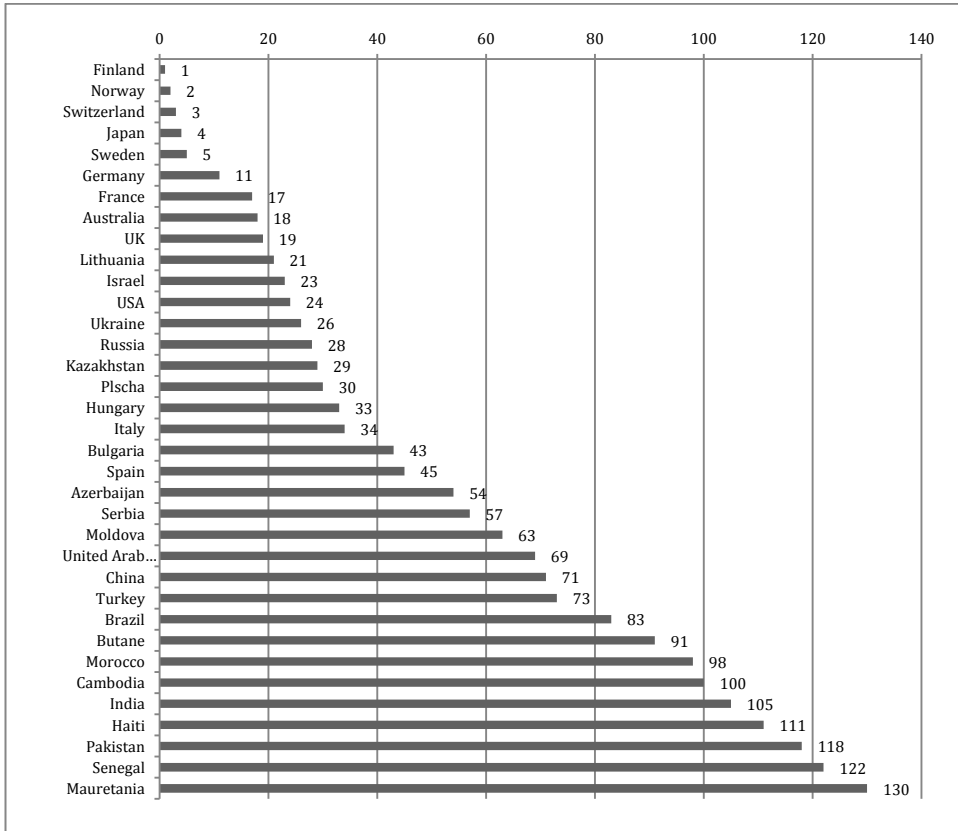
## Results

In a broad sense, intellectual capital as a new value created on the basis of knowledge, experience, competence and moral values, and being able to give its owner a competitive advantage, has turned more complex. The major structural elements of the intellectual capital of the national economy are structural, market and human capital (Figure 1).



*Figure 1. The structure of the intellectual capital  
(formed on the basis of Butnik–Siverskyi, 2002)*

It should be noted that in a globalized and highly competitive world human resource is the most valuable and most promising part of the development of national economy. According to the World Economic Forum in 2016 Ukraine ranked 26-th among 130 countries by the Human Capital Index; it is better than in the previous year by 5 points (Figure 2).

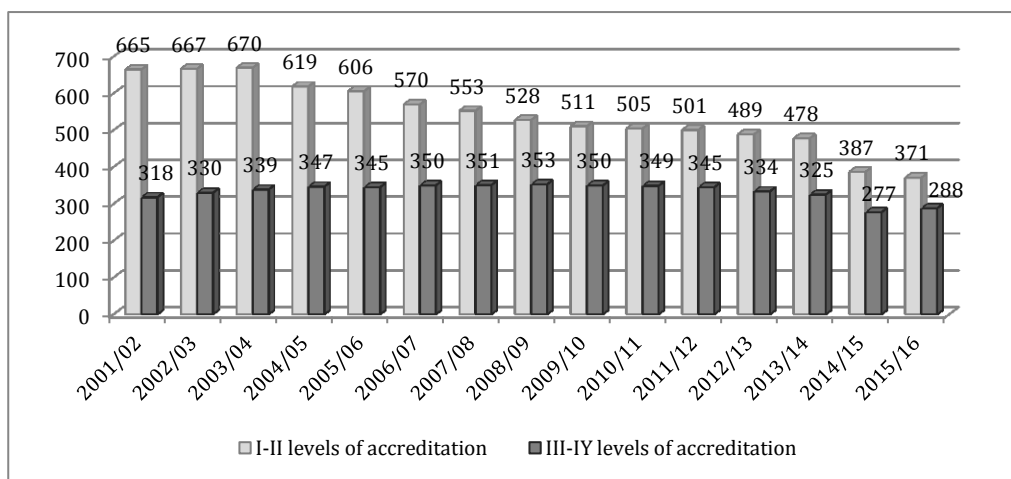


**Figure 2. Positions of some countries by Human Capital Index – 2016**  
*(formed on the basis of Rating of Human Capital 2016)*

By several parameters Ukraine received the world's primacy in the rating or won a place in the top ten. Strong positions of our country are connected with the educational direction. Specifically, 100% of Ukraine's population get the basic education; in addition, by the level of completion of secondary education we are in the top ten (State Statistics Service of Ukraine).

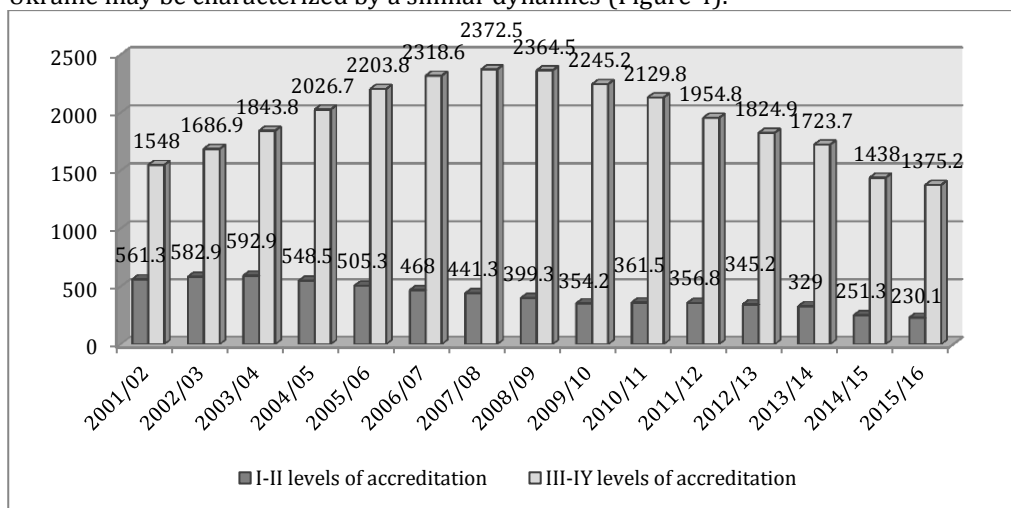
Traditionally, human resources in Ukraine have had a relatively high educational level. In particular, the proportion of specialists with higher and secondary special education was 29% in 2015. It should be noted that higher education is not only the bearer of intellectual capacity, but also a highly productive force in society and requires constant attention from the state and adequate financial support (Pochtovyuk, 2015).

The number of universities in Ukraine grew from 149 in 1990 to 353 in 2009 – that is 2.4 times. In recent years there has been a downward trend of the number of higher educational institutions (Figure 3).



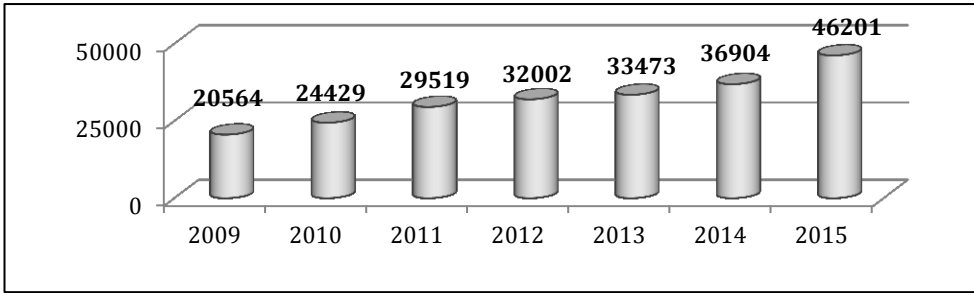
**Figure 3. Dynamics of the number of higher educational institutions in Ukraine for the period from 2001 to 2016**  
(formed on the basis of the State Statistics Service of Ukraine)

The number of university students and the number of highly qualified personnel in Ukraine may be characterized by a similar dynamics (Figure 4).



**Figure 4. The number of students at universities of Ukraine from 2001 to 2016, thousands of persons**  
(formed on the basis of the State Statistics Service of Ukraine)

The Ukrainian society has disbursed for education about 7.0% of GDP from public and private sources in recent years; it corresponds to the best international practice. For comparison, the countries of the Organization for Economic Cooperation and Development spend at average 6.0% of GDP [5]. However, in terms of GDP per capita Ukraine is among the group of countries with its level of social development “below average” (Figure 5, Table 1).



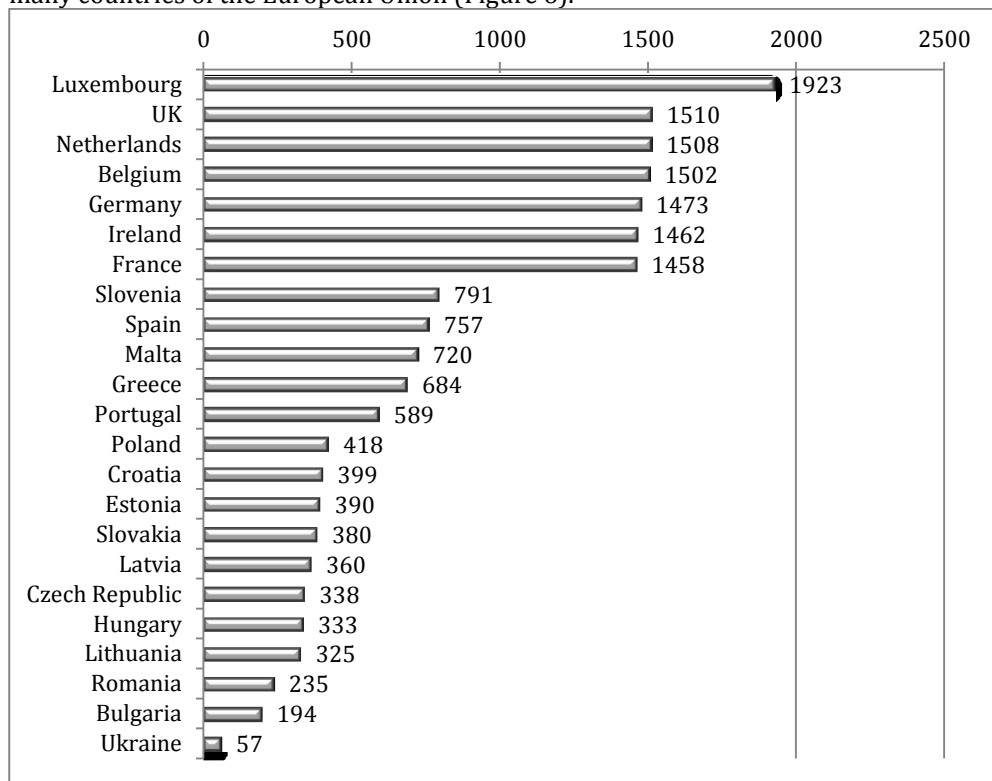
**Figure 5. Ukraine's GDP per capita, UAH**  
*(formed on the basis of the State Statistics Service of Ukraine)*

*Table 1*

**GDP per capita of some countries in the world, USD**

Country	2013	2014	2015
Qatar	141830	137343	132870
Luxembourg	92914	96163	99506
Singapore	80767	83798	85382
Switzerland	56864	58246	58647
USA	52705	54502	56084
Saudi Arabia	51020	52466	53802
Netherlands	47015	48362	49624
Sweden	44907	46256	48199
Australia	45258	46648	47644
Austria	45883	46504	46986
Germany	45055	46347	46974
Canada	43673	45049	45602
Belgium	41964	43105	44148
France	39912	40704	41476
Finland	40490	40739	41109
Japan	36782	37492	38148
Italy	35278	35141	35781
Spain	32270	33393	34861
Czech Republic	29097	30432	32076
Slovenia	28542	29922	30918
Slovakia	27285	28447	29758
Poland	24023	25286	26499
Greece	25206	26006	26391
Hungary	23802	25200	26275
Russia	26046	26688	25965
Bulgaria	17610	18295	19169
Georgia	8526	9210	9591
<b>Ukraine</b>	<b>8676</b>	<b>8733</b>	<b>7987</b>
Armenia	7761	8170	8492
Nigeria	5755	6061	6121
Uzbekistan	5185	5637	6081

Fairly high educational level of the workforce in Ukraine is coupled with low wages. The level of the minimum wage in Ukraine is several times lower than in many countries of the European Union (Figure 6).



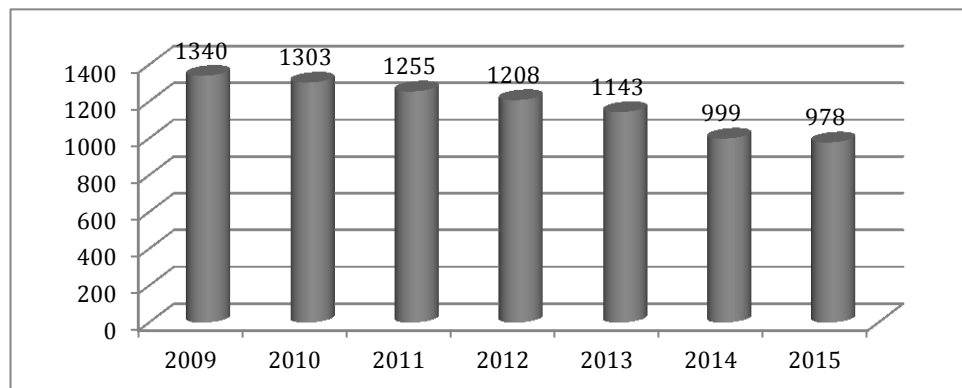
**Figure 6. The level of the minimum wage in Ukraine and the EU in the second half of 2015 (in euros per month)** (Minimum wage: UKRAINE and EU)

Thus, in December 2015 it was 57 euros per month, and in January of this year, due to the devaluation of the hryvnia, it has fallen to 52 euros. In the end of 2015 the minimum wage in Ukraine in euros was at the level of 2000; as compared to 2005 and 2010 it fell by 20% and 32% respectively. The average monthly salary in Ukraine decreased from EUR 308 in 2013 to 173 in 2015, i.e. 1,8times.

Analysis of the statistics shows that the negative feature of the motivational mechanism of wages in the context of achieving an adequate level of intellectual capital is the existence and dynamics of arrears of wages. Thus, during 2008–2009 a rapid increase in this index according to the regions and in Ukraine in general was noted; a negative dynamics was observed also during the period of 2012–2016. The total amount of arrears of wages during January 2016 increased by 11,3%, as of February 1 this year it has amounted to 5,9% of payroll calculated for January 2016. Comparing the growth rates of nominal and real wages also highlights the factors braking down material incentives to employees.

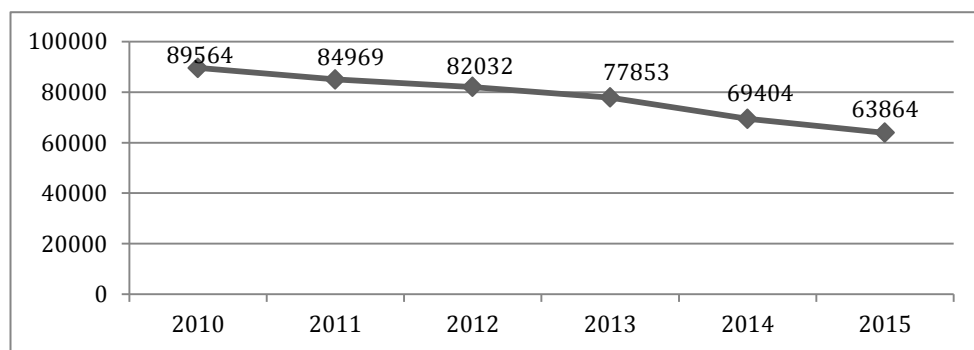
Human capital is an important factor in the formation of scientific and technological potential of the country as the basis of an effective implementation of innovative models of the development of national economy.

According to the State Statistics Service of Ukraine, in 2015 the number of organizations which carried out scientific and technical activities totaled 978 units, i.e. 2% higher than the previous year and 27% less than in 2009 (Figure 7).



**Figure 7. Dynamics of the number of scientific organizations in Ukraine in 2009–2015** (Scientific and innovative activity of Ukraine, 2016)

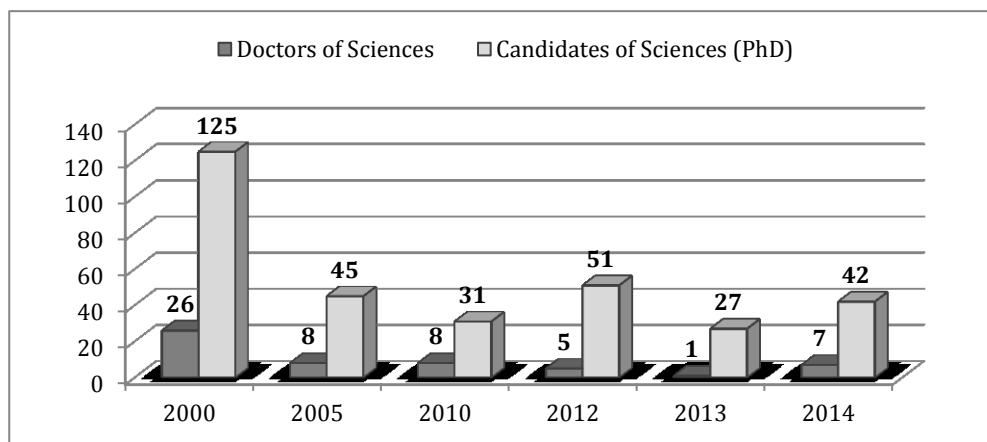
One of the most significant reasons for this negative trend is the military intervention and occupation of part of the Ukrainian territory. There is a trend of reduction in the total number of employees of organizations that carry out scientific and technical work in recent years; similar to 2010 the number of employees of scientific organizations declined almost 28% (Figure 8).



**Figure 8. Number of employees in scientific organizations in Ukraine** (Scientific and innovative activity of Ukraine, 2016)

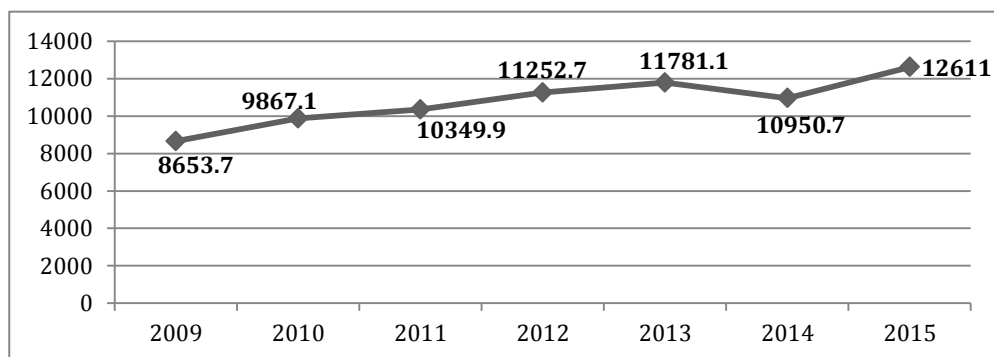
The number of scientific and technical workers per 1000 executors amounts to 5 persons in 2014. For comparison: in Germany – 21,8 persons, in Slovakia – 12,2, in the Czech Republic – 18,8.

The current mismatch between the development level of human resources and the standards of living encourages an outflow abroad of highly skilled professionals. Today the risk of the emigration of scientists is growing because of military intervention and a sharp decline in the hryvnia (Figure 9).



*Figure 9. Departure of specialists with scientific degrees outside Ukraine (formed on the basis of the State Statistics Service of Ukraine)*

However, the volume of scientific and research activities has been increasing throughout the study period, with the inclusion of 2014 (Figure 10).



*Figure 10. Dynamics of the executed scientific and technical work in Ukraine in 2009–2015, mln UAH (Scientific and innovative activity of Ukraine, 2016)*

The major share (51,72%) in the structure of scientific and technical work performed by Ukrainian enterprises and organizations in 2015, is experimental development (Figure 11).



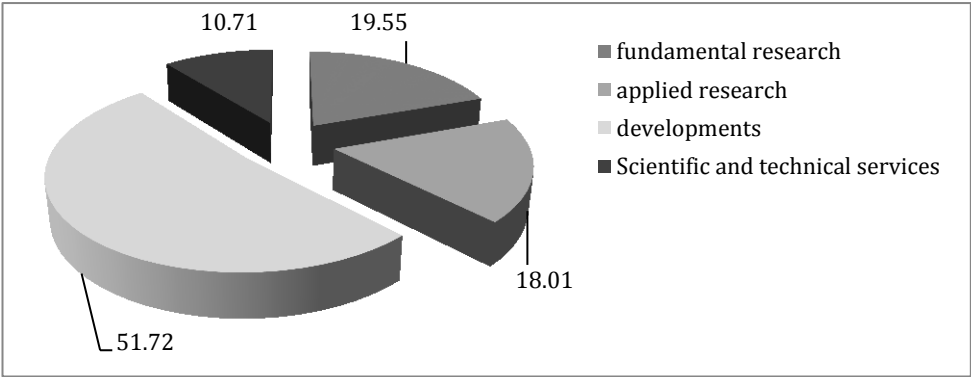


Figure 11. The **structure of the performed scientific and technical work by the Ukrainian enterprises in 2015, %**

The main performers of the basic research were the public sector, of the applied research – higher education sector (41,9%), of the scientific and technological development and scientific and technical services – organizations of business sector (respectively 97,6% and 87,2%).

Today a promising form of implementation of the priority directions of science and technology around the world are considered to be the program-targeted methods, the use of which makes it possible to move from the funding of the process to the funding of the results (Lawler, Boudreau, 2012). This is of particular importance for increasing the competitiveness of the economy during the crisis.

In Ukraine, where the state target scientific and technical programs are the main form of the realization of legally defined priority directions of the development science and technology, the share of budget funding in the overall financing of research and development remains low. It was less than 7,0% during last 10 years; in the 2014–2015 it reached the minimum value (1,2%) (Figure 12).

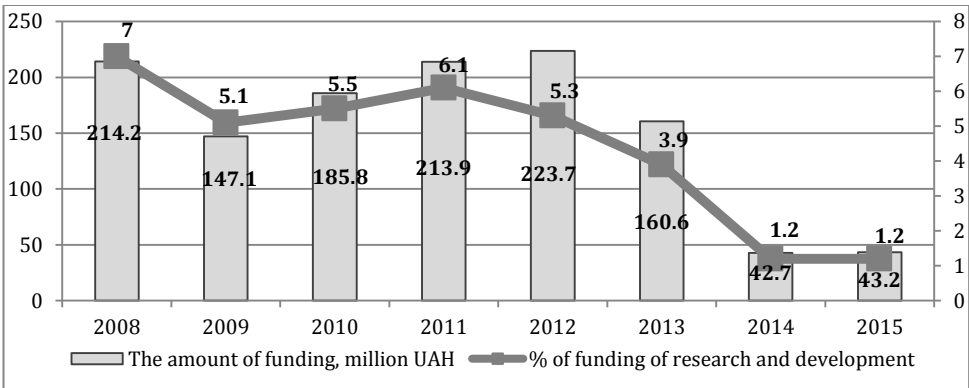
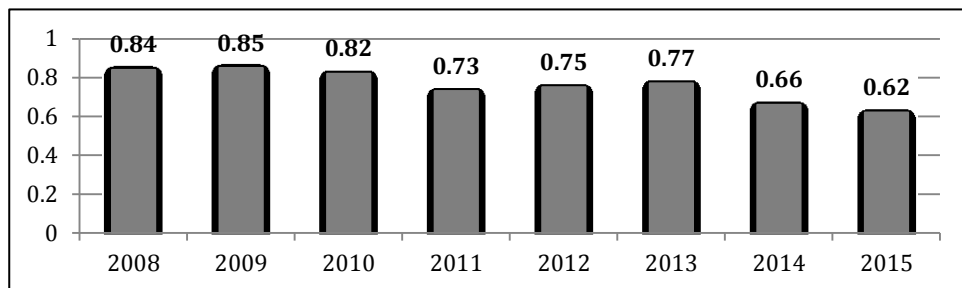


Figure 12. **The dynamics of funding of the state target scientific and technical programs at the expense of the state budget**

(Analytical reference “Status of science and technology, of the results of scientific, technical, innovation, technology transfer for 2015”)

Indicators of financial provision of science in Ukraine are far below the world standards, which leads to further intensification of the technological backwardness of the Ukrainian economy from the leading economies of the world. Total expenditures on research and development as a share of GDP (research intensity of GDP) in 2015 were 0.62%, including the state budget 0.21% (Figure 13).



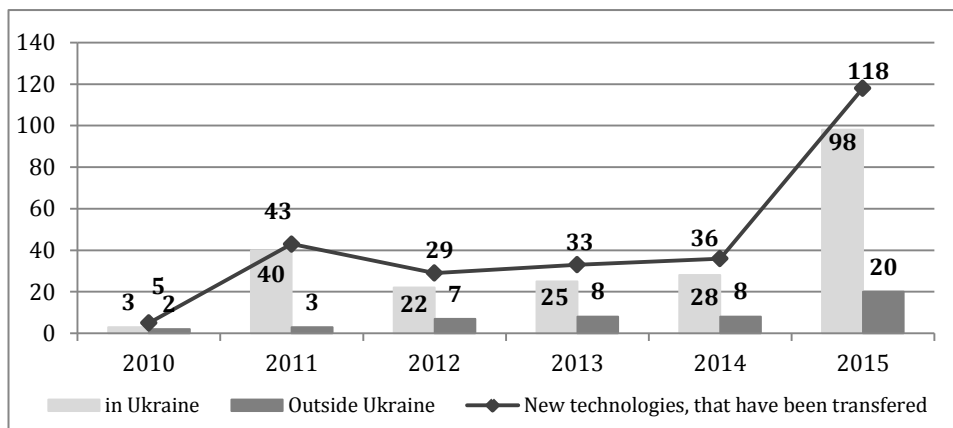
*Figure 13. Research intensity of Ukraine's GDP, %*

In 2016 expenditures on research decreased to 0.18% of GDP. For comparison – in the countries of the EU the indicator of research intensity of GDP is on average 1,9%, in Finland and Sweden – 3,7%, in the USA and Germany – 2,7%. International experience confirms that the value of this indicator being less than 0.4% of GDP, the country's science can only execute its social and cultural function. In passing through this border it acquires the ability to give some scientific results and perform cognitive function in society. Only when spending on science exceeds 0.9% of GDP, science can perform its economic function.

Among the negative factors of the development of the Ukrainian intellectual capital should also be noted the presence of a significant gap between the classical cycle of transformation of scientific knowledge into the final product or service. Creating of technologies by national research centers is carried out without taking into account the needs of the market. A large number of developments are offered as a prototype or laboratory sample, which necessitates additional cost from the customer for their implementation. This leads to the fact that much of the high potential designs are not implemented in the final product or service. The vast majority of scientists are not able to commercialize results of their research through ignorance of the mechanism of commercialization – the technological audit, the features of valuation, the protection of intellectual property, the mechanisms of transmission elaborations to consumers.

In 2015 118 units of new technologies have been transferred (in 2014 – 36). Of the total number of transferred technologies the largest shares were allocated to the targeted recruitment of qualified specialists – 48.3%, the know-how and agreements to purchase technologies – 30.5%, respectively.

In 2015 from Ukraine 20 technologies have been transmitted (in 2014 – 8). New technologies were transferred in two directions: production of fabricated metal products, except machinery and equipment – 18, printing and reproduction of information – 2 new technologies (Figure 14).

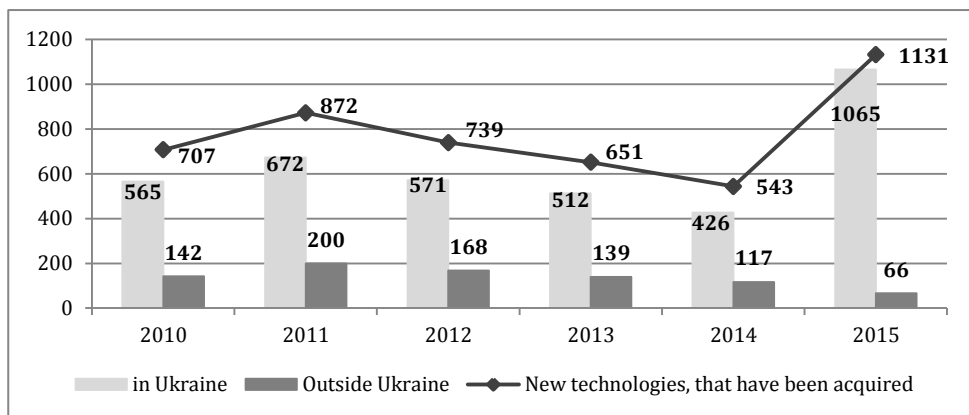


**Figure 14. Dynamics of transmitted technologies in Ukraine and abroad in 2015, %** (Analytical reference “Status of science and technology, of the results of scientific, technical, innovation, technology transfer for 2015”)

In order to implement innovations in 2015 in Ukraine 181 companies acquired new technologies in Ukraine and abroad (in 2014 – 154), of which 32 (in 2014 – 54) – abroad (Figure 15).

These trends are evidence of the lack of competitiveness of the national intellectual property on the international market and are the results of the series of problems of the development of intellectual capital in Ukraine: the inadequate funding of science and technology, imperfection of legislation on protection the rights on intellectual property, long term of the consideration of applications for the protection of intellectual property objects, low level of stimulation of the domestic researchers. To ensure the reproduction of intellectual capital there should be a high level of social and economic development. In a country with low income and consumption, opportunities for the development and implementation of intellectual capital are limited.

The enterprises producing food products have been the most active in the acquisition of technology – 14.9% of the total number of enterprises engaged in the acquisition of new technologies, production machinery and equipment – 10.5%, manufacture of basic pharmaceutical products and pharmaceutical preparations – 6.1%. In 2015 industrial enterprises purchased 1065 new technologies in Ukraine and 66 – abroad (in 2014 – 426 and 117 respectively).



**Figure 15. Dynamics of the number of acquired technologies by the Ukrainian industrial enterprises, 2010–2015**

(Analytical reference “Status of science and technology, of the results of scientific, technical, innovation, technology transfer for 2015”)

Of the total number of technologies the largest shares are: 439 technologies or 38,8% – the purchase of equipment, 34,7% – the purchase of the results of research and development. There is a small fraction of patent rights, licenses to use inventions, industrial designs – 10,6%, indicating a weak market maturity of Intellectual Property.

Thus, the main prerequisites of the development of intellectual capital are the socio-economic changes in society caused by scientific and technological progress, namely, deep qualitative and quantitative transformation in the structure of the productive forces (Maslak, Kwiatkowska, Bezruchko, 2012). Intellectual capital is a phenomenon caused by the objective tendencies of education, science, their deep penetration into all spheres of economic life, by the growing importance of the human mind, knowledge and information society. The intellectual capital is one of the key factors of innovation development of economy along with investments, infrastructure and economic structure (Kravchuk, 2013). The management of intellectual resources and targeted development of intellectual capital are the basis of improving the competitiveness of the national economy and successful participation in the globalization processes.

Today Ukraine has a considerable intellectual potential, opportunities for scientific and technological development in the long term; however, a number of problems create some barriers to the formation of the “knowledge economy” and the successful implementation of an innovative model of development.

## Discussion

Thus, the current conditions of the formation and development of the intellectual capital of Ukraine are rather complicated. Many problems remain unresolved to this day, among them: formation of the atmosphere of the common interest in the

work of intellectuals; the transition of the educational system to a new level of work to ensure the individual needs and desires, personality development, improving people's welfare and the quality of their life; elaboration of national projects in the introduction of management technologies and social innovation; intensive development of promising domestic branches of science; the formation of effective links between science and economy (Kravchuk, 2013; Maslak, et. al, 2015).

## Conclusions

Accordingly, the main components of the development and improvement of the effectiveness of realization of the intellectual capital of Ukraine should be:

- strengthening innovation and investment activities, in particular – attracting foreign and government investment in the formation and development of intellectual capital, which is associated with providing a long-term economic development;
- solving the task of optimizing financial resources, their reasonable distribution between levels of education, the effective use of funds securing the availability and quality of education, improvement of social security and creating favorable conditions for the development of the intellectual capital of the country;
- the development of science as the first priority of the social development, increasing the role and importance of science;
- integration with the international scientific community and forming of a stable regulatory system to support innovation and investment; providing an efficient management of the intellectual capital of Ukraine.

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## INTERCULTURAL COMPETENCE IN MULTICULTURAL ORGANIZATIONS

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### *Abstract*

*The **aim** of the present research is to assess intercultural competence level for two subcultures: specialists and managers working in multicultural organizations. In order to determine the intercultural competence level a **new model** based on Hofstede G., Chen and Naquin, and Warr theories of competence has been proposed. The paper is part of an international research project on intercultural competence organized in several countries. The research done is an example of how specialists and managers working for Latvian multicultural organizations assess Lithuanian, Estonian and Finnish co-workers. The main **method** used of the data collection for the statistical analysis is an online self-completion questionnaire. The basic **conclusion** is that the main forms of the augmentation of intercultural competence level of organizations are internships and business trips. The authors **recommend** to focus not only on the proposed or just one intercultural model, but compare and assess several intercultural models in the given context as building blocks of adopting a systems approach to intercultural competence in organizations.*

**Keywords:** intercultural competence, intercultural cooperation, multicultural organization, organizational culture.

### **Introduction**

We are living in a complex, multicultural world. Due to the trends of the globalization, organizations from different industries constantly apply new business models and integrate them into their systems. Such a business model can involve groups of people from different cultures who are able to achieve common goals. Development and integration of the business processes of a definite business model of the multicultural organization require intercultural cooperation and challenge organizational culture of the organization. Important role can be played by shared service centers of the organization to identify the core competencies needed for performance evaluation of the business model.

Shared service center of the organization is a purposely created business unit of the organization to move selected business processes out from the individual business unit level towards overall level to further consolidate them together in order to improve cost efficiency, service level, and market responsiveness of the organization. Shared service centers can be established in many industries, especially within large, global organizations and companies. Organizations can



freely extract and redeploy knowledge to get effect at other locations within their global production network; and spaces of corporate learning are now fully global in scope (Gertler and Vinodrai, 2005).

Companies realize more and more projects with an international scope on hand which involve and implement many stakeholders from different cultures. A major challenge for different level managers of the organization is to seek the cooperation and coordination between task forces and project teams through social networks, and human interactions between geographically distant individuals (Atamer and Schweiger, 2003). When people interact in/ and across organizations cultural challenges, e.g. communication, misunderstandings, different values and beliefs, lack of a codified approach can occur. This approach to the training of people to work in multicultural environments are most common for multicultural organizations (Grisham and Walker, 2008).

To work successfully with people from different cultural backgrounds, where multiple actors seek to optimize outcomes by combining resources from multiple sites, organizations, cultures, and geographies, additional competence is required through a combination of contractual, hierarchical, and network-based modes of organization (Orr, 2011). Intercultural competencies are deeply studied by Hofstede, who argued that the globalization of business does not necessarily lead to the globalization of culture and, therefore, generic managerial solutions may not be useful in specific cultural contexts (Hofstede, 2010). There are several aspects to be considered when evaluating intercultural skills, such as previous experience of interacting with other cultures, experience of international travels, interest in international work, and openness to new experiences. Aspects such as intercultural skills, cultural intelligence, global mindset, cultural flexibility, and low ethnocentrism are also important (Tariquea, Schulerb, 2008).

## **1. Organizational culture**

Unfortunately, a fixed, universal understanding between researchers of organizational culture, what the term “culture” exactly is, does not exist. In the human sciences research of a culture has been the field of anthropologists. Most sociologists find acceptable the definition of a culture given by Edward B. Taylor (1971) as: “that complex whole which includes knowledge, beliefs, art, morals, law, custom, and any other capabilities and habits acquired by man as a member of society”. Management science scholars agree that a culture can be identified as either a whole encompassing a group’s survival and compatibility program (Banks and Banks, 2007); or, according to Hofstede and Hofstede, (2005) and Kets de Vries, (2001) the core of a culture is based on values.

Regarding organizations there exists the concept of organizational culture. Researchers of organizational culture and the related discipline of management science began historically investigating organizations in terms of culture as early as the 1930’s. The first theory is known as X and Y Theory, where two contrasted sets of shared assumptions are identified. Later, in the early 1980’s, most of the organizational culture researches were focused on the relationship between corporate (organizational) culture and its performance. In the 2000’s researchers linked together organizational culture and strategy alignment, where culture and

strategy support each other. One of the most well-known definitions of organizational culture has been provided by Schein (2004): "A pattern of shared basic assumptions that the group learned as it solved its problems of external adaptation and internal integration, that has worked well enough to be considered valid and, therefore, to be taught to new members as the correct way to perceive, think, and feel in relation to those problems". According to Schein (2004), there are four categories of culture: (1) macro cultures (nations, occupations that exists globally), (2) organizational cultures, (3) subcultures (groups within organizations), and (4) micro cultures (microsystems with or within organizations). Schein identifies three levels of culture: (1) artifacts (visible), (2) espoused beliefs and values (may appear through surveys), and (3) basic underlying assumptions.

Organizational culture comprises a complex, interrelated, comprehensive, and ambiguous set of factors (Cameron, Quinn, 2011). Multicultural organization can be recognized as an organization where workforce includes people from diverse racial, religious and gender backgrounds and minorities. It is equally integrated across all levels of the company, including management and executive positions. A multicultural organization can have no discrimination and prejudice, with skills and talent being primary criteria for building a career.

## **2. Intercultural cooperation and intercultural competence**

Researchers and academics provide different definitions of intercultural cooperation and international competence, albeit most of them have a common approach. Cooperation can be defined as a relationship that takes place between persons of different cultures. The term "intercultural" usually refers to the meeting of two cultures or two languages across the political boundaries of nation states (Kramsch, 1998). Intercultural competencies are fluid rather than fixed (Zakaria, 2016).

Competence is defined as an intellectual capacity that has various possibilities of transfer, i.e. communication skills, selecting relevant information, assessment of information, etc.; capacity which contains affective, motivational and attitudinal elements. Byram (1997) concluded that there are a lot of issues to be considered in trying to define intercultural competence, such as emphasis on knowledge about cultures and cultural practices vs. skills "to analyze consciously" interactions between cultures. Byram has paid special attention to: (1) the role of nonverbal communication in forming intercultural competence, (2) the limits within which the concept of intercultural competence should be defined, (3) focusing on psychological traits versus "capacity to act", and (4) the influence of social factors and policy on defining and assessing competence of intercultural communication. Rakotomena (2005) formulates intercultural competencies as a set of competencies necessary for a successful interaction in a group of persons from different cultures. Byram (2000) considers that intercultural competencies symbolize the capacity "...to see relationships between different cultures—both internal and external to a society – and to mediate, that is interpret each in terms of the other, either for themselves or for other people". Intercultural competence is understood as "...the capacity to notice, respect, appreciate and celebrate individual differences" (Ortiz, 2012).

There are many similarities among theories explaining intercultural competence, mostly used in management science. There are three dimensions based on intercultural competence: (1) cognitive dimension, (2) affective dimension, and (3) behavioral dimension. Cognitive dimension includes knowledge about cultural norms, values, behaviors and issues. Affective dimension includes flexibility to adapt to new situations, open-mindedness to encounter to new values. Behavioral dimension includes critical skills such as resourcefulness, problem solving skills and culturally appropriate people skills.

Chen and Naquin, (2006) have stated that intercultural competence is based on the attitudes: (1) emotional dimension, which is formed mainly by respecting the values of other cultures, fostering tolerance, (2) cognitive dimension is formed by the learning process, but the (3) behavioral dimension is formed by experiences. It is important to note that the concept of intercultural competence provided by Chen and Naquin is universal – it can be attributed to the professional learning, studying school subjects, etc.

In fact, the intercultural competence model derives from the organization culture approach and reflects the value system (Namatevs and Dubkevics, 2013). Values determine attitudes towards people, work, and organization. Attitude is usually defined as assessment of other people, things, rules, processes (Warr, 2002). Values are not only the basis of the attitudes, but also influence knowledge and behavior, thereby contributing to employee integration in the organization, helping to accept their role (Louis, 1980). The universal model of intercultural competence is presented in Figure 1.

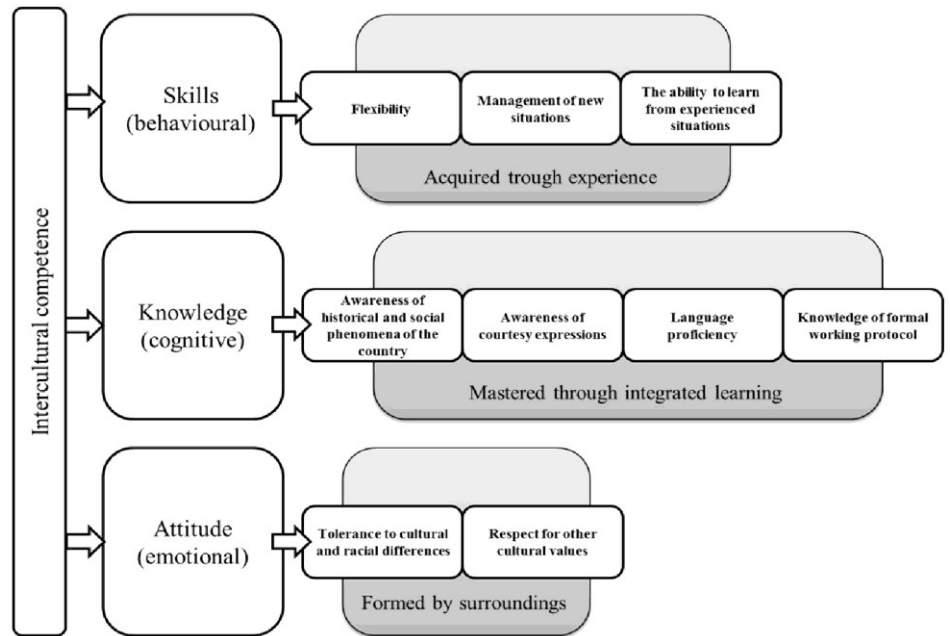


Figure 1. The intercultural competence model

Source: Authors, based on Hofstede, G., 2013; Chen and Naquin, 2006; Warr, 2002

The proposed intercultural model fits in with its three main components it values: skills, knowledge, and attitude. Also categories of importance of intercultural cooperation are experience, integrating learning, tolerance to culture, and respect of other cultures.

### **3. Methodological Framework**

#### **3.1. Methodology**

A self-completion questionnaires method for data collection (Collis and Hussey, 2009) was used to find out the respondents' self-assessment of their intercultural competence level: knowledge, skills and attitudes. The survey was conducted by using an online questionnaire. Distributed questionnaire as a research instrument consisted of eight multiple choice type questions and two 5-point Likert scale type question groups. Statements were evaluated from absolute agreement (5 points) to absolute disagreement (1 point). In total, the 5-point Likert scale type questions contained 58 statements about different aspects of the respondent's intercultural competence. Two subcultures were being addressed and questioned, i.e. specialists and managers. Altogether 63 respondent responses were collected.

Survey of the same research design was conducted as part of an international research project about intercultural competence in several other countries. Previous research results based on the same methodology were published in Human Resources Management & Ergonomics Scientific Journal in 2015 (Dubkevics et. al., 2015).

This study was conducted in four subsidiaries of the multinational trade companies located in Latvia and selling different products on the Baltic and Finland market. Management of these four companies seek for synergies and a common approach through all subsidiaries and coordinate these efforts by allocating cross functional responsibilities of the team leaders. The team leaders have to manage functions beyond their domestic borders; thus they have to apply multicultural skills on everyday basis. One of the four companies was used as a shared service center for a larger geographical region.

Two subcultures were addressed during research: specialists and managers. Specialists have to support colleagues in other countries, as well as to have regular training in multicultural teams. While managers have to lead multicultural sales teams and maintain financial and market performance of the company under their responsibility in all subsidiaries. This research cannot be generalized for all shared service centers in the respective region. It reflects results only in a particular multinational trade company.

#### **3.2. Research results**

The survey has revealed that 53% of the respondents communicate with people from other countries several times a quarter. 72% of respondents travel outside their country for work duties; while more than half of the respondents travel for reasons unrelated to work more often than once a year.

Referring to communication with people from other countries, more than 70% of respondents communicate with people from other Baltic countries, i.e. Estonia and Lithuania. About 50% of respondents communicate with people from Scandinavian countries (Sweden, Norway, Denmark), about 20% with Eastern Europe, e.g. Russia, Ukraine, Belarus, and a little below 50% with Western Europe, e.g. France, Germany.

The research shows that majority of communication abroad is respectively between geographically neighbouring countries, i.e. the Baltic countries and Scandinavia. Both subcultures report quite similar responses (see Figure 2).

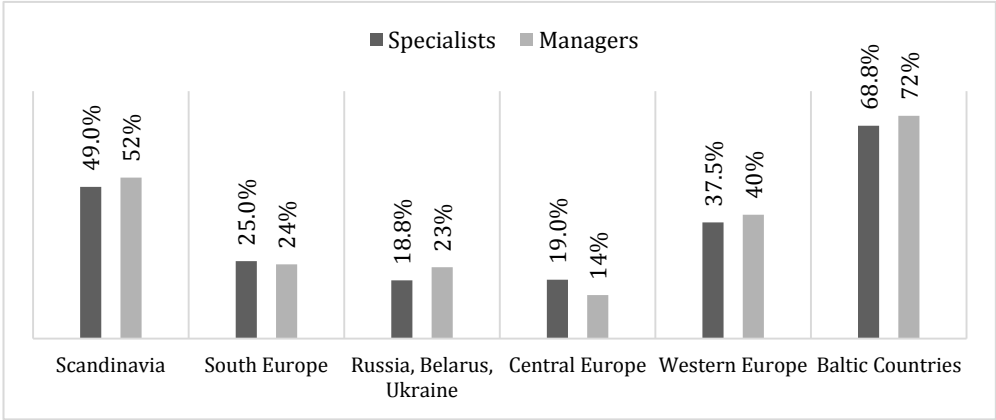


Figure 2. Regions that respondents communicate most with

Elements of intercultural competence that respondents consider most important are language skills, respect of values of other cultures, ability to learn from experiences, flexibility, and tolerance towards cultural differences. Both subcultures demonstrate consensus regarding most important elements. Knowledge of the main historical and social phenomena of another country has the lowest self-assessment scores (see Figure 3).

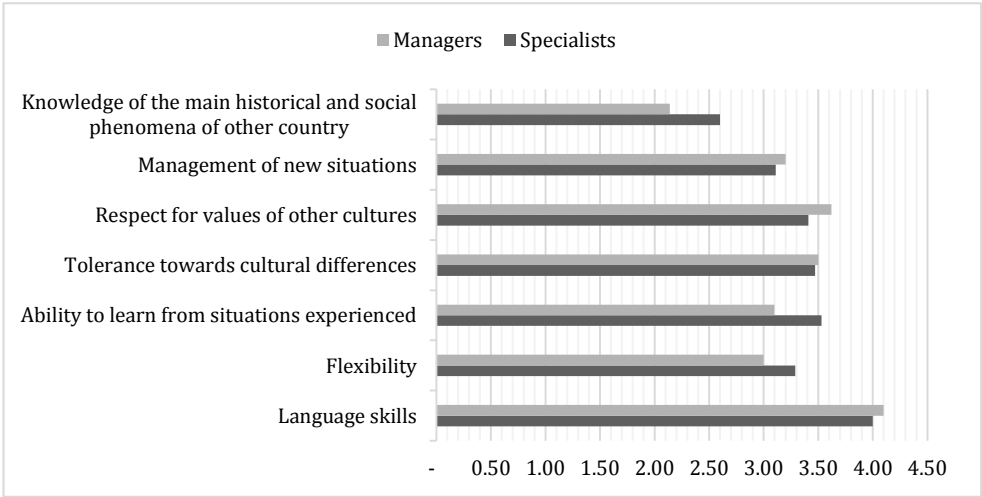


Figure 3. Most important elements of intercultural competency

Regarding support for development of intercultural competence from their employer, the majority of respondents report that they have been sent to training and exchange programs; especially, managerial positions report almost 60%. About 30% believe that the development of intercultural competence skills must be considered to be their own responsibility. There is a significant difference between two subcultures. Specialists seem to be rating spread of good experience and sharing best practices higher than managers. While the managers pay more attention to internships and business trips (see Figure 4).

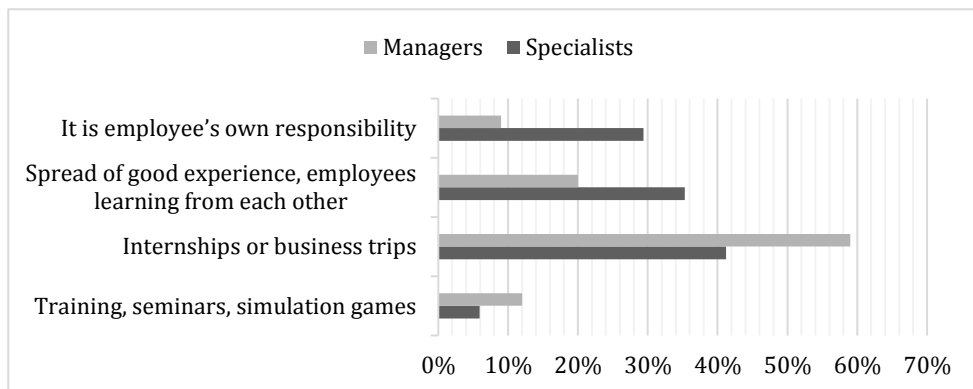


Figure 4. Organizational support for intercultural competence development

However, most of the respondents believe that improved intercultural competence would foster their career growth. It can be concluded that specialists are more optimistic regarding their improved intercultural competence and career development in the present workplace than managers. Managers more often, if compared to specialists, foresee increased opportunities for their international career. There is a small number of respondents – 11% of specialists and 6% of managers – who believe that their career growth does not depend on the level of their intercultural competence (see Figure 5).

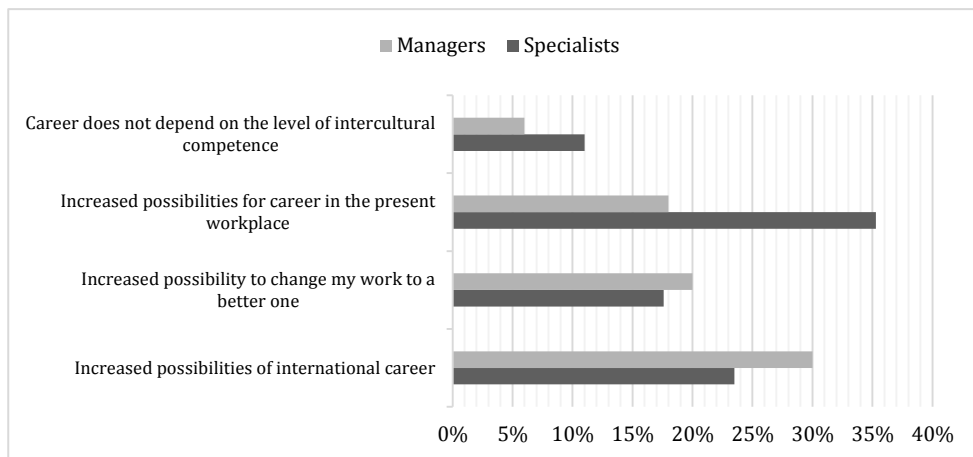


Figure 5. Individual advantages of improved intercultural competence

The majority of the respondents believe that improved intercultural competence would foster their organization's abilities to reach its goals and build partnerships with organizations from other countries. However, some respondents have reported that success of the organization does not depend on the level of employee intercultural competence. In percentage it means almost 25% of specialists and 17% of managers, accordingly (see Figure 6).



Figure 6. Business advantages of intercultural competence

Having been asked how intercultural communication will change over the next five years, respondents – especially managers: 60%, believe it will increase. About 35% of specialists report the same. There is a surprisingly high percentage of respondents who find it difficult to answer this question, namely, 25% of managers and 18% of specialists (see Figure 7).

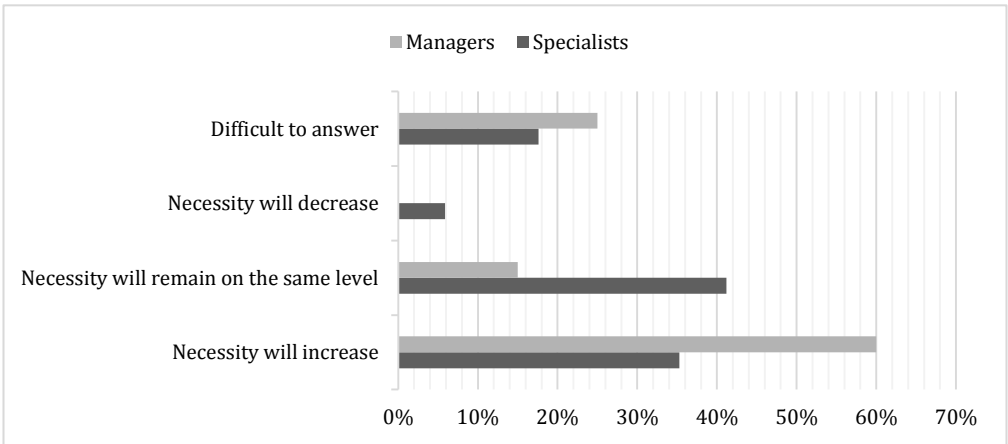


Figure 7. Necessity for intercultural communication in the next 5 years

When asked to evaluate their own intercultural competences, respondents believe that their knowledge and skills are relatively good. There is a visible difference in a few responses between manager and specialist positions. Managers are more confident and value their competencies higher. The highest scores are for: (1) knowing the dress code for business meetings, (2) knowing how to properly present themselves, (3) exchange greetings, and (4) talk to foreigners. The lowest scores are related to knowledge regarding the specific political and cultural norms, and traditions of specific countries. These are: (1) knowing the acceptable timing for meal, (2) typical food, (3) amount of the tip for restaurant, and (4) knowing what are 'suitable' and 'unsuitable' issues to discuss while communicating with foreigners (see Figure 8).



Figure 8. Evaluation of intercultural competence

Respondents are significantly less confident when asked about their conflict resolving skills. The highest score is given for the statement that “communication to a foreigner is not stressful for me or does not raise distrust in myself” for both subcultures. At the same time in case of conflicts or misunderstandings caused by cultural differences, responses are not so convincing – rated at 3 for managers and 2.63 for specialists only (see Figure 9).



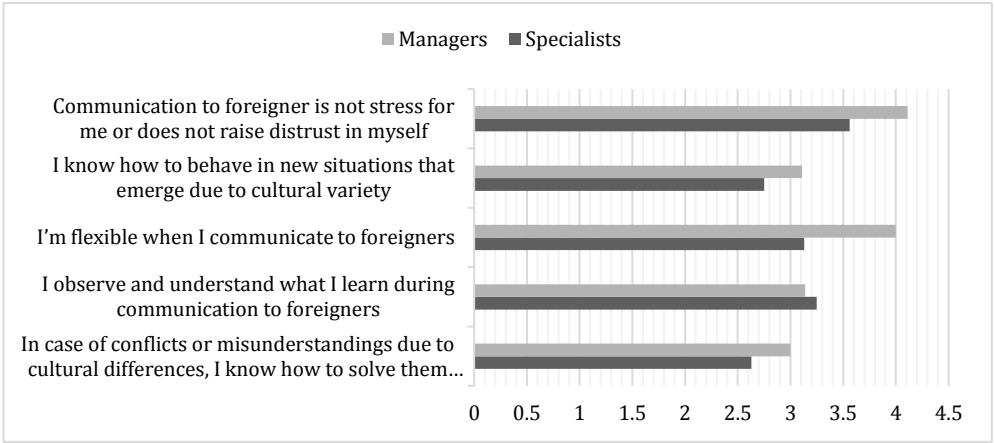


Figure 9. Intercultural communication and conflict resolving skills

Despite the fact, that respondents believe that they are almost perfectly capable to communicate in a foreign language for work purposes, the main issue related to intercultural competence seems to be the language barrier (see Figure10).

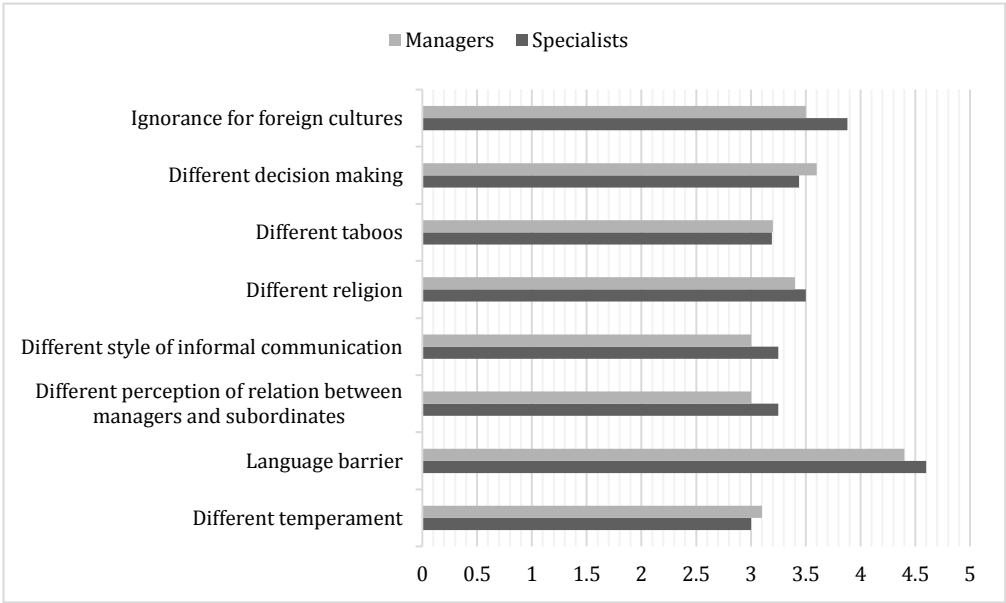


Figure 10. Main issues related to intercultural competence

Different decision making and different religion, as well as ignorance for foreign cultures have been reported as the main issues. Both subcultures demonstrate consensus in their responses.

## **Conclusions**

Application of intercultural competence model is recognized as an important paradigm to support and develop individuals' skills, knowledge, and attitudes towards establishment of well-acting intercultural cooperation and making organizational goals. Management of organizations should consider and develop these competencies, and integrate them into the organizational culture.

Most of the respondents – more than 70% – communicate with people from other countries as part of their everyday work duties. More than half of the respondents travel for work related purposes at least once a year and reported improvement of their intercultural competence level. From this it follows that the main forms of organizational support for the development and increase of intercultural competence level should be internships and business trips.

Knowledge of the main historical and social phenomena, as well as knowledge regarding the specific political and cultural norms and traditions of the particular countries has shown the lowest self-assessment scores.

Most communication of the questioned Latvian multicultural companies with business partners or customers located abroad is being done with representatives from other Baltic countries, and about 50% from Scandinavia. Thus, we can conclude that in majority of situations the communication is between neighbours or countries of a geographically close region.

Respondents agree that improved intercultural competence would foster their possibilities for the career growth; at the same time about 30% of respondents believe that the development of these skills are more considered as their own responsibility.

Intercultural competence in general is recognized as an important factor of organization's success for building relationships with other organizations abroad. However, almost 25% of specialists and 17% of managers reported that the success of the organization does not depend on individual intercultural competence level.

Responses to the question regarding the necessity of intercultural communication for organizations in the next five years demonstrated the biggest difference between the two subcultures – managers and specialists. Managers score this necessity significantly higher than specialists.

Respondents believe that the most important element to increase their intercultural competence level is the language skills, at the same time they reported weakness in the use of language at an appropriate level.

Resolving conflicts or misunderstandings caused by cultural differences are an area where respondents feel less confident. In turn, some other areas need effective communication within an organization – highlighting the importance of intercultural skills for a long-term organization's success and explaining how organization plans its development for the next five years; as well as emphasize where and how these skills should be improved.

The proposed intercultural competence model described in this paper can be used to identify gaps and areas for improvement of organization's intercultural cooperation. There are other theories which describe and assess intercultural competence. It should be necessary to create intercultural competence models

based on other theories, i.e. Rakotomena, Byram. Using and comparing the results from several models can establish better processes and instruments for further investigations, and what instruments can be used to improve intercultural competence in organizations.

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## INNOVATIONS IN PUBLIC PROCUREMENT

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### **Abstract**

*The term “innovations” has become very popular in the last decade both in theory and practice. Nevertheless, there is no certainty that it is understood and clear to all involved in procurement. The aim of this research is to get an overview of the term, its usage and ways how it is incorporated in public procurement to help practitioners understand ways to implement it better, since new possibilities will become available with the new Public procurement law, like innovation partnership procedure. The following objectives are defined to achieve this aim: to analyse the rules of innovation in public procurement, to analyse political and legal documents and legal writers’ point of view about them, and to make a proposal to address the issues found. The research methods used are descriptive, comparative and analytical methods. The authors conclude that already there are possibilities to achieve innovations through tools available, for example, by using variants or functional requirements in technical specifications. However, both new and old possibilities require willingness to use them, as well as deep knowledge of both legal and technical aspects, since procurement gets more complex when contracting authority decides to use these opportunities. So, not only a new regulation is needed, but, more important, a clear understanding how to introduce knowledge and practical know-how that is required to implement tools provided in public procurement. That could drive innovation and help achieve all the goals set on both national and European level.*

**Keywords:** public procurement, innovations, innovation partnership

### **Introduction**

Innovation plays an increasing role in our economy. It provides benefits for citizens as both consumers and workers. It accelerates and improves the design, development, production and use of new products, industrial processes and services. It is essential to creating better jobs, building a greener society and improving our quality of life, but also to maintaining European Union (hereafter – EU) competitiveness in the global market. Innovation policy is the interface between research and technological development policy and industrial policy and aims to create a conducive framework for bringing ideas to market. It will occupy a place of growing importance in European legislation (Gouarderes, 2016). Aforesaid justifies the topicality of the chosen theme. Innovation is a key source of competitive advantage, for both firms and nations (Dmitri, Piga, & Spagnolo, 2006, 483). It has been argued that public procurement can help counteract market and systemic failures hindering innovation. Put simply, the public sector can overcome

market failures by enlarging the market for certain goods and services, thus ensuring sufficient critical mass to encourage R&D investment. The public sector also influences standards through procurement, thus facilitating diffusion. Public procurement can also help offset systemic failures by enabling interaction between users and potential suppliers, and by articulating and signalling unmet needs to the market. Innovation scholars have provided empirical evidence of the impact on innovation of public procurement vis-à-vis traditional innovation policy instruments (Uyarra, et. al., 2014, 631). The results of research at the level of the EU countries shows that in all versions of the models that analysed the impact of various instruments of innovation policy on innovation, public procurement for innovation was revealed to be an influential factor (Markovic-Hribernik, Detelj, 2016, 258).

It is well known, for example, that the US government's defence procurement has been a major driving force for the development of such innovations as large passenger jets, semiconductors, and the Internet. These examples highlight that public procurement mechanisms can play a crucial role in stimulating or hampering private innovative activity. Since governmental large-scale purchases can be oriented toward goods with different R&D contents, governments must take into account the effects of their procurement decisions on R&D investment in the private economy (Dmitri et. al., 2006, 483-484). In another research it has been stated that innovation benefits are increased economic development (the amount of demand, for example, first or lead buyer can make changes in market to stimulate economics and boost the competitiveness of enterprises in future markets, by creating new enterprises and by increasing level of employment); better products and services (direct benefits to the society as an end user of state services can be the result of creation of new ideas in the market. The ideas could later be implemented more effectively, fully and cheaper); addressing the challenges of the society. The result of these processes can help solve the main challenges that society faces, for example, health and well-being; food safety; sustainable agriculture, clean and effective energy sector; sustainable and integrated transport; or climate changes and efficiency of resources (ICLEI, Latvijas vides investīciju fonds, n.d., 15).

The uncertainty surrounding the innovative activity, and the dynamic perspective that it necessarily involves, make the procurement of innovation one of the most difficult issues in the theory and practice of procurement (Dmitri et. al., 2006, 527). Balancing the efficiency and cost-effectiveness on the one hand and innovation on the other hand often leads to situations of conflict. Moreover, heavy regulations and control mechanisms in public procurement limit buyers' freedom of action. While private sector investments in innovation sometimes follow "trial-and-error" patterns, public spending is often subject to rigid rules and the demand for traceability and accountability, which pose major challenges for policy makers who want to invest in innovation (Obwegeser, Müller, 2015, 2). Of importance is not only the bidding process, but also activities before and after the procurement phase (Rolfstam, 2014, 3).

By looking at the new innovation partnership procedure that is introduced in the Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC (hereafter – Directive) among other things, the aim of this article is to analyse

regulation and aim of innovations, and the practical implications of innovations in public procurement.

The descriptive, comparative and analytical methods of research are used in this research. As the result of this research we will be able to gain some impression about the close interaction between innovations and public procurement, to see some problems arising from it in practice and possible solutions.

## **1. Concept, policy and regulation**

In the Directive innovation is described as the implementation of a new or significantly improved product, service or process, including but not limited to production, building or construction processes, a new marketing method, or a new organisational method in business practices, workplace organisation or external relations inter alia with the purpose of helping to solve societal challenges or to support the Europe 2020 strategy for smart, sustainable and inclusive growth (Directive 2014/24/EU, 2014, 2.22.) This term has been used in the Directive 41 times (also related to introduction of the new procedure – innovation partnership). In comparison, in the basic text of the Directive 2004/18/EC this term was not used at all. At the same time, it should be indicated that the possibility to use innovations in public procurement has always been present, because there are many ways to pursue and implement innovations, and they will be dealt with in this article.

The innovation policy is pursued in different levels, for example, M.Rolfstam has pointed out the role of these institutions in the process of innovations and public procurement: 1) global level – General Procurement Act, United Nations Model Law; 2) European Union level – European Commission directives in public procurement; 3) national level – national procurement law; 4) public agency (national, regional, local) – policies, internal directives, 5) procurement division – “practice” (Rolfstam, 2014, 9). It is possible to promote innovation in each of these levels. In another study it has been evaluated in which fields the term “innovations” has been studied and it showed the following lines – public procurement for innovation (how can public procurement drive innovation?); public procurement of innovation (how can public services be innovated?); innovative public procurement (how can public institutions procure innovatively?) (Obwegeser, Müller, 2015, 24).

In the context of Latvia, the most important are ongoing processes on the EU level. The legal basis of the EU general industrial framework is Article 173 of the Treaty on European Union and the Treaty on the Functioning of the European Union (hereafter – Treaty), in which it is stated that the Union and the Member States shall ensure that the conditions necessary for the competitiveness of the Union's industry exist (Consolidated versions of the Treaty on European Union and the Treaty on the Functioning of the European Union, 2012; 173). The legal basis of EU research and technological development (hereafter – RTD) are Articles 179 to 189 of the Treaty. The main instrument of EU RTD policy is the multiannual framework, where the aims, priorities and amount of the financial support for the following years has been set. European Parliament and Council adopts RTD frameworks according to the usual legal proceedings and by consulting with the European Economic and Social Committee (hereafter – EESC). In the Communication from

the European Commission (hereafter – EC) about the Europe 2020 strategy for smart, sustainable and inclusive growth (hereafter – Strategy 2020) it has been noted that a first critical step in designing a post-crisis growth strategy for the EU is to understand clearly the full impact of the crisis and to share a common diagnosis of where Europe stands. In so doing, it is also important to bear in mind that seeking to return to the growth “model” of the previous decade would be both illusory and harmful (European Commission, 2014, 6). EC points out that a network of experienced and professional people and organisations in the Member States should be established which can be called upon to reinforce a purchaser’s own resources for the more advanced innovative projects (EESC, 2009, 1.11.). EC also suggests that public purchasers could also join forces to exchange expertise and ideas and to reach a critical size of the order. This would stimulate demand for innovation, while allowing public authorities to acquire higher quality products and services (Commission of the European Communities, 2006, 12). The authors believe that it would be most important in relation to the requirements and evaluation criteria set in public procurement, and this kind of joining forces could happen by centralising biggest and most important procurements and setting up a knowledgeable team of specialists.

In the preamble of Directive, it is stressed that research and innovation, including eco-innovation and social innovation, are among the main drivers of future growth and have been put at the centre of the Europe 2020 strategy for smart, sustainable and inclusive growth. Public authorities should make the best strategic use of public procurement to spur innovation. Buying innovative products, works and services plays a key role in improving the efficiency and quality of public services while addressing major societal challenges. It contributes to achieving best value for public money as well as wider economic, environmental and societal benefits in terms of generating new ideas, translating them into innovative products and services and thus promoting sustainable economic growth. It should be recalled that a series of procurement models have been outlined in the Commission Communication of 14 December 2007 entitled ‘Pre-commercial Procurement: Driving innovation to ensure sustainable high quality public services in Europe’, which deals with the procurement of those R&D services not falling within the scope of this Directive. Those models would continue to be available, but this Directive should also contribute to facilitating public procurement of innovation and help Member States in achieving the Innovation Union targets (Directive 2014/24/EU, 2014, 47).

In the National Development Plan of Latvia for 2014–2020 in the priority “Growth of the National Economy” is a strategic objective “Advanced Research and Innovation and Higher Education”, and in the introduction it is pointed out that ensuring high quality and raising productivity constitute some of the most important preconditions for increasing the competitiveness of our businesses, which is why entrepreneurs are encouraged regularly to assess the effectiveness of their use of resources and the productivity and innovation potential of their employees to ensure that Latvia exports processed products and services with added value as much as possible. Fewer and fewer of our resources are exported in the form of raw materials. And as an individual measure to be carried out within the strategic objective is wider supply of energy-efficient and ecological goods and



services in public procurement (“green public procurement”) (Cross-Sectional Coordination Centre, 2012, 17; 439).

It can be concluded that the role of innovations as a tool for solving economic and other problems is emphasized at various levels both globally and in the EU, thus also in Latvia. So many more regulatory frameworks and policy documents will be devoted to innovation.

## **2. The possibility of innovation in public procurement**

New knowledge must be created to produce goods, and therefore the buyer must ensure that the suppliers have enough incentives to invest in the innovative knowledge that will eventually be incorporated in the goods it needs. Procurement policy can have important indirect effects on innovative activity, for example by enlarging the market for new goods, by facilitating the adoption of new standards, by changing the input and output market structure and prevailing prices so as to make them conducive to faster innovation etc. (Dmitri et. al., 2006, 485). Thereby contracting authority's (hereafter – CA) impact on these processes are huge and available instruments – multiple. The possible reasons that reduce the willingness of suppliers to innovate should also be mentioned. For example, one study points out that the main barriers reported by firms were a lack of interaction with procuring organisations, the use of rigid as opposed to outcome-based specifications, low competences of procurers and a poor management of risk. Additional key concerns expressed by suppliers included poor feedback, a low appreciation of unsolicited ideas and previous private sector delivery history, and cumbersome pre-qualification procedures and conditions (Uyarra et. al., 2014, 640). At the same time, it should be taken into account that innovation public procurement is one of the most complex questions both in procurement theory and practice. That could explain the low level of use of innovative procurements in Latvia. It may plausibly be concluded that the public sector is missing out on fully capturing innovation through procurement. The identified barriers may be preventing firms from increasing their commitment to R&D and their rate of (particularly product) innovations. Equally, it could be argued that innovative companies do not see the public sector as an intelligent customer and thus fail to exploit their full innovation potential. At the same time there is a danger that small firms are not able to get into contracts that would help them innovate (Uyarra et. al., 2014, 641). One of the reasons why potential of innovations has not been fully exploited is that the system requirements are not fully developed. Innovation is not regarded as an important value in our society. As EC points out, innovation requires a regulatory environment that is predictable, accommodates and even encourages new developments in goods and services, protects intellectual property and provides open, interoperable standards (Commission of the European Communities, 2006, 7).

Further the multiple tools that could be used when innovating will be looked at, as well as obstacles that could impact the usage.

## 2.1. The level of competition and the amount of economic operators

Procurement can be designed in such a way as to create more or less competition among potential suppliers. For example, contracts can be awarded through negotiations, beauty contests, or many different types of competitive mechanisms and tendering processes. The degree of competition induced by the chosen procurement design may affect suppliers' incentives to invest in R&D and innovate. The relationship between the degree of competition in a market and the firms' incentive to innovate is a complex issue. Traditional economic analysis suggests that there exists a positive correlation between innovation and market power: tougher competition erodes the innovator's prospective monopoly rents, and is therefore detrimental to his incentives to invest in research for innovation (Dmitri et. al., 2006, 511). We can conclude that, perhaps, if a strong competition exist, companies would be reluctant to innovate because not sure of their profitability.

The existence of opposing effects means that the overall impact of more intense competition on the incentive to innovate is generally ambiguous, perhaps making the relationship between the intensity of competition and innovation non-monotone. Some recent studies find that the relationship between competition and innovation has, indeed, an inverted-U shape: *ceteris paribus*, the market share effect (whereby competition stimulates innovation) tends to dominate at lower levels of competition, whereas the 'Schumpeterian' effect (competition erodes expected profits from the innovation hence the incentives to invest in R&D) tends to dominate at high levels of competition. When procurement can be designed to induce more or less competition among suppliers, in light of the discussion above, we can conclude that: if in the past procurement was not very competitive, fostering competition in procurement tends to increase suppliers' innovation; if procurement is already highly competitive, and the leading supplier has a strong advantage on followers, a further increase in competition may reduce suppliers' incentives to innovate (Dmitri et. al., 2006, 512).

Thereby, in every individual case CA could create more possibilities for innovation by selecting appropriate procurement methods and requirements and expertly adjusting the necessary level of competition. Choice should be based on its knowledge of the market and the market investigation.

Another factor affecting innovative public procurement, is the number of suppliers and contract volume. The larger the market for an innovative good, the stronger the incentive to invest in it. By affecting the size of the market, procurement design can therefore significantly impact the development of innovative products. Centralized procurement of large bundled contracts for innovative products or services provide the prospect of a sufficiently large and certain demand to recover large investments in R&D. Moreover, the larger the demand a producer can satisfy with his innovation, the more intensively economies of scale can be exploited (this effect relates to the industry cost structure). These effects suggest that split-award procurement contracts can be bad for innovation. However, when the research contest is bundled with a procurement contract for the supply of the innovative good, a large bundled contract makes it harder for small firms to participate in the contest. This is unfortunate as ideas tend to be widely distributed among

individual firms, and important innovations are often achieved by small and medium enterprises (SMEs) and start-ups. When SMEs conduct most of the research, large bundles make the participation of SMEs in the research contest more difficult and so may in fact reduce overall innovation. Using large bundled contracts where the winner takes all, gives large, mature incumbents a competitive advantage and makes entry by small innovative firms more difficult. In the long run, it may also induce excessive exit from the market. Apart from the effect on competition this may: reduce the 'diversity' of research paths thereby lowering the aggregate probability of success. A well-diversified research portfolio is important, as is also recognized by venture capitals who often finance several startups working on similar projects, in order to maintain high technological variety and improve their selection of the best one; reduce the competitive pressure on the incumbent(s), which may induce him to rest on the laurels of his past success, and cut the investments for future innovation; increase the distance between the technological leader and the follower. This reduces 'neck-and-neck' competition, which is bad for innovation, as both the laggard's reward to catching up with the technological leader and the latter's incentive to escape competition may fall. These problems are exacerbated when firm size or experience are among the criteria of admission to procurement contests, as is often the case for a variety of reasons. The optimal size of supply contracts and number of contractors selected are therefore difficult to choose, as they depend on several economic variables which are hard to estimate. Given our limited knowledge of the strength of the various forces at play, one way out is to let competing firms endogenously determine the optimal demand size. This can be achieved by splitting competitive procurements in many small lots, but allowing for 'package bidding'. Package bidding means that bidders can condition their bids on the number, and possibly the type, of the lots awarded. The small size of lots allows small and perhaps more innovative firms to participate in the contest, but large suppliers can exploit economies of scale in R&D and production if these are substantial (Dmitri et. al, 2006, 513–515).

It can be concluded that in innovative procurement the CA must take into account very different aspects and should thoroughly get to know the market, to both select the optimum procurement method, which will provide the most suitable level of competition for innovation, and the appropriate volume of the procurement object (division of lots) not to exclude participation of companies that are new or small, but with a significant potential of innovation and new ideas. CA should also pay attention to the qualification requirements in this aspect.

## **2.2. Requirement of technical specifications**

Given that the innovation (specially in the meaning of the Directive) is directly related to the object of procurement, technical specifications are one of the most important instruments for the promotion of innovation. Directive states, inter alia, that the technical specifications drawn up by public purchasers need to allow public procurement to be open to competition as well as to achieve objectives of sustainability. Consequently, technical specifications should be drafted in such a way as to avoid artificially narrowing down competition through requirements that favour a specific economic operator by mirroring key characteristics of the

supplies, services or works habitually offered by that economic operator. Drawing up the technical specifications in terms of functional and performance requirements generally allows that objective to be achieved in the best way possible. Functional and performance-related requirements are also appropriate means to favour innovation in public procurement and should be used as widely as possible (Directive 2014/24/ES, 2014, recital 74). In the Directive it is reflected as one of the specification formulation types. So one of the ways technical specifications shall be formulated is – in terms of performance or functional requirements, including environmental characteristics, provided that the parameters are sufficiently precise to allow tenderers to determine the subject-matter of the contract and to allow CA to award the contract (Directive 2014/24/ES, 2014, 42.3a).

This option is already allowed and Procurement Monitoring Bureau (hereafter – PMB) regarding this formulation option indicates that it should be used, if the CA knows the result it wants to get, but is not aware of the possibilities that the market offers and it trusts the members of the market to offer effective and innovative solutions, for example, in the fields of information technology systems, construction design, public relationships. This approach allows to reach the most effective solution, if the CA thinks of functional or operational characteristics as the most important. CA should carefully consider whether the functional requirements will ensure the most advantageous tender for achieving the procurement goal. As possible advantage of this approach could be – great freedom for suppliers to offer innovative solutions; it is easier to prepare technical specifications; responsibility for the goal moves to the supplier; increased competition. By contrast, the disadvantages are – more complex evaluation process, a wide range of prices can be offered; a more complex set of evaluation criteria needed; the CA could not be satisfied with individual processes or methods by which it is proposed to meet the goal (it can be avoided by imposing the main processes and methods, or by prohibiting the application of specific methods). Also, the CA can draw up technical specifications by combining the forms, partially defining specific technical characteristics and by reference to standards as well as including functional or performance requirements (PMB, 2014, 4, 5). Although that assessment is given with regard to the technical specification regulations in force prior to the implementation of the Directive, it should still be taken into account, because the basic principles remain the same.

Output or outcome specifications should be well constructed in order to stimulate suppliers in proposing innovative solutions. A well-defined outcome can go a long way towards challenging suppliers to generate ideas. A well-constructed output specification identifies the outputs from, rather than the inputs to, a requirement. An outcome specification takes this one step further and only specifies the end result to be achieved. It is equivalent to specifying the problem and inviting proposed solutions. In allowing suppliers freedom to submit innovative bids, procurers should specify compliance with standards where appropriate, for example to ensure compatibility. In order to stimulate innovative solutions (process, integration, production, or delivery), requirements as well as evaluation criteria have to be based on a set of functionalities that the contractor must provide, regardless of the technology used to implement them (making intelligent use of standards). Of course a good management of the tendering process must

ensure suppliers sufficient time and opportunity to develop innovative proposals. Often, tenders have to be submitted in a very short time, and this does not allow suppliers to find innovative solutions. The duration of the procurement process should be fine-tuned with the role played by innovative solutions (Dmitri et. al, 2006, 517).

Also the Supreme Court of the Republic of Latvia has concluded that in the applying the 1 paragraph of Article 17 of the Public Procurement Law (hereafter – PPL) (currently regulates the preparation of technical specifications) it has to be taken into account that the law does not allow only unjustified restrictions to competition, not all of them. In the specific case the facts show a case where CA has chosen to use such pipelines that, considering the small amount of manufacturers, at the point in time should be considered innovation. This could be a threat to a wider competition. But the choice of innovative solution could also be justified, even if it narrows the circle of competitors in the procurement. In the long run it could enlarge the offer of the product in the market, thereby providing opportunity for innovation to win a position also in the public procurement. Innovations, as well as protection of environment (especially energy efficiency), is a value to society, that is also set out in the Green Paper on the modernisation of EU public procurement policy: Towards a more efficient European Procurement Market. In view of this, in such cases it is important to ascertain whether the reference to the protection of the environment and the need to use the best available goods are not too substantially restricting competition. In this case Court did not saw unnecessary restriction of competition (Supreme Court of the Republic of Latvia, SKA-1033/2013, 7).

In the context of technical specifications, the opinion of European Parliament should be mentioned. It emphasizes that any extension of the EU procurement rules into the area of ‘what to buy’ would represent a significant change to the current regime and should be carefully assessed (..) the directives are often perceived as too detailed and they have become increasingly technical and complex, while at the same time the legal risk of non-compliance has increased considerably for CA and suppliers alike; the fear of challenge leads to a risk-averse approach, which stifles innovation and sustainable development, resulting far too often in CA opting for the cheapest price rather than the best value. That is why European Parliament is supporting clear and easy rules, that would be less detailed (European Parliament, 2011, 25–26).

The authors fully join this view. It could be concluded that CA already has had a wide access to innovative solutions, that could be used by cleverly preparing technical specifications and by paying special attention to the functional requirements. At the same time this approach is demanding both motivation of the CA to obtain an innovative solution (for example, as a management setting or suggestion from experts), and knowledge and skills of the officials (broad knowledge about the object of the procurement, its technical and legal aspects, as well as knowledge in the public procurement field). The activities mentioned includes some risk when compared to the technical specifications with specific requirements, so it requires more potential use of resources from the CA. In circumstances where the resources are limited and the knowledge of the procurement specialists is largely fragmented and based on everyday needs, the long-term benefits of innovations can go unnoticed so the possibilities may not be

used in practice. For example, A.Cepilovs points out that public procurement is one of the least professionalized areas of public administration (Cepilovs, 2014, 17). Consequently, in order to facilitate the use of functional requirements in practice, it is necessary in particular to motivate and educate CA, enabling them to provide safe and effective ways to use the functional requirements of the technical specifications. Special attention should be paid to the benefits and practical aspects, as well as ways to reduce the potential allocation of resources and risks, including litigation.

### **2.3. Variants**

Another way of promoting innovation is the possibility to submit variants in public procurement. In the preamble of the Directive it is said that because of the importance of innovation, CA should be encouraged to allow variants as often as possible. The attention of those authorities should consequently be drawn to the need to define the minimum requirements to be met by variants before indicating that variants may be submitted. (Directive 2014/24/EC, 2014, recital 48). The use of variants is regulated in the Article 45 of the Directive. Variants mean more choice to the CA, so they lead to more appropriate solutions and the possibility that they will answer CA needs.

By allowing to submit variants CA is relying on the creativeness of the tenderer and on the knowledge of the market and by that obtaining broader basis to make decision. Variants are not important only for technical solutions, they could be allowed also for other elements of the tender (Hjelmborg S. E., Jakobsen P. S., Poulsen S. T., 2006, 202), for example, use of environmental friendly materials. In such way both tenderers can optimize their tender and CA obtain more advantageous offer. European Court of Justice in the case C-368/10 points out that it must be possible to submit tenders which reflect the diversity of technical solutions. CA that wish to define environmental conditions for the technical specifications of a given contract may lay down the environmental characteristics, such as a given production method, and/or specific environmental effects of product groups or services. They can use, but are not obliged to use appropriate specifications that are defined in eco-labels, such as the European Eco-label, (multi-)national eco-labels or any other eco-label providing the conditions for the label are drawn up and adopted on the basis of scientific information using a procedure in which stakeholders, such as government bodies, consumers, manufacturers, distributors and environmental organisations can participate, and providing the label is accessible and available to all interested parties. The technical specifications should be clearly indicated, so that all tenderers know what the conditions established by the CA cover (European Court of Justice, 2010, 29). On the other hand, it has been observed that increased emphasis on performance/function based specifications, the possibility to use a technical dialogue (or now preliminary market consultation) and specific procedures designed to elicit technically suitable specifications, reduce the need to rely on variants in most instances (Lichère, Caranta, Treumer, 2014, 372).

The authors conclude that, as in the case of functional specifications mentioned above, also in this case it is important to have a competent procurement committee. The setting of minimal requirements and assessment of variants requires more

complex knowledge than evaluation of tenders without variants. Therefore, this possibility is rarely used in practice and that does not promote innovations.

## **2.4. Competitive dialogue, competitive procedure with negotiation and design contest**

In the PPL the procurement procedure “competitive dialogue” is included since 2009. A competitive dialogue is a procurement procedure, which the CA is entitled to apply if the procurement contract is considered to be particularly complex. And it could be considered to be particularly complex if at least one of the following criteria exists: 1) the CA cannot objectively prepare technical specifications conforming to the requirements thereof in accordance with Section 17, Paragraph four, Clauses 2, 3 and 4 of this Law and it cannot select the most corresponding tender in an open or restricted procedure; 2) the CA cannot objectively specify the legal or financial solution of the project (PPL, 2006, 64.<sup>1</sup>). Whereas in the new project of PPL it is set out that the CA could apply competitive procedure with negotiations and competitive dialogue among other if the procurement contract includes designing or innovative solutions (PPL project, 2016, 8.5.2.). The CA assess whether competitive dialogue suits the project on the basis of a specific assessment of the individual case. If the matter of the contract is assessed be so complex that the CA cannot describe the acquisition in full, there is sufficient reason to start a dialogue with the suppliers on the acquisition before they make a bid for the task. During the dialogue phase, the input of suppliers can help the CA identify and define its’ requirements (which is similar to the negotiated procedure) (Haugbølle, Pihl, Gottlieb, 2015, 558).

In the preamble of the Directive it is noted that use of the competitive dialogue has significantly increased in terms of contract values over the past years. It has shown itself to be of use in cases where CA are unable to define the means of satisfying their needs or of assessing what the market can offer in terms of technical, financial or legal solutions. This situation may arise in particular with innovative projects, the implementation of major integrated transport infrastructure projects, large computer networks or projects involving complex and structured financing. Where relevant, CA should be encouraged to appoint a project leader to ensure good cooperation between the economic operators and the CA during the award procedure (Directive 2014/24/EC, 2014, recital 42).

Nevertheless, as the practice shows, this procedure is not widely used in Latvia. In the website of PMB only 13 notices can be found and they are about 4 competitive dialogue procedures, from which 2 are terminated, one has a result (identification number – RDITC 2015/013, one tender received) and in one no decision is made in the moment of preparation of this article (PMB, 2016, 1). At the same time in United Kingdom already in 2009, the former OGC published guidance on “Driving innovation through public procurement”. In that guidance it recommended the use of the “competitive dialogue” procedure to drive innovation. That procedure was introduced in the Public Contracts Regulations 2006 and has been extensively used in the UK and across the EU (Bennet, 2015, 1). The use of competitive dialogue in UK is confirmed also by other sources. Competitive dialogue is not used to the same extent as open and restricted procedures. The procurement procedure is still

considered relatively new, which perhaps is one of the reasons for the modest use. In 2010 to 2013, the aggregate number of contracts reached 778 in the EU, representing 0.6 per cent of the total contracts entered into by public tenders and approximately 5 per cent of the number of restricted tenders. Most of the agreements on competitive dialogue in the EU – some 79 per cent – are concluded by authorities in France and the UK. Denmark and Norway have announced an equal number of tenders in competitive dialogue, but Norway has not concluded any contracts. It is not clear, however, whether the tasks have been assigned using another contract form or the tasks have not been assigned due to lack of funds by the CA (Haugbølle, Pihl, Gottlieb, 2015, 558). When evaluating the experience in UK, it can be concluded, that the procurement procedure is generally perceived in Britain to be costly – both for the CA and the supplier. The procedure is expensive, time-consuming and/or complex to carry out in practice. The high costs are mainly related to: 1) poor preparation and planning process, 2) inadequate resource coverage for the procedure, 3) meetings with an extremely long time horizon and length, and 4) the requirements for unnecessary information from bidders. According to the UK Treasury competitive dialogue procurements are generally accepted as costlier compared to traditional procurement routes. To get the best opportunities to reap the benefits, the Confederation of British Industry recommends that the CA set up a “resourceful” procurement team. The group should include expertise in several areas, such as law, economics, technical aspects, as well as skills in business negotiation (Haugbølle, Pihl, Gottlieb, 2015, 559). CA could receive innovative solutions also by competitive procedure with negotiations, as well as with design competition that allows for a CA to acquire a design (plan or project) (PPL, 2006, 70), so new ideas could be offered.

The authors conclude that a competitive dialogue procedure is practically not used in Latvia. It could be because it requires “resourceful” procurement team, which should include knowledge in several areas, as the British Industry Association puts it. So it would also be expensive process that our CA could have some problems with.

## 2.5. Criteria for Selection of Tenders

Taking into account their impact on the end result, the evaluation criteria could also be used as a tool to enable innovations. PMB head D.Gaile as an example points out that for award there may be taken into account factors like work, supplies or service quality, functional characteristics, environmental characteristics, technical merit, etc., as well as clean and energy efficient transport choice (Gaile, 2014, 13). Accordingly, to promote innovations, multiple criteria not connected with the price could be used. Nevertheless, in Latvia the selection criteria “lowest price” is widespread, because it is the easiest and fastest evaluation type. Although the innovative solution could also have the lowest price, mostly it is connected with better quality. It should be pointed out, that in public procurement, especially, if the selection criterion is lowest price, there is small hope that the entrepreneurs will act in a socially responsible way and will offer innovative solutions instead of the option to offer lowest price and win the procurement.

Professor M.Rolfstam – one of the researchers studying innovations in public procurement – has concluded that, even if the changes in the field of innovations



overall could be considered positive, there are multiple institutional factors that interfere with usage of available tools for innovation in public procurement. A.Cepilovs continues that, when analysing situation in Latvia, it could be concluded that the directives or national legislation is not the main factor that restricts more effective and creative usage of the budget. As one of the main obstacle still remains the usage of the lowest price as the primary selection criterion. In practice there are many reasons for that. From the reasons that A.Cepilovs has pointed out authors distinguish these: 1) the public procurement function is distributed and fragmented among a number of very diverse public organisations – starting with relatively large, such as regional hospitals of large municipalities, and finally with a very small organisations and local municipalities. The size of a CA is often directly related to its capacity, which may not be sufficient to implement the complicated procurement procedures. Namely, CA does not have the technical knowledge and time needed, to fully manage the pre-procurement negotiations; 2) lack of administrative capacity to develop a full, detailed and technically sound procurement specification; 3) the qualitative criteria that are often used in the most economically advantageous tender selection opens up the possibility of subjective interpretation, which in turn may mean a challenge to the results. If CA capacity for the defence of decision is insufficient, the only solution is to make all the requirements in the form of quantitative indicators, thus not allowing CA to interpret the demands freely nor for the tenderers to challenge procurement outcomes. One of the possible solutions to overcome these difficulties could be the organisation of joint procurements of several CA (for example – municipalities). In this way the municipalities can assess their needs and combine the resources available to them in order to increase the impact on the procurement market, as well as improve the technical and administrative capacity for the implementation of complex procurement procedures. In order to improve the quality of procurement it is useful also to share examples of good practice both in Latvia and abroad, thus creating and raising awareness of new possibilities and ways to use public procurement to promote innovation and sustainability. Until now, partly because of the economic crisis, the public procurement practice was more focused on the efficient use of resources, which is mostly confined to the lowest price criterion (Cepilovs, 2016, 1).

The authors agree with the solutions, while in U.Skrastiņa's view, since the selection of tender ensures the link between the requirements set in the procurement documents and the result (when the tenderer is chosen in public procurement), the view that the criterion of lowest price is the main reason for all failures in public procurement is devious. Such belief is often unfounded because it is due ignorance and lack of comprehension. Focusing on the lowest price as the cause of all failures prevents us to see the real reasons for the problems, but they lie elsewhere. Not the lowest price criterion is to blame for the poor procurement planning, the lack of time, and of incompetence and ignorance of the procurement commission (Skrastiņa, 2015, 7). The most important aspect is the professionalism and expertise of the commission.

Thus, the authors conclude that the most important in the use of possible potential of selection criteria is the commission's expertise. There are multiple solutions for increasing the competence, both associated with a set of detailed guidelines and competence centres and further training.

### 3. Innovation partnership

As already mentioned earlier about competitive dialogue and competitive procedure with negotiation, one of the grounds for using them is “innovative solutions”. Generally new procedures are to be welcomed because they offer something different and better than the previous procedures. This therefore begs the questions, why has a new procedure been introduced for “innovation” and does it offer a clear advantage over competitive dialogue or competitive negotiation? (Bennet, 2015, 1)

It is indicated in the preamble of the Directive about the innovation partnership that where a need for the development of an innovative product or service or innovative works and the subsequent purchase of the resulting supplies, services or works cannot be met by solutions already available on the market, CA should have access to a specific procurement procedure in respect of contracts falling within the scope of this Directive. This specific procedure should allow CA to establish a long-term innovation partnership for the development and subsequent purchase of a new, innovative product, service or works provided that such innovative product or service or innovative works can be delivered to agreed performance levels and costs, without the need for a separate procurement procedure for the purchase. The innovation partnership should be based on the procedural rules that apply to the competitive procedure with negotiation and contracts should be awarded on the sole basis of the best price-quality ratio, which is most suitable for comparing tenders for innovative solutions. Whether in respect of very large projects or smaller innovative projects, the innovation partnership should be structured in such a way that it can provide the necessary ‘market-pull’, incentivising the development of an innovative solution without foreclosing the market. CA should therefore not use innovation partnerships in such a way as to prevent, restrict or distort competition. In certain cases, setting up innovation partnerships with several partners could contribute to avoiding such effects (Directive 2014/24/EC, 2014, recital 49).

It can be concluded that the precondition of the use of this procedure is the need for innovation, that is also stressed in the regulation – the innovation partnership shall aim at the development of an innovative product, service or works and the subsequent purchase of the resulting supplies, services or works, provided that they correspond to the performance levels and maximum costs agreed between the CA and the participants (Directive 2014/24/EC, 2014, 31.2.).

The reason for the introduction of innovation partnership is linked to the Europe 2020 strategy, to which reference is made in the preamble of Directive, including indication about the need for special procedure (Bennet, 2015, 1). Further we will look at the aspects that differ this procedure from other procedures with multiple stages and negotiations.

Every procurement begins with a determination of the value of the procurement object, for CA to be able to choose the appropriate procedure. In the case of innovation partnerships, the value to be taken into consideration shall be the maximum estimated value net of VAT of the research and development activities to take place during all stages of the envisaged partnership as well as of the supplies, services or works to be developed and procured at the end of the envisaged

partnership (Directive 2014/24/ES, 2014, 5.6.). Authors find it difficult to predict how the following contract price determination could take place in practice, taking into account the fact that innovations by nature is something unknown, non-existent yet, so the predicting of the cost could cause difficulties to the CA, since, in order to determine the value, you need to understand, what you want to buy.

With regard to this process the Directive indicates that in the procurement documents, the CA shall identify the need for an innovative product, service or works that cannot be met by purchasing products, services or works already available on the market. It shall indicate which elements of this description define the minimum requirements to be met by all tenders. The information provided shall be sufficiently precise to enable economic operators to identify the nature and scope of the required solution and decide whether to request to participate in the procedure (Directive 2014/24/EC, 2014, 31.1.). In the view of authors, it is important to stress that the minimal requirements must be “sufficiently precise”, that could lead to difficulties in some individual cases, since this term is uncertain and the answer whether the economic operator can identify the nature and scope of the required solution and decide whether to request to participate in the procedure CA could be able to ascertain only after the advertising of the procurement. At the same time in the Directive it is set out that the estimated value of supplies, services or works shall not be disproportionate in relation to the investment required for their development (Directive 2014/24/EC, 2014, 31.7.), so the estimate value should be proportionate, therefore – based on some reasonable consideration.

In the process of preparing the procurement also the qualification requirements should be chosen. In case of innovation partnership, The Directive indicates that in selecting candidates, CA shall in particular apply criteria concerning the candidates’ capacity in the field of research and development and of developing and implementing innovative solutions (Directive 2014/24/EC, 2014, 31.6.). Taking into account the different nature and content of the innovations, also this process could cause some problems for the CA, especially, if the innovative solutions is so innovative, that nothing like that has been made before or there are very limited number of economic operators working in particular field.

Regarding tender selection criteria in the innovation partnership the contracts shall be awarded on the sole basis of the award criterion of the best price-quality ratio in accordance with Article 67 (Directive 2014/24/EC, 2014, 31.1.). What also should be taken into account is that negotiations during innovation partnership procedures may take place in successive stages in order to reduce the number of tenders to be negotiated by applying the award criteria specified in the contract notice, in the invitation to confirm interest or in the procurement documents. In the contract notice, the invitation to confirm interest or in the procurement documents, the CA shall indicate whether it will use that option (Directive 2014/24/EC, 2014, 31.5.).

About the innovation partnership procedure process the Directive indicates that the innovation partnership shall be structured in successive phases following the sequence of steps in the research and innovation process, which may include the manufacturing of the products, the provision of the services or the completion of the works. The innovation partnership shall set intermediate targets to be attained

by the partners and provide for payment of the remuneration in appropriate instalments (Directive 2014/24/EC, 2014, 31.2.). The innovation partnership shall be structured in “successive stages”; with “intermediate targets” and remuneration in instalments. Such a partnership therefore opens up the possibility to enter into an agreement in the form of an incremental contractual arrangement using two distinct stages – the first being the “R&D” or design stage to develop the solution; followed by the service contract that delivers the solution. The ability to incorporate both a research and a commercial phase in a single procurement may have been the driver for the introduction of this process though, being a common law jurisdiction, our (UK) contracts already allow for this flexibility. The procedure may also feature the termination of the partnership after each phase (Bennet, 2015, 1). Based on those (intermediate) targets, the CA may decide after each phase to terminate the innovation partnership or, in the case of an innovation partnership with several partners, to reduce the number of partners by terminating individual contracts, provided that the CA has indicated in the procurement documents those possibilities and the conditions for their use (Directive 2014/24/EC, 2014, 31.2.).

When drafting the contract CA should remember that the CA may decide to set up the innovation partnership with one partner or with several partners conducting separate research and development activities (Directive 2014/24/EC, 2014, 31.1.), respectively, there can be several contracts. Likewise, in the procurement documents, the CA shall define the arrangements applicable to intellectual property rights (Directive 2014/24/EC, 2014, 31.6.). So the key element that is new with innovation partnerships is that it expressly deals with the structuring of the contractual position after contract award, not just the award procedure itself (Bennet, 2015, 1).

While there is nothing to prevent any other procurement process resulting in the award of more than one contract, this new procedure seems to offer the flexibility to set up a contractual “partnership” with a limited number of chosen providers, then ask them each to develop component parts of an overall solution to a complex problem, before awarding a delivery contract or contracts to the partners that deliver the “best” solution at that design stage. It is difficult to find clear examples of when the innovation partnership may be used. However, it could be helpful in designing a technology-based multi-agency business transformation project, or a waste project involving recycling, landfill and waste to energy technologies. Or even in the design and commissioning of innovative surgical techniques. This all assumes the arrangement is commercially attractive both to CA and economic operators (after all, designing new solutions is not cheap and the management of the IP rights complex) (Bennet, 2015, 1).

The authors conclude that the CA should be clear about “the sequence of steps in the research and innovation process”, to be able to provide that the innovation partnership steps correspond to them. The Directive also specifies that the CA shall ensure that the structure of the partnership and, in particular, the duration and value of the different phases reflect the degree of innovation of the proposed solution and the sequence of the research and innovation activities required for the development of an innovative solution not yet available on the market. The estimated value of supplies, services or works shall not be disproportionate in

relation to the investment required for their development (Directive 2014/24/EC, 2014, 31.7.).

In the authors view CA should be very knowledgeable regarding object of the procurement that it is about to obtain, in order to ensure that these conditions are met.

The regulation of the negotiations stage does not essentially differ from other procedures. The requirement of equal treatment of all tenderers is emphasized and the non-disclosure of confidential information without special permission.

CA should bear in mind that, even there are regulations about the ability to modify contracts in the Directive, it does not include any particular exemptions for “innovation partnership”, so the general rules apply to it. In which case, it would seem the same difficulties in structuring contractual arrangements will apply to the use of innovation partnerships as to those previously faced by the use of competitive dialogue/competitive negotiation (Bennet, 2015, 1).

Regarding application of this procedure in practice nothing could be said since the Directive is not yet fully transposed in Latvian legislation. At the same time, for example, in United Kingdom, since the PCR 2015 came into force, no CA have published OJEU notices inviting suppliers to participate in a proposed innovation partnership. However, it is early days and it remains to be seen if practitioners will move away from tried and tested procedures to a new procedure that appears to have similar limitations. The grounds for using competitive dialogue or competitive negotiated (innovation, complexity or inability to specify) would seem to overlap with the grounds for innovation partnerships. All processes arguably offer the same flexibility during the procurement process, and all the processes have difficulties both commercially and with the limitations on changing contracts after award. The justification for the introduction of this new procedure may rest, at least partly, on its branding rather than any real differences it offers from that which can be achieved through one of the other procurement routes (Bennet, 2015, 1).

Authors cannot comment on the above, since they have not applied the new procedure. One of the problems with the use of existing competitive dialogue or competitive negotiated procedures has been in identifying, costing and describing (at least in outline terms) the need for an “innovative” solution; whilst being reliant on economic operators to suggest that very innovation. Whilst it is common to outline the problem faced (rather than the solution) there still remains the need for a degree of precision in estimating the contract value, in describing the technical specification and in describing the contract flexibilities sufficiently transparently to avoid the risk that planned changes during the life of the contract are not be deemed to be materially different to the arrangement originally advertised. Unfortunately, (the introduction of innovation partnership) does not seem to have removed these difficulties (Bennet, 2015, 1)

The authors conclude that the innovation partnership procedure offers the opportunity to innovate, however, the price of it is relatively high and procedure requires considerable resources from the CA. As A.Cepilovs points out, to ensure that the new initiatives really work, the CA and economic operators must be trained and informed not only about the requirements of the new directives or the

new PPL, but also on how to properly use all the opportunities afforded by the new directives (Cepilovs, 2016, 1). Authors fully agree with this conclusion.

## Conclusions

1. The concept of innovation has been used public procurement field already for a while. It has become increasingly important both to EU and Latvia. Since innovations is considered as a solution to the various economic and social issues its place in EU legislation will grow. However, on one hand, the balancing of effectiveness, and, on other hand, innovations, can lead to conflict, because of the complex rules and control mechanisms for CA that limits the discretion (flexibility) which is essential in innovation process. Consequently, innovative public procurement is one of the most complex issues of public procurement, both in theory and in practice. That in some way explains the low level of enforcement of innovative procurement in our country.
2. Innovation, especially in the meaning of the Directive, is directly related to the object of the procurement, which is defined in technical specification. For that reasons it is one of the main instruments for promoting innovation in public procurement. Functional or performance requirements instead of strict technical description should be used more often, because it is the most appropriate means to promote innovation. However, this requires both CA motivation to obtain innovative solution, and knowledge and skills to prepare high-quality technical specifications. But, if the competence of CA is low, it is virtually impossible to successfully implement this in practice.
3. Also in case of evaluation of variants it is important to have a competent procurement committee, because laying down minimum requirements and assessment of variants requires more complex knowledge than evaluation of offers without variants. Therefore, in practice tenderers are rarely allowed to use variants and it certainly stifles innovation.
4. Fear of complex tasks leads to risk aversion, which stifles innovation and sustainable development. Therefore, too often the selection criterion "lowest price" is used instead of the most advantageous tender. Also in this case as a solution could be offered training of procurement commission for better competence and procurement centralization (latter could be threatening to SMEs).
5. The competitive dialogue procedure has not been practically used in Latvia, since it requires "resourceful" procurement team, which should include knowledge in several areas, as the British Industry Association puts it. So it would also be expensive process that our CA could have some problems with.
6. Innovation partnership offers an opportunity to innovate, but the price of it is relatively high and requires considerable resources from the CA. To ensure that the new initiatives really work, CA and suppliers must be informed and trained not only about the new directive or the new PPL requirements, but also on how to properly use all the opportunities afforded by the new directive.
7. The most important in implementing innovations in public procurement is the competence of CA and its willingness to invest resources needed for the

preparation of procurement. In order to promote innovative public procurement and reduce the risks arising from the poor quality of procurement documents, PMB together with industry professionals should develop standardized models of procurement phases. Also regarding innovative offers and solutions it would be complicated to deal with without participation of professionals. Experts of each sector could publish in PMB website their proposals on how to evaluate offers, select the criteria and how to determine algorithms.

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## SOURCES OF ADMINISTRATIVE LAW IN LITHUANIA AND LATVIA

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### ***Abstract***

*The aim of this article is to present a historically comparative background of the development of legal doctrine and legal norms about the sources of administrative law in two Baltic countries – Lithuania and Latvia. The authors analyse points of view and legal regulation on the sources of administrative law in Rome, France, Lithuania and Latvia. The research done can be of major importance for the improvement theory of administrative law, as well as in the practice of law applies how to use the sources of administrative law. The authors outline the common understanding of the sources of administrative law in the legal environment of the European Union and the differences in constitutional regulation in Lithuania and Latvia for the hierarchy of legal acts, where in the Constitution of the Republic of Latvia there is no legal norm on legal acts as it is done in Article 7 of the Constitution of the Republic of Lithuania. The article conveys the opinion that the Constitution of the Republic of Latvia should have regulations on legal acts and their force.*

**Keywords:** sources of administrative law, Constitution, common principles of law, laws, treaties, Acts of the Constitutional Court, Doctrine of administrative law

### **Introduction**

The article studies sources of administrative law that contain traditions, legal enactments, case law, law principles and legal doctrine. As in every state, in Lithuania and Latvia the proper performance of sources of administrative law is significantly affected by a targeted and coherent public policy in the society and an adequacy of managerial and legal measures for their implementation. Nowadays it is significant to have a historical comparative background of the development of the sources of law to make administrative law sources valid.

However, political priorities are constantly changing; their implementation is fragmented and often limited to the term of office of elected institutions; ineffective measures are selected; adopted legislation causes public discontent and increase the administrative burden; and declared objectives have not been met. The judge made law and administrative law doctrine as well; so all the legal enactment procedure should be developed.

## 1. Traditions

Traditions of the category of the source of law. The writings and discussions on the sources of law date back to the times of the Roman law. The first mention of the term “the source of law” is related to Titus Livius (Titus Livius Patavinus. 59 BC – AD 17). This Roman historian considered the Law of the Twelve Tables as a source of information about the Roman legal norms of the time and the Roman legal mind. Gradually this term caught on among lawyers. As the historical experience of the use of the term “the source of law” shows, the meaning of this category has, to a large extent, depended on the definition of the content of a particular concept of law. The broader the content of the concept of law, the broader the interpretation of the category of the source of law. Therefore, this factor determined the polysemy of the use of the term “the source of law” related to various economic, ethical, religious, cultural and other social elements and conditions of the development of law, the will of the state and the nation, as well as its means of expression, etc. *From the etymological point of view*, “the source” is one that initiates (Red. kol. Keinys St., 1993; Lazdiņš J. u.c., 2015, 51–119).

The source of law is the cornerstone of the existence of law on the basis of which the law regulates social relations and which reveals the status of the legal system in a state.

The change of the meanings of the source of law has been observed ever since the first mentioning of this category. The sources of the Roman law may be interpreted in a broader way – as patterns of the origin of legal norms or the development of the forms of their outer expression, also as Roman law monuments. At the same time, one can evaluate the early sources of the Roman law in retrospective. At that time, the process of the formation of the law was determined by:

- 1) customs;
- 2) laws (during the times of the republic – resolutions of the assembly of the people; during the times of the principate – senate resolutions by which the will of the principate was implemented; under absolute monarchy – emperors constitutions);
- 3) magistrates’ edicts (orders and commands of the king, the emperor, the magistrate of Rome, the governor of a province);
- 4) jurists’ activity (jurisprudence) (Girard Paul Frederic, 1931, 3–128)

These are the sources of law appreciated by history; scientists consider them as a historical fact, an influential element of the legal systems of various countries.

Petras Leonas, in analysing the issues related to the creation of the positive (active) law, revealed the role of the source of law as well: *“First of all, law originates in the human mind, feeling; clashes of interests have to be managed, tied, thus one has to think of ways to do it. Later, the subjective feeling of law, the subjective consciousness of law is expressed in an active, positive legal norm. This expression of the consciousness of law in an active legal norm (the positivisation of law) is carried out under the impact of various external, from the point of view of the legal subject, occurrences that are commonly referred to as ‘the sources of law’”* (Leonas P., 1931, 161). P. Leonas identified several different meanings of the category of “the source of law”. From the point of view of historical heritage, the sources of the cognition of law are intended for obtaining knowledge about the law

of a certain society. These are texts of laws, written sources of customs, court cases, yearbooks, literature, etc.

Primary factors of the objectivisation\* of law that materialise the ideas of law, “give birth” to law through the legal consciousness. Among such factors, in the opinion of the author, were various interests of the society, ideas of morality, religious beliefs.

In our opinion, such a materialised “giving birth” to law allows a schematic representation of certain stages of the conversion of law, while the whole process of the objectivisation of law reveals the characteristic features of the formation of the sources of law: society culture (interests, ideas of morality, religious beliefs of the society) ↔ legal ideas ↔ legal doctrine ↔ outline (conception) of a certain law ↔ scheme (programme) of the drafting of a certain law ↔ draft law, law ↔ implementation of the law (Urmonas A., 2002, 107; Pleps J. u.c., 2004, 427– 443; Pleps J. u.c., 2014, 291–324).

In the formal sense, Leonas refers to the established “forcible legal norms” as the sources of law. As the author states, “there is no law unless it is coercible; until the moment when the law becomes coercible, there is only consciousness, the feeling of law”. Therefore, the material content of the sources of law “lies deep in the relations and consciousness of society members”. (Leonas P. 1931, 161–162).

Thus, in the opinion of Leonas, the source of law, *in the material sense*, is the precondition for the formation of legal norms, i.e. the factors that determine the content of legal norms and allow determining their meaning, while *in the formal sense* it is the external form of the establishment of a legal norm. The representatives of the positive doctrine “closed” the discussions on the sources of law within the frame of the “pure law” (Hans Kelsen) by establishing the hierarchy of the sources of law. *“The theory of legal stages as developed by Merkl (Beachte auch Kelsen.1923., Neudruck 1960). and later taken by Kelsen (Kelsen, H., 1960, 313). and used in his Pure Theory of Law, should explain legal norms and related forms of legal constructions. This connection between legal norms and the forms of legal constructions appears as a systemic sequence from superior to inferior norms that may, therefore, be called steps, as these norms are in the determinant/conditionate relation.”* (Schambeck H. Hanso, 2011, 18(4), 1287). Eventually, this understanding of the conception of the source of law as a form of the establishment of the external law was finally entrenched by the normative (statist) doctrine. It had a long-lasting impact on the scientists and practitioners of law, formed this tradition of the meaning of the usage of the category “the source of law”.

Even today in the Lithuanian law, as well as in the Latvian law, the legal category “the source of law” is used in the traditional sense of the objectification of certain norms with some modifications determined by new social relations. For example, in the new textbook of constitutional law, it is stated that “the Constitution, its constituent parts comprise an integral system of norms and principles of the highest regulation level” (Birmontienė T., 2012, 65).

Constitutional norms regulate the fundamental aspects of the life of an individual, a society, a state, but, for instance, The Constitution of the Republic of Latvia, has no article about supremacy, but due to the state law doctrine, it is clear that other legal acts have less legal force. (The Constitution of the Republic of Latvia; Balodis R., u.c., 2014, 37–38, 196– 199).

Although being the supreme legal act, the Constitution does not directly regulate administrative legal relations; it rather formulates the basic principles for administrative law, establishes the marginal models for the regulation of the most important administrative legal institutes, as well as the whole administrative law system. The specific features of the Constitution are determined by the subject of its regulation, the procedure for its adoption and amending. In case of the collision of laws, constitutional norms play the role of a moderator and have supremacy over all other laws. From this point of view, the real implementation of the principle of the supremacy of the Constitution is accepted in the majority of countries. In Lithuania, this principle is set forth in Article 7 of the Constitution that stipulates that any law or other act that contradicts the Constitution is invalid. The whole Lithuanian and Latvian legal system is developed on the basis of the provisions clearly expressed in the Constitution.

V. Mikelėnas holds to the conception of the sources of law classified in the nowadays widely accepted continental law tradition (Mikelėnas, 1996, 49; Rezevska, 2015, 32). Namely:

- Common principles of law;
- Written (statutory) law (laws, substatutory legal acts);
- Case-law;
- Customs;
- Legal doctrine;
- International law.

## **2. The specific features of the systemic approach to the sources of the administrative law**

Sources of the administrative law started receiving attention of scholars when the development of the French administrative law began. Nowadays, issues regarding both the sources of law and the sources of administrative law are also important as they are related to the at all times relevant conception of law and thence administrative law. The definition of the source of administrative law should be based on the theory of law's 'attitude' towards the source of law in general.

In many countries, the choice of the definition of the sources of administrative law is related to the fact that administrative law is the law of governance. Therefore, democratic and rule-of-law states follow the modern definition of law that determines a wider choice of the sources of law. The normative (statist) model of the sources of law is more suitable for totalitarian and authoritarian regimes, as it allows easier imposition of coercive authority on the majority of people in dealing with issues of state governance.

The Lithuanian and Latvian administrative law is oriented towards the values of a democratic, rule-of-law state. The course of its transformation is marked by the impact of social changes and a shift from normative to modern legal doctrine with a clear perception of the sources of administrative law. These changes were mainly caused by the legal process of the accession to the European Union and the related process of the alignment of the national law with the EU law. The procedural activity of the Constitutional Court of the Republic of Lithuania and Constitutional

Court of the Republic of Latvia (Constitutional Court Law, 1996, 16; Načičionis J., Gintautas D., 2014, 1461–1475) and later of the administrative courts gave a strong impulse to these processes. The Constitutional Court, in its rulings in cases of certain categories having an impact on the establishment of constitutional legal order in the sphere of public governance, was the first to refer to the common principles of law. The application of principles in the constitutional case-law signified the importance of these principles in the system of the sources of law; also, it formed the judicial practice, helped to evaluate the compliance of the primary sources of law – the laws – with the Constitution, highlighted the significance of the legal doctrine with regard to the most important issues of jurisprudence. Therefore, such rulings were based on the multiplicity of the sources of law and a systemic approach to all sources of law.

For example, the Constitutional Court, in its Ruling of 25 May 2004, (Valstybės žinios, 2004, 85–3094) stated that “it is impossible to treat law solely as a text in which expressis verbis certain legal provisions and rules of behaviour. <...> The Constitution as a legal reality is comprised of various provisions, the constitutional norms and the constitutional principles, which are directly consolidated in various formulations of the Constitution or derived from them. Some constitutional principles are entrenched in constitutional norms formulated expressis verbis, others, although not entrenched therein expressis verbis, are reflected in them and are derived from the constitutional norms, as well as from other constitutional principles reflected in these norms, from the entirety of the constitutional legal regulation, from the meaning of the Constitution as the act which consolidates and protects the system of major values of the state community, the civil Nation, and which provides the guidelines for the entire legal system.” (Valstybės žinios, 2004, 85–3094). In the same Ruling, the Constitutional Court emphasised that “the Constitution is an act of the supreme legal force. The source of the Constitution is the national community, the civil Nation, itself”. It is possible to claim that in this Ruling, the hierarchy of the sources of law is clearly identified and the fountainhead of law is emphasised: “the national community, the civil Nation, itself”. On the other hand, the interrelation between the legal consciousness and the legal doctrine is shown from such an interpretative perspective that principles “which are directly consolidated in various formulations of the Constitution or derived from them”. According to the Constitutional Court, the case-law of the European Court of Justice is also a source of law (Konstitucinio Teismo, 2006, 2007; 2008; 2009 ; 2011; The Supreme Court of the Republic of Latvia, 1993, 1,43; Miķelsone G., 2015.). Such legal attitude shows that both the European law and the case-law formed by courts are considered as the sources of law.

### **3. The system of the sources of administrative law**

It has already been emphasised that the sources of law, from the perspective of scientific classification, are understood as a hierarchical system revealing the desired relevant levels of a certain branch of law. Thus one can easily “move” through this system of hierarchical relations and study its separate segments. Furthermore, it is convenient to compare the sources of administrative law to the sources of other branches of law, reveal the specific features of the sources of administrative law, highlight the common and individual features of this object of

law, as well as their interrelation in a single source. Therefore, the significance of the sources of law and their classification are different in every system of law and depend on the purposes of classification. In textbooks, priority is usually given to the arrangement of the interrelations of the sources of law according to the legal power, because thus the arrangement of sources is based on the hierarchical principle. The main classification criterion is the hierarchy of institutions adopting the sources of law, their legal status. For example, according to legal force legal acts are grouped into the Constitution, laws and substatutory legal acts. It is important to mention that the characteristics of the sources of law and administrative law, as well as their classification were and are affected by various factors\*:

- The historical fact of the origination of the sources of law and their change in various legal systems;
- Different legal doctrines in different countries;
- Interrelations between the social legal factors.

If one grouped the sources of administrative law according to the institutes of law, the sources would be classified into groups the legal norms of which regulate the issues of administrative liability, registration, civil service, police activity, etc.

From the general perspective, the sources of administrative law, similarly to other branches of law, can be classified, according to the legal force (the level of hierarchy), into primary (direct) and secondary (indirect).

Primary sources of administrative law contain clearly and explicitly formulated specific rules of behaviour and other normative instructions of high level of abstractiveness (legal principles) or the will of a competitive subject directly expressed in the text of an adopted document (source of law) directed towards the creation, change or abolition of a norm of the administrative law.

Secondary sources of law are derivative results of the interpretation of legal norms.

The dominant primary sources of administrative law are as follows:

- The Constitution of the Republic of Lithuania and The Constitution of the Republic of Latvia;
- Common principles of law;
- Laws of the Republic of Lithuania and laws of the Republic of Latvia;
- Treaty on the European Union and its protocols and amendments;
- International treaties of the Republic of Lithuania and International treaties of the Republic of Latvia;
- Substatutory legal acts.

Secondary (derived from primary sources) sources of administrative law are:

- Acts of the Constitutional Court of the Republic of Lithuania and The Constitutional Court's of the Republic of Latvia judgements (Constitutional Court Law, 1996, 32);
- Acts of the European Union secondary law;
- Doctrine of administrative law.

## 4. The specific features of the primary sources of administrative law

### 4.1. The Constitution of the Republic of Lithuania and the Constitution of the Republic of Latvia

The Lithuanian civil Nation is the source of the Constitution as, expressing its civil will, on 25 October 1992 it adopted by referendum and declared the Constitution of the Republic of Lithuania (The Constitution of the Republic of Lithuania, 1992; Konstitucinio Teismo, 2004, 85–3094). Thus, this Constitution is a legal act of constitutive nature, the source of administrative law of the supreme legal force that at the constitutional hierarchical level, starting from the highest and ending with the lowest level, controls (develops) any other sources of law. It is “the most senior law of a state that creates legal grounds (title) for both the whole established state power (*“pouvoir constitué”*) and all other laws of a state” (Romeris M., 1994, 25).

In this respect, the Constitution performs the function of the highest standard of values not only for the primary national sources of administrative law but also, upon necessity, for the sources of EU and international law. Therefore, the Constitution, by performing the fundamental function of the formation of administrative law, expands the value strategy of its norms and principles to separate normative acts of administrative law, establishes the possible top and bottom lines of the legal regulation, legal protection and liability of separate administrative legal norms.

Thus, the Constitution entrenches the institutional system of state government, the institutions of executive power, their competence, the main principles of the formation and activity of this government, the distribution of the functions performed by the subjects of public administration, the legal grounds for the territorial arrangements of a state, the rudiments of the legitimacy of public administration and the control of this legitimacy. With reference to the far-sighted teaching of a German scientist and judge Fritz Werner, administrative law is to be considered concretised constitutional law (Werner Fritz, 1959, 527–533).

In Lithuania, Egidijus Šileikis was one of the first to follow this opinion. As he states, “the constitutional law, form of the formal approach, can be understood as a system of the Constitution, the laws concretising it and Government resolutions or Presidential decrees provided for in these laws, as well as the Constitutional Court Rulings evaluating the constitutionality of the abovementioned acts.” (Šileikis E., 2002). These ideas can be concretised by the following example. Paragraph 3 of Article 5 of the Constitution stipulates that “state institutions shall serve the people”. This constitutional provision is concretised, at the level of laws, by the Law on Public Administration of the Republic of Lithuania Article 1 (“Purpose of the Law”) of which clearly sets forth: *“this Law shall create the preconditions for the implementation of the provision of the Constitution of the Republic of Lithuania stipulating that all the state institutions serve the people; shall establish the principles of public administration, the spheres of public administration, the system of entities of public administration and the foundations of organising administrative procedures; shall guarantee the right of persons to appeal against the acts or*



*omissions or administrative decisions of entities of public administration as well as the right to statutory and impartial consideration of applications, complaints and statements submitted by persons; shall approve other rights and duties of persons and entities of public administration in the sphere of public administration.*" One of the normative acts concretising this law is the Resolution of the Government of the Republic of Lithuania "On the approval of the description of the grounds for licensing" (Valstybės žinios, 2013, 113–5644). Under the hierarchical level of the sources of law, the Minister of Agriculture approved, by an order, the Description of the Procedure for the Issuing of Licences to Engage in Business Activity of Animal Insemination Centres, Copulation Stations and Embryo Transfer (TAR, 2015, 11251) At the institutional level, the Head of the State Animal Breeding Supervision Service under the Ministry of Agriculture adopted an order "On the usage of the semen of sire pedigree bulls" (Valstybės žinio, 2010, 105–5462).

## 4.2. Laws of the Republic of Lithuania and Republic of Latvia

The Constitution of the Republic of Lithuania establishes the main provisions of administrative legal regulation and legislation on the basis of this Constitution. "A law is an original legal act adopted in the procedure prescribed by the Constitution of the Republic of Lithuania and the Statute of the Seimas which expresses the legislature's will and which has the supreme legal power. <...> a law can be amended or its validity can be nullified only upon the adoption of another law or recognition of it as contradictory to the Constitution by the Constitutional Court". (Lietuvos Respublikos Konstitucinio Teismo, Valstybės žinios, 1994, 7–116; Constitutional Court Law, 1996, 16). At the level of laws, according to the legal power one may distinguish constitutional, ordinary and organic (codification) sub-types of laws.

**Constitutional laws** (not typical for the Republic of Latvia) are understood as laws supplementing the Constitution. They provide grounding for the form of the state, political system, the legal status of individuals, the procedure for establishing the supreme state institutions, the limits of their competence, set the main legal principles. These are normative acts of a narrower legal power in comparison to the Constitution. They regulate a single highly important sphere of the life of a state. Their difference from ordinary laws lies in the procedure for their adoption and amendment that is related to the higher position of constitutional laws in the legal system and the relations of the norms of constitutional laws with the norms of ordinary laws justified on this basis. That is also why they serve as the legal basis for adopting ordinary laws. Under the Constitution of the Republic of Lithuania and the Statute of the Seimas, constitutional laws are "laws which are directly specified in the Constitution as well as other laws which give specific expression to constitutional norms and are set forth in the Law on the List of Constitutional Laws". As stipulated by the Constitution, the Seimas establishes the list of constitutional laws by a 3/5 majority vote of the Members of the Seimas (Article 69). Constitutional laws of the Republic of Lithuania are adopted if more than a half of all the Members of the Seimas vote in favour thereof, and they are altered by not less than a 3/5 majority vote of all the Members of the Seimas (Paragraph 3 of Article 69 of the Constitution). The following laws are included in the list of the constitutional laws of the Republic of Lithuania (Valstybės žinios, 2012, 36–1772):

- Constitutional Law on the State Language of the Republic of Lithuania;
- Constitutional Law on the State Coat of Arms, other Coats of Arms and Armorial Signs of the Republic of Lithuania;
- Constitutional Law on the Lithuanian State Flag and other Flags of the Republic of Lithuania;
- Constitutional Law on the National Anthem of the Republic of Lithuania;
- Constitutional Law on the Referendum of the Republic of Lithuania;
- Constitutional Law on the Approval, Entry into Force and Implementation of the Electoral Code of the Republic of Lithuania;
- Constitutional Law on the Civil Legislative Initiative of the Republic of Lithuania;
- Constitutional Law on Petitioning of the Republic of Lithuania;
- Constitutional Law on the State of Emergency of the Republic of Lithuania.

**Organic (codification) laws** are integral in the juridical sense, internally coordinated laws characterised by a high level of normative generalisation and meant for complex regulation of a certain sphere of social relations. An example of such laws is the Code of Administrative Violations of Law of the Republic of Lithuania (Vyriausybės žinios, 1985, 1–1), since 01-01-2017, the Code of Administrative Offences of the Republic of Lithuania (TAR, 2015, 11216; Latvian Administrative Violations Code, 1985).

**Ordinary laws** (this is common for both republics) are adopted on the basis of the Constitution, constitutional laws and ratified international treaties in order to concretise, develop or implement the legal instructions concisely and explicitly formulated in the abovementioned legal acts, emphasize the need for the protection and implementation of human rights and freedoms. Ordinary laws are necessary such and as many as needed for the implementation of the Constitution and other abovementioned legal acts and the protection of citizens' rights and freedoms.

## 5. Primary European Union law

It is comprised of the founding Treaty and its protocols with amendments (Europos Sąjungos sutarties suvestinė redakcija; Latvia in the European Union, 2016) defining the legal system of the European Union. "A distinguishing feature of EU law is that it can be directly enforceable before the courts of the EU Member States ("direct effect") and that laws of the EU Member States may be held inapplicable when they are in conflict with EU law ("supremacy" of the latter)." (ES teise; ES tiesības)

## 6. International treaties of the Republic of Lithuania and international treaties of the Republic of Latvia

The ratified international treaties of the Republic of Lithuania have the force of law and are a component of the national legal system (Valstybės žinios, 2004, 111–4123; On International Treaties of the Republic of Latvia). Article 11(1) and (2) of

the Law on Treaties (Valstybės žinios, 1999, 60–1948) specifies that the treaties of the Republic of Lithuania that have entered into force are binding in the Republic of Lithuania and that if a ratified treaty of the Republic of Lithuania which has entered into force establishes norms other than those established by the laws, other legal acts of the Republic of Lithuania which are in force at the moment of the conclusion of the treaty or which entered into force after the entry into force of the treaty, the provisions of the treaty of the Republic of Lithuania prevail. Thus ratified treaties, even though being of the same legal status as laws, take priority in respect of laws. *“Currently, the most popular in Europe is the so-called parallel system of the coordination of international and internal law that is based on the rule that international treaties are transformed in the national legal system (incorporated into it). Such method of the <...> realisation of international treaties is established in the Constitution of the Republic of Lithuania.”* (Lietuvos Respublikos Konstitucinis Teismas. 2010: 129.). Therefore, the role of international treaties can be compared to the importance of constitutional laws (Давид П., 1999, 80). According to the provisions of the Law on Treaties of the Republic of Lithuania currently in force, a treaty of the Republic of Lithuania means an international agreement regulated by the principles and norms of international law and concluded between the Republic of Lithuania and foreign states and international organisations in a written form, whatever its particular designation and regardless of whether it is embodied in a single instrument or two or more related instruments (Valstybės žinios, 1999, 60–1948; Latvia in the European Union). Decisions on the expediency of the conclusion of treaties of the Republic of Lithuania are taken by the President, the Government or the Ministry of Foreign Affairs on the instruction of and according to the procedure established by the Government. When taking a decision on the expediency of the conclusion of a treaty of the Republic of Lithuania, the conformity of the provisions of the draft treaty with the Constitution of the Republic of Lithuania, the basic principles and objectives of the foreign policy and national security of the Republic of Lithuania, the requirements of the Law on Treaties, the principles and norms of international law must be considered. For example, the **Convention for the Protection of Human Rights and Fundamental Freedoms** is a constituent part of the legal system of the Republic of Lithuania. The Convention is a source of international law and an act of direct application. With reference to the principle of the superiority of international law over the national law (Article 11(2) of the Law on Treaties, Article 135 of the Constitution), priority should be given to the norms of the Convention, if the rules established by the national law are different to the ones stipulated by the Convention or the norms of the national law are insufficiently explicit and various interpretations are possible (LVAT biuletenis 25: 7 30.).

## 7. Common principles of law

The principles of law that prevail in the legal system and define its nature, content and main specific features are called the *common principles of law*. These principles of law formulate the common aim, sources of the unity of rights and duties and the conditions for its realisation. These principles affect every branch of law and determine how in a certain way the legal norms of a particular branch of law should be revealed and their implementation conducted in order to effectively

reach the specific aims and tasks of legal regulation. The principles of *social justice, humanism, equality, legal certainty, legitimate interests, legal protection, unity of rights and duties, democracy* and others are mentioned most often.

## 8. Specific features of the sources of administrative law

**Secondary administrative legislation.** In comparison with laws, substatutory legal acts have less legal force and significance. Substatutory legal acts are adopted by institutions that do not have the right of lawmaking. Usually these legal acts are adopted by state governance and local self-government institutions. The Constitutional Court of the Republic of Lithuania has asserted that “a substatutory legal act is a legal act adopted by a competent body on the basis of and according to the procedure prescribed by law. A substatutory act is usually an act of administration. The norms of a law are realised by it, however, such an act may not replace the law itself and create new legal rules of general nature that in their power would compete with the norms of the law. It is an act of application of the norms of a law irrespective of the fact whether this act is of one-off (*ad hoc*) or permanent validity” (Valstybės žinios, 1994, 7–116).

Various classifications of substatutory legal acts exist. Most often, the classification is based on the legal force: resolutions of the Seimas, decrees of the President of the Republic of Lithuania, resolutions of the Government, directives and resolutions of the Prime Minister, orders of ministers and department directors, normative legal acts of enterprises and other establishments, resolutions of the Board of the Bank of Lithuania, decisions of Municipal Councils.

**Resolutions of the Seimas.** These are normative legal acts adopted by the Seimas and concretising the constitutional norms established in laws.

**Decrees of the President of the Republic of Lithuania.** The President issues acts-decrees. Under Article 85 of the Constitution and Articles 15 and 16 of the Law on the Office of President of the Republic of Lithuania, the Presidential decrees can be either *countersigned* or *not countersigned*.

Presidential decrees concerning issues of the diplomatic representatives of the Republic of Lithuania to foreign states, the granting of highest military ranks and the declaration of a state of emergency enter into force when signed by the Prime Minister. Presidential decrees concerning the granting of the highest diplomatic ranks and special titles as well as the granting of the Lithuanian citizenship are countersigned by the Minister of Foreign Affairs and the Minister of Interior respectively. Responsibility for such a decree lies with the Prime Minister or the Minister who signs it.

The majority of the decrees of the President of the Republic of Lithuania are individual normative legal acts. However, some Presidential decrees might contain generally binding common rules such as in a decree on the declaration of a state of emergency. As stipulated in Article 144 of the Constitution, in cases of urgency, between sessions of the Seimas, the President has the right to adopt a decision on the state of emergency.

**Resolutions and orders of the Government.** Under Article 95 of the Constitution, the Government of the Republic of Lithuania decides the affairs of state governance

at its sittings by adopting resolutions by a majority vote of all the members of the Government. As stipulated by the Constitution, resolutions of the Government are adopted while deciding the affairs of state governance. Resolutions of the Government are acts of the general, more often than individual, norms of law. Resolutions of the Government are adopted collegially, but they are signed by the Prime Minister and the Minister of the respective area. Directives are signed by the Prime Minister. Resolutions of the Government mainly concretise the procedure for the implementation of laws. Compare with regulations of Article 61 of the Constitution of the Republic of Latvia and Articles 31 and 32 of Law Structure of Cabinet of Ministers (The Constitution of the Republic of Latvia; Structure of Cabinet of Ministers.)

### **Rulings of the Constitutional Court of the Republic of Lithuania**

As established in Paragraphs 1 and 2 of Article 107 of the Constitution, the power of the decisions (rulings) of the Constitutional Court may not be overruled by means of a repeated adoption of laws or other acts by the Seimas, the president of the Republic or the Government. Therefore, under the Constitution, decisions (rulings) of the Constitutional Court are obligatory to everyone. Thus the acts of the Constitutional Court are a source of law (Valstybės žinios, 2003, 53–2361). The same regulation is in Article 32 of the Constitutional Court Law of the Republic of Latvia (Constitutional Court Law).

While discussing the acts of the Constitutional Court as a source of law, the fact of their different legal force and significance must be taken into consideration. According to their form, the acts of the Constitutional Courts can be classified into rulings, decisions and conclusions.

Rulings and conclusions may be interpreted as closing acts as they are issued after the hearing on the merits of a case.

Decisions are usually adopted after certain procedural actions are performed. However, the legal force of a ruling or a conclusion is different as a conclusion is of a recommendatory nature. The final decision in all cases rests with the Seimas.

Rulings are the main type of legal acts issued by the Constitutional Courts. It is issued after the hearing on the merits of a case, i.e. when the question concerning the compliance of a normative legal act of the Seimas with the Constitution or the compliance of a legal act issued by the President of the Government with the Constitution and other laws is decided. The rulings of the Constitutional Court under which laws and resolutions adopted by the Seimas, Presidential decrees, Government resolutions are recognised being in conflict with the Constitution, are the acts of the implementing acts of law.

## 9. Judicial precedent

The Judicial precedent is very urgent source of law. The doctrine of judicial precedent means that judges can refer back to previous decisions to help decide similar cases where the law and facts are alike. Judicial precedent is the source of law where past decisions create law for judges to refer back to for guidance in future cases. Precedent is based upon the principle of *stare decisis et non quieta movere*, more commonly referred to as 'stare decisis', meaning to "stand by decided matters". A binding precedent is where previous decisions must be followed. The very similar opinion is said by Kūris E. (2009: T.2 (116): 139 and very good examples of such understanding we can find in judgements of The Supreme Court of the Republic of Latvia archived as rulings in The Council for Judiciary (The Supreme Court of the Republic of Latvia). For instance, in its Ruling of 28 March 2006, the Constitutional Court of the Republic of Lithuania formulated the doctrine of judicial precedent (Valstybės žinios, 2006, 36–1292). Under this and later Rulings of the Constitutional Court correcting the doctrine of judicial precedent, national courts, when adopting decisions in cases of corresponding categories, are bound by their own created decisions in analogous cases. Here, the principle of judicial decision-making and the hierarchy of judicial institutions are followed. The courts of lower instance, when adopting decisions in the cases of corresponding categories, are bound by the decisions of the courts of higher instance – precedents in the cases of the same categories; the courts of higher instance, while revising decisions of the courts of lower instance, must assess these decisions by always following the same legal criteria; these criteria must be clear and known to the subjects of law, to the courts of general jurisdiction of lower instance. Thus, the jurisprudence of the courts must be predictable (Valstybės žinios, 2006, 36–1292).

In the system of administrative courts, the Supreme Administrative Court develops a uniform case-law of administrative courts in the interpretation and application of laws and other legal acts. (Valstybės žinios, 1994, 46–851).

The precedents of the Court of Justice of the European Union\* are binding on all European Union member states.

## 10. Sources of the EU secondary law

Secondary law is created not by the member states, but by the European Union institutions which have been granted this competence under the founding Treaty and its Annexes. There are three main types of EU legal acts: regulations, directives and decisions. Other sources of secondary law are opinions and recommendations.

A *regulation* (European Union law legal acts lt; European union law legal acts lv) is a binding legal act. It must be applied in its entirety across the EU. For example, when the EU wanted to make sure that there are common safeguards on goods imported from outside the EU, the Council adopted a regulation.

A *directive* is a legal act that sets out a goal that all EU countries must achieve. However, it is up to the individual countries to devise their own laws on how to reach these goals. One example is the *EU consumer rights directive*, which strengthens rights for consumers across the EU, for example by eliminating hidden

charges and costs on the internet, and extending the period under which consumers can withdraw from a sales contract.

*A decision* (European Union law legal acts lt; European Union law legal acts lv) is binding on those to whom it is addressed (for example, an EU country or an individual company) and is directly applicable. For example, the Commission issued a decision on the EU participating in the work of various counter-terrorism organisations. The decision related to these organisations only.

*Recommendations* (European Union law legal acts lt; European union law legal acts lv) are not binding. When the Commission issued a recommendation that the EU countries' law authorities improve their use of videoconferencing to help judicial services work better across borders, this did not have any legal consequences. A recommendation allows the institutions to make their views known and to suggest a line of action without imposing any legal obligation on those to whom it is addressed.

*An opinion* (European Union law legal acts lt; European Union law legal acts lv) is an instrument that allows the institutions to make a statement in a non-binding fashion, in other words without imposing any legal obligation on those to whom it is addressed. An opinion is not binding. It can be issued by the main EU institutions (Commission, Council, Parliament), the Committee of the Regions and the European Economic and Social Committee. While laws are being made, the committees give opinions from their specific regional or economic and social viewpoint. For example, the Committee of the Regions issued an opinion on the clean air policy package for Europe.

## 11. Doctrine of administrative law

The doctrine belongs to a group of legal phenomena marked by constant transformation and the change of its status but also able to vanish away, become invisible in the legal science, case-law, common principles and other sources of law. The term of a "doctrine" may be used to describe such phenomena as legal science and the theory of legal philosophy, opinion of legal scholars on various issues of law-making and the application of law, works by the most famous researchers on the issues of the state and law. For example, a special edition of the collection of scientific articles "Public Security and Public Order" was published celebrating the fifteenth anniversary of the administrative courts of the Republic of Lithuania. The main topic of this edition was "Symbiosis of Administrative Doctrine and Jurisprudence: Ensuring Effective Protection of Human Rights". The authors of the articles published in this journal analysed the topical issues of administrative jurisprudence, reviewed Lithuanian and foreign practice (Administracine doctrine, 2016.). The definition of doctrine presented in the website of this court and Supreme court of Latvia includes works by Lithuanian and Latvian scholars and practitioners on doctrines of law (Bičkovičs I., Strada-Rozenberga K. The Importance of the Latvian Legal Doctrine in Case Law, 2014; Constitutional values in Contemporary Legal Space, 2014), the principles of administrative law, the Convention for the Protection of Human Rights and Fundamental Freedoms, the jurisprudence of the European Court of Human Rights, European Union law, administrative law development, public administration and other spheres of administrative law and procedure.

## Conclusions

The conception of sources of administrative law in Lithuania and Latvia historically developed in a very similar way.

The Constitution of the Republic of Lithuania has regulations on legal sources and their force.

The case law and doctrine of law are still developing and become an instant source of administrative law in Lithuania and Latvia.

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## KOPSAVILKUMS

### **Domino efekts risku un krīžu komunikācijā juridisko aspektu kontekstā**

*Jolanta Derkevica–Pilskunga*

Šī darba mērķis ir izpētīt, kā komunikācija kā biznesa faktors ietekmē risku un krīžu situācijas Latvijas uzņēmumos domino efekta un juridisko aspektu kontekstā.

Šajā darbā ietverti pilotpētījuma rezultāti, kuros izzināti uzņēmumu viedokļi un pieredze Latvijā. Tika iesaistīti 70 mazie uzņēmumi, kuros nodarbināti mazāk nekā 10 darbinieki, kuri sniedza 50 dažādas atbildes. Autore pētījumā izvirza konkrētus jautājumus, izmantojot aptauju metodi. Pētījumā tiek izmantoti gan nestrukturēti, gan strukturēti atbilžu vairanti. Strukturētie jautājumi tiek izmantoti ar jau sagatavotiem atbilžu variantiem. Aizpildītas 93 no 100 aptaujas anketām.

Komunikācijas juridiskie aspekti, kas attiecas uz risku un krīžu vadības procesiem Latvijas organizācijās, iepriekš Latvijā nav pētīti. Risks ir ikdienas dzīves sastāvdaļa. Uzņēmumi var sastapties ar dažāda veida risku un krīžu situācijām. Dažām no tām ir minimāla ietekme, un tās var viegli pārvaldīt, bet ir situācijas, kas var radīt draudus uzņēmuma turpmākai pastāvēšanai ilgtermiņā. Abi no šīm iepriekš minēto situāciju veidiem var izraisīt domino efektu un radīt bažas ieinteresēto personu vidū.

### **Nosacīto noteikto iemaksu vecuma pensiju shēmas pilnveidošana pensiju ilgtspējas nodrošināšanai**

*Ināra Dundure*

Raksta mērķis ir pilnveidot nosacīto noteikto iemaksu (NDC) vecuma pensiju shēmu, lai nodrošinātu vecuma pensiju sistēmas ilgtspēju. Lai sasniegtu šo mērķi, ir definēti šādi zinātniskie izpētes uzdevumi: balstoties uz zinātnisko literatūru, analizēt un raksturot Eiropā un citās valstīs izplatītākās vecuma pensiju sistēmas un shēmas, to veidus un ilgtspējas kritērijus; pilnveidojot NDC vecuma pensijas shēmu, izveidot ilgtspējīgu vecuma pensijas shēmu, kam pamatā Latvijas un starptautiskā NDC vecuma pensiju shēmu pieredze, un izvērtēt, vai izstrādātais vecuma pensiju shēmas modelis nodrošina ilgtspēju.

### **Multikulturālisms globālās migrācijas apstākļos**

*Vladimiras Gražulis*

Mūsdienu pasaulē politiķi, zinātnieki, mediji un daudzu valstu iedzīvotāji izrāda lielu interesi par multikulturālismu. Viens no iemesliem ir pasaules globalizācija un starptautisko migrācijas plūsmu pieaugums. Lietuvā šis temats pētīts reti, un parasti šie pētījumi koncentrējas tikai uz atsevišķām ar multikulturālismu saistītām problēmām. Rakstā aplūkotas ārzemju, lietuviešu zinātnieku un starptautisko organizāciju (UN, UNESCO, utt.) pieejas multikulturālisma fenomenam un tā izpaušmēm mūsdienu sabiedrībā, un analizēti rezultāti 2015. gadā veiktam empīriskam pētījumam ar 1100 dalībniekiem. Pamatojoties uz apkopotajiem datiem, rakstā izvērtētas multikulturālisma attīstības tendences un tam raksturīgie "vājie punkti".

## **Nefinansiālā sociālā atbalsta ģimenēm bērnu dienas aprūpes centros novērtējums: situācijas analīze Lietuvā**

*Vladimiras Gražulis, Janina Čižikienė*

Rakstā apskatītas nefinansiālā sociālā atbalsta sniegšanas īpatnības sociālā riska ģimenēm bērnu dienas aprūpes centros. Pētījumā analizēti nelabvēlīgo ģimeņu un to bērnu sociālā atbalsta sniegšanas aspekti, kā arī iztirzātas nefinansiālā sociālā atbalsta sniegšanas iespējas bērnu dienas aprūpes centros. Raksta mērķis ir noteikt nefinansiālā sociālā atbalsta efektivitāti un tā iespaidu uz sociālā riska ģimenēm un šādu ģimeņu bērniem. Pirmkārt, pētījumā atklāts, ar kādām grūtībām, veicot savus pienākumus, sastopas nefinansiālā sociālā atbalsta sniedzēji un bērnu dienas centru darbinieki un, otrkārt, precizēts, kā bērnu dienas centros sniegtais nefinansiālais sociālais atbalsts palīdz samazināt nelabvēlīgo ģimeņu sociālo atstumtību. Pētījuma rezultāti atklāj arī nefinansiālā atbalsta organizēšanas un uzlabošanas iespējas bērnu dienas centros.

## **Infrastruktūras finansējums dzelzceļa transporta ilgtspējīgai attīstībai Latvijā**

*Māris Jurušs, Līva Landmane, Anastasija Ivanova*

Transporta un uzglabāšanas nozare Latvijā rada aptuveni 10% no valsts IKP, tāpēc tai ir ievērojama ietekme uz ekonomiku. Tranzīta un loģistikas nozarē kopumā ir nodarbināti vairāk nekā 70 tūkstoši cilvēku.

Dzelzceļa nozare katru gadu nodokļos dod vairāk nekā 100 miljonus eiro. Attiecībā uz īpašām precēm un galamērķiem dzelzceļa transports ir ilgtspējīgāks, ekoloģiski un ekonomiski efektīvāks transporta veids salīdzinājumā ar autotransportu, tādēļ tas būtu jāveicina atbilstoši transporta politikas prioritātēm un ES attīstības stratēģijai "Eiropa 2020" – padarīt dzelzceļa pārvadājumus konkurētspējīgākus nekā autotransportu.

Lai palīdzētu īstenot šo stratēģiju, dzelzceļa nozarei ir nepieciešams valsts atbalsts. Alternatīva būtu pārskatīt valsts akcīzes nodokļa politiku degvielai, ko izmanto dzelzceļa transportā. Ieteikums būtu novirzīt ieņēmumus no akcīzes nodokļa par dīzeļdegvielu, ko izmanto dzelzceļa transportā, uz dzelzceļa infrastruktūras uzturēšanas un attīstības finansēšanu.

## **Mazumtirdzniecības nozares darba efektivitātes izvērtējums Baltijas valstīs**

*Iveta Liniņa*

Mazumtirdzniecības nozare (NACE, G47) ieņem nozīmīgu vietu jebkuras valsts tautsaimniecībā. Mazumtirdzniecības uzņēmumiem, kā jebkuriem uzņēmumiem, darbības pamatā ir peļņas gūšana, apmierinot patērētāju vajadzības. Lai sasniegtu šo mērķi un nodrošinātu konkurētspēju, mazumtirdzniecības uzņēmumiem nepieciešams veikt savu darbību pēc iespējams efektīvāk, tas ir, rezultātus sasniegt ar mazākiem ieguldījumiem. Šī pētījuma mērķis ir salīdzināt mazumtirdzniecības darbības efektivitātes rādītājus visās trijās Baltijas valstīs un noskaidrot to uzlabošanas virzienus.

## Intelektuālais kapitāls kā Ukrainas ekonomiskās attīstības faktors

*Olga Maslak, Natalya Grishko, Olha Hlazunova, Maria Maslak*

Raksta mērķis ir pētīt intelektuālo kapitālu kā nozīmīgu faktoru inovatīvas nacionālās ekonomikas attīstības modeļa ieviešanā.

Daudzi zinātnieki jau ir pētījuši šo tematu, tomēr, ņemot vērā tā aktualitāti un plašumu, ir nepieciešams tā izpēti turpināt. Jautājumi par intelektuālā kapitāla efektīvu realizāciju konkurences uzlabošanai un nacionālās ekonomikas attīstībai kļūst īpaši aktuāli attiecībā uz integrācijas procesu intensifikāciju.

Lai sasniegtu šo mērķi, pētījumā tika izmantotas empīriskās un fundamentālās zinātniskās pētniecības metodes, tostarp analīze un sintēze, indukcijas un dedukcijas metodes, salīdzināšanas metode un grafiskā metode.

Ir definēta cilvēkkapitāla nozīmīgā loma kā augstas veiktspējas spēks modernajā sabiedrībā un daudzsoļīgākā komponente konkurētspējas un ekonomiskās attīstības uzlabošanā. Rakstā analizētas Ukrainas pozīcijas pasaules reitingos pēc dažādiem cilvēkkapitāla ieviešanas kritērijiem. Ir noteiktas galvenās tendences augstākās izglītības attīstībā, augsti kvalificēta personāla apmācībā un izglītības virzienu finansēšanā. Rakstā izpētītas zinātniskās un tehniskās darbības iezīmes, kā arī darbaspēka un finanšu resursu pieejamības līmenis.

Lai attīstītu un uzlabotu intelektuālā kapitāla realizācijas efektivitāti kā ekonomiskās krīzes efektu samazināšanas un Ukrainas nākotnes attīstības paātrināšanas faktoru, nepieciešams stiprināt inovācijas un ieguldījumu aktivitātes, piesaistīt ārzemju un publiskās investīcijas intelektuālā kapitāla formēšanas un attīstības procesiem, risināt zinātniskās un tehniskās darbības finansēšanas optimizācijas radītās problēmas, paaugstināt sociālās aizsardzības līmeni valstī, izveidot stabilu regulācijas sistēmu inovāciju un investīciju atbalstam.

## Starpkulturālās kompetences multikulturālās organizācijās

*Ivars Namatēvs, Viktors Turlais, Lotārs Dubkēvičs*

Raksta mērķis bija novērtēt starpkultūru kompetences līmeni divām subkultūrām – speciālistiem un vadītājiem, kas strādā organizācijās ar multikulturālu vidi. Lai noteiktu starpkultūru kompetences līmeni, tiek piedāvāts izmantot jaunu tās izvērtējuma modeli, kas izveidots, balstoties uz Hofstede G. (*Hofstede G.*), Čena un Nakvina (*Chen and Naquin*), Vara (*Warr*) kompetences teorijām. Rakstā aprakstītais ir daļa no plašāka starptautiska pētījuma, kas tika realizēts dažās Eiropas valstīs. Iegūtie rezultāti parāda, kā speciālisti un vadītāji, kas strādā Latvijas uzņēmumos, novērtē tās pašas organizācijas kolēģus Lietuvā, Igaunijā un Somijā. Kā galvenā datu vākšanas metode tika izmantota tiešsaistes aptaujas anketas, kuras aizpildīja paši respondenti. Pētījums atklāja, ka savstarpējās prakses apmaiņas braucieni un biznesa ceļojumi ir tas veids, kā organizāciju speciālisti un vadītāji palielina savu starpkultūru kompetences līmeni. Lai veicinātu ticamu un validu starpkultūru līmeņa novērtējumu, raksta autori piedāvā salīdzināt un izvērtēt vairākus starpkultūru modeļus, tādējādi izveidojot organizācijas starpkultūru kompetenču sistēmu.

## Inovācijas publiskajos iepirkumos

*Una Skrastiņa, Džeina Gaile*

Inovācijas nozīme mūsu ekonomikā turpina pieaugt, tā paātrina un uzlabo jaunu produktu, rūpniecisko procesu un pakalpojumu koncepciju rašanos, izstrādi, ražošanu un izmantošanu. Lai gan termins “inovācija” gan teorijā, gan praksē ir kļuvis īpaši populārs pēdējā desmitgadē, nav pārliecības, ka tas ir saprotams un skaidrs visiem, kas iesaistīti publiskajā iepirkumā. Pētījuma mērķis ir analizēt, kāds ir inovāciju regulējums un iespējamā praktiskā nozīme, to izmantošana un veidi, kā tās tiek iekļautas publiskajos iepirkumos. Mērķis ir palīdzēt praktiķiem saprast, kā labāk īstenot inovācijas. Jaunās iespējas būs pieejams ar jauno *Publiskā iepirkuma likumu*, iepirkuma procedūru – inovāciju partnerība. Lai sasniegtu šo mērķi, tiks analizēti tiesību akti, politiskās plānošanas dokumenti, tiesību zinātnieku viedokļi, lai rezultātā konstatētu problēmas un piedāvātu esošo problēmu risinājumu. Pētījuma veikšanai tiks izmantota deskriptīvā, salīdzinošā un analītiskā zinātniski pētnieciskā metode. Pētījuma rezultātā varēs gūt priekšstatu par inovāciju ciešo saistību ar publiskajiem iepirkumiem. Lai gan jau pastāv iespējas inovāciju veicināšanai, izmantojot variantus vai funkcionālās prasības tehniskajās specifikācijās, gan esošās, gan jaunās iespējas prasa vēlmi tās izmantot, kā arī dziļas zināšanas par juridiskajiem un tehniskajiem aspektiem, jo, kad pasūtītāji nolemj izmantot šīs iespējas, iepirkumi kļūst daudz sarežģītāki. Ņemot vērā minēto, ir vajadzīga ne tikai jauna direktīva un likuma regulējums, bet vēl svarīgāka ir skaidra izpratne un praktiskās zināšanas, kas ir nepieciešamas, lai īstenotu šos rīkus publiskajā iepirkumā.

## Administratīvo tiesību avoti Lietuvā un Latvijā

*Algimantas Urmonas, Jānis Načisčionis*

Raksta mērķis ir vēsturiskā skatījumā parādīt tiesību doktrīnas par administratīvo tiesību avotu attīstību divās Baltijas valstīs – Lietuvā un Latvijā. Autori analizē viedokļus par administratīvo tiesību avotiem un to tiesisko regulējumu Romā, Francijā, Lietuvā un Latvijā. Dotais pētījums ir nozīmīgs pienesums administratīvo tiesību teorijas pilnveidei un praktisks devums administratīvo tiesību avotu piemērotājiem ikdienas praktiskajā rīcībā. Autori piedāvā skatījumu uz kopīgo, kas ir administratīvo tiesību avotiem Eiropas Savienības telpā, un atšķirīgo, kas konstitucionāli tiesiskajā regulējumā Lietuvā un Latvijā, parādot, ka atšķirībā no Lietuvas Konstitūcijas 7. panta, kas nosaka tiesību avotu hierarhiju, Latvijas Republikas Konstitūcijā nav regulējuma par tiesību avotiem un to juridisko spēku. Rakstā ir izteikta doma, ka arī Latvijas Republikas Satversmē būtu jābūt konstitucionāli tiesiskajam regulējumam par tiesību avotiem.

Journal of Turība University  
**Acta Prosperitatis Nr. 7**

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CONTENT

THE DOMINO EFFECT IN RISK AND CRISIS COMMUNICATION IN THE CONTEXT OF ITS LEGAL ASPECTS

*Derkevica-Pilskunga Jolanta*

IMPROVEMENT OF NOTIONAL DEFINED CONTRIBUTIONS OLD-AGE PENSION SCHEME FOR ENSURING PENSION SUSTAINABILITY

*Dundure Ināra*

MULTICULTURALISM IN THE WORLDWIDE MIGRATION CONDITIONS

*Gražulis Vladimiras*

EVALUATION OF NON-FINANCIAL SOCIAL ASSISTANCE TO FAMILIES IN CHILD DAY CARE CENTERS: SITUATION ANALYSIS IN LITHUANIA

*Gražulis Vladimiras, Čižikienė Janina*

INFRASTRUCTURE FUNDING FOR SUSTAINABLE DEVELOPMENT OF RAILWAY TRANSPORT IN LATVIA

*Jurušs Māris, Landmane Līva, Ivanova Anastasija*

COMPARISON OF THE RETAIL EFFICIENCY INDICATORS IN THE BALTIC STATES

*Liniņa Iveta*

INTELLECTUAL CAPITAL AS A FACTOR OF ECONOMIC DEVELOPMENT OF UKRAINE

*Maslak Olga, Grishko Natalya, Hlazunova Olha, Maslak Maria*

INTERCULTURAL COMPETENCE IN MULTICULTURAL ORGANIZATIONS

*Namatēvs Ivars, Turlais Viktors, Dubkēvičs Lotārs*

INNOVATIONS IN PUBLIC PROCUREMENT

*Skrastiņa Una, Gaile Džeina*

SOURCES OF ADMINISTRATIVE LAW IN LITHUANIA AND LATVIA

*Urmonas Algimantas, Načisčionis Jānis*

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ISSN 1691-6077

**Publishing house of Turība University**

Telephone: +371 67623521

Address: 68 Graudu Street, Riga, LV 1058

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