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FOREIGN MODELS AND POLICIES FOR STATE-OWNED ENTERPRISES

The article presents and analyzes various foreign models and policies for state-owned enterprises. The models of management of state-owned enterprises, the need for their existence and the types of state-owned enterprises are considered successively. The results of the article outline a wide range of national policies for state-owned enterprises. The main factors for their determination are a consequence of the historical development and the social commitments made for economic reforms. The existence of social goals of state ownership creates serious differences between corporate governance in the public and private sectors. The increased complexity in the management of state-owned enterprises stems from the combination of social and economic goals.

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State-owned enterprises are not a new phenomenon, but they have never attracted as much attention as they do today (Wang and Gallagher, 2016). The effects of the global financial crisis have boosted the expectations for transparency of the corporate governance of state-owned enterprises (Daiser et al., 2017). The increase in public debt added a new function to the activity of state-owned enterprises – achieving financial results in parallel with the supply of public goods (Grossi et al., 2015).

Since their establishment, state-owned enterprises have had the role of maximizing social welfare rather than profit (Aharoni, 1981). Therefore, in order to constitute a state-owned enterprise, it is necessary to define the social goals that it must pursue, as well as the ways in which the behavior of the enterprise must be determined and its performance assessed. Taken together, these specifics of state-owned enterprises determine their traditionally weaker financial results compared to those within the private sector (Sokol, 2009). Furthermore, in most cases the principal, i.e. the government, may have competitive goals that the management of the state-owned enterprise must achieve. As result of this dichotomy, it is difficult to supervise the functioning and results of state-owned enterprises.

The corporate governance of state-owned enterprises is a major challenge for any government (Daiser et al., 2017). The government must exercise its function of an owner without political interference in the management of the enterprise. In addition, the outcome of the corporate governance is determined by a multitude of goals that are sometimes conflicting and compete with one another. The functions of the state as a shareholder and as a regulator are a reflection of the specifics of the corporate governance of state-owned enterprises in order to achieve a balance between increasing the welfare of the principal and the stakeholders (Chen, 2016).

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Models of management of state-owned enterprises

The institutional framework for the corporate governance of state-owned enterprises refers to the ways in which power relations between state authorities and enterprises are organized. Based on practice, three main models of such relationships have been outlined in the literature: a decentralized or sectoral model, a dual model, and a centralized model (Vagliasindi, 2008).

In the case of the decentralized model, state-owned enterprises are dispersed among the different authorities and their respective line ministries oversee them. In the dual model, state-owned enterprises are under the shared governance of a line ministry and another central ministry, most often the Ministry of Finance. The centralized model is characterized by a concentration of responsibilities for managing state participation in the hands of a single ministry.

The decentralized or sectoral model is the most common form of organizing institutional relations with state-owned enterprises. This model was widely used in Eastern European countries, such as the Czech Republic, Hungary, Lithuania and Poland, before their transition to a market economy and is prevalent in the developing countries in many regions. Of the developed economies, Finland, where nine line ministries exercise ownership rights over more than 50 state-owned enterprises, is an example of such a model of governance.

Under this model, it is possible for a line ministry to have a coordinating role, by being responsible for the development of a comprehensive policy for state participation in all sectors. A different practice exists in Lithuania, where a specialized coordination unit for state-owned enterprises was established in 2012 (OECD, 2018a). It is tasked with monitoring and reporting on compliance with disclosure standards and preparing an annual report on the activities and performance of state-owned enterprises. Another part of the unit’s mission is to methodically support the strategic development of state-owned enterprises, as well as their corporate governance. The unit is part of the Monitoring and Forecasting Agency, which reports to the Ministry of Economy.

The biggest advantage of the decentralized model is the expertise in the respective sector. Its main weaknesses are related to the combination of the ownership function with the regulatory role, the risks of interference of state institutions in the daily operational functions of enterprises and the multidirectional and often diverse practice of managing state participation in enterprise ownership.

The dual model is widespread in many countries such as Greece, Italy, Mexico, New Zealand, South Korea, Turkey and others. In this model, the exercise of ownership rights is performed simultaneously by the sectoral and functional ministries. Most often, the role of a functional ministry is performed by the Ministry of Finance. It is common practice for both responsible ministries to have the right to nominate their representatives to the boards. This is the case in Mexico, where representatives of both the Ministry of Finance and the line ministries or agencies are present on the board of state-owned companies. The shared responsibilities often include the joint approval of major deals and strategic projects. In New Zealand, the shared responsibility is directly reflected in the distribution of capital of the state-owned enterprises, which is divided equally between the line ministry and the Ministry of Finance.

The Minister of Finance is often directly responsible for certain specific ownership functions, such as the nomination of board members and the reporting and financial control of state-owned enterprises. These specific functions can be performed in coordination or in consultation with the relevant line ministries.

The advantages of the dual model lie in the combination of the sectoral with the financial expertise. Its main shortcomings are the problems of the coordination between the various state institutions, which, especially in developing countries.

The centralized model is often developed in countries where privatization programs have recently been completed. In this model, most state-owned enterprises are under the control of a single ministry or agency. Most often it is the Ministry of Finance (Denmark, the Netherlands, Spain) or the Ministry of Industry (Norway and Sweden), which is responsible for the largest state-owned enterprises as a line ministry. In Belgium, there is a special ministry – the Ministry of State-Owned Enterprises and Participation. In several cases, a specific autonomous agency has been established and this agency usually reports to a ministry. This is the situation in France, where the Agence des participations de l'État reports to the Ministry of the Economy and Finance. The strengths of the centralized model are the unified procedures, rules, databases and methodology for managing the participation in the equity of state-owned enterprises, the ability of the government to exercise strict fiscal supervision and form a coherent policy for these enterprises, as well as the possibility to specialize in this function by the state administration. The main disadvantage of this model is the lack of sectoral expertise and direct links with company management.

The OECD Guidelines on Corporate Governance of State-Owned Enterprises (OECD, 2015a) recommend applying the centralized model using a specialized agency. Section II, titled "The state's role as an owner", clearly defines that:

- The exercise of ownership rights must be clearly identified in the state administration. It should be centralized in a single ownership principal or, if this is not possible, by a coordinating authority. This "principal of ownership" should have the capacity and competence to carry out its duties effectively.
- The principal of ownership should be accountable to the relevant representative authorites and have a clearly defined relationship with the relevant public authorities, including the supreme state audit institutions.

The holding structure, which is similar to the centralized model, was used more widely in the past to manage state participation. In a holding structure, the ownership rights of the enterprises are transferred to specially established state holdings. These holdings usually have a sectoral or cross-sectoral specialization and are subordinated to the relevant line ministry.

Such holding structures were formed in the 1970s with the idea of reducing political interference in the management of state-owned enterprises, creating more flexibility in their management and introducing stricter budgetary constraints. In Italy, the holding company Istituto per la Ricostruzione Industriale (IRI) was also established to support the development of the southern part of the country and to rehabilitate companies that were experiencing difficulties (Amatori et al., 2011).

Currently, such holding structures are often used to consolidate state participation in the capital of enterprises in the infrastructure or mining sectors. In Poland, such an example is Polska Grupa Górnicza, which is a large holding company that unites many coal mines in the country (Wasowska and Postula, 2018).

However, the holding structure has failed to demonstrate its effectiveness, in terms of both corporate restructuring and financial management, as well as regional development in the Italian case. Therefore, it is gradually being abandoned, or if it still exists, its scale is very limited.

An exception to this trend is Austria, where there is a powerful state-owned holding company, Österreichischen Industrieholding Aktiengesellschaft (ÖIAG), which manages the participation in the equity of a significant number of state-owned enterprises and at the same time is responsible for their privatization. In this way, one of the main advantages of the holding model is used – namely, that it can serve for the implementation of a national program for privatization and for the restructuring of state-owned enterprises. Its main drawback is that it does not in itself solve the problems of the poor corporate governance of state-owned enterprises. Instead, it simply raises the issues of corporate governance to a higher level, such as the holding company, which, however, does not solve the problem of choosing a suitable institutional set-up for corporate governance.

The trend observed in recent years in the institutional set-up of corporate governance of state-owned enterprises is to move towards greater centralization of the state participation in the equity of enterprises. The reasons for this are the shrinking portfolio of state-owned enterprises and the desire to list them on stock exchanges. The transition from one model to another is not always one-way. In Poland, for example, the management of state-owned enterprises was centralized under the Ministry of the Treasury, however, after it was closed in 2017 this function was taken over by the line ministries (Gliniecki and Zaleska-Korziuk, 2017).

Rationales behind the need for and the objectives of state-owned enterprises

Statehood is born from the transition from private to state ownership and in particular – from the establishment of the institutions for the regulation and control of ownership. In the era of the Industrial Revolution, a scientific direction was introduced in order to compare the advantages and disadvantages between private and state ownership when building new infrastructure and in the mass consumption of services such as drinking water, gas, transport, communications, telegraph and railways (Sánchez, 2016). The model of the state as an entrepreneur for the production of public goods and conducting social policy (Megginson, 2005) formed the so-called “golden age” of state-owned enterprises – 1945-1980 (Millward, 2011), during which state ownership was used as a regulatory instrument in the public interest. State ownership was beginning to be seen as a means of tackling market failures and establishing a monopoly in strategic sectors of the economy (Shirley and Walsh, 2001). Since the 1990s, the efficiency of state ownership has been put into question and the process of the privatization of inefficient state-owned enterprises has begun (MacCarthaigh, 2011).

There is currently no generally accepted definition of the nature of state ownership (European Commission, 2016). Each country adopts its own definition for state ownership depending on its benefits for the specific economic sector and time period. Regardless of the variety of definitions, it can be summarized that in the case of state ownership there is a mandatory presence of a social goal and that in some cases it is combined with a financial goal:

- Finland: the state strives to achieve the best possible economic and social result.
- France: to contribute to the better valorisation of state-owned shares in state-owned enterprises.
- Hungary: state ownership is an alternative to over-regulation, and strives to ensure sufficient investment in some sectors (Christiansen, 2013).
- Israel: providing activities where there is no alternative for the private sector.
- Latvia: the state may establish and may continue to own a commercial enterprise in the presence of a market failure in sectors where there is a natural monopoly; in strategically important sectors; in sectors that require large capital investments in order to develop; and / or in sectors where higher quality standards must be met in order to protect the public interest (OECD, 2015b).
- The Netherlands: structural change in network industries and elimination of market failures.
- New Zealand: preparing for the privatization or efficient delivery of public services in which state-owned enterprises to be "as profitable and efficient as comparable non state-owned enterprises" (World Bank, 2014).
- Norway: the purpose of state ownership is to participate in the common good.
- Sweden: The government's overall goal is to create value for owners (OECD, 2007).
- UK: to ensure that government shares provide a sustainable, positive return and return on capital expenditure over time within the political, regulatory and customer parameters set by the government, acting as an efficient and intelligent shareholder.

There is a rich set of rationales for the existence of state ownership in the specialized literature, the most important of which are, as follows (Advisory Council for Science Technology and Innovation, 2010):

- Natural monopoly. In certain sectors of the economy, due to technical requirements or the achievement of economies of scale, it is justified to have only one supplier – for example for the construction of railway infrastructure, water supply and electricity distribution. In order to prevent abuses of the monopoly and price increases, and as a means for achieving high quality, it is appropriate to establish a state-owned enterprise. The alternative of setting up a private enterprise involves high costs of supervision and regulation.

• Investment risk. In certain sectors of the economy, there is a weak investor interest from the private sector given the long period of investment and the corresponding increased risk. In such cases, it is advisable to establish a state development bank in order to finance risky long-term ventures.

• Spill-over effects. Private sector investors have no incentive to invest in sectors that benefit other industries and the economy as a whole without being paid for the effects of the investment. For example, when offering public goods such as education and research, free-rider behavior and the need for state intervention are often observed.

• Equity. In certain sectors of the economy, equity is required, which is a barrier for certain geographical areas and social strata. State involvement is needed to reduce disparities in regional development, such as building a broadband Internet connection for sparsely populated regions, as well as in regions with lower incomes.

Table 1

State policy for participation in ownership

Country	Ownership policy	Financial supervision	Board of a state-owned enterprise
Czech Republic	•Social, strategic and community-based goals •The role of ownership is transferred from the Privatization Agency to the Ministry of Finance, while the line ministries maintain operational control	•Financial results controlled by the Ministry of Finance	•Adoption of principles for remuneration structures •New mechanisms for transparency and accountability •Nominations require professional qualifications •Evaluation by external audit of the board's results
Croatia	•Definition of strategic state-owned enterprises and state-owned enterprises for privatization •Decentralized ownership •Privatization has progressed at a slow pace and has partially failed	•Attempts to strengthen the monitoring framework •Limited supervision, without medium-term performance indicators	•A new selection framework for improving qualifications and providing candidates from the private sector •Even external recruitment companies are not completely independent
Estonia	•Objectives: public purpose and revenue generation •Ownership and regulation functions are separated, there is no official ownership policy document	•Coordination Department of the Ministry of Finance for monitoring the financial statements and publishing a consolidated annual report •Internal audit operates only outside a certain size	•Direct instructions from ministers to directors of public administration have been revoked •Board members are equally from the private and public sectors
Hungary	•The State Assets Act regulates the management of state-owned enterprises •Objectives: long-term management, value creation •State holding company subordinated to the Ministry of Development, but also to other government authorities	•An interdepartmental council has been set up to control holding companies and the management of state-owned enterprises	•Qualification requirements for supervisory boards •Public and independent representatives, but without explicit political preferences •Minimum wage restrictions
Latvia	•New law on state-owned enterprises •Rationale for ownership: market failures, natural monopoly, strategic sectors •Decrease in the initial ambition for a central holding structure	•Coordinating institution for the monitoring and evaluation of the performance of state-owned enterprises on the basis of return criteria •Municipal enterprises are not included	•Introduction of boards with appropriate professional experience •The nomination / appointment process is unclear •Remuneration regulations set by the cabinet
Lithuania	•Ownership guidelines: profit maximization, strategic interest, social goals •Specific responsibilities of state-owned entities •Separation of ownership and policy functions •Unsuccessful establishment of a holding company	•Objectives for implementation based on return on equity •Established monitoring mechanism •Dividend policy set out in the company's articles of association •Coordination department in the State Ownership Fund	•Criteria for appointment •Database of potential board members •At least 1/3 of the board members to be independent •Autonomy needs to be improved
Poland	•Legislation to separate ownership from regulation and promote value creation and competition, while maintaining state control in strategic cases •Several cases of privatization, but with limited change of control; a new impetus to increase the role of state-owned enterprises	•Supervision delegated by the office of the Prime Minister to the line ministries •Dividends set in relation to profitability ratios and liquidity ratios	•Opportunity for open competition and recruitment of consultants •The appointment is subject to an opinion by a special council in the prime minister's office
Slovenia	•Separation of ownership and policy functions •Consolidation of ownership and management by a holding company •Long-term strategy for government assets and sales classification	•Overall profitability target: 8% return on equity by 2020 •Individual performance indicators of each state-owned enterprise •Dividend policy: annual payment of at least 1/3 of the net profit	•Improved transparency of rewards and bonuses •Commitment to assess the performance of the management of a state-owned enterprise based on objective criteria

Source. Böwer, 2017.

In most cases, the state policy for participation in ownership in Eastern Europe reflects the results of privatization (see Table 1).

Types of state-owned enterprises

The term “state-owned enterprise” became modern in the 1990s. Government plans to rescue national companies from the beginning of the 21st century have led to a “Renaissance” of state-owned enterprises (OECD, 2009), which has also led to the need for a clear definition of the concept.

Despite the large number of studies on state-owned enterprises, a uniform definition has not been reached (Krause, 2013). Most research on the management of state-owned enterprises has been conducted through qualitative approaches (cases) for a given sector of the economy and there is no quantitative overview of the policies of individual countries (Sokol, 2009). Each country uses its own definition, which further complicates the formulation of a consensus on the content of the concept of “state-owned enterprise” and the conducting of a comparative analysis between countries (Kowalski et al., 2013).

The conceptual issues of the definition of a “state-owned enterprise” are deceptively easy (Backer, 2017). The definitions differ primarily in terms of the objectives of the supervision, i.e. in distinguishing one ownership structure from another in the application of legal requirements. The dynamics in the definitions of a “state-owned enterprise” reflect the transition to the new reality:

- 1995: state-owned or state-controlled economic entities that generate most of their revenue from the sale of goods and services (World Bank, 1995).
- 2005: an enterprise in which the state has significant control through full, majority or significant minority participation (OECD, 2005).
- 2015: any legal entity recognized by national law as an enterprise in which the state exercises ownership (OECD, 2015a).

Since 2015, the scope of state-owned enterprises has been expanded to include both joint-stock companies and limited liability companies. State-owned enterprises also include legal entities constituted by special laws, so long as their purpose and activities or parts of their activities are largely of an economic nature.

The literature on state-owned enterprises describes them as “special” due to the uniqueness of the stakeholders, the strong political influence, and the many goals for the implementation of state-owned enterprises (Wasowska and Postula, 2018). The specifics of state-owned enterprises are, as follows:

- The creation of state-owned enterprises may be related to the need to address certain market failures (World Bank, 2012). As the very origin and existence of state-owned enterprises differs from those of private enterprises, different corporate governance practices should be used, rather than simply copying them from the private sector.
- The government combines the roles of shareholder, regulator and guarantor (OECD, 2010).

●State-owned enterprises provide a public good, the quality of which is difficult to determine in the management contract and in measuring their effectiveness (Sokol, 2009). Given the social objectives of state-owned enterprises, their performance cannot be assessed using only financial indicators, such as the ones applicable in the private sector (Putniņš, 2015).

●In maximizing public welfare, state-owned enterprises simultaneously pursue multiple goals (Kim et al., 2019). This characteristic makes it difficult to assess both economic efficiency and social efficiency.

According to the OECD, the benefits of state-owned enterprises are (OECD, 2018b):

●Political – the redistribution of power in society in order to achieve a balance between the private and the public sector (Toninelli, 2008).

●Social – guarantee of full employment. Applies to economic crises and policies for the recovery of the national economy (France and Italy).

●Economic – creating a strong public sector in order to deal with market failures. Another benefit is the guarantee of high quality and affordable prices (in the supply of electricity for example), which reduces the need for a sectoral regulator. The exploitation of natural resources as a natural monopoly by state-owned enterprises in the Netherlands and Norway or the stimulation of economic development through accessible infrastructure as illustrated by the highway system in Germany and the railway sector in the United States are all good examples of this (Sánchez, 2016).

In terms of the main shortcomings that must be overcome, the following recommendations are made for improving the activity of state-owned enterprises:

●clarifying the objectives of state-owned enterprises – Estonia (Klovienea et al., 2015).

●a clear separation of the functions of the state as a shareholder from any other function that may affect the activities of state-owned enterprises, especially the market regulation function – Estonia (Klovienea et al., 2015), Colombia (Lehuedé, 2014), and Serbia (Mirić et al., 2018).

●definition of the policy and rationales for state ownership, which in most cases are fixed in the statutes of state-owned enterprises themselves – Argentina (OECD, 2018c), Colombia (OECD, 2015c), and Latvia (OECD, 2015b).

●restricting and eliminating of non-transparent procedures for the nomination of board members – Poland (Gliniecki and Zaleska-Korziuk, 2017).

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The immanent goal of the state for intervention in ownership is to correct market failures, as well as to provide affordable and controlled prices and quantities of certain services considered essential for the population or business.

Views on state ownership and state-owned enterprises exists within a certain historical context. The dynamics in them reflects the development of society and the economy. The existence of social goals of state ownership creates differences between corporate governance in the public and private sectors. Despite the attempts to unify the practices in the two sectors, the existence of more than one goal behind state ownership, and especially the social one, is the reason behind the greater complexity in the management of the public sector.

In a synthesized form, the institutional framework used for the corporate governance of state-owned enterprises exists in three main forms: the decentralized, dual and centralized models.

The decentralized model is the most widely used one. It makes it possible for a line ministry to have a coordinating role and be responsible for developing a comprehensive policy for state participation in the economy. Another existing practice is the use of a specialized coordination unit for state-owned enterprises in the system of the state administration.

In the dual model, the management functions of state-owned enterprises are shared between the line and functional ministries. Most often, the functional ministry is the Ministry of Finance, which takes more responsibility in the methodological guidance, accountability and control over these enterprises.

The trend observed in recent years and recommended by the OECD is to use the centralized model. The reasons for this are the shrinking portfolio of state-owned enterprises and the desire to list them on stock exchanges. The advantages of this model are the same procedures, rules, databases and methodology for managing participation in the equity of state-owned enterprises, the government's ability to exercise strict fiscal supervision and to form a coherent policy for these enterprises, as well as the possibility to specialize in the development of this function of the state.

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