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CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES IN CENTRAL AND EASTERN EUROPE

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The international conference focusing on the subject of "Corporate Governance of State-Owned Enterprises in CEE" was organized by the Central and Eastern European Company Law Research Network at the National University of Public Service (14 October 2016).

The so-called state-owned enterprises (hereinafter: SOEs) serve a special function in economic life and in politics alike. Therefore it is recommended to set up unified and stricter regulations compared to general rules relating to SOEs. However, these enterprises are far from homogeneous. Some of them have a monopoly in certain areas, whereas others operate under actual free market conditions. Some of them are functioning as for profit organisations whereas the others can be evaluated as non-profit enterprises.

Nevertheless, these enterprises are of strategic importance for the state, regardless of the differences within their unified legal status. It is no coincidence that the OECD Guidelines on Corporate Governance for SOEs issued in 2005 have been revised in 2015. These Guidelines contain "recommendations to governments on how to ensure that SOEs operate efficiently, transparently and in an accountable manner". Perhaps one of the most important of these Guidelines is "the state's role as an owner".

The participants of the conference comprehensively elaborated on the issue of regulating SOEs. The relationship between the OECD Guidelines and national law, the legal status and legal forms of these enterprises, the centralisation of ownership rights and the management of SOEs has been analysed in detail, furthermore, several studies have addressed the specific legal and economic status of shareholder as well.

Experts of seven countries have presented different approaches and introduced different regulatory frameworks. All presentations, however, highlighted the importance of SOEs and pointed out their special features in the Central European Countries. Regarding the role of the state, the experts emphasized that it is necessary to find the right proportion in using the elements of private and public law, or in other words, in placing SOEs between the free market and politics.

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Foreword

The following contributions result from a conference held in October 2016 at the National University of Public Service in Budapest, which was organized by Societas,[1] an academic network of CEE company law scholars. The conference's subjects were company law aspects of state owned enterprises (SOEs), an issue of paramount importance as the state very often – and especially in CEE countries – owns significant holdings or even all shares in core industries; therefore, inefficiencies can have major fiscal and economic impacts.

Consequently, the OECD in 2005 issued Guidelines on Corporate Governance for SOEs, which have been revised in 2015. The Guidelines assume that SOEs can be operated as efficiently as private firms and aim at providing a high bar for good corporate practice in this context. They put special emphasis on the creation of a rules-based environment on the equitable treatment of (outside) shareholders, on encompassing transparency and disclosure, and on the freedom of boards from political interference. An introduction is not the correct place to delve into all of these issues; a few words on the last subject must suffice.

The Guidelines recognize that it is for the state as the owner to set the strategic objectives for the SOE; this is in line with the public interest in the SOE's functions. However, according to the Guidelines setting the objectives must be distinguished from interference in operational issues; for the latter SOEs should have full autonomy. Supposedly, operational autonomy is a pre-condition for the efficiency to be attained. Let me make three remarks on this issue.

First, political influence on operational decision-making is hard to detect in the first place, as it generally is not public knowledge. To mitigate this problem, the Principles try to increase transparency by mandating disclosure of the areas in which instructions will be given. Provisions in the articles and the by-laws for various management bodies of the SOE help to achieve this aim. However, it would be naïve to believe that political influence necessarily or even regularly makes use of legal tools; very often it subtly works via pressure on managers (e.g. the threat of losing the job) or hidden incentives (e.g. the possibility of another, more attractive position). In this respect, transparency is much harder to achieve and possibly rather a result of critical media than legislative efforts.

Second, shareholder influence as such is not a bad thing. The Guidelines recognise this by promoting the state's role as an "active owner"; for the same reason many company laws, especially for the private company type, empower (both private and public) shareholders to give binding instructions to management. Thus, it is not the influence as such, which is problematic, but the aims politicians try to achieve by exercising their right. While this may

1 societas-cee.org.

seem a truism, its relevance becomes immediately apparent if one looks at the justification for shareholder influence under general company law: shareholders as principals should be able to protect themselves against abuse of their agent's (i.e. the management's) powers. This justification is valid in the SOE context as well with the only difference that a principal–agent relationship exists at two levels: the managers are the agents of the politicians, who in turn are agents of the people. At the end of the day, it comes down to the question which agent to distrust more: the politicians (solution: insulating management) or the managers (solution: empowering politicians). While the vox populi probably favours curbing political influence, this by no means is a foregone conclusion. Rather, the fear of undue interference and the need for management oversight have to be continuously re-balanced. Overall, the issue cannot be solved by rules on SOEs alone, but is also an issue of political accountability.

Third, the solution to these problems does not lie in legal rules on influence alone. Rather, the correct selection of managers is another core issue. As a general rule expertise in running a business and in the field the company is operating in is an important curb on improper shareholder influence (which, by the way, also happens in privately owned companies). Managers who actually realise the detrimental effects of a certain measure upon the company are less likely to cave in to political demands. Although it may be practically impossible to appoint SOE managers without political ties, the more realistic aim of appointing competent managers (if need be with political affiliations) will for this reason help immensely in mitigating the negative effects of public ownership.

The legal rules on SOEs in Austria, where I come from, have grappled with these issues for at least 60 years and the solutions have been changing over the years: sometimes increasing autonomy was the main issue, sometimes it was felt that SOEs must be put on a tighter leash. I do not feel that we have come anywhere closer to a correct solution, but rather that an increase in autonomy leads to (real or perceived) abuse by management, whereupon the pendulum swings in the opposing direction and vice versa.

Therefore, it was very interesting (and to some extent consoling) to realise during our conference that other countries encounter the same issues and are not by necessity closer to a balanced and, if at all possible, stable solution. The contributions of the present volume will hopefully help the reader in getting a picture of the issues at stake (which may be similar internationally) and the legal mechanisms in place to address these issues (which diverge widely). I sincerely hope that the results will be one, if small, stepping-stone towards a better understanding of the subject.

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Anita Boros

OECD GUIDELINES ON CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES FROM HUNGARIAN STATE-OWNED ENTERPRISES' POINT OF VIEW

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The OECD regularly monitors and analyses the activities of economic operators and draws up recommendations in order to provide the OECD Member States with existing suggestions based on several decades of experience.

The OECD developed recommendations on the issue of responsible corporate governance systems and suggested some principles for the effective, transparent and responsible operation of state-owned enterprises for the first time in 2005. In these principles, the OECD made suggestions on how the state should conduct itself as regards the exercise of state proprietary rights in order to make it the most appropriate.[1]

Keywords:
company law, business law, corporate governance, state-owned company

1 OECD Guidelines on Corporate Governance of State-Owned Enterprises. Source: www.oecd.org/corporate/guidelines-corporate-governance-SOEs.htm 3. (25 October 2016)

1. GENERAL CHARACTERISTICS OF HUNGARIAN STATE-OWNED ENTERPRISES

Prior to the regime change of 1989–1990 the companies were almost exclusively owned by the state in Hungary, and as a result of the privatization carried out in several steps private ownership became dominant and the number of state-owned enterprises significantly decreased.

Nowadays, the Hungarian State has ownership interest in more than six hundred business entities. It is a general asset policy goal that the uniform supervision of state-owned enterprises shall be implemented, however, in some cases if it is needed by the professional supervision of the enterprise, proprietary rights over the enterprises are not exercised in line with the general rules (see below). According to the general rules[2] the proprietary rights and obligations are exercised and fulfilled by the Hungarian National Asset Management Ltd. (hereinafter: MNV Zrt.) as owner over the state asset entrusted thereto,[3] unless otherwise stipulated by law[4] or ministerial decree,[5] whereas the state shareholder's rights of the MNV Zrt. are exercised by the Minister of National Development responsible for state assets with the exemption defined in CVI of 2007 on State Assets (Vtv.).[6]

General provisions concerning domestic business entities are laid down in Act V of 2013 on the Civil Code (hereinafter referred to as Civil Code), which provides that business entities are incorporated enterprises established with the financial contribution of their members in order to engage in joint professional economic activities, and whose profit or loss are shared by members.

At the same time, Article 29(1) of Vtv. sets out a restrictive condition with regard to the State, providing that the State shall only participate, through a body acting as its legal representative, in a business entity or shall primarily establish a business entity in which its liability does not exceed the amount of its financial contribution. Therefore, a State-owned company may only be established as a limited liability company or a private limited company.

Pursuant to Act CXXII of 2009 on the more economical functioning of business entities in public ownership (Act CXXII of 2009), business entities in public ownership are business entities in which the Hungarian State, a local government, an incorporated partnership of the local government with legal personality, a multi-purpose micro-regional association, a development council, an ethnic minority self-government, a partnership of an ethnic

2 See Act CVI of 2007 on State Assets (hereinafter referred to as Vtv.)

3 Article 3(1) of Vtv.

4 For example the proprietary rights are exercised by the Ministry of National Development (NFM) over VPE Rail Capacity Allocation Office based on Article 67/U (1–2) of Act CLXXXIII of 2005 on Rail Transportation, or over the HungaroControl Zrt. based on Article 61/A (1–2(d)) of Act XCVII of 1995 on Air Transportation, or the above mentioned Act on the Hungarian Development Bank is also an act of this type.

5 The minister responsible for the supervision of state assets exercises proprietary rights over eighteen strategic priority business entities on the basis of the NFM Decree 77/2012 (XII. 22) on the designation of the organization exercising all state proprietary rights and obligations.

6 Article 19(1) of Vtv.

minority local government with legal personality, a budgetary body or a public foundation exercise, individually or collectively, majority influence. Majority influence, however, means a relationship through which the influential party owns, directly or through the voting rights of another incorporated entity (intermediary) having voting rights in the incorporated entity concerned, more than fifty percent of votes in an incorporated entity, provided that, on identifying indirect influence, the share of votes of another incorporated entity (intermediary) having voting rights in the incorporated entity shall be multiplied with the share of votes of the influential party in the intermediary or intermediaries; where, however, its share of votes in the intermediary is more than fifty percent, it shall be taken into account as a single whole. On calculating influence, indirect influence below twenty-five percent needs not be taken into consideration.

In other words, the concept of a business entity in public ownership is defined by the law in a manner to ensure that companies under the majority influence of incorporated entities associated with the State or with local or ethnic minority self-governments fall into that group. That solution ensures that subsidiaries are also included in the scope of the system of rules to ensure transparency and economy.

On the basis of the Civil Code, a limited liability company is established with an authorised capital consisting of capital contributions of a prescribed amount, while members are obliged vis-à-vis the company to provide their capital contributions and other services of a pecuniary value as provided for in the articles of association. Unless the Civil Code otherwise provides, members shall not be responsible for the liabilities of the company.

A company limited by shares operates with a share capital consisting of shares of a prescribed number and nominal value, while shareholders are obliged vis-à-vis the company to provide an amount equivalent to the nominal value or issue value of their shares. Unless the Civil Code otherwise provides, shareholders shall not be responsible for the liabilities of the company. Companies limited by share, whose shares have been listed on a stock exchange are public limited companies (hereinafter referred to as PLC), while those whose shares are not listed on a stock exchange are private limited companies (hereinafter referred to as Ltd.).

Based on the regulation of the inheritance act, i.e., in the absence of other heir the state, without the right of refusal, shall act as a necessary heir, business shares of other corporate forms, mostly limited partnerships, are temporarily also added to the ownership of the Hungarian State.

The State inherits business shares in a range of businesses, where the activities of these companies do not fall under the role of the State in any aspect.

Within the properties entrusted to MNV Zrt., there are currently 237 business shares inherited by the State. On average, 100 to 120 shares of varying value and representing a varying ratio of ownership are inherited by the State each year; the owner's rights over these shares are exercised by MNV Zrt.

The distribution of companies within the total properties entrusted to MNV Zrt. is as follows:

Companies, total	498
majority ownership	306
minority ownership	192
Directly managed	424
majority ownership	237
minority ownership	187
Active	261
majority ownership	133
minority ownership	128
liquidation pending	72
majority ownership	41
minority ownership	31
forced deletion pending	74
majority ownership	51
minority ownership	23
procedure for the declaration of being defunct	2
majority ownership	1
minority ownership	1
final settlement pending	15
majority ownership	11
minority ownership	4
Conferred on commission (functioning)	71
majority ownership	69
minority ownership	2
Conferred for property management (functioning)	1
minority ownership	1
Under its property management (functioning)	2
minority ownership	2
Type of company	
Agricultural co-operative	2
minority ownership	2
State-owned company	6
majority ownership	6
Limited partnership	10
majority ownership	1
minority ownership	9
Other co-operative	4

majority ownership	1
minority ownership	3
Limited liability company	264
majority ownership	167
minority ownership	97
Public benefit company	2
majority ownership	2
Non-profit limited liability company	92
majority ownership	75
minority ownership	17
Non-profit joint stock company	5
majority ownership	4
minority ownership	1
Joint stock company	112
majority ownership	50
minority ownership	62

Source: data provision of MNV Zrt. (2 November 2016)

The Ministry of National Development supervises twenty-five business entities directly and more than five hundred entities indirectly through the MNV Zrt. Out of the twenty-five business entities directly supervised by the Minister of National Development the companies related to the financial service system, such as the MFB Group, the Magyar Posta and the public utility companies are managed by a government commissioner.

From among the further twenty-one business entities the MNV Zrt., the Magyar Államvasutak Zrt., the Győr–Sopron–Ebenfurt Vasút Zrt., the Antenna Hungária Hungarian Broadcasting and Radio Telecommunications Ltd., the Magyar Közút Nonprofit Zrt., the Hungaroring Sport Zrt., the HungaroControl Zrt., or the MAHART PassNave Személyhajózási Kft. are the best-known.

From among the more than five hundred entities included in the portfolio of the MNV Zrt. and supervised indirectly by the Minister of National Development three hundred and thirty-seven are in operation, the largest of them are the MVM Hungarian Electricity Ltd., the Szerencsejáték Zrt., the Volán companies, the water utility companies[7] and the waste-management holding.[8]

Aggregated data of the composition of company shares included in the portfolio of the MNV Zrt.

7 ÉRV Északmagyarországi Regionális Vízművek Zártkörűen Működő Részvénytársaság, ÉDV Északdunántúli Vízmű Zártkörűen Működő Részvénytársaság, TRV Tiszamenti Regionális Vízművek Zrt., DMRV Duna Menti Regionális Vízmű Zrt., DRV Dunántúli Regionális Vízmű Zrt.

8 The NHKV Nemzeti Hulladékgazdálkodási Koordináló és Vagyonkezelő Zrt. is the waste-management holding The NHKV Zrt. has qualified sixteen companies as its subsidiaries.

Company shares	The amount of company shares (pcs)	The amount of company shares (%)
The total amount of company shares included in the portfolio of the MNV Zrt.	498 pcs	100,00%
The total amount of shares directly managed by the MNV Zrt.	424 pcs	85,14%
The total amount of shares transferred for entrustment or asset management	71 pcs	14,25%
The total amount of shares of majority state-owned (50%+1 votes) companies directly managed by the MNV Zrt.	237 pcs	47,59%
The total amount of shares of minority state-owned companies directly managed by the MNV Zrt.	187 pcs	37,55%
The total amount of shares of operating companies directly managed by the MNV Zrt.	261 pcs	52,40%
The total amount of shares of non-operating (v.a, f.a, kt.a) companies directly managed by the MNV Zrt.	163 pcs	32,73%

Source: data provision by the MNV Zrt. (2 November 2016)

The business entities directly and indirectly supervised by the Minister of National Development employ nearly a hundred thousand employees.

The above-mentioned companies show a rather heterogenic picture regarding the tasks (e.g. public service companies, or market oriented companies), the internal operation (e.g. of holding system, independent or business entities having one or two subsidiaries), the business operation and management (e.g. companies operating purely from budgetary resources, or their own turnover/profit). Therefore different organizing principles have been formulated considering which business entities are supervised by the Ministry of National Development and which by the MNV Zrt. Regarding this issue, of course, the effective legal regulations are the most determinant, since in principle those who are exercising proprietary rights are designated on the basis of legislation.[9]

The MNV Zrt. exercising general proprietary rights is responsible for providing the structure of exercising effective proprietary rights as regards the wide range state-owned company assets.

Besides this, central budgetary institutions or other entities can exercise ownership (membership or shareholders') rights on behalf of the state in state-owned business entities on the basis of a contract concluded with the MNV Zrt.[10] In this case another entity may

9 See Article 3 of Vtv.

10 According to Article 29(5) of Vtv. 29.

proceed in the name and on behalf of the entity, who exercises proprietary rights according to the shares in the company, as agent while exercising the specified parts of the proprietary rights. In accordance with the agency agreement, the agent is limited in exercising the proprietary rights, which are stipulated in the agency agreement, over the business entity, for example the agent shall ask for the principal's prior agreement to the exercise of the voting rights related to the shares in certain issues defined in the agency agreement.

In addition to the general exercise of proprietary rights (MNV Zrt.) the exercise of proprietary rights based on an agency agreement is an exemption; most of the ministries manage the business entities on this ground.

Regarding the determination of the person exercising proprietary rights we shall consider the characteristics of the operation, structure and task fulfilment of the business entities as well, for example there are business entities whose task can be fulfilled and the ownership control related thereto can be carried out in a more effective way if the owner also has regional/territorial agencies (e.g. water utility companies, or the VOLÁN companies). It is expedient to have these business entities supervised by the MNV Zrt., i.e. to let the principle prevail regarding the exercise of proprietary rights. There are also areas where the fulfilment of public task can be supported more effectively under the direct supervision of the minister since the competent ministries have separate state secretariats related to these areas, thereby the ownership and professional supervision can be more effective. For example, the Minister of National Development responsible for transport policy exercises proprietary rights over the Magyar Államvasutak Zrt. and the Magyar Közút Zrt., or the Minister of Agriculture responsible for agricultural policy exercises proprietary rights over the Agrármarketing Centrum Kft.

2. RESPONSIBLE CORPORATE GOVERNANCE AND THE GOVERNING BODIES OF STATE-OWNED ENTERPRISES

2.1. State-owned business entities from ownership point of view

The effective supervision of the state-owned business entities requires that each business entity shall operate according to the same principles and corporate regulations while considering the characteristics due to the special situations of the certain entities. The normative and other standard thereof shall primarily be provided by those who exercise proprietary rights. According to this, the tasks of the state secretariat responsible for asset policy are the professional support of state-owned enterprises, the elaboration of a uniform standard and to provide the operation thereof. In the course of our company management not only do we make efforts to enforce uniform company management principles but we also provide strategic support as a party exercising proprietary rights by conveying the business entities' individual requests for direction to the minister exercising proprietary rights.

Regular and effective management and operation are accompanied by the establishment of effective ownership control. We know several tools thereof, especially the control of the

business entities' operation and measures through the governing bodies and primarily through the supervisory boards.

In addition to the ownership control the Ministry of National Development has a major role in the elaboration of the appropriate sectoral business strategy for business entities, and enhances the cooperation of entities in several fields through the rationalization of tasks (e.g. joint fulfilment of functional tasks) and the joint improvement of conditions necessary for the operation (e.g. joint procurement procedures). The governance of asset management also means the recovery of these common platforms and the appropriate use thereof, so that the business entities working in different sectors can operate more effectively through harmonized activities.

In some cases the state-owned enterprises have two-tier boards that separate the supervisory and management function into two different bodies. Others only have one-tier boards, which may or may not include executive (managing) directors. In the context of the EOCD Recommendation, "board" refers to the corporate body charged with the functions of governing the enterprise and monitoring management. Many governments include "independent" members in the boards of SOEs, but the scope and definition of independence varies considerably according to the national legal context and acts on corporate governance. A CEO is the enterprise's highest-ranking executive officer, responsible for managing its operations and implementing corporate strategy. The CEO is accountable to the board.

The Hungarian Civil Code enables both governance models. While in the Anglo-Saxon legal system, corporate management and supervision by the owner are carried out by a single body, in continental legal systems, management and executive functions are carried out by the management body whereas supervision by the owner is carried out by another corporate body, the supervisory board, which is independent of the management body.

In the case of LLCs, the management and supervisory functions are carried out respectively by the managing director and the supervisory board; in Ltds, the management function is carried out by the board of directors. Since, however, management is not necessarily carried out by a board, the Civil Code allows that, instead of a board of at least three members, a single person is appointed to carry out the management functions. That person is called the general manager (*vezérigazgató*). His function and legal position, however, are different from those of other employees, also called general managers, who are responsible for the management of the work organisation of the company yet do not carry out management functions in that capacity. While a number of companies have both a board of directors and a general manager, their general managers are leaders of the organisation rather than directors.

In the case of public limited companies, the Hungarian corporate laws enable shareholders to choose from the two alternative systems of governance.

As a model, the Civil Code, following its traditions, provides for a divided system of corporate governance, i.e. unless the parties agree otherwise, the traditional Hungarian system is adopted, i.e. separate managing (board) and supervisory (supervisory board) boards are set up. If, however, in the statutes, the shareholders stipulate that, in lieu of the two bodies, they will set up a single body in a manner that such single body, i.e. the board of directors should

carry out both management and supervisory functions, the company will be operated under single governance and its operation shall be governed by the relevant rules.

Since, in such cases, the board is charged with two functions at the same time, the law provides that the minimum number of its members shall be five. Where a single system of governance is adopted, it may be a problem for the board to efficiently perform both management and the supervision of management, i.e. to supervise its own activities.

This problem is solved by the Civil Code by specifying that the majority of the members of the board shall be elected out of persons qualifying as independent, who can be reasonably expected to critically observe the activity of the company. Since their independence is a crucial factor in ensuring efficiency, the Civil Code provides that the requirement concerning independent members is a cogent requirement.

In some cases it is obligatory to ensure employer participation in the control of the companies (typically in the case of companies employing at least 200 people) by providing membership in the supervisory board. Where a Ltd. functions under a single system of governance, i.e. without a supervisory board, yet the conditions for electing a workers' delegate are fulfilled, the board and the works council shall agree on the method the workers' delegate should participate in the board.

In Hungary, Article 3:289 of the Civil Code provides for the rules governing the responsible corporate governance report. On the basis of the above, the Boards of Directors of all public limited companies are required to submit to the annual general meeting a report presenting the corporate governance practices of the public limited company, drawn up in the manner prescribed for participants on the stock exchange concerned. The report is adopted by the general meeting. The decision of the general meeting and the approved report must be published on the website of the company. Any provision of the statutes contrary to such provision shall be void.

Only public limited companies ("PLCs") are required to draw up a report, including, as a matter of course, both PLCs with a minority public interest, such as MOL Plc. and PLCs with a majority public interest, such as RÁBA Plc.

The Boards of Directors of public limited companies are required by the Civil Code to draw up and submit to the general meeting a corporate governance report in the form prescribed by participants of the stock exchange concerned.

Public limited companies are typically large organisations, important for the national economy or even by international standards, whose activities may affect entire markets or entire sectors of the national economy and, therefore, the consequences of their activities may go far beyond their shareholders. That is why a requirement has emerged vis-à-vis such companies that, in carrying out their activities, they should keep in view the interests of their immediate and broader social environment in addition to those of their shareholders. That system of expectations includes requirements that, rather than being strict legal standards, i.e. orders of conduct that can be enforced by the State administration, demonstrate the responsible behaviour and the commitment of these companies vis-à-vis the society. These requirements of conduct are institutionalised in different ways. There are codes of

conduct collated by groups of theoretical experts of high reputation, there are collections of rules published by specialised institutes, while similar rules are published by economic interest representation bodies and stock exchanges will also publish such requirements vis-à-vis companies whose shares are listed.

In the case of public limited companies, information to the public includes a statement concerning the extent and the method of the company complying with the applicable requirements of corporate governance. To that end, a corporate governance report is drawn up and adopted each year by public limited companies, simultaneously with the annual financial statements.

The Civil Code provides for the corporate governance report based on the assumption that since a joint stock company is considered to operate as a public limited company if its shares have been offered on a regulated market presumably regulated by rules for corporate governance, the legislation may be private in most cases.

The majority of Hungarian public limited companies will presumably be in that status since their shares have been listed on the Budapest Stock Exchange. The Budapest Stock Exchange has implemented Recommendations on Corporate Governance. Listed companies are required to submit an annual report on compliance with the Recommendations, i.e. to inform the general public of their compliance. Where a company fails to comply with the Recommendations, it does not necessarily imply sanctions. Rather than full compliance, the stock exchange requires that where a company deviates from the Recommendations, its conduct must be made public and its reasons must be explained. Regulation based on the "comply or explain" principle is partly the result of the fact that the stock exchange is not a legislative body. In a legal sense, its recommendations are therefore not enforceable and statutory norms; also, with regard to the individual characteristics of these companies, a deviation from a recommendation may have valid reasons for the company concerned, the awareness of which may be important for investors without the need to impose sanctions against the company.

The rule concerning the corporate governance report is cogent as it serves the purpose of informing the public, satisfying a social need. Therefore, it would not be acceptable if partners in a company were able to evade that obligation to their liking.

The RÁBA Járműipari Holding Részvénytársaság, whose legal predecessor was established in 1896, must be highlighted in the current corporate portfolio system. The Company's initial public offering took place on 17 December 1997. Rába's shares are publicly traded on the Budapest Stock Exchange. Accordingly, Rába is required to comply with the Hungarian corporate governance principles and the related statutory legislation.

Based on the (estimated) shareholding and ownership structure of **MOL Magyar Olaj- és Gázipari Nyrt.** as of 31 March 2016, the Hungarian State (MNV Zrt.) owns a business share of 24.74%.

MOL Nyrt. has always been committed to implementing the highest standards of corporate governance structures and practices. In addition to compliance with Hungarian requirements, MOL has also been adhering to the constantly evolving norms of international corporate governance.

Among others, the Company's commitment was demonstrated by the adoption by MOL's general meeting of a declaration on the Recommendations on Corporate Governance of the Budapest Stock Exchange in 2006, ahead of the statutory time limit. Moreover, prior to the launch of its shares on the Warsaw Stock Exchange in December 2004, the Company issued a declaration on the adoption of the recommendations on corporate governance of the Warsaw Stock Exchange. The Company submits an annual statement on the subject to both stock exchanges. MOL's corporate governance practices are in accordance with the requirements of the Budapest Stock Exchange and the applicable capital market legislation. Moreover, MOL has regularly reviewed its policies with a view to ensuring compliance with the constantly evolving best international practices also in that area. First adopted in 2006, MOL's Code on Corporate Governance, setting out the Company's corporate governance principles, was last updated in 2015. Setting out the rights of MOL's shareholders and the functioning of its main managing bodies, the document also discusses issues regarding remuneration and ethical conduct. MOL's Code of Corporate Governance has been published on the Company's website.[11]

2.2. The exercise of state proprietary rights from ownership entity point of view

The OECD guidelines also include the ownership entity. The ownership entity is the public body responsible for the ownership function, or the exercise of proprietary rights in state-owned enterprises. In understanding the Recommendation "Ownership entity" can mean either a single State ownership agency, a co-ordinating agency or a government ministry responsible for exercising State ownership.

As we have already mentioned, in Hungary the rules for exercising proprietary rights regarding the state-owned enterprises are provided for in the Vtv.

In addition, the Act CXCVI of 2011 on National Assets (hereinafter referred to as Nvtv.) shall also be highlighted, which stipulates that the entity who is entitled to exercise all proprietary rights and obligations vested in the state or local government over the national assets entrusted thereto is considered the party exercising proprietary rights.[12]

In the meaning of the Nvtv., the persons who may exercise proprietary rights may be as follows: ministers, central budgetary bodies, business entities in 100% State ownership, or business entities in the 100% collective ownership of the State and a business entity in 100% State ownership.[13]

A more limited group of persons is provided for by the Nvtv. with regard to business shares qualifying as national property of key importance for the national economy, as the exercising of proprietary rights is limited to the minister specified by the law, central budgetary bodies, or business entities in 100% State ownership.[14]

11 See https://molgroup.info/hu/befektetoi-kapcsolatok/tarsasagiranyitas/mol-iranyelvek (15 September 2016)
12 Article 3(1) (17) of Nvtv.
13 Article 7/A(1) of Nvtv.
14 Article 7/A(3) of Nvtv.

Regarding the state-owned enterprises, the responsibility of bodies and the relationship between the companies and the owner have a key role. However, state-owned enterprises differ from non-state-owned enterprises in several aspects: a) the organizations of these business entities are often limited by the fact that the entity exercising proprietary rights favours a single decision maker (e.g. executive), or the decision-making by a board (e.g. board of directors). It cannot be stated either that state-owned enterprises have the same organizational structure in each corporate form. There are differences also between public limited liability companies and limited liability companies: in certain cases, of course, organizational requirements are stipulated by relevant legal regulations (e.g. in the case of the MNV Zrt.), but it also occurs that a business entity of strategic importance has a supervisory board instead of a directorate based on the decision of the entity exercising proprietary rights (e.g. in the cases of the National Infrastructure Development Ltd. or the Magyar Közút Zrt.); b) decisions made by the owner of state-owned enterprises take longer than by business entities in the market. This is due to the fact that in cases of certain business transactions (e.g. significant investment, or risky investments or acquisitions) the Government's decision is also necessary; c) in cases of state-owned enterprises it is also a problem that as a result of the controls at several levels the organizations are complex, of several tiers, thereby the internal decision making process is sometimes more time consuming than in other cases; d) the financial control of the state-owned business entities is not only a process of the internal audit of the companies and the auditor regarded as external auditor, but the management of the companies is subject to the agencies monitoring the efficient and economical use of public funds, especially to the State Audit Office; e) it is a principle of major importance that the business plan of the state-owned enterprises shall be prepared according to the same, so called ownership premises every year, and the different bodies shall operate according to the same ownership directives and principles. Therefore, a uniform rules of procedure have been established for the supervisory boards of the business entities subject to direct and indirect proprietary rights exercised by the Ministry of National Development, and continuous trainings are organized for the supervisory board members.

We think that it has primary importance because our experience shows that the monitoring role of the supervisory board was mostly limited to the mandatory duties determined by legislation.[15]

As we have already mentioned, the MNV Zrt. plays a major role in the management of state assets and in the supervision of a significant part of state-owned enterprises.

The MNV Zrt. is a one-man company limited by shares, founded by the State, whose shares are non-negotiable. The Minister for National Development is responsible for the approval and amendment of its deed of foundation. The MNV Zrt. shall not be transformed,

15 See: Domokos László – Várpalotai Viktor – Jakovác Katalin – Németh Erzsébet – Makkai Mária – Horváth Margit (2016): Szempontok az állammenedzsment megújításához. Fókuszban az állami és önkormányzati tulajdonú-gazdasági társaságok irányítása. (Aspects for the reform of state management. State and municipality owned enterprises in focus.) *Pénzügyi Szemle, 2016/2. 198.*

demerged, or merged with any other company. It may be wound up by an Act of Parliament. In MNV Zrt., the shareholder's rights of the State are exercised by the Minister. The MNV Zrt. is managed by a Board of Directors consisting of up to 7 members. The Chair and members of the Board are appointed and recalled by the Minister. The Chair and members of the Board are appointed for a term of five years and may be recalled from their position at any time.[16] In addition to the functions provided for by the Civil Code, the Board is responsible, among others,[17] for submitting proposals to the Minister concerning guidelines related to the development, utilisation and disposal of State property, adopting decisions on disposing of State property, including property swaps, where the available value of the property concerned (audited property value, value assessment), net of VAT, is HUF 500 million or more, adopting decisions on developing a position to be represented at the general meetings and partners' meetings of State-owned business entities and, for business entities in one-man State ownership, issuing the founder's decision where

– the company is in exclusive State ownership,
– the company's shares grant any additional right with regard to additional rights,
– the State's share in the company's equity is HUF 200 million or more,

founding, acquiring a business share in, reorganising or winding up a business entity, providing State property to such business entity as non-pecuniary contribution, if the value of such contribution is more than HUF 200 million, submitting a proposal to decision-makers for the gratuitous transfer of property, subject to the provisions of the annual law on the budget, adopting decisions on borrowing and the issue of bonds, adopting decisions on the work organisation of MNV Zrt., approving the company's internal rules of procedure, drawing up the MNV Zrt's business plan, its report according to the Accounting Act, its annual statement on the property entrusted to it and its property management plan and drawing up reports to the supervisory board.

The members of the Board of Directors are only subject to legislation, the deed of foundation and the resolutions of the minister exercising shareholder's rights over the MNV Zrt. In exceptional cases the minister exercising shareholder's rights may give the Board of Directors a written instruction, which it shall execute but in this case the members are exempt from the responsibility defined by the Vtv.

The members of the Board of Directors shall proceed in their tasks with due care and in the primary interest of the State. The members of the Board of Directors, according to the Civil Code on the rules of tort, have unlimited and joint and several liability to the State and the MNV Zrt. for the damage caused by the breach of laws, the deed of foundation, and the resolutions made by the minister exercising shareholder's rights, and for the damage caused by the imputable failure to comply with their obligations. If the damage was caused by a board resolution the member is only exempt from liability if he/she has not participated in the decision, or voted against the resolution.[18]

16 Article (1)–(2) of Vtv.
17 Article 20(4) of Vtv.
18 See detailed in Article 22(5)–(12) of Vtv.

The operation of MNV Zrt. and its management of State property are supervised by the Supervisory Board, which consists of five members. The Chair and members of the Supervisory Board are appointed and recalled by the Minister. The Chair and members of the Supervisory Board are appointed for a term of five years and may be recalled from their position at any time. Members of the Supervisory Board shall carry out their activities with the care reasonably expected of persons fulfilling such positions, on the basis of the primacy of the interests of the State. In accordance with the provisions of the Civil Code concerning the causing of collective damage, members shall have joint and several responsibility vis-à-vis the State and MNV Zrt. for damages caused due to the breaching of their control obligations for reasons within their control. Where such damage has been caused by a collective decision, members not having participated in making the collective decision or having voted against it shall be relieved of their responsibility. The Supervisory Board shall submit to the Minister a report on its operation each year by 31 August of the year following the year under review. Such report shall also be forwarded by the Supervisory Board to the State Audit Office.[19]

According to the OECD guidelines the State should act as an informed and active owner, ensuring that the governance of state-owned enterprises is carried out in a transparent and accountable manner, with a high degree of professionalism and effectiveness.

In order to ensure that the proprietary rights of the State are exercised in an informed and active manner, the primary tools are a clear and unambiguous ownership policy, broad mandates and objectives.

In accordance with the provisions of the Civil Code and the specific features of particular state-owned enterprises, the deeds of foundation of state-owned enterprises clearly specify the areas of decision-making competence of the State as the owner.

The Ministry of National Development has acted in accordance with the OECD guidelines in its exercising of its proprietary rights on behalf of the State, has limited its powers of instructing state-owned enterprises to strategic issues and public policy objectives, including in particular the approval of state-owned enterprises' business plans and statements. Interventions in the operational decisions of state-owned enterprises, such as the hiring of personnel, are uncommon.

2.3. The exercise of state proprietary rights and competencies for monitoring

The exercise of proprietary rights is effective if the systemic monitoring of those determined by the party exercising proprietary rights is carried out. The Ministry of National Development, as the party exercising proprietary rights, has felt a need for developing and introducing a Corporate Monitoring system to enable the monitoring of the operation of companies. That project was launched in the spring of 2015. The monitoring system implemented is based on the quarterly reporting of data, where information is requested by the owner concerning the profit, balance sheet, investment, staff number, earnings, accounts payable

19 See detailed in Article 20/A of Vtv.

and accounts receivable of each company. Within the Project, in addition to general financial and other indicators, company-specific KPIs are developed and analysed.

Regarding the Hungarian liability clauses Article 3:287 of the Civil Code shall be highlighted, which defines the concept of "independence" with regard to the boards of public limited companies. The definition guarantees the requirement of objectivity and essentially intends to define a system of conditions to ensure that board members should be capable of monitoring the activities of the company and, in particular, of the management of the company independently and free of any influence. The rules governing the definition of independence are cogent rules.

Section (1) provides for the conditions at which a person is considered to be independent. A board member is thus independent if he does not have a contract with the company other than the ones concerning his board membership and based on transactions to satisfy the needs of board members as part of the normal activities of the company.

Section (2) provides for the conditions at which a person cannot be considered to be independent.

A member of the Board shall not be independent if he

(a) is an employee or a former employee of the company, for a period of five years from the termination of his employment;
(b) carries out any activity under a contract as an expert or in any other capacity for and to the benefit of the company or its senior officials for a fee;
(c) is a shareholder in the company, directly or indirectly owning thirty percent or more of votes or is next of kin to or POSSLQ of the former;
(d) is next of kin to or POSSLQ of a non-independent senior official or manager of the company;
(e) is entitled to remuneration on the basis of his board membership if the company generates profit, or receives any kind of remuneration from the company or an affiliated company in addition to the fee due to board members;
(f) is under a contractual relation with a non-independent board member in another business entity, such contract granting rights of management and control to the non-independent board member;
(g) is the auditor of the company or a member or employee of the auditing company, for a period of three years from the termination of his employment;
(h) is a senior official of or holds a management position in a business entity where an independent board member is a senior official of the public limited company.

The State exercises the ownership of state-owned enterprises in the interest of the general public, therefore it should carefully evaluate and disclose the objectives that justify State ownership and subject these to a recurrent review.

On the basis of the mandate vested in it by the Fundamental Law, the Nvtv. sets out an itemised list of economic activities that are reserved for central or local government entities (i.e. subject to a concession as the main rule).

Among the exclusive economic activities reserved for the State, Section 12(1) of the Nvtv. lists the passenger and goods transport on the main national railway network. The law provides that the railway network including railway tracks that are part of the main national network and their accessories or a railway network that includes a railway track that is part of the main national network or its accessories shall only be operated by the State or a business entity in which the State is the sole member or shareholder or which is, directly or indirectly, in the majority ownership of the State.

Since it was established, for example the State has been present in the ownership structure of MÁV Zrt. since the Group's two core activities are public duties, which are of primary importance, and on the other hand cannot be financed solely from revenues generated on the market. As both the maintenance of the rail network and passenger transport require participation by the State under Hungarian conditions (length and condition of the rail network, the needs of passengers, fares and schedules in passenger transport).

Under the Nvtv., economic activities related to the organisation and operation of gambling are reserved for the State. Due to the risks it involves for society, gambling is not a normal commercial product, while the organisation of gambling is a special type of economic activity that is governed by Act XXXIV of 1991 and Decree No. 32/2005 of 21 October 2005 of the Minister for Finance. The purpose of legislation on gambling is to protect the society, including in particular public order, public health and public security. Szerencsejáték Zrt. is the business entity authorised to exploit the State monopoly specified in Section 3(1) of Act XXXIV of 1991 on the organisation of gambling. In Annex 2 to the Nvtv., it is listed among State-owned business shares qualifying as a national property of key importance for the national economy, which is in 100% State ownership. According to Act CVI of 2007 on State property and to the Nvtv., maintaining long-term State ownership is necessary in order to carry out State functions, satisfy the needs of society and to facilitate the implementation of the Government's economic policy. Consequently, there are profitable state-owned enterprises which, on the one hand, contribute to the domestic budget by significant dividend income, on the other hand they fulfil a task (e.g. the HungaroControl Zrt. in the field of air traffic management) which makes the strengthening of the market position of the company and thereby the involvement of the State in these market segments expedient.

3. REQUIREMENTS IMPOSED ON DOMESTIC STATE-OWNED ENTERPRISES

A significant part of our business entities fulfil some kind of public duty, therefore the most important requirement imposed thereon is to increase the efficiency of the public duty. The party exercising proprietary rights provides several tools thereto, but I think that the commonalities between the business entities belonging to similar sectoral public administration (e.g. transport companies, the energy sector or even public utilities) shall be found so that the synergies between the business entities can be exploited, the cooperation

can be increased and the efficiency of company operation can be enhanced.[20] The efficiency of cooperation affects the standard of the services provided by the business entities, for example the integrated timetable search system developed by the MÁV-START Zrt. and the VOLÁN Egyesülés in the spring of 2016 shall be highlighted, whereby the national, regional and suburban services are available on one surface.

In case of a minority of state-owned enterprises it is not the fulfilled public duty that is dominant but the achievement of the best possible result in a certain market segment, thereby increasing their business results. The HungaroControl Hungarian Air Navigation Services Pte. Ltd. Co., the ANTENNA HUNGÁRIA Hungarian Broadcasting and Radio Telecommunications Ltd., the MAHART PassNave Személyhajózási Kft., the MVM Hungarian Electricity Ltd. and the Szerencsejáték Zrt. can be listed in this group, for example.

In addition we also have business enterprises carrying out tasks in the field of development policy, which aim at targeting the increase of state involvement in certain areas (for example the NIPÜF Nemzeti Ipari Park Üzemeltető és Fejlesztő Zrt.), or develop facilities which later significantly determine the improvement of the standard of public duty (for example the NIF National Infrastructure Development Ltd., which carries out transport infrastructure (road and rail) network development tasks, or the BMSK Beruházási, Műszaki Fejlesztési, Sportüzemeltetési és Közbeszerzési Zrt., which engages in, among others, the development of sport facilities and the complex implementation of sport investment projects). The most important requirement imposed on these business enterprises is that the facilities are finished in time by using the available funds cost effectively and in the best quality.

In addition, we also have state-owned enterprises which carry out tasks that previously proved to be imperfect. The Magyar Fejlesztési Központ Nonprofit Kft., whose primary task is to elaborate the effective system of the harmonisation of the direct public funds usage, or our business entities (for example the Nemzeti Fejlesztési és Stratégiai Intézet Nonprofit Kft., the Nemzeti Fejlesztési Programiroda Nonprofit Kft.) that act as consortium leaders in important fields related to certain EU obligations (e.g. the projects funded by the Environment and Energy Efficiency Operational Programme targeting the increase of energy efficiency and the application of renewable energy sources, which affects the distant heating sector) are of this type.

4. THE MNV ZRT. RECOMMENDATION FOR STATE-OWNED ENTERPRISES

In addition to the above mentioned OECD guidelines the MNV Zrt. has elaborated a manual including around two hundred recommendations (in this chapter referred to as Recommendation),[21] which aim that the MNV Zrt. promotes the compliance with the

20 See: Auer Ádám: *Corporate Governance. Állami részvétellel működő gazdálkodó szervezetek.* Budapest, NKE. 18–21.

21 See detailed: www.mnv.hu/felso_menu/tarsasagi_portfolio/eljarasi_dokumentumok/vallalatiranyitasi_ajanlasok/ajanlas_allami_tulajdonu_tarsasgok_szamara.html (15 September 2016).

requirements of responsible state asset management regarding the state-owned enterprises included in the portfolio of the MNV Zrt. through the Recommendation. It is a public expectation from the entities that the defence of assets as lasting value and the responsible, transparent and effective asset management to keep the value thereof shall be more effective, successful and cost-effective.

The update of the Recommendation and its extension to the full company portfolio under the supervision of the Minister of National Development is currently in progress.

It has been determined in the introductory provisions of the Recommendation that

- the State as the owner and the state-owned enterprise shall cooperate with the stakeholders of the state-owned enterprises;
- a state-owned enterprise applies a system where the competence and responsibility of the management is transparent and dedicated;
- state-owned enterprises shall focus on the increase of value in the course of their management;
- in the course of state asset management efforts shall be made not to violate the interests of the minority shareholders,
- state-owned enterprises shall be operated publicly so that publicity is provided without violating the company's business interests;
- owners shall be provided with all the information by the company management which is necessary for the exercise of proprietary rights;
- the decision making process of the state-owned enterprises shall be created so that the protection of the company assets against abuse, negligent or unintentional tort is provided proportionately to the risk capacity of the entities;
- in the course of state asset management the creation of value shall be aimed at;
- in the decision making process the state-owned enterprises shall particularly focus on the social and environmental sustainability.

The Recommendation also includes detailed guidelines on the operation and decision making system of the state-owned enterprises:

- the responsible and ethical decision making system of the sate-owned enterprises shall be built up so that it provides the increase of the entity's value and the management appropriate for ownership interests (individual decisions and strategic guidelines);
- the requirement of safeguarding state assets and keeping the ownership investments safe in cases of mixed ownership companies is an objective;
- the decision making system, on the one hand, shall provide for the protection of the entity's value, on the other hand the effective usage thereof. The optimal decision making system has to provide for the effective use of the tools and the consistency of the business activities with the legal and ethical requirements;
- the decision making system shall be based on the unequivocal share of responsibilities and tasks thereby providing accountability.

In addition the Recommendation includes detailed suggestions related to the management issue concerning the State as a non-single owner, for the relevant entities as follows:

- general rules for the development of competences;
- the ownership involvement of the State – the rules on exercising proprietary rights, convening and arranging general meetings/assemblies of members and exercising proprietary rights;
- the operation and the rules of procedure of the directorate, and the provisions on the senior manager (chief executive) and the executive;
- the role of the management, the internal coordination of the entity;
- supervision and monitoring agencies;
- the monitoring role of the Supervisory Board in cases of business entities without a directorate;
- the independent internal audit of the entities;
- monitoring – informing function of the Directorate/chief executive/management;
- the monitoring system;
- auditors;
- human resources policy and the rules on conflict of interest;
- the composition of the directorates, conflict of interest;
- remuneration rules and policy;
- professional preparedness of the senior manager;
- the regulation of the conflict of interest, individual declarations – the elaboration of immunity procedures;
- dealing with "Related parties";[22]
- the appointment of the chair person and the members of the Supervisory Board;
- internal monitoring and risk management;
- risk management of contracts;
- the determination of the sphere of public information.

22 See Section 149 of the Recommendation: The business entities are recommended to regulate on the rules of procedure for making deals where a conflict of interest may occure.

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CORPORATE GOVERNANCE IN STATE-OWNED COMPANIES IN HUNGARY

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From the development to the comprehension of the regulation it is necessary to ascertain, in our view, the subject of the regulation is the operation of the company. The regulation regulates the problems arising specifically during the course of the operation of the company, as an "ex ante" tool and by the avoidance of that upon the cessation of the public company, any unjustified or inconceivable costs (social costs) should rise. As an example, there are the infamous earlier corporate scandals (Enron, Parmalat, Vivendi Universal), the infringements of which drew critical social (budget) costs, as they left behind unsettled creditors' claims, and plenty of workplaces were terminated, etc. To prevent this, one of the techniques is corporate governance, as it focuses on such mechanisms during the course of the operation of the company as direction and control. With this, the cessation of the company can presumably be avoided, as it is publicly acknowledged that the majority of corporate scandals descend from the faults of leadership, direction and control. Based on the above, we may ascertain that in our perception, under "corporate governance" it is the legal facts or interests relevant in the course of the operation of the company that become regulated in terms of corporate law.

Keywords:
company law, business law, corporate governance, state-owned company

The phenomenon, the subject of corporate governance is one such topic in corporate law, that has received extra attention for the past decade in professional literature and from policy makers. The legal definition of corporate governance was set by the Cadbury Report in 1991, as: corporate governance is the system by which companies are directed and controlled. It is as abstract as needed; this definition is appropriate enough to be applicable to define corporate governance in all parts of the world, yet further approaches are required to the unfolding of the content of the topic.

1. WHAT DOES CORPORATE GOVERNANCE REGULATE?

From the development and to the comprehension of the regulation it is necessary to ascertain that in our view, the subject of the regulation is the operation of the company. The regulation regulates the problems arising specifically during the course of the operation of the company, as an "ex ante" tool and by the avoidance of that upon the cessation of the public company, any unjustified or inconceivable costs (social costs) arising. As an example, there are the infamous earlier corporate scandals (Enron, Parmalat, Vivendi Universal), the infringements of which drew critical social (budget) costs, as they left behind unsettled creditors' claims, plenty of workplaces terminated, etc. To prevent this, one of the techniques is corporate governance, as it focuses on such mechanisms during the course of the operation of the company as direction and control. With this, the cessation of the company can presumably be avoided, as it is publicly acknowledged that the majority of corporate scandals descend from the faults of leadership, direction and control. Based on the above, we may ascertain that in our perception, under "corporate governance" it is the legal facts or interests relevant in the course of the operation of the company that become regulated in terms of corporate law.

1.1. The subject of corporate governance regulations

The first key-term generated from the above approach is which situations, state of affairs, interests are regulated by law? Having reviewed the corporate governance rules (codes on best practices), we may constate that such situations are regulated by law as state of affairs, which cannot traditionally be considered as a field of corporate law. For instance how to (technically) summon the general assembly, what instruments should be applied for the efficient conduction of the general assembly?[1] What sort of legal powers the company should assign to the nomination committee, how it should regulate the standing orders and daily work-schedule of the managing directorship, and what HR selection criteria should be applied?[2] None of these fields has formed the set of regulations for corporate law before. This statement certainly needs fine adjustments, as the set of rules on corporate law can alter by eras and economic settlements. The continuous expansion of the rules

1 E.g. the Corporate Governance Recommendations [hereinafter: FVA] of the Hungarian National Assets Management plc (hereinafter: MNV Zrt.) as per recommendations no. 15–33., especially 17. and 18.

2 MNV Zrt.'s FVA recommendations on supervisory-board no. 59–77., on HR criteria 13.

of responsibility in Hungary can serve as an example of continuous development.[3] At the examination of the classical fields of regulation of corporate law, we may claim that the rules of corporate law have covered the categories of economic companies (numerus clausus), the foundation mechanism (company procedure), and rules of the same branch applied to termination as well, especially to the procedures of liquidation and bankruptcy as linked with insolvency. These are the terrains where legal regulations give no choice of an option, nor allow for any private autonomy, but provide an entirely exhaustive, flawless legal governance instead. Certainly, the assurances of a "rule-of-law" state the company's operation are implemented by the acts of law, providing a standard rule for the operation in several cases, such as: the scope of authority, as in the case of the principal organ, conference general assembly, voting by post.

The exhaustive regulation upon the operation of the company (the period from the registry of the business association until the decision on its termination was made) was one of the areas where the private autonomy of the members used to be of the broadest spectrum. Yet, assumably due to the numbers of corporate infringements the legal regulation had to react, and was required to provide a sufficient solution to the occurrences during the course of operation. Since corporate infringements could be traced back to organizational operation, the recommendations of corporate governance apply by nature to the operational period of the company.

1.2. The legal feature of corporate governance rules

Another examined conceptual element of corporate governance is the legal assessment on the quality of the regulation. Corporate governance has known two types of rules in accordance with international trends: recommendations (for example for the companies listed on stock exchange in Lithuania, Poland, Romania and Hungary)[4] and suggestions. Corporate governance comprises genuinely self-regulatory, non-binding prescriptions, however, in Central and Eastern Europe there exists one peculiar example of it, demonstrated in that the to-be regulated topic in terms of corporate governance rules appears defined by acts of law (typically in act), instead of codes and self-regulatory documents. In the process of the codification of corporate governance rules it can also be observed, that part of the recommendations is not realized in the areas of the recommendations, but on the level of law (e.g. Romania, Slovenia and Hungary), when regulating a given corporate governance topic-area the policy maker genuinely privileges the change in the rule of law (e.g. in Slovenia and Romania in terms of organizational rules).[5] Certainly, this can be found in the

3 To this as a summary see: Papp Tekla szerk. (2011): *Társasági jog.* Szeged, Lectum. 249–251.

4 International workshop: "Corporate governance in state-owned companies", 11. 04. 2016., Gdańsk, University of Gdańsk, Faculty of Law and Administration, Societas CEE Company Law Research Network.

5 Djokic, Danila (2009): The Corporate Governance Statement and Audit Committee in the European Union and Republic of Slovenia. *Croatian Yearbook of European Law & Policy, 2009/5. 283–289.;* Manolescu, Maria – Roman, Aureliana Geta – Roman, Constantin (2010): Corporate Governance of Romanian Public Interest Entities. *DAAAM International, 2010/1. 1127–1128.*

Hungarian corporate governance practice, for example in the case of the publicly owned business associations it is the matter of remuneration as per Act CXXII of 2009.

The system of comply or explain commenced in Great Britain, where the requirement was specified that public disclosure qualifies a sanction, this encourages the company to align with the practice defined by itself.[6] The proper standards in accordance with the recommendation are applied, yet it is at once questionable to set forth an optimum in the matter of the headcount for the board of directors or the supervisory board to operate. The term "comply or explain" means that in case a company shall not apply a given recommendation, then an explicit explanation must be supplied for the reason why, more precisely it must publicly disclose the practices that are followed. In the EU member states it was the directives to introduce the technique of "comply or explain", thus this sets the directive for stock-exchange companies in Hungary.[7] The regulation of comply or explain does not equal the traditional denotation of an act of law, as it lacks the potential of state enforcement capability, and legal enforcement only relies on the applicable prescriptions of mandatory public disclosure of the corporate governance report. This indeed is no regulative mistake, but the conceptual element to corporate governance, in which the regulation on the stock exchange alongside the respective publicity is a sufficient sanction. The question of course is whether or not enforcement-potential is required, or is publicity itself a sufficient sanction? As we see it, it depends on stock-exchange culture, and stock-exchange investors' discipline. The impacts of stock-exchange culture and strictness can effectuate, if the stock exchange's trading turnover takes up a decisive segment off the economy. Consequentially, the enforcement potential would be necessary to establish in Hungary, as the scope of the economy is not the stock exchange.

From the aspect of the topic of this study, the question arises more intensely within the field of state-owned enterprises as their property is not private but public property.[8]

2. CORPORATE GOVERNANCE IN THE PUBLIC SECTOR

In our view, the previously mentioned general assumptions on corporate governance are applicable to state-owned enterprises. Special weight is granted to this field by the state being a proprietor and raises the duplicity as well as the turning into each other of the principal–agent relations. If the state is the proprietor, then behind it are the taxpayers. If the company ceases, then it will also result in consequences upon the budget, thus behind it are also the tax payments of the citizens. These two areas are interconnected, so it is a theory of a duplex commissioner-agent that applies which results in one triangular process as they turn into each other.

6 Winner, Martin (2012): Der UK Corporate Governance Code. *ZGR, 2012/2–3. 246–272., 252.* and Dine, Janet (2003): A new look at corporate governance. *Company Lawyer, 2003/5. 130–131., 130.*

7 It is also a legal regulation minimum, that acts must regulate the public disclosure of the affidavit. This prescription in Hungary is also included in the Accountancy Act and the Civil Code.

8 In Hungary, The Fundamental Law of Hungary decrees the principle of responsible and transparent management of the public finances. The Fundamental Law of Hungary article N), article 39 (2)

2.1. The definition of state-owned enterprises

Rules over state-owned public companies in Hungary must be divided into two. State-owned enterprises certain form a part of the notion. On the other hand, there are the municipalities that may also hold corporate property.

As per The Fundamental Law of Hungary (formerly the Constitution) the economy of Hungary is founded on value-adding work as well as the freedom of enterprises.[9] Everyone possesses the right to select work and occupation freely, and to begin an enterprise, however, everyone is obligated to contribute by his or her capabilities and circumstances to the growth of the community.[10] Besides the freedom of occupation and enterprises, everyone possesses the right to own property, which is bound by social responsibility.[11] Relating especially to this the Fundamental Law of Hungary decrees that the proprieties of both the state and the municipalities comprise the national property.[12] The Fundamental Law of Hungary decrees that any legal entity established upon the basis of acts of law is entitled to hold such fundamental rights and is subject to such liabilities that are not only applicable to humans by their nature.[13] In terms of the national wealth, The Fundamental Law of Hungary regulates the wealth of the state and the municipalities, and also the principles of economy in a unified manner; specifically highlighting that the economic organizations owned by the state and the municipalities conduct their economy in a manner determined by acts of law, independently and responsibly, in accordance with the demands imposed by legality, appropriateness and productivity.[14] The National Assets Act as of 2011. CXCVI. [hereinafter: Nvtv.] also keeps this duplicity, and alongside the state property it marks the property of the local government as well. For this reason, in the study of the economic organizations operating through state-involvement, we must expand the notion to the local governments, too.[15]

Act CVI of 2007, on the wealth of the state, that is the State Property Act [hereinafter: Ávtv.], came into force after the termination of institutional privatization, and regulated

9 The Fundamental Law of Hungary, article M (1)

10 The Fundamental Law of Hungary, article XII (1)

11 The Fundamental Law of Hungary, article XIII (1). The constitutional legal status of the state property demonstrates a clear system in The Basic Law, yet the earlier Constitution – not only in its authentic text, but also after the change of regime – decreed upon the status of public property. § 9 (1) of the Constitution decreed, that the economy of Hungary is such a market economy, in which the public property and the private property share the same rank. The Constitutional Court evaluated this as the expansion of the discrimination interdict to the property right, which in essence defines a discrimination interdict to any forms of property. § 70/A. of the Constitution, Const. Court Provision 1990. 81. To the dismantling of the privileges of state property See: Sólyom László (2001): *Az alkotmánybíráskodás kezdetei Magyarországon.* Budapest, Osiris. 128–130.

12 The Fundamental Law of Hungary, article 38

13 The Fundamental Law of Hungary, article I. (4), which decree equals the earlier provisions of the Constitutional Court (first 21/1990. (X. 4.) Const. Court Provision, 7/1991. (II. 28.) Const. Court Provision, with laid principles.

14 The Fundamental Law of Hungary, article 38

15 To the property of the local governments see: Patyi, András – Rixer, Ádám eds. (2014): *Hungarian Public Administration and Administrative Law*. Passau, Schenk Verlag. 342–345.

the property conditions of the state arranged in a new frame.[16] As per the prescriptions of the Ávtv., the following items are the constituents of the property in the proprietorship of the Hungarian state: the things in the proprietorship of the state, and also the natural forces that can be utilized like things; other than this all such property, respective of which the act specifies the exclusive proprietor's right of the state, such stock-paper in the proprietorship of the state which identifies membership rights, and also any other corporate shares that are due to the state, any such immaterial rights bearing property value that are due to the state, which are specified by an act as a right of property value, the monetary assets in the proprietorship of the state.[17]

The duty of the exercising of proprietorial rights and assets management examined from the aspect of our topic is: to ensure the efficient, cost-saving, value-preserving, value-adding application (direct application) of the state-property in compliance with its function – necessary for the fulfilment of state duties, sufficing of social necessities, and fostering the realization of the economy policy of the Government, based on unified principles and appearing as an individual branch –, as well as the indirect utilization (including its sale resulting in the change of the property index), and also the enhancement of state property (including the expansion of the property index).[18] Rules of law designate the Hungarian National Assets Management plc (hereinafter: MNV Zrt.) to exercise the proprietorship rights.

Beside the companies operating through state-involvement in the case of the local governments, the board of representatives holds the right to found various types of organizations, in order to conduct the public services that are forming its scope of duties.[19] Examples to that may be budget organs, economic organs, non-profit organs and other organs.[20]

Based on the above, we can declare that "public property" can be segmented into two, due to the Hungarian constitutional traditions and also according to the effective system of law: first to the property of the state, and then to the property of the municipalities. Regarding the property of the state, it can be declared, that it can be segmented further: to treasury property and business property.[21] The function of treasury property is of the exclusively state-owned property, the restrictedly negotiable property, the national property of highly distinguished concern from a national economy's perspective, all of which are itemized in the Act on National

16 Property obviously covers a broader range as compared to propriety, yet the chapter only analyzes the rules included in the portfolio of economic companies.

17 Ávtv. 1. § (2)

18 Ávtv. 2. § (1)

19 Act CLXXXIX of 2011. § 41. (6)

20 To the topic area of the corporate governance of the local government see: Horváth M. Tamás (2013): Felelős társaságirányítás – közszektorban? *Gazdaság és Jog,* 2013/1. 12–16. and Horváth M. Tamás (2014): *Vállalati részesedés igazgatása – köztulajdoni körben.* In Lapsánszky András – Patyi András (szerk.): *Ünnepi kötet Verebélyi Imre 70. születésnapjára. Rendszerváltás, demokrácia és államreform az elmúlt 25 évben*. Budapest, Akadémiai (Wolters Kluwer). 221–229.

21 Torma, András (2013): A nemzetgazdaság igazgatása. In Lapsánszky András szerk.: *Közigazgatási jog II. – Fejezetek szakigazgatásaink köréből.* Budapest, *Complex. 23–59., 43.* Analyses the notion of business property: Sárközy Tamás (2009): *A korai privatizációtól a késői vagyontörvényig.* Budapest, HVG-Orac. 192–195.

Assets.[22] The business property is the property that forms no part of the whole of the treasury property.[23] Following this scheme, Tamás Sárközy argues the existence of business property, yet acknowledging meanwhile that it can still exist, like: the backup companies of the state (for instance companies pursuing educational, research activities), companies of strategical interest, which are in the permanent proprietorship of the state as they are facilitating the fulfilment of public duties.[24] Nonetheless, this system in this composition does not work immaculately, but both the existence and the scope of the business property are in perpetual change, aligning with the ever up-to-date tendencies of economy politics.

From an administrative perspective, based on Act CVI of 2007 in terms of the state property, the entirety of all rights and liabilities of proprietorship due to the Hungarian state shall be designated to be exercised by the Hungarian National Assets Management plc (hereinafter: MNV Zrt.).[25] The MNV Zrt. is a one-man joint-stock (public) company founded by the state, the stock of which is non-negotiable.[26] From among the items of state property included in the duties of the MNV Zrt., the Ávtv. specifically mentions the stock-paper in the proprietorship of the state, which identifies membership rights, and other company shareholdings, that are due to the state.[27]

In Hungary, there are no such special company forms as to conduct publicly owned economic activities; however, the state applies the company forms regulated by the Civil Code while conducting these activities.

It is not only that the Hungarian legal system is unfamiliar with any peculiar company types, but also that it fulfils many public duties in the form a public business associations. These companies have peculiar public-law relevance, status, such as Hungary's central bank, The Hungarian National Bank (MNB), as an example. The Hungarian National Bank is a legal entity, operating in the form of a joint-stock (public) company. In our view, the MNV Zrt. falls in the same category as well, which is a one-man joint-stock (public) company founded by the state, and the stock of which is non-negotiable. The Hungarian National Assets Management plc pursues state service, among others executes proprietary rights over the state fortune. However, the realization of the general prescriptions of civil law varies with respect to each one of the scenarios, and in fact, the specific prescriptions affect relevant elements of the regulation.

2.2. The corporate governance question

In our perception, regarding the companies owned by the state, the realization of corporate governance should be differentiated depending on the economic profile that they bear.

22 Torma 2013, 43.

23 *Ibid.*

24 Sárközy 2009, 193.

25 Act CVI of 2007 § 1 (6a)

26 The approval as well as the amendment of the foundation deed of the MNV Zrt. forms the competence of the minister. The MNV Zrt. may not transform, may not disunite, may not unite with another company. Upon its termination the Parliament may decree in Ávtv. § 18 (1)

27 Ávtv. § 1 (2) c)

The first (1) are the activities conducted by the state through its monopolist position, with the formation of the regulation. More precisely, it does not permit any other market players to enter, yet the activity itself is profitable. Second (2) is the economic situation, when the activity itself is non-profitable, but it could not even be, as it identifies the social function of the state. The sector of public services is an example of this. The (3) last one is the marketplace situation, which means that the state as a player in economic competition is involved in competition. In this case, only the membership position can be linked with the state. Each one of the above economic situations connects with a different governance problem scenario. In the first case (1), the demands for the transparency on the operation of the management can come forth. The second (2) is a special case, as this field of the economy has been blending with the legal system of the European Union, at the arrangement of the activity, specific requirements must be justified, so the membership position of the state and the internal operation of the company may just as well be the subject of corporate governance rules. The role of the state can appear the most conspicuously in the third (3) case, when the state may not create a more advantageous situation against other market-players.

We assume that the variant economic grounds impose variant emphases upon the fields of corporate governance, yet none of the economic grounds can overshadow the relevance of corporate governance. Concerning the question of the state property, we believe, the real corporate governance question is whether the state, as a member of the company, possesses more or any different rights than a traditional company does? Are these, at all, ensured by corporate law even as an option, or not?

For the sake of entirety, let us note that it qualifies as a different situation from the above aspect, when as a special state-intervention, the public company becomes designated by the Government as a strategically outstanding concern. This has a relevance when the activity of the company is distinctive (for instance it conducts public services, it has a connectivity to national defence). This designation only matters when it comes to the condition of insolvency, as those procedures prescribe peculiar rules.

3. THE APPLICABLE RULES TO STATE (PUBLIC) COMPANIES

Corporate governance can be scrutinized from two perspectives in the case of economic organizations operating through state or municipality involvement. One of them is intern relations, namely how do the principles of corporate governance become implemented in economic organizations established by the state or the municipality. In answer to this there are the principles developed by the OECD. The OECD first issued the collection of recommendations in 2005, and then it was in 2015, when during the general review of corporate governance the new code was introduced. The recommendations are applicable to such business associations as legal persons, in which the state executes the proprietorship rights – and holds an influential, a sovereign role –, and also to such public-law legal subjects, which have an economic role.[28] Here, in our view, the emphasis falls on whether the state as

28 OECD 2015. 15.

a shareholder has relevant influence on the decision-making of the company. Certain forms of influencing (golden share, majority shareholder etc.) draw different governance-issues, and with this different resolutions, too. According to the recommendation, the performance of this sector gives a competitiveness factor.

The explanation for the creation of the recommendations directive to the economic organizations operating through state or municipality involvement is the aim to professionalize the ownership function of the state, the implementation of efficiency, transparency and mandatory reporting to the degree of the private economy, and to ensure equitable treatment rules in such cases when the state-owned company is active on the same marketplace with the competition-field.[29] Corporate governance plays a vital role in the development of these warranties, furthermore, the recommendation highlights that the utilization of corporate governance practices is an essential prerequisite to financially effective privatization as well. Special relevance must be attributed to this particular objective in Hungary and in Central and Eastern Europe, although after the privatizations accomplished in the past, it is now the utilization of recommendations directive to the state as a role player of the active economy that can be detected.

In the recommendations directive to state companies, it is recorded that the document includes specific prescriptions, complementary requirements against the document on general corporate governance,[30] thus the efficient system of corporate governance can be composed by the concurrent reading of the two recommendations.

Based on the recommendations, throughout the involvement of the state, distinct attention must be paid so that the state provide an efficient legal regulation framework to the market players, without distorting the competition by its presence. With respect to the regulation, the state must avoid the creation of special, merely self-applicable rules, as that would demonstrate a market-distorting impact; moreover, it must aim at the standardization of legal subject categories whilst avoiding the establishment of a peculiar type of a state company.[31] The state as the owner is advised to develop such a procedure that can fulfil the obligation of accounting by means of transparency, without any distortion. All through this, the following must be considered by exercising the voting right, transparency of the nomination of the directorship board, ensuring independent and impartial decision-making to all participants of the decision-making. Beyond these, the recommendations also affect the obligations of the board, the stakeholders, the requirements of transparency, and the enforcement of the demands of equitable treatment, yet with respect to these, the prescriptions do not include special provisions against general rules, but the collection of recommendations itself refers back to general rules.[32]

We claim that there is another possible way and concept to the application of corporate governance: this means the extern processes, namely those, in which the state participates

29 OECD 2015. 11.
30 OECD/G20 Corporate Governance Principles
31 OECD 2015. 38.
32 Papp Tekla szerk. (2011): *Társasági jog.* Szeged, Lectum. 532–533.

as a contracting party. One point of connectivity is that the Act on National Assets has introduced the notion of transparency, meaning fundamentally the analysis via tax liability criteria and the revelation of membership.[33] The core principle of the management of the national property is that an agreement can only be concluded by an organization, if it is transparent.[34] In our view, the state may just as well apply such principles in its procurements, in the course of public procurement. Investments and procurements accomplished under the course of public procurement can be compatible to take into account further aspects besides profit, thus the utilization and enforcement of corporate governance principles can appear as a requirement equivalent to this.[35]

3.1. The corporate governance recommendations by the MNV Zrt.

The MNV Zrt. has issued a document alongside the international standards of the corporate governance, to reinforce the Hungarian corporate governance practice. By this, we believe, that it has taken a regionally prominent place in terms of corporate governance thinking.

The Hungarian National Assets Management plc (MNV Zrt.) has issued a recommendation to companies in the ownership of the state, inclusive of recommendations and guidelines in a complex system, addressing the society of economic organizations operating through state-involvement.

The code was proclaimed in the spring of 2013, by the MNV Zrt. The corporate governance ground directive to the companies constituted several parts:[36]

- Corporate Governance Recommendations
- Code of Ethics, according to the initial idea, for the employees of the public service, they are ethical norms of a higher level than on average are set for directives, and they are also required to comply with professional ethical principles that apply exclusively to those in the public service.
- Risk-management Manual, the target of which is to promote the recognition of direction problems, the shaping of the propositions for a sound resolution beyond a risk-management methodology, grounded on an analysis of abilities to direct, and the familiarization with the applicable control-models.
- Investment policy-related recommendation. The target of the recommendation is to provide support in terms of the utilization of free monetary assets and currency rate risk-management, by the application of which the regulations of the companies can be compiled.
- Liquidity planning recommendation. In the case of the companies owned by the state, it projects the operation of a so-called four-week rolling liquidity planning system.

33 Nvtv. § 3 (1)
34 This aspect appears in the Nemzetivtv. among others in: 8. § (1), 12. § (13)
35 See European Court of Justice C-368/10 European Commission – Dutch Kingdom case
36 Available at: www.mnvzrt.hu/vallalatiranyitasi_ajanlasok/vallalatiranyitasi_ajanlasok.html

Primarily, the collection of recommendations reinforces the stream of information towards the leadership of the company; it provides alternatives for the management on liquidity-problems, and cornerstones to elicit the selection of proper investment options, given a liquidity surplus.

3.2. The place of the recommendations among the Hungarian corporate government requirements

The Hungarian rules of law prescribe business associations registered on the regulated market to publicly disclose their corporate governance affidavit. Act LII of 2007 incorporated the mandatory preparation of a corporate governance report into the corporate law, which has been upheld by the Civil Code as well. The board of directors of the publicly traded joint stock company is mandated to present the report, exposing the corporate governance practice followed by the joint-stock company, which is compiled in the format prescribed for the participants of the given stock exchange, to the annual ordinary general assembly, the approval of which shall be decided by the general assembly. The provision of the general assembly along with the approved report is mandated to publicly disclose on the website of the joint-stock company.[37]

Then the public disclosure of the corporate governance affidavit was also incorporated into the Accountancy Act – in line with the obligation on the harmonisation of law in the European Union [38] – as regards such entrepreneurs, whose tradable stock-papers have been entered in the regulated market of a state within the European Economic Area.[39]

Besides the corporate governance affidavit, the decrees of the corporate law on the rules of public disclosure were complemented in a special field in 2009, that was: the remuneration, as the publicly-traded joint stock companies entered into the regulated market, were obligated to publicly disclose on an annual basis on their website, at the time of summoning the annual ordinary general assembly, the names of the directorship or the board of directors and, where applicable, also the names of the members of the supervisory-board, along with all monetary and non-monetary remuneration allocated to the members by their membership quality, in a way itemized by member and legal title of remuneration, and in a detailed format. In addition, the joint stock companies had to ensure continuous access to all such data on their websites as well.[40] The rule has been amended by the Civil Code, and the new norm delegates the due definition of the principles upon the long-term remuneration and incentives' system to leading officers, members of the supervisory-board and management employees, into the exclusive competence of the general assembly.[41]

37 Act IV of 2006 on business associations (hereinafter: Gt.) § 312 (1)–(2), Civil Code. § 3:289, which is a cogent rule.

38 Act CXXVI of 2007, having served the compliance with the directive 2006/46/EK.

39 Act C of 2000, § 95/B (1)–(3)

40 Gt. § 312/A

41 Civil Code § 3:268 (2)

The corporate governance affidavit is to be prepared on the basis of the Hungarian Corporate Governance Recommendations (FTA) issued by the Budapest Stock Exchange in 2004, for the first time. The FTA touches upon four topic-areas: (1) the rights of the shareholders and the respective procedures, (2) the competence of the directorship/ board of directors, and the members of the supervisory-board, (3) the committees, (4) transparency and public disclosure, and the respective recommendations and guidelines. The introduction of the recommendation declares that the alignment with the prescriptions of the document is advised, yet non-mandatory.

According to the FTA, the companies are ordered to report their governance practice in two ways. The first part of the report must supply a comprehensive elaboration on the corporate governance applied in the targeted business year, also marking the instances of any incidental peculiar circumstances with that. Thereafter, an announcement must be made upon the compliance with the points of the FTA, in a manner identical with the international practice: a public statement is to be given based on the comply or explain principle. This means that whereas the compliance with the recommendation of the FTA must not, yet the incompliance must be well explained, however, there is no obligation for any explanation regarding the guidelines. The code was significantly revised in 2008, the amendments of which gained force on 16 of May, 2008. The code was then revised in November 2012, again, but this time no relevant, comprehensive changes were drawn.

In the case of the FVA, the recommendation stays unresponsive in this matter. However, we have not traced any references as to whether the companies should issue any form of a statement regarding what is covered by the collection of recommendations. Thus, the question remains open as to what is the form, in which the company may be expected to give an account, and can issue a public statement.

3.3. The guidelines of Responsible Corporate Governance Recommendations (FVA)

The regulation occurs on three levels. Corresponding to the OECD principles is that every single chapter starts with a main principle, expressing the reason why the regulation at all occurs, why the given topic, at all, must be regulated and what are the major requirements of it content-wise. Alongside the main principles, recommendations and suggestions can be found in a segregated format from each-another.

The international practice on the deviation of the regulation can thus be traced back to which rules are to be deviated from, and in the case of which is it possible to explain. This is the principle, in adherence to which the recommendations and guidelines segregate from each-another, however, also the regulation system of the Civil Code, of the Accountancy Act, and that of the FTA conform to this. The FVA clarifies distinguishing via the principle that the recommendations are generally to be abided by, and that the guidelines are to be abided by, in alignment with the individual characteristics and size of each company, whereas the rules of the FVA cannot be fitted in on this scale. The issuance of the affidavit is entirely missing (without even any respective references in the text), thus, in our view, there is no point in the making of any distinction in terms of the regulation. The difference

is demonstrated by every single recommendation in essence identifying either a general principle or a specific rule.

The purposes of the FVA are congruent with the international trend that focuses on the enhancement of the efficiency of corporate governance, embraced by its constant development.[42] One of the reasons why the operation of the companies in public ownership is crucial is that a decisive part of the GDP is produced by them, and as they are actively involved in employment. In addition to this, we can note that public companies must stand for setting the example, in other words they can serve as a model in terms of the best practices. The FVA expresses that the efficient and transparent governance of the companies also occurs as an intensifying social expectation. They shall set appropriate objectives alongside the precedence of corporate and ownership interests, and achieve them throughout efficient inspection. These factors obviously increase their value as well.

Beyond these, the FVA declares further objectives and principles, which are held to be abided by, as regards the entirety of the collection of recommendations:[43]

– The cooperation of the stakeholders of the company
– The transparent, as well as allocated management directorship responsibilities
– To increase the proprietary value
– The protection of the interests of minority shareholders
– The principle of the accessibility of information and publicity
– The accessibility of information provided for the owners
– The principle of the protection of corporate property
– The principle of sustainable value-creation
– The principle of sustainability

The concept of the principles complies with the construction of the corporate governance requirements assumed classic by the OECD. Two motifs deserve highlighting: one of them is that information is a merit, as the key-element to the efficient operation of the company is also conceived separately. This bears relevance, as it appears among both the OECD principles and the specific principles directive to state-owned companies as well, although not in an equally privileged place. The other is that the FVA can be considered as a blended-type of a code with respect to its topicality, as both sustainable value-creation and sustainability can be considered as forming part of corporate social responsibility, and not responsible corporate governance.[44] Yet, sustainability is one particular objective, which is only accomplished through the sufficient application of corporate governance, and in this given form, it may be considered as the ultimate objective of the collection of recommendations.

42 FVA Introduction
43 FVA chapter no. II.
44 Cf. Auer Ádám (2012): A felelős társaságirányítás és a vállalatok szociális felelősségvállalásának fejleményei az Európai Unióban I–II. *Céghírnök, 2012/6. 9–12. and 2012/7. 12–14.*

3.3.1. The effect and the target of the recommendation

The FVA affects the companies owned by the state, comprising the endowed property of the MNV Zrt. and within this the public limited joint-stock companies and the limited liability companies.[45] Within the circle of economic organizations operating through state or municipality involvement, as explained previously it results from constitutional rules, it can be deduced that we shall separate the state-sector from the municipality-sector. Our standpoint is that even though sharp as the separation is, the ownership nature (public property) in itself does not automatically draw the equivalent analogy that the requirements of responsible corporate governance should or could be separated still. In the following, we shall deem it as quintessential, that the principles are equally applicable to the companies operating with municipality-shareholding, as a predominant rule.

3.3.2. The organization structure of the company

Complying with the OECD principles, the FVA describes *the shaping of the decision-making system of the company* as a main criterion.[46] At the establishment of the decision-making mechanisms, central merits are defined that are mandatory to be recognized during the course of the actual operation and the shaping of the organization. Such nominated interests and principles are the preservation of the state-property, the security of proprietors' investments, the protection of the value of the company, the clear division of responsibility and duties. These are general rules, which must be taken into account in general at the establishment of specific regulations.[47]

The key-factor to the efficiency of decision-making is the treatment of information. At the shaping of the organization system, the regulation on traceability must be implied. Consequentially, every underlying process to each decision-making instance can be reconstructed, and this counts as a key-question in regard to whether the company can be inspectable and accountable.

3.3.3. The undertaking of the state as the proprietor

According to the OECD principles, we have specifically outlined that the state must exercise its proprietary, regulative and commissioner's role-undertakings independently from one another. The same principle has also been adopted by the FVA as a central phenomenon.

The FVA imposes declarations on the summoning of the general assembly and its conduct, and also on the pursuing of the proprietorship rights and the operation of the directorship and its standing orders under separate titles. The FVA complies with the formerly settled general principles in this respect, as per which a proper flow-of-information must be

45 FVA chapter no. III.
46 FVA chapter no. V. 1-8
47 *Ibid.*

provided in-between the individual organs, shareholders.[48] The competence of the chief organ is declared in an exhaustive manner, related to which it can be constated that the replication of the exhaustively set prescriptions of acts may be dismissed, as it is applicable without any separate declaration.[49] Yet on the other hand, the FVA imposes further volumes of competence on the chief organ that are unrecorded by separate acts of law. The approval of a medium-term business, operational and organizational strategy is an example of this.[50]

The FVA imposes declarations on the *management* under a separate title. This has an outstanding relevance, and as in the framework of the material on corporate law regulations they do not clearly demarcate from each other. The Corporate Governance Recommendations of the BÉT (Budapest Stock-Exchange) also adapts a differentiated approach in terms of the management, as it demarcates between the fulfilment of duties as of the management directorship and the management. This option is also implicitly included in acts of corporate-law; nevertheless, it is not unambiguously conspicuous by the reading of the norms.[51]

As a result of traceability and demarcation, the shaping of the internal regulation occurs as a central principle to the system of the FVA, more precisely that the duties, competences and procedures of each organization must be demarcated and segregated in accordance with the duties.

3.3.4. The inspection of the companies

Inspection belongs to the basic corporate functions. The fact that this must be attributed to a superior value within the circle of economic entities operating through state involvement, does not demand any special explanation. Several types and forms of inspection can be distinguished. Some of these do not require any regulation by either corporate or a separated set of regulative rules, whereas a particular type of a controlling form can be observed which can undergo external inspection, or maintains the same internally in the company. Beyond this, we can also categorize on the basis of whether this originally is the duty of the organ of the company, or if it only exercises inspection complementarily.

The FVA acknowledges the next forms of inspection[52]
1) supervisory board
2) independent internal auditorship
3) management directorship
4) MNV Zrt.

48 FVA chapter no. V. points 15, 17

49 Such as at rule no. 24 points a), b), c), e), f); or in terms of management directorship no. 39 q)

50 No. 24. l)

51 The Civil Code is non-inclusive of this, either at the legal person's or at the economic company's common ground rules, and neither specifically in the chapter on joint-stock companies. To the earlier corporate law, the "Gt." see: Kisfaludi András – Szabó Marianna szerk. (2008): *A gazdasági társaságok nagy kézikönyve.* Budapest, Complex, *334–335.; Sárközy Tamás szerk. (2009): Társasági törvény 2006–2009. Budapest, HVG-Orac. 45.*

52 FVA chapter no. VI.

5) controlling
6) book-auditor

1. In terms of the supervisory board, the FVA exposes recommendations with respect to what role the supervisory board should fulfil in the life of the company. In this configuration, it can be considered a special form. Acts of corporate law prescribe partially assigning it to the decision of the company, if it introduces a supervisory board. However when it determines such perviously mentioned circumstances this type of an inspection organ is mandatory to formulate. Beyond these, Act CXXII of 2009, prescribes it as mandatory to formulate in every company of the majority's proprietorship.
2. In terms of independent internal auditorship[53] the FVA is briefer, as it only regulates the basic interrelations between the supervisory board and the management directorship. In this respect the FTA is setting an example, as it supplies the company with a comprehensively applicable model-regulation.
3. In terms of the management directorship, not a primary but a secondary role is meant by us when commenting upon the duties of the management directorship in the matter of inspection. The management directorship pursues an inspective duty regarding information-supply and information-flow.

In terms of points 4)–6) it is a peculiarly public-property feature that brings on the peculiarity of the inspection form by drawing the book-auditor's inspection into this sphere, which can indeed be considered a classic form of external inspection.

The FVA regulates a broad range of internal inspection activities within the company, both by organizations and procedural types. The listing of various organs in the same place does facilitate in itself the construction of responsible corporate governance. Yet it must be emphasized that the most important feature of this chapter, we believe, consists of rules to carry model-quality, based on which the inspection of an efficiently operating organization can be constructed and shaped. The operational mechanisms of the individual organs along with the variety of the options available (for instance, what sorts of transactions, what types of decisions must the inspection cover) shall present guidance to companies, that could only access and adapt this volume of information by the utilization of heavy resources.

3.3.5. Personnel policy and conflict of interest rules

In our view, alongside the internal organization guarantees, exceptional attention is to be devoted to human resources recruitment and the assessment of personal and professional competencies. This bears a peculiar value in the case of companies in public proprietorship, thus it shall be highlighted as well as endorsed that the FVA includes the respective recommendations in a separate chapter.[54] Human resources management plays a vital role.

53 Here, the FTA issues a comprehensive model rule.
54 FVA chapter VIII.

In the course of exercising the proprietor's right and the activity of property management, such duties shall just as well be executed, to which human resources management is indispensable, and according to the FVA, it is the functions of incentive-management, selection, and performance-evaluation.[55] The recommendation is inclusive of the criteria to apply at the selection of leadership candidates, remuneration rules and policy,[56] it elaborates on the professional and personal requirements of the chief leader.

It is remarkable that it extends conflict of interest rules over to leadership employees. Beyond this, directive rules on personnel policy also cover *related parties' transactions* (in-between connective parties) and special requirements, directive to the members of the supervisory board.

3.3.6. Transparency and disclosure

Transparency and disclosure are the most highly accentuated areas of corporate governance. Within the field of economic organizations, operating through state-involvement it carries a duplex value. On the one hand, transparency forms a significant part of corporate governance, since one of the guarantees for keeping the non-mandatory recommendations is ensured by publicity. This of course presupposes the consciousness and the objectivity of investments, whilst the raising of the idea is not dismissible, that public appearance can mean a sort of a conscious discipline to the company. On the other hand, transparency in terms of state-companies is a fundamental constitutional requirement (for example in connection to the right for the knowledge on data of public interest).

In accordance with the FVA, the following must be covered by public disclosure:

- the objectives of the company,
- the results of the activity, and of the management of the company,
- the remuneration and refunding policies of board-members and members of the management
- the full set of relevant information on the employees and other stakeholders,
- the corporate governance practice, and the structure of the corporate governance system,
- the ownership structure.[57]

55 FVA chapter VIII. Introduction

56 Which is regulated in a detailed manner by the remuneration rules of the MNV Zrt. Moreover, Legal Act no. CXXII as per 2009, § (2) the directive on economic companies in terms of prescribing mandatory publicity of the remuneration of leading officials, supervisory board members, leadership employees and also employees entitled to individually exercise company registry right, or the right to the treatment-decision on the bank account.

57 FVA 187.

4. SPECIFIC PRESCRIPTIONS

Regarding the regulation of state-owned companies, it can be established that for these companies also, it is the Civil Code and not special norms, that are to be applied in general.[58] We can also assert that to complete any public assignment, to provide any public services may be demonstrated in accordance with the general (Civil Code) regulations and the specific prescriptions are to be applied as a directive only to the organization of state-owned companies.[59]

The corporate governance has relevance at state-owned companies in both intern (a) and extern (b) relations:

– how the principles of corporate governance can be effective at the economic organizations founded by state or by local government (see OECD Guidelines on Corporate Governance of State-owned Enterprises 2005, focused examination by Worldbank Group and Act CVI of 2007, on state property in Hungary);
– how the state or the local government contracting party can be (see the aspects in tax law and public procurement in Hungary).[60]

Neither the Hungarian Civil Code,[61] nor the Recommendations of the Budapest Stock Exchange for Corporate Governance of Public Company Limited by Shares 2012, contain special provisions for economic enterprises owned by state or by local government. However, the MNV Zrt. has Recommendations for Corporate Governance of Enterprises Owned by State or Local Government, with principles for lawful operation of these companies.[62] The special regulation for state- (or local government)-owned companies can be basically found in two acts: Act CXXII of 2009 on more economical operation of state-owned companies and Act CXCVI of 2011 on national assets.

In the following, we describe the special rules of these two acts for the enterprises of state and local governments on the base of seven aspects.

58 Zoványi Nikolett (2015): *Kié a felelősség? A társasági jog útvesztőiben.* (Who is responsible? Public enterprises in the labyrinth of company law) Source: www.kozjavak.hu/hu/kie-felelosseg-kozvallalatok-tarsasagi-jog-utvesztoiben (2015. 12. 18.); Fézer Tamás (2016): *Két úr szolgái – a közvállalatok vezető tisztségviselőinek felelőssége.* (Servants of two gentlemen – the liability of executive officers of public enterprises) Source: www.kozjavak.hu/hu/ket-ur-szolgai-kozvallalatok-vezeto-tisztségviseloinek-felelossege (19 February 2016)

59 Papp Tekla – Auer Ádám (forthcoming): Group Interest in Hungary. *Acta Universitatis Sapientiae* (Manuscript)

60 Auer Ádám (2015): *Corporate Governance. Állami részvétellel működő gazdálkodó szervezetek.* (Corporate Governance, Economic Organizations Participated by State) Budapest, *NKE. 13.,41.;* Auer Ádám (2015): *Corporate Governance az állami vagy önkormányzati részvétellel működő gazdálkodó szervezetek esetében.* (Corporate Governance at the Economic Organizations Participated by State and Local Government) In Lentner Csaba szerk.: *Adózási pénzügytan és államháztartási gazdálkodás.* Budapest, NKE. 811–812.

61 Act V of 2013

62 Auer 2015a, 58–68.; Auer 2015b, 816–824.

1. Special prohibitions of further association

Such companies owned in 100% by state or local government, which were founded to perform public duties, must not establish another company for these public duties.[63] The state and local governments must not found such companies and must not receive a share in companies which are not transparent.[64] A non-profit company with majority control of state/local government is permitted to create another non-profit company with majority control of state/local government – apart from recycling activity –, but this new non-profit company must not establish further companies.[65] These provisions also have to apply to the acquisition of shares in other business associations by enterprises owned by state or local government.[66]

2. Special issues relating to assets

The share of companies providing public service and with majority control by state may be available as contributions in kind or on the ground of other transferring legal title only for companies owned in 100% by state/local government.[67] The share of companies providing public and parking service, with majority control of local government and of Balaton Shipping Private Company Limited may be available as a contribution in kind or on the ground of other transferring legal title only for companies owned in 100% by state/local government.[68] This means the limited transferability of shares of state/local government in companies. The share in companies owned by state/local government must not be an object of assets management;[69] it means limited legal title and legal base of privity. In connection with the share in companies owned by state, which is a part of national assets and important for the national economy, only the minister thus appointed, or a central budgetary agency or an economic enterprises owned in 100% by state may exercise the owner's rights;[70] it means a limited circle of exercisers of proprietor's rights. To increase capital in a company owned more than 50% by state/local government they must reduce the proportion of state/local government and have:

– the consent of the exerciser of owner's rights is necessary,
– over 2 000 000 HUF , and the resolution of the government of Hungary or municipal council is required,

63 Act CXCVI of 2011 §8 (6)
64 Act CXCVI of 2011 §8 (1)
65 Act CXCVI of 2011 §8 (8), (9)
66 Act CXCVI of 2011 §8 (1), (8), (9)
67 Act CXCVI of 2011 §4 (6)
68 Act CXCVI of 2011 §5 (8)
69 Act CXCVI of 2011 §8 (7)
70 Act CXCVI of 2011 §7/A (3)

– between 5 000 000 HUF, and 2 000 000 000 HUF, the resolution of the minister responsible for supervision of state assets, or the municipal council, is needed;[71] it means limited and controlled capital movements.

In the name of the state MNV Zrt. and the Hungarian Development Bank Private Company Limited by Shares may give credits and loans to the companies with majority control of state.[72]

The reasonable undertaken business risks are determined by company activity and its background, the market surroundings.[73]

In Poland, the ownership rights in state-owned companies were centralized in one organization, the Ministry of Treasury, which was dismissed by the prime minister in September 2016.[74] Lithuania has a decentralised SOE ownership structure, with twelve ministries.[75] In Romania, there is neither single ownership entity: beside the Authority for Administration of State Assets several authorities, and ministries have ownership function.[76]

3. Special rules of organization

Among the state-owned companies, and private limited companies, the operative organ usually is the general manager and if the importance, size, type of operation of the company is explained, then the operative organ is the board of directors (with 3–5 members).[77] The legislator allows only the two-tier/dualistic system, but not the one-tier/monistic system for organization of state-owned companies;[78] the same can be found in Poland, Czech Republic,[79] Serbia[80] and Lithuania, but the one-tier organizational system is allowed

71 Act CXCVI of 2011 §8 (10)

72 Act CXCV of 2011 § 45 (1)

73 Fézer 2016.; BH 2004. 372.

74 Zaleska-Korziuk, Kaja: *Report on corporate governance in state-owned enterprises – the Polish perspective.* Presentation "Corporate governance of state-owned enterprises in Central and Eastern Europe"; 14 October, 2016.; Budapest; National University of Public Service and Societas CEE Company Law Research Network

75 Juchnevicius, Edvardas: The corporate governance of state-owned enterprises in Lithuania. Presentation "Corporate governance of state-owned enterprises in Central and Eastern Europe"; 14 October, 2016.; Budapest; National University of Public Service and Societas CEE Company Law Research Network

76 Veress Emőd: *The state's role as owner of enterprises: mandatory rules of corporate governance in Romania.* Presentation "Corporate governance of state-owned enterprises in Central and Eastern Europe"; 14 October, 2016.; Budapest; National University of Public Service and Societas CEE Company Law Research Network

77 Act CXXII of 2009 §3 (1)

78 About this see more details in Papp Tekla (2008): Corporate governance – felelős társaságirányítás. (Corporate Governance – Responsible Guidance of Companies) *Acta Juridica et Politica,* Tomus LXXIII, Fasciculus 1–64. 639–653

79 Eichlerova, Katerina: *Corporate governance of state-owned enterprises in the Czech Republic.* Presentation "Corporate governance of state-owned enterprises in Central and Eastern Europe"; 14 October 2016.; Budapest; National University of Public Service and Societas CEE Company Law Research Network

80 Malagurski, Branislav: *Challenges of Serbian public enterprises in the light of points II C and F of OECD Guidelines on corporate governance of state-owned enterprises.* Presentation "Corporate governance of state-owned enterprises in Central and Eastern Europe"; 14 October 2016.; Budapest; National University of Public Service and Societas CEE Company Law Research Network

in Romania.[81] According to the Austrian Public Corporate Governance Code, the state-owned companies with more than 30 employees or with more than 1 million euro turnover shall have a supervisory board consisting of state elected members.[82] In the state-owned companies in Hungary it is obligatory to form supervisory boards with 3 members (over 200 000 000 HUF between 3 and 6 members).[83]

4. Special provision for decision

At the companies with majority control of state/local government, the competence of supreme body includes the foundation, the termination of economic association, the acquisition and the transfer of shares in economic association.[84]

5. Special prescriptions for remuneration

The state-owned companies have to create a regulation about the mode, measure, principles and system of allowance of executive officers and of the members of the supervisory board;[85] non-compliance with this regulation is prohibited and unlawful.[86] The executive officer and the member of the supervisory board may receive remuneration only in one state-owned company, compared to the current minimum wage (sevenfold of current minimum wage for the president of the executive board, fivefold of current minimum wage for members of the board of directors, fivefold for the president of supervisory board and threefold of current minimum wage for members of supervisory board). [87] In Poland, there is a similar situation, namely the remuneration of executives equals the index of an average monthly wage in state-owned enterprises as of the last quarter of the previous year announced by the Central Statistical Office, at small state-owned enterprises multiplied by one to three, at the largest state-owned companies multiplied by seven to fifteen.[88]

81 International workshop: "Corporate governance in state-owned companies", 11. 04. 2016., Gdańsk, University of Gdańsk, Faculty of Law and Administration, Societas CEE Company Law Research Network

82 Winner, Martin: *Autonomy and Independence in SOEs.* Presentation "Corporate governance of state-owned enterprises in Central and Eastern Europe"; 14 October 2016.; Budapest; National University of Public Service and Societas CEE Company Law Research Network

83 Act CXXII of 2009 §4 (1)

84 Act CXCVI of 2011 §8 (14)

85 Act CXXII of 2009 §5 (3)

86 Act CXXII of 2009 §5 (4)

87 Act CXXII of 2009 §6

88 Gliniecki, Bartlomiej: *Current fundamental changes of the boards members' remuneration in Poland.* Presentation "Corporate governance of state-owned enterprises in Central and Eastern Europe"; 14 October, 2016.; Budapest; National University of Public Service and Societas CEE Company Law Research Network

6. Special regulation of transparency

The state-owned company shall publish the name, the function and the allowances of its executive officers and of its supervisory board members.[89] The head of the state-owned company shall be liable for the publication of these data, for its continuous availability and for the authenticity of publication.[90]

7. Special shareholder's rights

For the state-owned company providing fundamental services, the state may exercise the right of option to purchase shares, which are not its property in the interest of safety of supply, of supplying duties, of increasing efficiency, of national economic strategy.[91] Any shareholders at the state-owned company may request that the shareholder exercising the right of option to purchase shall buy his shares (the selling right).[92] These rights are obligatory and pecuniary rights, not rights in accordance with exercise of classical member's rights.

8. Special accounts requirements[93]

The public enterprises have to separate the state subventions in their internal accounting. The public enterprises must keep a record of the dividend, the financial benefits and the waiver of recovery of used state monetary assets. The public enterprises, whose net revenue exceeded 250 million euro in the previous business year, shall send to the competent revenue office within six months from the closing of the business year

– their account (with the balance sheet report),
– business report,
– statement about accounting policy,
– reports of executive officers,
– data about own shares, own business shares, preference shares, priority bonds,
– data about not-repayable supports, loans, guarantees,
– data about the paid-out dividends and the held-back profit,
– data about any kind of state intervention.

In Serbia, the State Aid Institution is legally obliged to conduct annual audits of state-owned companies.[94]

89 Act CXXII of 2009 §2 (1)
90 Act CXXII of 2009 §2 (1)
91 Act CXXII of 2009 §7/A (1)
92 Act CXXII of 2009 §7/F (1)
93 On the ground of 3009/2012. NAV útmutató (Guide of the National Revenue and Customs Office)
94 Malagurski, Branislav: *Challenges of Serbian public enterprises in the light of points II C and F of OECD Guidelines on corporate governance of state-owned enterprises.* Presentation "Corporate governance of state-owned enterprises in Central and Eastern Europe"; 14 October 2016.; Budapest; National University of Public Service and Societas CEE Company Law Research Network

9. Acceptance of discharge state duties of state-owned companies by central budgetary agency

The central budgetary agency may take over the discharge state duties from the companies owned in 100% by the state, then the concerned company must be terminated and for the debts of terminating company there is no liability of company's member (according to the Civil Code).[95] At the time, the point of acceptance of the discharge of state duties concerning the assets in the property of a company owned 100% by state devolve to the state and the trusteeship is due to the central budgetary agency.[96] Likewise, the point of acceptance of the discharge of state duties in the central budgetary agency is the successor of all rights and commitments of the company owned 100% by state.[97]

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The Hungarian regulation on state and self government owned companies are theoretically in keeping with OECD Guidelines, but not so detailed and comprehensive. The above discussed provisions are not so transparent and too general, *we – the outsiders – do* not have enough information on how these rules operate in practice in Hungary…

95 Act CXCV of 2011 § 11/A (1), (1a)
96 Act CXCV of 2011 § 11/B (2)
97 Act CXCV of 2011 § 11/C (1)

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Kateřina Eichlerová

CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES IN THE CZECH REPUBLIC

Comparison of Corporate Governance of State Enterprises and Business Corporations

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The author is interested in the comparison of state enterprises and joint-stock company with state participation, as both are types of state-owned enterprises. The author concludes that the state unjustifiably favours state enterprise.

Keywords:
company law, business law, corporate governance, state-owned company, Czech Republic

This paper discusses the legal regulation of the participation of the Czech Republic in legal entities focused on business and an appreciation of the legislation and practice from the perspective of OECD recommendations for entities with state participation as revised in 2015.[1] For the purposes of this article, we define an enterprise with participation of the state as a legal entity whose primary, but not sole, purpose is business, and in which the state has participation. The concept of an enterprise with state participation in this article follows the concept of enterprise under European law, but it is a subcategory which is also characteristic of legal personality, in addition to the state's participation.

Firstly, let us explain the system the state uses for the organization of state property. In basic classification, we can distinguish state organizational units and state organizations. The state organizational units do not have legal personality; they are only the internal division of the state, but with their own name, registered office and competences. Some of them are individual accounting units. They do not own property. They act on behalf of the state. Examples are ministries, other administrative offices, courts, etc.[2] On the other hand, state organizations have legal personality but they differ from other legal entities that do not have their own property, but manage state property. Under state organizations, we can include semi-budgetary organizations[3] and state enterprises.[4] While the primary purpose of the state enterprise is business, it is not as much for the semi-budgetary organization as for the other kind of state organization. Although these may also be involved marginally in the business, their primary mission is yet another: the fulfilment of public interest, e.g. the operation of schools, nurseries, hospitals, museums, theatres, etc. As legal entities of private law, they are closer to being institutes.[5] The nature of a state-owned enterprise is not only state enterprise but also business corporation with the majority participation of the state; but this cannot be classified as a state organization. We can speak of them both together as state-owned enterprises.[6] They are only the subcategory of state-owned entities, among them, we can reckon all listed above entities, i.e. state organizational units and state organizations.

1 OECD Guidelines on Corporate Governance of State-Owned Enterprises [available from www.oecd.org/corporate/guidelines-corporate-governance-SOEs.htm]

2 In detail: Plíva 2001, 8. Also Bakeš 2005, 139.

3 In detail: Mitwallyová 2014, 772 et seq.

4 In detail: Plíva 2001, 18.

5 Civil law divides legal entities into three basic types: corporate, foundation and institute. An institute is defined as a legal entity created for the purpose of pursuing socially or economically useful activities using its personal and property resources. An institute pursues activities the results of which are equally available to everyone under predetermined conditions (sec. 402 Civil Code).

6 Theoretically, we can imagine that the nature of the state-owned enterprise will also be a semi-budgetary organization in a particular case.

In short, state-owned entities are state organizational units,[7] state organizations,[8] including state enterprises[9] and business corporations.[10] Only a part of them can be described as state-owned enterprise. We can still come across as state-owned enterprise which is a national enterprise. A specific case of a legal entity as a national enterprise is Budějovický Budvar, n. p.[11]

How can we define a state-owned enterprise? There are three regular characteristics: 1. economic activity, 2. public policy objectives and 3. ownership and control of the state. Economic activity shall be the main purpose of existence, not only an additional purpose which we can recognize in some semi-budgetary organizations. Economic activity does not mean that its subject matter shall be only business, i.e. the purpose is only achieving profit. Economic activity is included and provision paid services given to the public. The public policy objectives can or cannot be given. The public policy objectives are not a necessary condition for inclusion among state-owned enterprises. This qualifying characteristic is declared, for a state enterprise, in the State Enterprise Act. But it is mostly absent in a joint-stock company with state participation. We can say that between economic activity and public policy objectives there is an indirect relation. The more the state-owned entity focuses on economy activity the more the importance of public policy objectives decrease. And vice versa, the more the importance of public policy objectives increase the more the state-owned entity is dependent on the state budget.

The last characteristic of state-owned enterprise is the ownership of the state.[12] The ownership and control by the state can be direct and indirect. State enterprises and business corporations with state participation can found and participate in other business corporations. The problem is that the state's attention, as owner, is paid only to direct state-owned enterprises and not to indirect state-owned enterprises. While directly-owned enterprises have a stricter regulation, indirectly-owned enterprises have a paradoxically freer regime. For example, the approval of the state as founder is required for many kinds of acting by state enterprise.[13] But when a state enterprise establishes a limited liability

7 Their position in the management of state property is regulated in the Act no. 219/2000 Coll. on Property of the Czech Republic as amended (State Property Act). The questions regarding rules of economy are regulated in the Act no. 218/2000 Coll. on Budget rules as amended (Budget Rules Act).

8 Their position in the management of state property is regulated in the Act no. 219/2000 Coll. on Property owned by the Czech Republic as amended (State Property Act). Questions regarding rules of economy are regulated in the Act no. 218/2000 Coll. on Budget Rules as amended (Budget Rules Act).

9 State enterprises are regulated in the Act no. 77/1999 Coll. on State Enterprise as amended (State Enterprise Act). This article reflects the valid wording after the last amendment by Act no. 253/2016 Coll., which will become effective on 1 January, 2017.

10 Business corporations are regulated in Business Corporations Act (Act no. 90/2012 Coll.) and Civil Code (Act no. 89/2012 Coll.). The state can be a founder only of a joint-stock company (sec. 28 State Property Act). For specific conditions the state can acquire participation in other forms of companies, but not by foundation.

11 Budějovický Budvar, n. p. is an important producer of beer. The reason for the unmodified form of this legal entity and conservation originating from the period of socialism is the fear of weakening rights to trademarks, which form a significant part of the value of the business enterprise.

12 Also counties and municipalities can own enterprises. They can establish their own semi-budgetary organizations and business corporations without any legal limitations. They cannot set up a state enterprise because a state enterprise can be established only by the state.

13 Sec. 17–17e State Enterprise Act.

company, then this company is not under this strict regulation. The difference is also this: for the foundation of a business corporation, the state represented by ministry needs the approval of government and the state can only establish a joint-stock company.[14] However, only the approval of the ministry is required for foundation of business corporation by state enterprise and there is not any restriction on choice of forms of business corporations.[15] In both cases the state assets for foundation are used. These differences are not reasonable and justified. The question is if the state enterprises shall be titled as a founder of business corporations. De lege lata it is possible. But de lege ferenda it might be considered whether a better solution is to be prohibited or to set the same conditions, as in the case of the foundation of a business corporation directly by the state. In the case of the participation of the state in a joint-stock company, we can consider another problem. A joint-stock company with state participation can construct a complex structure of a group of companies but the state as a "final owner" is not in the same position as head of the group of companies as it would be if somebody else would be in its position. The reason in question is whether the state can be qualified to be a directing person.

If we look at more important entities with state participation from a substantive point of view, we find that they hold an important place in the national economy, namely in transport (České dráhy, a. s.,[16] Řízení letového provozu, s. p.,[17] Český Aeroholding, a. s.[18]), in the energy sector (ČEZ, a. s.,[19] ČEPS, a. s.,[20] OTE, a. s.,[21] ČEPRO, a. s.,[22] MERO ČR a. s.[23]), in the financial sector (Česká exportní banka, a. s.,[24] Českomoravská záruční a rozvojová

14 Sec. 28 para 1 State Property Act.

15 Sec. 17a para 3 State Enterprise Act.

16 The national railway operator is a joint-stock company (addition in business name is a. s.). The state is a sole shareholder.

17 The air navigation services operator is a state enterprise (addition in business name is s. p.).

18 A holding company manages four subsidiaries operated in air transport, namely the operator of Prague Airport, Czech Airlines etc. The state is a sole shareholder.

19 The most important company in the energy market with many subsidiaries (operator of many power plants, including the two nuclear power plants Temelín and Dukovany). The state owns 69% shares.

20 The operator of Czech transmission system. The state is a sole shareholder.

21 The Czech electricity and gas market operator. The state is a sole shareholder.

22 The company is engaged in transportation, storage and sale of petroleum products. The state is a sole shareholder.

23 The owner and operator of the Czech section of the Družba crude oil pipeline and the IKL crude oil pipeline, is the only transporter of crude oil into the Czech Republic and the most important company ensuring storage of strategic emergency crude oil reserves. The state is a sole shareholder.

24 Specialized bank for state support for export. The state owns 84% shares directly and 16% indirectly through Exportní, garanční a pojišťovací společnost, a. s.

banka, a. s.,[25] Exportní, garanční a pojišťovací společnost, a. s.,[26] Státní tiskárna cenin, s. p.[27]), in agriculture (Lesy ČR, s. p.,[28] Povodí Vltavy, s. p.,[29] Povodí Labe, s. p.,[30] Povodí Ohře, s. p.,[31] Povodí Odry, s. p.[32]) or in society in general (Česká pošta s. p.[33]).[34]

State participation in business is indirectly affected through joint-stock companies and state enterprises.

To differentiate these entities with state participation sufficiently, let us first examine what is the same and what is different for such legal entities.

A joint-stock company is regulated by the Civil Code and the Business Corporation Act, in specific cases as well as by other laws (e.g. in business on the capital market). A state enterprise has its own regulation in the State Enterprise Act, with subsidiary use of the Civil code provisions related to legal entities generally.

It is typical for joint-stock companies and state enterprises to be incorporated upon registration in the Commercial Register. The consequence of registration is very important because it means that state enterprises and joint-stock companies are in a position as an entrepreneur in all legal relations. The law therefore puts them under specific rules, e.g. stricter requirements,[35] giving them weaker protection,[36] creating a wider framework for the exercise of freedom of contract for them.[37] The purpose of the state enterprise is always business but a particular business which has given rise to major strategic, economic, social, national security or other interests of the state (sec. 2 para. 1 State Enterprise Act). The goal of a joint-stock company may not always be business; a joint-stock company can be established for non-profit purposes. In fact, the state uses a form of joint-stock company only for business, not for the other purposes.

Let us try to categorize enterprises with state participation, depending on whether they are a form of enterprise accessible only to the state or not. Among the most important enterprises

25 Specialized bank is focused on providing assistance to small and medium-sized enterprises. The state is a sole shareholder but its shareholder´s rights are exercised by four ministries (ministry of finance, ministry of industry and trade and ministry of regional development).

26 A credit insurance corporation insuring credit connected with exports of goods and services from the Czech Republic against political and commercial risks is uninsurable by commercial insurance. The state is a sole shareholder but its shareholder´s rights are exercised by four ministries (ministry of finance, ministry of agriculture, ministry of industry and trade, and ministry of foreign affairs).

27 The state enterprise mainly provides the printing of banknotes, stamps, *securities etc.*

28 The state enterprise mainly provides the management of state-owned forests.

29 The state enterprise is an administrator of watercourses in the Vltava catchment area.

30 The state enterprise is an administrator of watercourses in the Labe catchment area.

31 The state enterprise is an administrator of watercourses in the Ohře catchment area.

32 The state enterprise is an administrator of watercourses in the Odra catchment area.

33 The state enterprise is a provider of the universal postal services.

34 Attachment no. 1 to the draft of an act on the choice of persons for executive and supervisory bodies of state-owned enterprises.

35 For example, we can state information obligation (s. 434 and 435 CC) or consumer contracts.

36 For example, we can state confirmation letter (s. 1757 CC), presumption solidarity obligation (s. 1874 CC) and exclusion of the possibility to require the contract to be cancelled at *laesio enormis* or invoke an invalidity of usury (s. 1797 CC).

37 For example, we can state commercial terms (s. 1751 CC).

with state participation in number, but also in size, include commercial companies and state enterprises.

Commercial companies as sub-legal entities primarily aimed at businesses are open in principle to all persons. For limited liability companies and joint-stock companies, special conditions for shareholders are not required. Both forms of these companies can be established by only one founder.

On the other hand, the state enterprise is a legal entity which may be established solely by the state. It cannot be founded by other public corporations such as the county or municipality.

A state enterprise differs from joint-stock companies in many ways. A joint-stock company has its own property, while a state enterprise does not have its own property, it has a right to manage state property entrusted to it or that is acquired by its activities.[38] The assets of the joint-stock company are separated from the assets of shareholders. Stock law contains rules, which ensure that their own resources cannot be distributed to shareholders to the detriment of creditors.[39] In a state enterprise it does not apply. State enterprise disposes of state property. The state has legal tools that put it in a better position with the creditors than a joint-stock company and its shareholders.[40]

We can distinguish state property in the managing of a state enterprise into two categories: indicated assets and the other assets. The indicated assets are specified in the Deed of foundation and registered in the Commercial Register. The state enterprise can dispose of them only with the previous approval of the state.

The state as a shareholder is not liable for the debts of the joint-stock company during its existence, after its termination it is liable for its debts up to the amount of their share of liquidation balance. The state is not liable for the debts of the state enterprise; neither is it liable for them after its termination.

In stock law, the protection of creditors is ensured by legal request to the creation of registered capital to the minimum amount. The same rule is absent in the legal provisions of state enterprise. Prohibition of undercapitalization is not stated as in other cases for the protection of creditors.[41] Theoretically, a state enterprise can be founded without any property. We can conclude that in the beginning of existence the creation of capital is mandatory in the joint-stock company and in the state enterprise it is voluntary.

In a joint-stock company, shares are a manifestation of equity investment. Shares are securities and as such subject to separate legal relationships. The state can dispose of shares which it owns. There is no manifestation of equity investment in shares or any other thing

38 From sec. 8 para 1 sub b) State Property Act implies that state assets could be used for business, not only for fulfilling state functions and providing public benefit activities.

39 For example, we can mention the prohibition of the return of contributions, the prohibition of the distribution of profit and the other resources in the case of the threat of bankruptcy.

40 For example, the state can decide on the transfer of property in the management of the state enterprise to another state enterprise, state organization or state organizational unit free of charge (sec. 17–17e State Enterprise Act).

41 In detail: Černá 2015, 183 et seq.

in the legal sense in the state enterprise. The reason is that only the state can be a founder, nobody else. The assets of a state enterprise may be privatized.[42] But there is a substantial difference. On privatization, the state enterprise is terminated. We can say that privatization is similar to a transfer of business enterprise in private relations. This means that the privatized enterprise is absolved from obligations of a public character (as taxes) and obligations of a private character in relation to the director and the members of the supervisory board of the state enterprise.

Other important differences are found in the organizational structure. A joint-stock company is entitled to choose between one-tier or two-tier structures. The member of its body can be a natural or legal person. The minimum number of members is not regulated. Codetermination is basically not required. A state enterprise creates only a two-tier structure. The executive body is a director. The controlling body is the supervisory board. The director is unipersonal.[43] The supervisory board is multi-personal.[44] Only a natural person may be a director or a member of the supervisory board.[45] One third of the supervisory board members are elected by employees.[46] The director and the members of the supervisory board of the state enterprise are obliged to exercise their functions with a duty of care and loyalty. But there is a difference in the space of responsibility. The State Enterprise Act reduces the responsibility of the director as if he was in the position of employee.[47] The same is substantially applied to the members of the supervisory board.[48] This moderation of duty of care cannot be considered as "commonly accepted corporate norms" as recommended by the OECD Guidelines.

If we look at the rules relating to representation – a legal person as a member of its body in a manner registered in a public register – the Civil Code generally sets the norm that no one may invoke that the legal person failed to adopt the necessary resolution, that the resolution was defective, or that a member of the body breached the resolution adopted (sec. 162 CC). For business corporations an exception is given in sec. 48 BCA from this rule for so called "legal limitation". Legal limitations mean legal acts to which the law requires the approval of the general meeting. The consequence of acting without approval is a possibility to request invalidity. Cases where the approval of the general meeting is required by law are few, e. g. sale or pledge of business or a substantial part[49] or the conclusion of a contract on silent partnership.[50] Next to legal limitations, we can distinguish internal limitations.

42 The process of privatization is mainly regulated in the Act no. 92/1992 Coll. on transfer of the state property to other persons as amended. A business enterprise managed by state enterprise may be subject to contribution into joint-stock company or subject to sale.

43 Sec. 12 para 1 State Enterprise Act.

44 Sec. 13 para 2 State Enterprise Act.

45 Sec. 13 para 3 State Enterprise Act.

46 Sec. 13 para 3 State Enterprise Act.

47 Sec. 12a para 2 State Enterprise Act.

48 Sec. 13 para 4 State Enterprise Act.

49 Sec. 421 para 2 l. m) Business Corporations Act.

50 Sec. 421 para 2 l. o) Business Corporations Act. In detail: Eichlerová 2015, 249 et seq.; Čech – Flídr, 2015, 9 et seq.

Internal limitations are only an internal request for approval by the other bodies (the supervisory board or the general meeting) given by the Articles of Association. A breach of these rules is not effective for third parties.[51] For state enterprises legal limitations are provided in sec. 16 of the State Enterprise Act. The scope of legal acts for which previous approval of the state as a founder under law is required is substantially wider than in the case of business corporations. Previous approval is required for the pledge of state property,[52] disposal of indicated assets,[53] acquisition of participation in legal persons,[54] transfer of real property free of charge.[55] The consequences of an absence of approval are the same as in the case of business corporations: a possibility to request invalidity. The law for request invalidity is also connected with the absence of prior approval required by statute of a state enterprise. And here a problem arises, because such restrictive rules in the Statute have the character of internal rules. The state transfers risk connected with wrongly chosen persons to the bodies of state enterprise to a third party entering into legal relations with the state enterprise. This gives rise to unreasonable inequality in rights and obligations, which does not contribute to security of trade. Additionally, this can be considered as a rule inconsistent with the recommendation of the OECD Guidelines to respect the generally applicable rules of corporate law.

In March 2014, the government set up the Government Committee for staffing nominations as an advisory body. The committee has three members and its role is to consider the nomination of candidates for members of the supervisory boards of state-owned enterprises. Its opinion is not binding for ministers as persons to whom the final decisions belong. Currently, the draft of an act on the choice of persons for executive and supervisory bodies of state-owned enterprises is in the legislative process. This act should detail modifications to the nomination process, extending to executive members of bodies and will make it binding. The draft Act extends the requirements for the exercising of members of bodies for indebtedness and a certain level of professionalism. What will be the fate of this legislative intent cannot be anticipated. It can be assumed that this nomination process might not be regulated by law, but merely by government resolution. Legal regulation again raises the question of the consequences connected with failure of the prescribed procedure for state-owned enterprise.

In passing, I would like to mention special conditions regarding state employees and some public officials. They may not be members of executive or supervisory bodies of business corporations operating in business, with the exception of cases where the state sent them to these bodies.[56] In such a case they are required to act in the interest of the state. They are not required to be remunerated by business corporations. The obligation to exercise the

51 Sec. 47 Business Corporations Act.
52 Sec. 16 para 7 State Enterprise Act.
53 Sec. 17 para 2 State Enterprise Act.
54 Sec. 17 para 3 State Enterprise Act.
55 Sec. 17e para 2 State Enterprise Act.
56 Sec. 81 para 2 Civil Service Act (no. 234/2014 Coll. as amended), sec. 303 para 3 Labour Code (no. 262/2006 Coll. as amended), sec. 4 and 5 Conflict of Interest Act (no. 159/2006 Coll. as amended).

function of a body member with due care and loyalty is unlimited. Remuneration is a basic motivational element in corporate governance. Its removal may endanger the functioning of business corporations with state participation.

CONCLUSION

In conclusion, we can say that the legal regulation regarding state enterprise as a specific legal person created solely for state participation in business is unjustifiably favourable compared to legal regulation regarding other legal persons. The question is whether the state as a legislature abuses its position to provide a greater protection of its interests than it provides other persons in the private sector. The question is whether a state enterprise as a legal person should exist and whether it would be desirable that the state uses for business only types of legal persons which are open for other persons, i.e. as a joint-stock company.

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THE STATE'S ROLE AS OWNER OF ENTERPRISES: MANDATORY RULES OF CORPORATE GOVERNANCE IN ROMANIA

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The role of state-owned enterprises in the post-socialist countries, after a complicated and painful historical experience is a central issue, because state-owned enterprises still represent and will represent a relevant sector of the economy in the new capitalist context. In 2011, Romania has adopted a hard law of corporate governance, based at least partially on the OECD Guidelines. This is the Emergency Ordinance 109/2011, which created the Romanian regulatory corporate governance of state owned enterprises. The Emergency Ordinance is a great step in the good direction but its implementation is still partial. The corporate government system created by the Ordinance seems clear and well-functioning enough to lead in time, if applied correctly, to a reasonable depoliticization, professionalization and also to the stability of boards, essential to a proper management of state-owned enterprises.

Keywords:
company law, business law, corporate governance, state-owned company, Romania, Emergency Ordinance

1. RELATIONSHIP BETWEEN THE OECD GUIDELINES ON CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES AND NATIONAL RULES

The Organization for Economic Co-operation and Development (OECD), in the context of its policy to improve the economic and social well-being of people, prepared and adopted in 2005 and updated in 2015 the Guidelines on Corporate Governance of State-Owned Enterprises (the Guidelines).[1] State-owned enterprises (SOEs) represent a very important economic sector in size and also in activities (in many cases performing public services), so their importance is self-evident and the corporate governance of such enterprises attracts international political and scientific attention.[2] The role of state-owned enterprises in the post-socialist countries, like Romania, after a complicated and painful historical experience – the nationalization of private (i.e. not state-owned) enterprises by the communist dictatorial regimes[3] and the complicated privatization process following the overthrown of such dictatorships – is a central issue, because state-owned enterprises still represent and will represent a relevant sector of the economy.[4] In the new capitalist context, the state-owned enterprise raises questions of political philosophy (what is the role of the state in the economy in general?) and also practical ones (what should be the extent of privatization and which companies must remain state-owned and how an efficient management of such entities can be achieved?).[5]

The Guidelines represent a set recommendations directed towards the governments, intended to serve as internationally agreed standards, created to ensure the efficient, transparent and accountable operation of state owned enterprises. The aim – according to

1 The reason for updating, as stated in the text of the Guidelines was "to reflect a decade of experience with their implementation and address new issues that have arisen concerning SOEs in the domestic and international context".

2 For example, beside the OECD, the World Bank is also active in this field. See *Corporate Governance of State-Owned Enterprises. A Toolkit*, World Bank, 2014.

3 Veress, Emőd (2014): Towards a Legal Theory of Nationalization. Controversies of Company Law History in Central and Eastern Europe. *Romanian Journal of Comparative Law, 2014/2. 185–201.;* Veress Emőd (2015): From Capitalism to Utopia – Communist Nationalization of Companies in Central and Eastern Europe. *Acta Universitatis Sapientiae,* 2015/2. 125–137.

4 The state-owned enterprises in Romania generate 8% of total output of non-financial corporations and employing close to 4% of the Romanian workforce. Based on the financial reporting submitted to the Ministry of Public Finance, there were 247 central-government-owned enterprises and a total of 1177 local-government-owned enterprises at the end of 2013. For detailed data, see Marrez, Helena (2015): The role of state-owned enterprises in Romania. *ECFIN Country Focus,* Vol. 12. Issue 1. January 2015. It is also important to know that in 2013, the aggregate SOE sector became profitable following several years of losses. See *International Monetary Fund Country Report no. 15/80. Romania*, March 2015, 20. But the same report states also the following remark which is slightly shading the image: "However, a closer look reveals that when five SOEs are excluded from the analysis the picture changes drastically. These are the state-owned gas, nuclear and hydroelectricity producers which benefited from deregulation in 2013, the gas transportation network which enjoys monopolistic conditions, and the Road Company which acts more like a project implementation unit. The remaining SOE sector was still loss making, albeit with a declining trend."

5 For the rationale of existence of state-owned enterprises, see *Corporate Governance of State-Owned Enterprises. A Survey of OECD Countries*, OECD Publishing, 2005, 20.

the Guidelines – is to establish a balance on "how governments should exercise the state ownership function to avoid the pitfalls of both passive ownership and excessive state intervention". In this context, the Guidelines practically tries to ensure the general conditions under which the sensitive balance between state passivity and encroachment could be achieved through best practices. As expressly stated, the Guidelines are recommendations, which can be qualified from a legal point of view at most as a soft law. Soft law was defined as "rules of conduct that are laid down in instruments which have not been attributed legally binding force as such, but nevertheless may have certain (indirect) legal effects, and that are aimed at and may produce practical effects".[6] Soft law is covering such instruments as recommendations, guidelines, notices, communications, declarations and codes of conduct. Soft law can be used in various situations, presenting advantages and disadvantages. One of the greatest challenges to soft law is that "in the case of conflicting approaches, choices made at the drafting stage might result in wording that would not necessarily be representative of any leading approach" and "a soft law instrument might have to be formulated so generally to be representative of all various approaches that it could not induce harmonization when specific questions have to be decided".[7] Soft law is used frequently to articulate universal (global) rules and standards. Soft law is much likely to attract consensus in international relations compared to harder forms of regulation, which cannot be agreed.[8]

Practically, based on the Guidelines, the best harmonization approach appears to adopt a national soft law instrument or a set of national recommendations, reflecting maybe the national specificities as well but in concordance with the aims and values revealed by the Guidelines.

Romania has chosen a different path: in 2011, a hard law of corporate governance was adopted, based at least partially on the OECD Guidelines. This is the Emergency Ordinance 109/2011,[9] which created the Romanian regulatory corporate governance of state owned enterprises.[10] An emergency ordinance is a regulation with legal force enacted by the Government under extraordinary circumstances and approved/modified/rejected *post factum* by the Parliament. The emergency, in general, was motivated by the need of reform and the necessity to avoid the perpetuation of the dysfunctionalities of state-owned enterprises. Starting with the overthrow of the communist regime 20 years of silence followed after which sudden emergency appeared. Nevertheless, the Constitutional Court of Romania confirmed that the constitutional requirements on emergency were met and the adoption of Emergency Ordinance 109/2011 is therefore not in breach of the fundamental law.[11]

6 Senden, Linda (2004): *Soft Law in European Community Law*. Oxford–Portland, Hart Publishing. 3.

7 Bjorklund, Andrea K. – Reinisch, August eds. (2012): *International Investment Law and Soft Law*. Cheltenham (UK) – Northampton (USA), Edward Elgar Publishing. 3.

8 Weeks, Greg (2016): *Soft Law and Public Authorities. Remedies and Reform*. Oxford, Hart Publishing. 8. The author also shows that *"the role, meaning and very existence of international soft law are all still contested". Ibid.*

9 Published in the Official Journal of Romania no. 883 at 14.12.2011.

10 For a general overview, see: Catană, Radu (2012): *The Reform of Corporate Governance of State-Owned Enterprises in Romania. A Critical Analysis*. București, Universul Juridic.

11 Decision no. 44/2013.

Emergency Ordinance 109/2011 represents hard law, created by the Government. Since its adoption it has been changed three times by the way of other ordinances (twice in 2013 and once in 2015)[12] and finally approved by the Parliament through a law adopted in 2016,[13] which introduced also a great set of modifications to the normative text, contributing negatively to the legislative stability and predictability (one of the main general adverse effects of legislating through ordinances) but correcting and updating some rules.

The scope of this article is to confront the requirements stated in the second chapter of the Guidelines entitled The State's Role as an Owner, on one hand, and the mandatory provisions of the Emergency Ordinance 109/2011, on the other hand.

Chapter II of the Guidelines requires generally that the state should be "an informed and active owner", ensuring that the corporate governance of the state owned enterprise is "transparent and accountable", acting "with a high degree of professionalism and effectiveness". These are very general terms, specific to soft law instruments, representing much more principles than norms. Nevertheless, under these principles there are six requirements (A–F), which can form the basis of the comparative analysis.

2. LEGAL FORMS OF STATE OWNED ENTERPRISES

The OECD Guidelines require that "Governments should simplify and standardize the legal forms under which SOEs operate. Their operational practices should follow commonly accepted corporate norms."[14]

Legal forms of state-owned enterprises represent a central issue because the legal form serves as the functional framework of such a corporation. Simplification, standardization and operational practices in concordance with the corporate norms applicable also for the private sector companies are desirable goals of corporate governance of state owned enterprises.

The scope of Emergency Ordinance 109/2011 covers, according to the legal text, "the public enterprises which are Romanian legal persons".[15] The notion of enterprise is not really helpful from this point of view, due to the fact that in the Romanian legal language enterprise means not a legal form but instead an economic activity, which may be realized in several forms recognized by the law.[16]

If we want to understand the present-day situation, we have to start with the communist notion of "state enterprise", which, compared to the existing notion of state-owned enterprise, was a legal form of economic activity more comparable to an administrative organ of the state than to a company. The state enterprise created in order to organize the direct economic presence of the state, which, during that period, covered almost the whole of the economic

12 Emergency Ordinance no. 51/2013, Ordinance no. 26/2013 and Emergency Ordinance no. 10/2015.
13 Law no. 111/2016, in force from 4 June 2016.
14 Guidelines, II, A.
15 Art. 1 from Emergency Ordinance 109/2011.
16 Art. 3 of the Civil code.

spectrum due to the nationalization and etatization of virtually all of the industrial and commercial activities in order to create a utopian and egalitarian society.[17]

After the change of the regime in 1989, a slow paced privatization process started (not ended even today). At the starting moment, it was a must to transform the state enterprises into commercial companies, to create the special relations between the owner and the company represented generally by shares, which also can be sold. A conversion of a non-privatizable legal form, i.e. the state enterprise into one that can be privatized occurred.

First, the state enterprises that the Government intended to privatize were transformed into commercial companies. Second, based on the French model of *régie autonome* ("autonomous holdings") in Romania so called *regii autonome* were also created, a perfect tool to salvage the state enterprise and maintain a very similar organizational structure.[18] In addition, the *regii autonome* were exempted from the application of insolvency rules until 2014.[19] The number of *regii autonome* decreased in time because a high number of such structures were transformed into commercial companies (for example, in the energy sector RENEL, PETROM, ROMGAZ etc. were established initially as *regii autonome* with the aim of "perpetual" state ownership). At that time, the widespread use of *regii autonome* was criticized: "Firms have not been chosen to be *régies autonomes* according to well-defined criteria, raising doubts as to whether many *régies autonomes* are engaged in activities that could be better handled by commercial companies and eventually the private sector. Neither legislation nor the constitution clearly specifies what enterprises should be *régies autonomes*. On the other hand, economic criteria, such as if the enterprise in a natural monopoly, provides a public good, or if there is a low demand elasticity for the product of *régies autonomes* in the Romanian economy creates doubts among domestic entrepreneurs and foreign investors about the sincerity of Romania's commitment to a market economy."[20] The directors of these structures were appointed by the relevant branch ministries and the Ministry of Finance.[21] Today the role and importance of *regii autonome* diminished, but there are some important economic structures still organized under this form at central or local level (there are 15 *regii autonome* at central and about 100 at local level).

Right after the collapse of the communist regime the general rules of company law were also adopted,[22] which contained just a minimal set of special rules regarding state-owned companies (for example, the derogatory rule that the state or the local government can be a single shareholder of a joint stock company, meanwhile for a private sector joint

17 For details on the state enterprise, see Pop, Aurel – Beleiu, Gheorghe (1983): *Drept economic socialist român*, vol. I. București, Universitatea din București, Facultatea de Drept. 148–153.

18 For details, see Law no. 15/1990 on conversion of state enterprises into autonomous holdings and commercial companies, Law no. 66/1993 on management contracts, Emergency Ordinance no. 30/1997 on the reorganization of autonomous holdings etc.

19 Art. 3 (2) from Law no. 85/2014 on procedures for insolvency prevention and insolvency.

20 Pannier, Dominique ed. (1996): *Corporate Governance of Public Enterprises in Transitional Economies*, World Bank Technical Paper Number 323. Washington D.C., World Bank. 49.

21 Art. 12 from Law. no. 15/1990.

22 Law no. 31/1990 on commercial companies (still in force, with its title changed to Law on companies due to the implementation of the monist system of private law in 2011).

stock company at least five shareholders were needed and from 2006 two shareholders are necessary for the establishment of such a company).

Later it was considered that state-owned enterprises are also best managed in form of joint stock companies, so two kinds of structures were created: national companies and national enterprises, both of which are organized as joint stock companies. The name in those cases never covered any genuine, special and comprehensive set of rules, instead it meant that these companies are of strategic importance and their privatization is not necessary, and in case of privatization, the state can opt to keep the control of these companies. This was the case for example of the Petrom National Company, the Romanian oil company owning refineries and the largest network of gas stations, but later this company was privatized as well in the staggered privatization process of Romania. In the case of "commercial" companies, the state exercised its influence as a shareholder, meaning an almost absolute and highly politically influenced control. Otherwise, the rules applicable for state-owned enterprises organized as joint stock companies were the same as the ones in force for the private sector. Therefore in Romania there were no clear and specific set of rules on how to operate state-owned enterprises and also it was evident that the general rules were not enough to ensure the proper functioning of such economic entities.

Emergency Ordinance no. 109/2011 was proposed in this context as a remedy for the poor performance of such entities, creating special rules for the corporate governance of state-owned enterprises, which have a complementary and derogatory character compared to the general norms as stated by Law no. 31/1990 for companies.

In the initial version of Emergency Ordinance no. 109/2011 the banking and insurance companies were excepted alongside with the companies performing activities of national interest for defense, public order and national security purposes. In 2016 the scope of the ordinance was extended and only two structures, respectively *Regia Autonomă "Rasirom"* and *"Romtehnica" S.A. National Company*, both active in the industry of military technologies were left out. The path created by the regulatory and mandatory instrument of corporate governance, which is Emergency Ordinance no. 109/2011, seems to be perceived and accepted as the viable solution for the future management of state-owned enterprises.

Emergency Ordinance no. 109/2011 defines the notion of public enterprises, as:

a) autonomous holdings (*regii autonome*) set up by the state or an administrative-territorial unit (local government);
b) national companies, national enterprises and companies having the State or an administrative-territorial unit (local government) as sole, majority or controlling shareholder;
c) companies in which one or more public enterprises as referred above hold a majority or controlling participation.[23]

Romania still has a dispersed regulation of the legal forms of the state-owned enterprises and the clarification and standardization process of state-owned enterprises has not finished

23 Art. 2.

and it will be raised also in the preparation phase of the necessary general reform of the company law which seems to start after the elections in December 2016.

3. FULL OPERATIONAL AUTONOMY AND INDEPENDENCE OF THE BOARDS

The Guidelines require that "the government should allow SOEs full operational autonomy to achieve their defined objectives and refrain from intervening in SOE management. The government as a shareholder should avoid redefining SOE objectives in a non-transparent manner".[24] The Guidelines also demand that "the state should let SOE boards exercise their responsibilities and should respect their independence".[25] These requirements on full operational autonomy and independence of the boards represent the second and the third precept from Chapter II of the Guidelines and are assayed together because of the close relation between the two issues: independence of the activity and of the board are interconnected.

However, these requirements are principled and generous but also unfeasible, idealistic and chimerical. A legal (regulative) reaction to the soft law principles cannot be anything else than a specific readback of the Guidelines. Emergency Ordinance no. 109/2011 states that the tutelary authority and the Ministry of Finance as monitoring authority cannot intervene in the management and leadership of the state-owned enterprise.[26]

In contrast, the International Monetary Fund reported on the reality that "the process of selection of candidates for the management positions was not always fully exempt from line ministries' interference and many appointments were subsequently reversed. Notorious examples include several SOEs operating in the transport sector where implementation of GEO 109 started in late 2012. In CFR Infrastructura, the management was dismissed three times since then, every time coinciding with the new transport minister appointment. In SOE Tarom, the composition of the board changed four times during two years… There is no clearly defined SOE ownership policy and the tutelary authority interference is extensive. This creates a potential for conflicts of interest in the SOEs governance framework, as the line authorities (usually line ministries) that exercise ownership role in SOEs are also responsible for establishing sectoral strategies, implementing government's policies and conducting privatizations. Consequently, they often have conflicting interests over various issues and may sacrifice good corporate governance objectives over other priorities including political expediency. In such cases, line ministries' interference, especially when done through the issuance of ministerial orders, can be quite disruptive for SOEs effective management".[27]

24 Guidelines, II, B.
25 Guidelines, II, C.
26 rt. 4.
27 *International Monetary Fund Country Report no. 15/80. Romania*, March 2015, 22–23.

4. EXERCISE OF OWNERSHIP RIGHTS

According to the Guidelines, "the exercise of ownership rights should be clearly identified within the state administration. The exercise of ownership rights should be centralized in a single ownership entity, or, if this is not possible, carried out by a co-ordinating body. This "ownership entity" should have the capacity and competencies to effectively carry out its duties".[28] In addition, the Guidelines state that "the ownership entity should be held accountable to the relevant representative bodies and have clearly defined relationships with relevant public bodies, including the state supreme audit institutions".[29]

This requirement is not fully achieved in the case of Romania and the Emergency Ordinance no. 109/2011 was not intended to introduce reform in this field. The Emergency Ordinance no. 109/2011 has in its scope to determine the relationship between any so-called tutelary authority and the state-owned enterprises and does not interfere with the problem of which state authorities should be or should be not tutelary authorities. Several authorities serve, beside the Authority for Administration of State Assets,[30] as tutelary structures of state-owned enterprises, especially ministries and other central administrative authorities as well, so there is no single ownership entity. Moreover, the Authority for Administration of State Assets had 10 state-owned enterprises under its tutelary supervision, while the Ministry of Transports 27, the Ministry for Economy 42, the Ministry of Education 60, and the Department for Energy 25 etc.

The International Monetary Fund concluded that "centralizing the ownership function may deliver separation of ownership interests and policy objectives thus constraining the line ministries' influence on SOEs governance. However, experience… suggests that without political will the institutional setup alone cannot ensure such a separation."[31] But this falls outside the purposes of Emergency Ordinance no. 109/2011. Romania fails to create a single professional and commercially oriented ownership entity and also Emergency Ordinance no. 109/2011, as a coordination mechanism, is not enough to eliminate the divergence of corporate governance standards applied by different public ownership entities.[32] An effective owner is also assertive for the accountability of state owned enterprises.

5. THE STATE AS AN INFORMED AND ACTIVE OWNER

The Guidelines' sixth and last requirement creates a set of rules, according to which "the state should act as an informed and active owner and should exercise its ownership

28 Guidelines, II, D.

29 Guidelines, II, E.

30 Between 1992–2000 State Ownership Fund (Fondul Proprietății de Stat), between 2000–2004 Authority for Privatization and Administration of State Property (Autoritatea pentru Privatizare și Administrarea Proprietății Statului), between 2004–2012, Authority for State Assets Recovery (Autoritatea pentru Valorificarea Activelor Statului), and from 2012, Authority for Administration of States Assets (Autoritatea pentru Administrarea Activelor Statului).

31 International Monetary Fund Country Report no. 15/80. Romania, March 2015, 26.

32 Monks, Robert A. G. – Minow, Nell (2011): *Corporate Governance*, fifth edition. Chichester, *John Wiley & Sons. 463.*

rights according to the legal structure of each enterprise. Its prime responsibilities include:

1. Being represented at the general shareholders meetings and effectively exercising voting rights;
2. Establishing well-structured, merit-based and transparent board nomination processes in fully- or majority-owned SOEs, actively participating in the nomination of all SOEs' boards and contributing to board diversity;
3. Setting and monitoring the implementation of board mandates and objectives for SOEs, including financial targets, capital structure objectives and risk tolerance levels;
4. Setting up reporting systems that allow the ownership entity to regularly monitor, audit and assess SOE performance, and oversee and monitor their compliance with applicable corporate governance standards;
5. Developing a disclosure policy for SOEs that identifies what information should be publicly disclosed, the appropriate channels for disclosure, and mechanisms for ensuring quality of information;
6. When appropriate and permitted by the legal system and the state's level of ownership, maintaining continuous dialogue with external auditors and specific state control organs;
7. Establishing a clear remuneration policy for SOE boards that fosters the long- and medium-term interest of the enterprise and can attract and motivate qualified professionals."

These points represent a much more detailed approach and influence, in a great part, the regulation adopted through Emergency Ordinance 109/2011. A complete and detailed analysis of the Romanian legal text is not possible in the context of an article. But at least the main elements and peculiarities of the Romanian system of mandatory corporate governance can be identified, with a focus on companies.[33]

Ad 1. There were no problems with the state as "active owner" (historically the state being a too active owner in most of the cases). The tutelary authority has the attribution to nominate the representatives of the state or of the administrative-territorial unit (local government) to the general meetings of shareholders and to approve their mandate.[34] According to the reform completed in 2016 with the parliamentary approval of the Emergency Ordinance 109/2011, the number of representatives of the state or of the administrative-territorial units (local governments) in the general meetings of shareholders is maximum two.[35] Also, a certain person (civil servant, contractual employee or public dignitary) can represent the tutelary authority in maximum two state-owned enterprises. The regulations regarding incompatibilities and conflicts of interest are applicable.[36]

In case of local governments the local council shall exercise on behalf of the administrative-territorial unit all rights and obligations arising from the shareholding in companies and

33 For autonomous holdings, see art. 5–24 from the Emergency Ordinance 109/2011.
34 Art. 3 from the Emergency Ordinance 109/2011.
35 Art. 64/3 (1) from the Emergency Ordinance 109/2011.
36 Law no. 161/2003.

from the control over the *regii autonome* (autonomous holdings) of local interest. Persons empowered to represent the interests of the administrative-territorial units in companies and autonomous holdings are designated by local council decision, with respect to the political configuration resulted from the latest local elections.[37] This mechanism is seen as a democratic one, because this text leads in general to the conclusion that in case of the enterprises owned by local governments the two biggest political parties delegate one representative each (local councillor) ensuring mutual political control[38] like the two consuls of Republican Rome having a veto right ("*intercessio*") over the actions of the other. Also, there is a greater chance of inability to make decisions and of impasse. Before 2016, the maximum number of representatives was not limited, and there are known cases when all members of the local council were elected as representatives and practically the composition of the general meeting of the company and of the local council was identical.

Ad 2 and 3. Regarding board nomination and mandates, the Emergency Ordinance 109/2011 contains detailed rules and this constitutes the heart of the regulation in the sense that the outcome of the reforms is expected to be produced by the procedures of management selection.

One-tier (unitary) and two-tier (dualist) board systems are both available.[39]

(a) One-tier (unitary) board system

The board (*consiliul de administrație*) consists of 3–7 members, natural or legal persons, with experience in performance improvement of companies or autonomous holdings that they have administered or managed.

In case of companies which fulfil certain conditions, namely if the state owned enterprise has an annual turnover exceeding 7,300,000 euros and has at least 50 employees, the board has 5–9 members.

At least two members must have economic or legal studies and 5 years of professional experience. Since 2016, in the first case (smaller state owned enterprises) only one member of the board can be a public servant or employee of the tutelary authority or other public authority and institution; and in the second case maximum two members.[40] The majority of the board consist of non-executive and independent members.[41]

The mandate of the board members may not exceed four years. Appointment of the board members who have properly fulfilled their duties may be renewed following an evaluation process, if the articles of association do not providing otherwise. Appointment of the board

37 Art. 37 from the Law 215/2001 on local public administration.

38 Otherwise is not possible to respect the "political configuration" resulting from the local elections, for example by nominating civil servants.

39 The SE (Societas Europaea) Regulation (Council Regulation (EC) 2157/2001) allows also for both one-tier and two-tier structures.

40 Reality: from other state institutions.

41 Art. 138/2 from Law no. 31/1990.

members following the cessation of any form of an original member's mandate coincide with the remainder time of the mandate of the discharged person.

Members of the board are appointed by the general meeting of shareholders based on the proposal made by the functioning board or by shareholders. The candidates proposed by the board of the company are evaluated and selected in advance and recommended by the nomination committee of the board. The nomination committee consists of non-executive board members, of which at least one is independent. A board decision may determine that in the evaluation process the nominating committee is assisted by an independent expert specialized in recruiting human resources whose services are contracted by the company under the law.

There is a previous compulsory selection of candidates by an independent human resources recruitment expert in case when the tutelary authority, as shareholder is proposing candidates for the board.

The tutelary authority may decide that the selection committee should be assisted or the selection should be carried out by an independent human resources recruitment expert whose services are contracted by the public authority or by the state owned company. In this second case, the public authority will pay the costs of the expertise. The selection of candidates must be done by an independent human resources recruitment expert if the state owned enterprise has an annual turnover exceeding 7,300,000 euros and has at least 50 employees.

The selection criteria for board members are set based on a unitary methodology[42] jointly approved by the Ministry of Public Finance and other ministries which are also tutelary authorities, by members of the nominating committee and/or the independent expert, as appropriate, taking into account the specificity and complexity of the company's business and the requirements of the letter of expectations. The letter of expectations is a working document issued by the tutelary authority, in consultation with any shareholder representing individually or jointly 5% of the share capital of the public enterprise, which determine the expected performance of the management and the public policy aims of the tutelary authority for a period of at least 4 years.

The announcement on the selection of board members shall be published at least in two economic newspapers and on the website of the state owned company. It should include the conditions to be met by candidates and their evaluation criteria. The selection is based on principles of non-discrimination, equal treatment and transparency and taking into account the specific activity of the state-owned enterprise, while ensuring a diversification of skills within the board. The publication of the announcement must take place at least 30 days before the closing date for applications.

The appointment of board members is voted by the general meeting of shareholders based on a short list, comprising maximum 5 candidates for each membership position of the board. The shortlist is made by the tutelary authority, nomination committee or the independent human resources expert. The short list contains the score obtained by each candidate.

42 Published in the *Monitorul Oficial* no. 803 din October 12, 2016.

If the candidates proposed by the Board are board members, an application for renewal is addressed to the general meeting of shareholders.

For companies managed according to the one-tier system, the board delegates the management of the company to one or more directors, nominating one of them as general director. This is mandatory requirement of Emergency Ordinance 109/2011.[43] The directors may be appointed from inside or from outside of the board (this fact being the major difference compared to the two-tier system where a supervisory board member cannot be nominated as member of the directorate). The chairman of the board of the company cannot be nominated as general director, contrary to the highly common practice in the private sector companies. Directors are appointed by the board upon the recommendation of the nomination committee following a selection procedure for the position, held after the appointment of board members. The board may decide to be assisted or that the selection be carried out by an independent person or entity specialized in recruiting human resources. The publication of the selection announcement must take place at least 30 days before the closing date for applications.

(b) Two-tier (dualist) board system

For companies managed according to the two-tier system, the supervisory board can have between 5 and 9 members, and the directorate (the actual management board) between 3 and 7 members. Supervisory board members are appointed by the general meeting of shareholders in a similar procedure applicable to board members in the unitary system of management of the company. Also for the selection of the directorate, the procedures analysed above for selection for directors in case of one-tier system are applicable.

(c) Common rules for the one-tier and two-tier board systems

At the request of shareholders representing, individually or together, at least 5% of the subscribed and paid share capital, the board or the directorate must convene a general meeting of shareholders with the agenda of electing the members of the management or supervisory board by cumulative voting. If the request is made by a shareholder holding more than 10% of the share capital of the state-owned enterprise, the cumulative voting method is mandatory.

An individual cannot exercise more than three mandates as a board or supervisory board member in state-owned enterprises whose headquarters are in Romania (in the initial text of Emergency Ordinance 109/2011 five such mandates were possible). The rule is applicable for representatives of legal persons, members in the board or in the supervisory board.

Ad. 4. Emergency Ordinance 109/2011 sets up a reporting system, which allows the shareholders to monitor the management performance regularly.

43 Art. 35.

The board and the supervisory board in case of the two-tier system draw up a proposal for the polity component of the management plan, in order to achieve the financial and non-financial performance indicators. The directors draw up a proposal for the management component of the management plan. The management plan is approved by the board or the supervisory board (in case of the two-tier management system).

In five days from the approval of the management plan, the general meeting of shareholders is summoned to negotiate and vote on the financial and non-financial performance indicators. The negotiation process is based on the letter of expectations and on the management plan and there is a 45 days period to reach an agreement. The deadline may be extended once by a maximum of 30 days at the request of any of the parties. In case of failed negotiations in the two rounds, the board or the supervisory board are removed without being entitled to payment of damages. In this case, the failure of negotiations must be justified and published on the company's own website.

Evaluation of board members is made annually by the general meeting of shareholders, as applicable, with the support of experts in such evaluation addressing the implementation of their mandate contract and of the management plan. The board members may be dismissed by the general meeting of shareholders according to the law, as determined in the mandate contract. If an unjust revocation occurs, the board member shall be entitled to payment of damages, according to the contract of mandate.

If, due to an attributable reason the board members do not meet performance indicators established by the mandate contracts, the general meeting of shareholders has to cancel their mandate. Board members who were revoked for non-performance cannot run for 5 years from the date the decision becomes definitive for other boards of state-owned enterprises. The legal text is not really clear. The revocation is an attribution and practically an obligation of the general assembly. The interdiction to be effective seems to require a "definitive or final decision", which can be granted only by the courts. The only plausible interpretation of the text is that the board member can be revoked by the general assembly, but the state-owned enterprise must request from the court the application of the interdiction and therefore the effect of the interdiction is not certain.

The annual evaluation, the possibility of revocation of the mandate and the interdiction on the candidacy for similar functions is applicable also for the directors and for the members of the directorate.

The board or the general director, or, where appropriate, the directorate shall submit to the Ministry of Finance, to the tutelary authority and to shareholders holding more than 5% of share capital, quarterly and whenever required, reports, analyzes, statements and other information on the activity of the state-owned enterprise. The corporate governance structures in the tutelary authority report quarterly the monitored performance indicators to the Ministry of Finance. The monitored performance indicators are established by the tutelary authority in the contract of mandate of directors.

Ad 5. Disclosure of information in the case of state-owned enterprises is a question of public accountability and also a tool for protection of minority shareholders. "An effective

reporting regime requires SOEs… to produce financial statements according to high-quality accounting standards; to increase the effectiveness of nonfinancial reporting; and to disclose publicly both financial and nonfinancial information."[44]

Under the Emergency Ordinance 109/2011, first of all, the state owned enterprise must operate a website and ensure the access of the shareholders and general public (practically the stakeholders) to the documents and information which disclosure is required by law.[45]

In case of shareholder general meetings, the agenda and the documents to be presented to the meeting must be published through the website of the company at least 30 days before the date established for the meeting. In case of publicly traded companies, the special capital market disclosure regime is mandatory.[46]

The shareholders and the stakeholders must have access to the following documents and information by the way of the website of the company:[47]

a) the decisions of the general meetings of the shareholders, in 48 hours after the general meeting;
b) the annual financial statements, in 48 hours after their approval;
c) semestrial reports on the accounts of the company, in 45 days from the end of the semester;
d) the annual audit report;
e) the names, the biographies and the remuneration of the management of the company;
f) the reports of the management of the company;
g) the annual report on the remuneration and other advantages given to management members;
h) the annual activity report of the company.[48]

The annual financial statements, the semestrial reports on the accounts of the company, the annual audit report and the reports of the management has to be available online at least for a 3 years period.

In addition, the president of the board or of the supervisory board can be fined by the Ministry of Public Finances if the disclosure obligations of the company are not respected.[49]

Ad 6. A continuous dialogue between external auditors and specific state control organs is an aim not really fulfilled in practice and also it is hard to achieve through regulatory means. This type of dialogue exists mainly during the period of controls. The annual financial

44 *Corporate Governance of State-Owned Enterprises. A Toolkit*, World Bank, 2014, 215. See also *Accountability and Transparency: A Guide for State Ownership*, OECD Publishing, 2010.

45 Art. 40 from the Emergency Ordinance 109/2011.

46 There are nine publicly traded companies in which the State is a majority shareholder (Antibiotice SA, CONPET SA, Electrica SA, Oil Terminal SA, Oltchim SA, Transelectrica SA, Nuclearelectrica CN, Romgaz SA, Transgaz SA) and also the state is a minority shareholder in several companies.

47 Art. 51 from the Emergency Ordinance 109/2011.

48 Art. 56 from the Emergency Ordinance 109/2011.

49 Art. 59/1 from the Emergency Ordinance 109/2011.

statement of public enterprises is subjected to statutory audit.[50] Contracting audit services is possible only with respect to the public procurement legislation.[51]

Ad 7. A central goal of Emergency Ordinance 109/2011 was also the establishment of a clear remuneration policy.[52] The balance between excesses and underpayment is not an easy aim to achieve, because the state-owned enterprise must competitively attract, motivate and retain professionals with outstanding results. The concept of Emergency Ordinance 109/2011 is to introduce a remuneration system, which is performance-based, competitive but transparent at the same time. As stated by the OECD, "it would be difficult in many countries to really enhance board professionalism and business perspective as long as remuneration does not permit attracting and retaining professional board members with the required expertise and experience".[53] Also it was proposed by OECD "that a prime responsibility of the State as an active owner is to ensure that remuneration schemes serve the long term interest of the company and attract the right people"[54] and it was identified as a good practice the remuneration which reflects "the market conditions to the extent that this is necessary to attract and retain highly qualified directors".[55]

The remuneration – in the context of the one tier management system the remuneration of board members, in case of two-tier system the remuneration of the supervisory board – is set up by the general meeting of shareholders under the conditions provided by Emergency Ordinance 109/2011.

The remuneration for the non-executive board members is composed of a monthly fixed allowance and a variable allowance. The fixed allowance may not exceed twice the median for the last 12 months of the average gross salary per month in the corresponding economic sector. The variable component is determined based on financial and non-financial performance indicators negotiated and approved by the general meeting of shareholders, other than those approved for the executive board members. The amount of the variable component of the remuneration of the non-executive board members may not exceed a maximum of 12 monthly fixed allowances.

The remuneration of the executive board members (also serving as directors of the company) is similarly composed of a monthly fixed allowance and a variable allowance. The fixed allowance may not exceed six times the median for the last 12 months of average gross salary per month in the corresponding economic sector. The variable component is

50 Emergency Ordinance no. 90/2008 transposing into national law the Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC.

51 Law no. 98/2016 on public procurements.

52 For a general overview of management remuneration see Kostyuk, Alexander – Stiglbauer, Markus – Govorun, Dmitriy eds. (2016): *The Theory and Practice of Directors' Remuneration. New Challenges and Opportunities*. Bingley, Emerald Group Publishing.

53 *Corporate Governance of State-Owned Enterprises. A Survey of OECD Countries*, OECD Publishing, 2005, 20.

54 *Boards of Directors of State-Owned Enterprises. An Overview of National Practices*, OECD Publishing, 2013, 68.

55 *Boards of Directors of State-Owned Enterprises. An Overview of National Practices*, OECD Publishing, 2013, 69.

determined based on financial and non-financial performance indicators negotiated and approved by the general meeting of shareholders, other than those approved for the non-executive board members.

The variable component of the remuneration shall be reviewed annually, depending on the level of achievement of the aims of the management plan and the fulfilment of financial and non-financial performance indicators approved by the general assembly of shareholders, attached to the contracts of mandate of board members.

The remuneration of directors is established by the board and cannot exceed the established remuneration for executive members of the board. It is the only form of remuneration for directors who are board members as well. The remuneration is composed of a monthly fixed allowance similarly established as that of the executive board members and a variable component consisting of the participation percentage in the net profits of the company, granting shares, stock options or an equivalent scheme, a pension scheme or other form of remuneration based on performance indicators. The same rule applies in case of the two-tier board system, where the remuneration of the directorate members is established by the supervisory board.

Policy and criteria for the remuneration of board members and directors in case of the one tier system, of the members of the supervisory board and directorate members in the case of the two-tier system, the level of remuneration and other benefits offered to each board member or director are made public on the website of the state-owned enterprise.

6. CONCLUSIONS

The *Emergency Ordinance* 109/2011 is a great step in the good direction but its implementation is still partial. As the International Monetary Fund concluded, "the legislation contains necessary provisions for depoliticization and professionalization of SOE governance through procedures for the selection, appointment, and functioning of SOE boards and managers. It provides for increased transparency and information disclosure to help enhance SOEs' accountability to the Romanian public. Minority shareholders' protection in SOEs is also integrated in the ordinance."[56] But this is just the normative content and the practice is far from the expectations, because, for example, several newly appointed boards were dismissed. The pace of the reform is slow, and the assumption of fast results is not really founded. Between 2000 and 2015, the Romanian national airline company TAROM was managed by 13 general directors, and the tutelary authority, the Ministry of Transports was also lead by 12 ministers. This information in itself is a clear enough sign of excessive politicization. The corporate government system created by Emergency Ordinance 109/2011 seems clear and well-functioning enough to lead in time, if applied correctly, to a depoliticization (to a possible minimum level because absolute depoliticization is an utopia), professionalization and also to the stability of boards, essential to a proper management of state-owned enterprises.

56 *International Monetary Fund Country Report no. 15/80. Romania*, March 2015, 24.

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CHALLENGES OF SERBIAN PUBLIC ENTERPRISES IN THE LIGHT OF POINTS C AND F OF OECD

Guidelines on Corporate Governance of State-Owned Enterprises: The Case of Public Companies

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This paper discusses the actual situation regarding the implementation of OECD Guidelines on Corporate Governance of State-Owned Enterprises (points C and F) in Serbia, through the case of public enterprises. Former and current legal solutions are compared and presented along with comments of competent bodies related to practice in order to identify positive steps towards the implementation of OECD standards. The focus is on how the state respects SOE boards exercising their responsibilities and independence, as well as whether it acts as an informed and active owner, exercising its ownership rights according to the legal structure of each enterprise.

Keywords:
Public Companies, SOE, independence, active owner

State-owned enterprises (hereinafter: SOE) in Serbia are regulated by a wide range of laws and therefore a range of different solutions is applicable to different kinds of SOEs.[1] In that sense, there are public companies, as specific enterprises owned by the state on national, regional and local levels, which conduct activities of public interest. Public companies in Serbia are regulated by the Law on Public Companies (hereinafter: The New Law).[2] There are agencies formed directly by the law, as well as agencies formed as not-for-profit limited liability companies. There are also public funds or other institutions in which state assets are managed. Furthermore, there are remnants of former socialist state-owned enterprises, which are in the process of privatization, where the state manages their equity in full or in part. It is estimated that there are around 1400 SOEs in Serbia, which are wholly owned by the state; while the number of those where the state holds a minority interest is substantially higher.[3] They employ some 250,000 people, a quarter of the total employment by companies in Serbia. Over two thirds of these employees are employed by the public companies, i.e. some 160,000 people working in 730 companies.[4]

Table 1. *State-owned enterprises in Serbia (estimated numbers)*

		Number of enterprises	Number of employees
State-owned enterprises	Total	≈1.400	≈250.000
	1. State public enterprises	≈40	≈80.000
	2. Commercial state-owned enterprises	≈10	≈20.000
	3. Enterprises under the jurisdiction of the Privatization Agency	≈670	≈90.000
	4. Local public enterprises	≈650	≈60.000

Source: Fiscal Council of Republic of Serbia, Assessment of state-owned enterprises in Serbia

It is estimated that a quarter of the budget of local self-governments goes to the local public companies that employ nearly half of all employees at the local level (77,000). The total number of local public companies is over 720, and among them 650 have a formal status of public company, while the remaining ones are budget users. The most important group of local public companies is a group of 350 utility companies, which employ more than 56,000 people.

1 There are companies under the control of the Privatization Agency: large public and state owned enterprises (subgroups monopolistic public companies and large state-owned enterprises operating in competitive industries) and local public companies, as well as agencies of various forms, funds and other entities.

2 Source: article 3 of the Law on Public Companies, source: Official Gazette of Republic of Serbia, No.15/2016 (hereinafter: the New Law); The New Law has substituted the earlier Law on Public Companies, source: Official Gazette of Republic of Serbia, No.119/2012, 116/2013 and 44/2014, in which the provision of the article 1 had the same definition of public companies.

3 Fiscal Council of Republic of Serbia (2014): *Assessment of State-Owned Enterprises in Serbia: Fiscal Aspects.* Belgrade, s.n., 7. Source: www.fiskalnisavet.rs/doc/eng/analysis_of_state-owned_enterprises-fiscal_aspect.pdf (15 July 2016)

4 *Ibid.*, 7.

These companies contribute to the economy modestly (2.4 percent of GDP is their added value), are illiquid, each year there are more loss-makers among them, and are generating and increasing losses despite significant direct and indirect subsidies. In addition, the utilities often receive indirect subsidies through "inflated" invoices for services delivered to the municipalities.[5]

Public companies, according to the law, can be established by the central state, municipalities and autonomous provinces. All but a handful of national public companies – including some of the largest ones, such as EPS, EMS, Post, Serbia Gas, Forestry Management, and Roads – and all 300 plus municipal utilities, fall under the law on public companies. A second group of companies have been corporatized into mostly joint-stock companies (JSCs) or in fewer cases to limited liability companies (LLCs), including Telekom, GALENIKA, JAT Aircraft Maintenance, Belgrade Airport, and Railroads. These companies operate under the Company Law that came into effect in February 2012.[6] In addition to these two laws, the Founding Acts and the companys' articles of association (except for limited liability companies) govern the rights, duties, and liabilities of the "founder" (in case of public companies) or the "shareholder" (in case of joint stock companies or limited liability companies) towards the enterprises and vice versa. The activities of both groups of companies are also regulated by sector-specific laws, although these laws focus more on sector policy-making and regulation rather than governance.[7]

In order to be able to concentrate on the topic of this article, OECD Guidelines of Corporate Governance of SOE in the light of points C and F, the study will focus on public companies as the most widespread and the most important form of Serbian SOEs. The paper will analyse how the Serbian state lets the boards of public companies exercise their responsibilities and to what extent it respects their independence. The prime responsibilities of the state as informed and active owner while exercising its ownership will also be analysed.

C. The state should let SOE boards exercise their responsibilities and should respect their independence

Up to this year, Serbian public companies were regulated by the Law on Public Companies,[8] (hereinafter: The Former Law) which defined two types of Serbian public companies regarding their strategic and operational management: 1. unicameral management, where company bodies are supervisory board and director, and 2. bicameral management, where company

5 Fiscal Council of Republic of Serbia (2014), 51.

6 Serbian Law on Commercial Companies, Official Gazette of Republic of Serbia, No Official Gazette of the Republic of Serbia, No. 36/2011, 99/2011, 83/2014 and 5/2015.

7 The World Bank (2015): *Report No. 67435-YF on International Bank for Reconstruction and Development Program Document for a Proposed Development Policy Loan to The Republic of Serbia for a First Programmatic State Owned Enterprises Reform Development Policy Loan*. Source: http://documents.worldbank.org/curated/en/967231468294609464/pdf/674350PGD0P127010Box385415B00OUO090.pdf (15 July 2016)

8 Source: Official Gazette of Republic of Serbia, No.119/2012, 116/2013 and 44/2014

bodies are supervisory board, executive board and director (CEO).[9] In both cases, however, the key body to transmit state power into operative management was the supervisory board. Its dependence on or independence of the state could be analysed following the provisions that define its formation. The executive board members were the nominated by the director (CEO), so they represented a part of his/her management team. The New Law does not differentiate between the unicameral and bicameral management, but simply defines that public company bodies are supervisory board and director (CEO).[10] The New Law after defining the director and his entitlements, as the person performing a public function,[11] also defines the executive director as the employee of the public company, exercising the entitlements defined by the director, founding act and by-laws of the public company.[12]

The Former Law defined that the Government of Serbia nominated the supervisory boards in public companies founded by the Republic of Serbia. It defined that one of its supervisory board members needed to be independent.[13] Independence was defined in the provision of article 14 of the Former Law, where it was said that such a member:

1. needs to be an expert in one or more activities of public interest for which the company has been founded;
2. that he/she has not been employed in any public, dependent or related company, two years prior to assuming the post of supervisory board member, i.e. that he/she has been in no way engaged by the public company, nor has been engaged in auditing financial reports of that company; or
3. is not a member of a political party.[14]

It can hardly be expected that one independent member of the body can ensure the whole body to act independently, however, it is an important step towards the culture of listening different opinions during the decision making process. On the other hand, it is not sure that the above mentioned characteristics of the independent member of the board are sufficient for his/her independence in acting. Furthermore, the whole body should act independently of party politics, rather they should act according to the adopted policy, strategies and measures of the government, or local self-government. However, it seems that the focus is on formal and not on essential issues, which should be to ensure the professional conduct of public enterprise officers, rather than the fulfilment of particular political interests of political parties (such as staffing or financial interests).

The New Law in relation to public companies formed by the Republic of Serbia defines that one of its members needs to be independent, while one of them needs to be an employee

9 Source: article 11 of the Former Law.
10 Source: article 15 of the New Law 2.
11 Source: article 24 and 25 of the New Law 2.
12 Source: article 27–29 of the New Law.
13 Source: article 13, paragraph 1 of the Former Law.
14 Source: article 14 of the Former Law. This complex provision insists on formal independence, persisting on criteria for particular person, who is to be nominated to be a member of the Board and not on his/her acting, i.e. decision making during his/her activity as the board member.

of the public enterprise.[15] This way, the New Law requires that two of five members of the supervisory board need to fulfil additional requirements, one of them to be independent and the other to be an employee of the public enterprise. The independence of a supervisory board member is deemed to be ensured:

a) if the member of the supervisory board has not audited financial reports of the company within the last five years,
b) if he/she is not a member of any political party, as well as
c) if he/she is not a state official, an employee or person on other basis engaged, by the public company or by the company, whose founder is that public company.[16]

As it can be seen, the independence should be guaranteed by various characteristics of the person, among which the important ones are the political engagement of the person and his/her engagement with the audit of financial reports of the public company. The third condition prevents a conflict of interest rather than ensures independence.

Which of these conditions ensures sufficiently the independence of the supervisory board member? It seems none. Being the member of a political party does not necessarily mean that such a person, with high moral integrity, will not act as an independent person when voting on a professional matter. On the other hand, a person fulfilling the above criteria might vote for all proposals on the supervisory board according to the ruling party's staffing or financial interests. It would be better to construct a legal standard that ensured independence by voting, than to select two or three characteristics of the person, which might represent, but not necessarily mean, the independence of the person. Also, one of the criteria excludes links with the public company that might represent a conflict of interest, which in itself prevents the nomination of such a person into the supervisory board.

In addition to an independent board member, the New Law requires that one supervisory board member needs to be an employee of the public company. Beside the general conditions that are valid for any person in order to be nominated for the member of the supervisory board, an employee of the public company needs to fulfil two additional conditions. It is curious that according to one of the three conditions that guarantee the independence of a person, the employee of the public company, in order to be nominated into the supervisory board, needs to fill two conditions, which are literally the same as the other two:

1. he/she has not audited financial reports of the enterprise for last five years, and
2. he/she is not a member of political party.[17]

As for this "semi-independence" of the employee of the public enterprise to be nominated into the supervisory board of the public enterprise founded by the Republic of Serbia, it is very interesting to see how this solution will work out in the practice.

The Former Law regulated the nomination of the supervisory board members of public companies founded by an autonomous province or a local self-government. The autonomous province or local self-government (i.e. the body defined in its by-laws) nominated

15 Source: article 17, paragraph 1 of the New Law 2.
16 Source: article 19 of the New Law 2.
17 Source: article 20, referring to Article 19, points 1 and 2 of the New Law.

supervisory boards, one member of which needed to be an employee of the public company.[18] These members of the Board had to be nominated according to the provisions of the by-laws of the public company.[19] At this governance level, it was not specified that an independent person should fill the post in the supervisory board, only that he/she should be an employee of the public enterprise.[20] Therefore, the regulations for supervisory boards of public companies formed by a lower governance level were different than the ones for public companies formed by the Government of Serbia. In addition, in article 14 of the Former Law it was suggested that the person employed in public company or dependent company cannot be treated as independent.[21]

The New Law does not require one supervisory board member of public companies founded by an autonomous province, or local self-government to be independent. However, it brings closer together persons deemed to be independent and employees of the company intermingling their characteristics. By the nomination for the supervisory board members, two conditions for nomination of an employee of the public company into the supervisory board are identical with the conditions that are set up for the independent person.[22] On the other hand, in article 20. par. 2 a new condition is added, which defines that an employee of the public company cannot be put forward for the position of supervisory board member by the supervisory board itself, by the director (CEO) or the executive director of the public company.[23] Why not? The answer could be to act independently.

The legislator should choose a uniform regulation for the nomination of the bodies of both the national and local public companies. Why should by national public companies one supervisory board member be independent, while by the local ones this is not required?

As far as the director (chief executive officer) of the public companies is concerned, according to the Former law, he/she had to be nominated by the Government of Serbia, in case the public company was founded by the central state. When founders of the public company were an autonomous province or a local self-government, the director had to be nominated by the body defined in the by-laws of the autonomous province, i.e. local self-government. In addition, the director should be nominated after a public competition procedure was conducted. The New Law did not introduce substantial changes to the regulations of the Former Law, except for the more complex nomination procedures.[24] Furthermore, among the conditions for selection, the candidate needs to prove that he/she

18 Source: article 13 paragraph 2 of the Former Law 8.

19 Source: article 15 of the Former Law 8.

20 It was more of a remnant of the earlier Yugoslav self-governance political system, than a step towards the independent exercise of modern boards in the public sector.

21 Article 14, paragraph 2 of the Former Law. So, in the same law, depending on the level of governance (central or local), different solutions are offered in order to resolve the same problems.

22 Source: article 20 and article 19, points 1 and 2 of the New Law. See also the above comment.

23 Source: article 20, paragraph 2 of the New Law. On the other hand, the Former Law defined only that the member of the supervisory board will be nominated according to the by-laws of the public company (article 16 of the Former Law).

24 Source: article 21, paragraphs 1 and 2 of the Former Law, and article 24, paragraphs 1–3 of the New Law. As for nomination procedures according to the New Law, see below.

is does not hold any office in a political party.[25] This means that the director should be a professional. It is questionable, however, that somebody who holds an office in the ruling political party after suspending his political activity to become the manager of a public company fulfills the necessary conditions of being an independent professional.

Regarding the practice in Serbian public companies, the Fiscal Council of the Republic of Serbia states that it widely held view that the internal inefficiency of SOEs is the sole or main cause of their poor performance. However, the improper management of public companies goes hand in hand with inadequate government policies through which fiscal and social considerations affect the public companies. These include: mandating low prices, enforcing delivery of goods to non-paying customers, support to non-productive employment, avoidance of closure of non-productive facilities (railway lines, some mines, etc.).[26] There is no reason not to accept the reasoning in the report of the Fiscal Council, that the public companies in Serbia are protecting the standard of living of the inhabitants, a tradition deeply rooted in the past. Therefore, a strong political pressure on their management to ensure low energy and services for the citizens. Non-productive employment in SOEs was, and still is, the artificial remedy to decrease the real unemployment rate, as well as to ensure work places for ruling party members. On the other hand, during political debates, in particular in pre-election campaigns, there is a strong demand for public companies to get a professional management.

Although the mentioned provisions regulating public companies in Serbia to certain extent are entering the path to allow independence of these bodies from the political parties' influence, there are still a number of obstacles in practice. Indicative is the following:

- In legislation there are obvious signs that intend to show that the supervisory board members are independent and exercise their responsibility by fulfilling their function,
- However, even legislative solutions are in contradiction and do not guarantee the independence of neither supervisory board members, nor the director (CEO) of the public company, because one independent member of the supervisory board or employee of the public company in the supervisory board is not able to guarantee the independence of the supervisory board as a whole. Not to mention that by the large majority of public companies, founded by local self-governments, it is not required that an independent member of supervisory boards should be nominated. The changes introduced in the New Law did not make much difference,
- Further, the mentioned practice that was identified by the Fiscal Council of the Republic of Serbia and their reasoning we have introduced in this article are not encouraging.

F. The state should act as an informed and active owner and should exercise its ownership rights according to the legal structure of each enterprise

It cannot be disputed that the state is interested in the activities of public companies in Serbia. However, how far it acts as an informed and active owner exercising its ownership

25 Source: article 22, paragraph 1, point 5 of the Former Law and Article 25, paragraph 1, point 7 of the New Law.
26 Fiscal Council of Republic of Serbia (2014), 15.

rights according to the legal structure of public company is questionable. In particular, unlike for public company there is no general assembly (shareholders' meeting), which is the usual ownership body in both companies and state entities.[27] The body whose members are directly nominated by the state is the supervisory board of the public company, into which the representatives of its founder are nominated (Republic of Serbia, autonomous province or local self-government), who hold the majority voting rights in this body. Thereby, the supervisory board brings both strategic and important operative decisions. The director (CEO) is nominated by the state, i.e. the government of Serbia, or, in case of the autonomous provinces and local self-governments, by the body, which is defined by its by-laws. It is obvious that various founding state entities that define the strategic and operative assignments of all public companies on their territory, have a substantial problem to understand and process information of various sorts and from different professional areas as efficiently as it could be done by the body acting within the public company. The supervisory board members, on the other hand, can have a little help from those who control all of them. Such outside bodies usually represent a "bottleneck" due to the overburdened agenda they have and the variety of problems they discuss. In such a situation, it is logical that these bodies pay attention only to those decisions that are the "hottest" and most acute issues on their list of priorities, and do not have time for a long-term and strategic thinking, what they actually should do.

Therefore, the statements of the Serbian Fiscal Council are critical and worrying. Evaluating current practice, the Serbian Fiscal Council states that in an environment where laws are not strictly enforced, it is pointless to discuss the quality of the legislation. The Former Law was not sufficiently implemented, and even when it was, the effectiveness of its provisions was questionable. The Law stipulated that executives should have been appointed through a public call, but during the year and a half the law was in force the deadlines for the public call and for the selection procedure were generally not met. In some cases, a public call was not announced at all (Srbijagas, Pošte Srbije [Serbia Postal Service], etc.). Concerning the weaknesses of the Law on Public Companies, the Fiscal Council evaluated the draft of the new law and pointed out the possibility of a pronounced Government influence on the selection of executives (the Government appoints three of five members of the Appointment Committee and makes the final decision on selecting the candidate to be appointed as head of a public company).[28]

1. BEING REPRESENTED AT THE GENERAL SHAREHOLDERS' MEETINGS AND EFFECTIVELY EXERCISING VOTING RIGHTS

Having in mind the process supervisory boards are formed and the nomination of the directors (CEOs) of Serbian public companies, there is no dispute that the state is

27 Serbian Law on Commercial Companies, *op. cit. in footnote 6*, foresees such a body both for shareholding companies, as well as for limited liability companies.

28 Fiscal Council of Republic of Serbia (2014), 17.

represented in them.[29] However, unlike the law on commercial companies, the law on public companies does not stipulate a general shareholders' meeting for public companies as its body, instead the adequate state level (Government of Serbia, or the provincial or self-government bodies nominated by them) directly controls the supervisory board and the director (CEO) of the public company.[30] This solution eliminates the existence of an "owner's body" within the public company, as the top body of the public company. So, the voting rights on strategic decisions related to the public company are not distributed in accordance with the percentage in which the state controls that body, but according to the number of supervisory board members that it controls. In addition, the nomination of the director (CEO) by the state (Government of Serbia, i.e. the body nominated by the autonomous province or self-government by-laws) helps to directly exercise the voting rights of the state. Even if we look back to the legal system before 2012, there were boards of directors and supervisory boards, as two bodies through which the state exercised its voting rights in public companies.[31]

Whether it is effective, it can be discussed with arguments pro and contra. Most of the problems come from the fact that the lack of shareholders' meeting diverts the state from concentrating on strategic decision-making towards participation in operative decisions, in particular in those that are concerned with financial or human resources management issues. The current practice supports the contra attitude. Another argument in favour of the general assembly (shareholders' meeting) as a body where the owner should be represented in the public company is the fact that the same principle that applies to corporate governance (as it functions by commercial companies according to the Law on Commercial Companies) should be valid for public companies, too. That way the system of "founder's consent", which is needed for certain public company decisions, could be replaced.[32] That way, the forming of a decision, which is crucial for the particular public company, is shifted to a state body (government or the defined commission), where the process is longer, with various conflicting interests and often with the participation of actors who are not too much interested in the strategic and operative problems of the particular public company.

29 Source the text under C. above.

30 Source: articles 13–15 of the Former Law, as well as article 15 of the New Law.

31 Transparentnost Srbija (2014): *Efekti novog Zakona o javnim preduzećima – politizacija ili profesionalizacija (The Effects of the New Law on Public Companies – Politisation or Professionalisation).* Belgrade, s.n., 7. Source: www.transparentnost.org.rs/stari/images/stories/inicijativeianalize/Efekti%20novog%20Zakona%20o%20javnim%20preduzecimapolitizacija%20ili%20profesionalizacija,%20oktobar%202014.pdf (15 July 2016)

32 National Alliance for Local Economic Development (2012): *Komentari na nacrt Zakona o javnim preduzećima (Commentaries to the Draft Law on Public Companies).* Belgrade, s.n., 3. Source: www.naled-serbia.org/upload/CKEditor/untitled%20folder/Komentar%20na%20nacrt%20zakona%20o%20Javnim%20preduzecima.pdf (15 July 2016)

2. ESTABLISHING WELL-STRUCTURED, MERIT-BASED AND TRANSPARENT BOARD NOMINATION PROCESSES IN FULLY- OR MAJORITY-OWNED SOES, ACTIVELY PARTICIPATING IN THE NOMINATION OF ALL SOES' BOARDS AND CONTRIBUTING TO BOARD DIVERSITY

The problem mentioned above, that public companies in Serbia do not have a general assembly (shareholders' meeting) hinders the establishment of a well-structured, merit based and transparent board nomination process. Currently this process occurs in the founder's organization, and happens usually after the elections, by nominating a number of representatives to the various public companies' supervisory boards. The priority of those who nominate them is often the distribution of the party's personnel to posts in public companies, which the particular party through cross-party political agreement has "gained" to fill. Such practice was often registered.[33] The particular cases varied from the nomination of exclusively ruling party members into supervisory boards and the nomination of a ruling party member as an independent supervisory board member to the nomination of the new board member according to the law that was not in force any more, as that law was substituted with a new law on public companies.[34]Similar is the situation with the nomination of representatives of employees into the supervisory board. There were cases where the director nominated the representative of the employees instead of the employees, or the collegium of directors nominated the employees' representative into the supervisory board, or even an outrageous one when the deputy director of the public company was the representative of the employees.[35]

As far as supervisory boards are concerned, there seemed to be a need for a new regulation: the members of the supervisory board to be appointed through an open call. This could foster professionalization and "de-partyzation" of public companies.[36] However, this did not happen, and legally it could be characterized, that the introduction of the principle to professionalize managers in public companies could not be deemed as obligatory for the supervisory board members.

The earlier practice of the nomination of commission members that conducted the open call for the selection of the director of the public company (which was in high degree volatile, without prior criteria to be set up) raised doubts that the open call for nomination of the director would lead to the professionalization of the management of public companies.[37] Beside this, it is interesting to note that the Anticorruption Agency of Serbia indicated in its earlier report that there was a risk of corruption in the nomination of directors of public companies.[38] It stated in particular that in the nomination process several institutions

33 Trasparentnost Srbija (2014), 18–20.
34 Ibid., 18–20.
35 Ibid., 20.
36 Fiscal Council of Republic of Serbia (2014), 17.
37 Trasparentnost Srbija (2014), 31.
38 Ibid., 32, 33.

participated, and their unclear competence and interwoven interests gave room for abuse.[39] The recommendation was to define the process of nomination of the director in more details in the law itself.

The New Law accepted this approach.[40] It determines three commissions for the nomination of the director of public companies:
– the Government's commission,
– the Commission of the Autonomous Province, and
– the Commission of the Local Self-Government Unit (article 31).

In addition, it defines the number of their members and the period for which they are nominated (articles 32 to 34); persons who cannot be members of these commissions (article 35); the procedures (articles 36 to 41) and how the director enters his/her post (articles 43 and 44). As the New Law entered into force this year, before evaluation we should wait to see how these provisions play out in practice.

However, based on the earlier practice, some experts pointed out that it there is no point in defining the required qualifications for executives and members of the supervisory board and demanding great responsibility and effort without any, or with modest remuneration. In any case, regardless of any changes in the legal framework, strict budget constraints, transparency and financial discipline of SOEs should be insisted on.[41]

3. SETTING AND MONITORING THE IMPLEMENTATION OF BROAD MANDATES AND OBJECTIVES FOR SOES, INCLUDING FINANCIAL TARGETS, CAPITAL STRUCTURE OBJECTIVES AND RISK TOLERANCE LEVELS

SOEs have an important role in the economy, but due to poor management, they have operated unsuccessfully imposing high fiscal burden on the state. In the past few decades, public companies were misused for hidden and very expensive social policies: manifested mostly through regulated or imposed low prices and tolerance of non-payments. There was also a tolerance for poor management, overstaffing, employee privileges, inefficiency, negligence and corrupt practices, and in some cases, they were used to absorb other loss-making enterprises with no real prospects.[42] Operational performance indicators are in most cases extremely low.[43]

Government decisions have even supported certain bad management decisions (Srbijagas, a large loss-maker, took over other loss-makers and rescued them from bankruptcy). Social peace was bought with artificial prices (at the cost of rising debt), and overstaffing

39 Ibid., 33.
40 See provisions of articles 30–45 of the New Law.
41 Fiscal Council of Republic of Serbia (2014), 17.
42 Fiscal Council of Republic of Serbia (2014), 9–10.
43 Ibid., 11.

was tolerated. Some of the examples of the Government inconsistence in the enforcement of its own decisions and laws: fiscal non-compliance, such as issuance of guarantees in case of exceeding the limits estimated by the Fiscal Strategy and the arrangements with the IMF; diverging from the wage policy in the public sector (with numerous exceptions and acceptance of the trade unions' demands); non-compliance with the Law on Public Companies in relation to the adoption of a business plan and the appointment of managers through a public call; ignoring the recommendations of the State Audit Institution. Failure to comply with the law in management of public companies is a signal that the state had no sincere intention to improve their performance. Once again, this is a signal that it pays out not to play by the book.[44]

The analysis shows that some of the characteristics of state companies are: inadequate control, poor results, mismanagement, and lack of transparency in business operations and of management responsibility. The consequence is larger fiscal costs and continuous pressure on public finances. Given the seriousness of the problems and the need to make a quick shift in this area, it would be rational to establish a body within the Government or the Ministry of Economy. This body would be charged with monitoring and coordinating plans for public companies, initiating reports and analysis, determining the procedures for developing objectives and operational indicators, initiating and ensuring cross-sector business analysis (including financial), and engaging in other activities that would contribute to transparent, accountable and successful operation of companies. This body would deal with what is common in the operation of public companies, while the relevant ministries would remain competent in specific sector policies. In the first phase, the centralized management should certainly focus on a significant increase in transparency (financial ratios and performance of companies) and identification of any violation of the law.[45]

The process of appointing the management of public companies and other state owned enterprises is much politicized. In theory board members and directors are appointed by the government, but in practice, their nomination is the outcome of cross-party negotiations and agreements.[46]

4. SETTING UP REPORTING SYSTEMS THAT ALLOW THE OWNERSHIP ENTITY TO REGULARLY MONITOR, AUDIT AND ASSESS SOE PERFORMANCE, AND OVERSEE AND MONITOR THEIR COMPLIANCE WITH APPLICABLE CORPORATE GOVERNANCE STANDARDS

Public companies' reports on business plans is limited to annual plans, and the reporting usually lacks clear objectives and operational performance indicators. Business plans are adopted with delay (sometimes even at the end of the year for the previous year). Little attention is

44 Ibid., 14.

45 Fiscal Council of Republic of Serbia (2014), 17–18.

46 Arsić, Milojko (2012): Reform of State Owned and Public Enterprises. *Quarterly Monitor,* No. 28., 76. Source: http://fren.org.rs/sites/default/files/qm/L2.pdf (15 July 2016)

paid to the evaluation of the achieved results. In addition, some companies ignore the legal obligation to publicly disclose their business plans and financial statements, or they do so with unacceptable delay (sometimes even of several years). The relevant ministry (currently the Ministry of Finance) supervises the business plans and financial statements; however, this supervision is mainly focused on financial indicators, rather than on planning and ongoing management. The opinion of the Fiscal Council is that the public must be informed in detail, accurately and timely about the operations of SOEs in order to identify problems and provide timely and adequate responses from both the public and the Government.[47] This includes the public companies as well.

Although the Ministry of Finance supervises the business plans and financial statements of public companies, this surveillance is largely focused on the compliance with financial guidelines, and not on the quality of strategic planning and management.[48] The criteria according to which independent supervisory board members shall not have audited the financial reports of the public company in the last five years needs to be reconsidered. This criteria should be replaced with ones that ensure the real independence of supervisory board members (providing conditions for them to act independently and professionally, rather than insisting on characteristics which do not guarantee their independence).

The introduction of general assemblies (shareholders' meetings) as owner's bodies within the public enterprise would better ensure their regular monitoring. This way the evaluation of public companies, their directors and supervisory boards would be much more productive. For sure more productive than sending numerous reports to one coordination body formed by the Government of Serbia or competent body within the particular local self-government or autonomous province.

5. DEVELOPING A DISCLOSURE POLICY FOR SOES THAT IDENTIFIES WHAT INFORMATION SHOULD BE PUBLICLY DISCLOSED, THE APPROPRIATE CHANNELS FOR DISCLOSURE, AND MECHANISMS FOR ENSURING THE QUALITY OF INFORMATION

As a consequence of the relatively closed system of information flow between the public company and its founder (the Republic of Serbia, autonomous province or local self-government), the publicity of information related to activities of public companies is also limited. The transparency in publishing the results of operations is limited, especially when it comes to operational indicators, plans and results. Reporting on business operational indicators is almost entirely limited to the annual business plans, which are not publicly available. Although business plans contain plenty of detailed information, they are primarily related to short-term financial plans (i.e. annual plans for the next year), and very little attention is paid to the evaluation of the results achieved. The lack of focused and coherent results evaluation framework is also noticeable, which could, for example, consist of a small

47 Fiscal Council of Republic of Serbia 2014, 16–17.

48 Arsić (2012), 76.

number of carefully selected financial and operational performance indicators (which should also be internationally comparable), which could be used to monitor the public enterprise by the owner (state) and would be publicly available.[49]

Too much politics within public enterprises prevents the availability of wider range of information for the public. Due to the distribution of the key positions in public companies among the political parties in power, they are often the subject of attacks by political opponents, which may involve unfounded accusations. That causes the supervisory board members and executives not to reveal more information than necessary for annual reports. In consequence, they usually withhold information not to prevent the public from being informed, but rather not to give political opponents too much material to develop affairs.

6. WHEN APPROPRIATE AND PERMITTED BY THE LEGAL SYSTEM AND THE STATE'S LEVEL OF OWNERSHIP, MAINTAINING CONTINUOUS DIALOGUE WITH EXTERNAL AUDITORS AND SPECIFIC STATE CONTROL ORGANS

As far as this topic is concerned, there is no lack of communication between external auditors and specific state organs and between public companies.

According to the Serbian Law on State Audit Institution,[50] the State Aid Institution is legally obliged to conduct annual audits of public companies.[51] The engagement of auditors to check the financial reports of public companies and their communication have educative aspect, too. There are reports that the capacities of the State Audit Institution has recently been increased to perform a better control of the operations of public companies.[52]

Auditors, as well as the finance and accounting inspectors, during their visits to public companies, take the opportunity not only to control their records, but also to educate. They draw the attention of finance and accounting professionals who work in public companies to particular demands concerning operations, or how to cover such operations properly with adequate records in the books, with proper financial and accounting documentation. All these operations in public companies need to be adjusted to numerous legal provisions and international standards that need to complied with.

On the other hand, the control organs of the Ministry of Finance of Serbia continuously follow the balances and accounts of public companies, both of those that are founded by the Government of Serbia and of those that are founded by local self-governments.

49 Arsić (2012), 76.

50 The Law on the State Audit Institution, The Official Gazette of the Republic of Serbia, No 101/2005, 54/2007 and 36/2010.

51 See in Government of the Republic of Serbia (2014): *Negotiation Position of the Republic of Serbia for the Intergovernmental Conference on the Accession of Serbia to the European Union, Chapter 32, Financial Control,* Belgrade, s.n. Source: http://eukonvent.org/eng/wp-content/uploads/2016/05/Negotiating-Position-of-the-Republic-of-Serbia.pdf (15 July 2016)

52 Ibid.

Public companies also need to have external audits with a number of projects they implement. They submit project proposals to various funds in order to find additional financial resources in addition to those provided by the government, ministries or local self-governments, i.e. which are received for the services they render to citizens and companies. An auditing is also required according to the provisions of loan contracts they conclude with the World Bank, European Bank for Reconstruction and Development, or other banks when receiving loans. Similar obligations come out of contracts with international donors when public companies receive certain grants – foreign donations.

Therefore, it can be concluded that the communication with external audits and specific state control organs is not lacking.

7. ESTABLISHING A CLEAR REMUNERATION POLICY FOR SOE BOARDS THAT FOSTERS THE LONG- AND MEDIUM-TERM INTEREST OF THE ENTERPRISE AND CAN ATTRACT AND MOTIVATE QUALIFIED PROFESSIONALS

A clear remuneration policy in SOE boards that would attract and motivate qualified professionals is not established. There is also strong criticism related to the costs of improving the management of public companies. The difference in remuneration in public companies in various local self-government units is usually based on their economic strength. A lot of innovation related to the motivation and attraction of professionals could be facilitated without large resources. It is unclear why this matter is not adequately regulated, because there are no high social costs for such a measure (as it would be the case with the release of surplus employees in the public sector or increasing the prices of products and services of public companies). However, improving the management of public companies would lead to a loss of personal and political rent, and reduce irregular employment (political party, family, etc.). In order to successfully improve the management of public companies, it is necessary to take measures to prevent these illegal interests.[53]

What has recently been happening is the introduction of a salary cap in the whole of the public sector in Serbia, which entered into force at the end of 2013 and was prolonged for a further period at the end of 2015. This encourages the deprofessionalization of the management of public companies as it prevents the adequate remuneration of executives and board members who achieve results and show creativity and talent. Further actions should be taken to decrease the number of employees in public companies. Strong political criticism is directed against the high number of managers in public companies; in particular in those founded by the Republic of Serbia. Excess in quantities, however, affects the quality of management, which needs to be addressed.

53 Arsić (2012), 75.

8. CONCLUSIONS

The following can be concluded:

Serbia as a country in transition and the EU accession process urges the country to harmonize the functioning of its public companies with the OECD Guidelines on Corporate Governance of State-owned Enterprises. However, there is still work to be done, both in legislation, and in the practical implementation of the law.

The key problem concerning the independence of the public companies' boards (which should be respected by the state – II C), is the lack of criteria to ensure the independence of supervisory boards and directors in implementing what they are expected to do as professionals. The problems stem from the inherited practice that the boards and management of public companies are considered to be posistions to employ ruling party personnel rather than bodies to be managed by the professionals. The New Law opens space for changes in a positive way.

Regarding the State as an informed and active owner that exercises its ownership rights according to the legal structure of each enterprise (II F) one of the key problems is the lack of a general assembly, where the state, via its representatives could execute its owner's rights within the body of the public company. A further problem is the structure and formation of supervisory boards and the nomination of directors, particularly due to the vaguely defined procedures of their nomination, and how the result of their activities on these posts are to be evaluated (lack of criteria, insufficient procedural protection from corruption and abuse of rights of those evaluating their results). Therefore, monitoring is inadequate, while the transparency of their work is questionable, due to the fact that only financial statements are obligatory to be published and distributed. Auditing and the public companies' communication with auditing and financial control bodies is a bright spot, while the remuneration of boards members is not adequately regulated and quite volatile (earlier the remuneration of public company board members was high, in particular at national level, while nowadays, the remuneration cap in the public sector makes these posts less attractive, in particular at the local levels). The New Law raises hopes that this issue will evolve in a positive way.

9. SUMMARY

The author in this article analyses current challenges of Serbian SOEs with regard to the implementation of Points C and F of OECD Guidelines on Corporate Governance of State-owned Enterprises. First, the legal provisions of the earlier and current laws concerning public companies are compared, then the Serbian Fiscal Council's stance on their implementation is presented, finally some concluding remarks are offered. These remarks refer to responsibilities and independence of the public companies' boards, as well as to the conduct of the state as an informed and active owner. Several problems are highlighted: first, the lack of a general assembly within public companies; second, the problems with the structure, formation, monitoring and control of supervisory boards with a special emphasis on the disclosure policy of public companies; third, the remuneration of board members. The author points out the willingness of the state to cope with these problems, however, with poor results so far.

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REPORT ON CORPORATE GOVERNANCE IN STATE-OWNED ENTERPRISES – THE POLISH PERSPECTIVE

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Since the last Polish parliamentary elections in 2015, some deep changes have been announced in the legal framework of state-owned companies. The changes are supposed to be mainly targeted at setting different rules of remuneration policy of the boards' members compared to private-owned companies. They are meant to conquer recognised abuses in management and supervision areas of state-owned companies, which have not been overcome by recent, quite liberal legal regulations, nor by self-limitation and self-control. In addition corporate governance in Polish state-owned enterprises is facing massive changes. At the beginning of 2016, former Minister of Treasury Dawid Jackiewicz announced liquidation of the Ministry of Treasury in January 2017, and the revision of State's supervision over the SOE. After liquidation of the Ministry of Treasury, ownership rights over SOEs will be exercised by sector ministries. The aim of the paper is to analyse the implementation of Chapter II of the OECD Guidelines on Corporate Governance of State-Owned Enterprises' provisions into Polish legal order governing state-owned enterprises.

Keywords:
state-owned enterprises, Ministry of Treasury, Polish legal order

1. INTRODUCTION

The aim of this paper is to analyse the implementation of Chapter II of the OECD Guidelines on Corporate Governance of State-Owned Enterprises' (hereinafter: the OECD Guidelines) provisions into Polish legal order governing state-owned enterprises (hereinafter: the SOE).

More than 25 years ago in Poland a wide and rapid transformation of state enterprises into commercial companies began, making them operate according to roughly the same economic and legal rules as private-owned companies. Their insufficient supervision by the major shareholder (the state or other public authority) as well as common lack of wise management and self-limitation of people responsible for running state-owned companies combined with repeating nominations to the boards of persons with a decent political background instead of solid experience in business led to widely acknowledged abuses in managing state-owned companies in Poland over that time. They were especially seen as a privilege of interests for certain individuals and tied to political and business connections over unquestioned goals for the companies and their major shareholder. Since the great political and economic transformation in Poland in the late '80s, state-owned companies were recognised as "spoils of war" by the winners of parliamentary elections, which was a common sin of all political parties governing Poland over that time. After the elections, state-owned companies were subject to deep personal changes, which most of the times were not entirely motivated by merits.

Several months ago, as a result of the recent elections in Poland that took place in the fall of 2015, some deep changes have been announced in the legal framework of state-owned companies. It is worth mentioning that no significant changes have been made over the last 15 years, although the legal framework was far from perfect. The changes are supposed to be mainly targeted at setting different rules of remuneration policy for the boards' members compared to private-owned companies. They are meant to conquer recognised abuses in management and supervision areas of state-owned companies, which had not been overcome by recent, quite liberal legal regulations, nor by self-limitation and self-control. Also corporate governance in Polish state-owned enterprises is facing massive changes. At the beginning of 2016, former Minister of Treasury Dawid Jackiewicz announced the liquidation of the Ministry of Treasury in January 2017, and revision of State's supervision over the SOE. On 4 October 2016, the Prime Minister announced that ownership rights over SOEs would be exercised by sector ministries.

2. THE SOES' LEGAL FORMS (POINT A OF THE OECD GUIDELINES)

In Poland State-owned enterprises most commonly operate in the forms of capital companies, either a limited liability company or a joint-stock company. A marginal role is played by state enterprises which are entirely owned by the Treasury and operate by virtue of the State Enterprises Act on 25 September 1981. Currently, there are only two state enterprises which

are supervised by the Ministry of Treasury.[1] State enterprises are separate legal persons from the Treasury, but do not constitute capital companies within the meaning of the Commercial Companies Code of 15 September, 2000.

The majority of state-owned enterprises operate in the form of capital companies, to which provisions of the Commercial Companies Code of 15 September, 2000, are generally applicable. Thus, in external relations state-owned companies are generally subject to the same legal framework as private companies. Nonetheless, there exist specific provisions of competition law and law on public aid which apply to stated-owned companies.

Further differences between state-owned and private companies consist of the way state-owned companies' internal relations are conducted. However, such differences are allowed under the OECD Guidelines.

When discussing the internal relations in the SOEs, consideration must be given to the regulations and ordinances of the Minister of Treasury or Prime Minister, which supplement generally applicable legal acts but lack sanctions for non-compliance. As a result, in Poland, there is no binding corporate governance code designated to state-owned companies. However, there exist The Principles of Corporate Supervision over Companies with State Treasury Shareholding (second edition) introduced by the Ministry of Treasury in 2005, but these should be regarded as a soft-law act with a rather limited practical impact.

The Principles contain recommendations regarding corporate governance, e.g.

- aims of corporate supervision;
- functioning of supervisory boards;
- functioning of management boards;
- monitoring entities within Treasury shareholding;
- cooperation of supervisory board and shareholder's proxy with a certified auditor, monitoring company audit;
- cooperation of supervisory units with supervisory boards or shareholder's proxies;
- supervision over subsidiaries.

The Principles were introduced in accordance with regulation No. 41 of the Minister of Treasury. While drafting The Principles the Ministry of Treasury collected comments, observations and suggestions from bodies managing and supervising commercial entities within State Treasury shareholding in order to further improve, streamline and increase the effectiveness of corporate supervision.

The Principles shall be considered as a soft law, since the Minister of Treasury is not empowered to issue generally applicable legal acts which regulate corporate governance in state-owned companies. Accordingly, the Principles do not provide for any specific rules on corporate governance, but rather gather existing principles into one document and express expectations of the state authority. Those expectations are treated as a guideline for government bodies or public entities in the process of developing their own solutions.

1 I.e. *Biuro Urządzania Lasu i Geodezji Leśnej* and *Kopalnie i Zakłady Przetwórcze Siarki "SIARKOPOL" w Tarnobrzegu*.

There is a good practice, that being a copy of The Principles is sent to every newly appointed member of state-owned companies' supervisory board together with the notice of appointment. However, no *comply or explain* rule applies consequently and the Principles are rarely observed.

In its report of 2009, the Supreme Audit Office noted that establishment of internal regulations (including the Principles) enabled corporate supervision over state-owned companies. However, the regulations were not observed in practice (even by the Ministry of Treasury itself) or were improperly implemented. Furthermore, the Supreme Audit Office pointed out a number of irregularities, e.g. lack of analyses of companies' financial and economic standing.

In practice, major importance for the functioning of supervisory boards have schedules in the Principles, particularly Schedule 1 in the Principles, i.e. Recommendations for the Treasury's sole-shareholder companies and Treasury's majority-shareholder companies preparing annual financial statements of the company. The financial statements which are to be presented during the general meeting are based on Recommendations. Introduction of precise rules of reporting, especially the standard forms for financial statements, is an element of corporate governance in state-owned companies.

It is worth noting that state-owned companies listed on the Warsaw Stock Exchange are subject to the Best Practice of Warsaw Stock Exchange Listed Companies. In such event state-owned companies are obliged to observe the *comply or explain* rule. Nonetheless, the Best Practice of the GPW Listed Companies is generally applicable to all companies listed, regardless of whether the companies are state-owned or not.

3. THE SOES' MANAGEMENT AND INDEPENDENCE (POINTS B AND C OF THE OECD GUIDELINES)

Subsequent governments continue to intervene in the SOE's management and redefine SOE objectives in a non-transparent manner.

The difference between interest of the SOE and interest of the State – its major shareholder – is still not observed. This is exemplified by a practice of increasing SOEs share capital from reserve capital in order to advance budget revenues due to the CIT.

However, widening control over capital companies by majority shareholders is a regular practice, it seems to be a particularly sensitive issue in the SOEs.

Currently, the burning issue is political impact on hiring decisions in SOE, which is subject to wide criticism since the boards' members are removed regularly after parliamentary elections.[2] The SOEs' bodies which are most commonly put in jeopardy are supervisory

2 Postuła, Igor (2013): *Nadzór korporacyjny w spółkach Skarbu Państwa.* Warszawa, Wolters Kluwer Polska S.A. Source: https://sip.lex.pl/#/monografia/369268038/3 (9 October 2016); Wiatrowski, Piotr (2014): *Niekonstytucyjna regulacja tzw. konkursów do rad nadzorczych spółek Skarbu Państwa.* In Kidyba, Andrzej ed.: *Skarb Państwa a działalność gospodarcza.* Warszawa, Wolters Kluwer S.A. Source: https://sip.lex.pl/#/monografia/369301832/66 (9 October 2016)

boards, as in state-owned companies' management board members are usually appointed and removed from the office by the supervisory board.[3] It should also be noted, that supervisory boards not only appoint management boards' members, but also run the qualification procedure for management boards. Thus, from a political perspective supervisory boards are the first port of call.

The Commercialization and Privatization Act is silent as regards qualification requirements of members of management boards'. Nevertheless, according to sec. III (1) (2) of the Principles of Corporate Supervision over Companies with State Treasury Shareholding, boards members are expected to: possess appropriate educational background and experience, combined with resourcefulness and drive to continually improve the economic and financial standing of the company as well as aim at increasing its value and competitiveness. They should also have the ability to cooperate with the rest of the company employees. Such wording is open to a wide range of interpretations.

As regards supervisory boards, the selection process is conducted through a public qualification procedure, in accordance with Ordinance No. 45 of the Minister of Treasury of 6 December, 2007, on the principles and procedures for selecting candidates for the composition of supervisory boards in state-owned commercial companies and for supervisory boards of other legal entities supervised by the Minister of Treasury. Supervisory board members are appointed and removed from the office by the general meeting. However, in former state enterprises (which existed prior to 1989, now operating as commercial companies) two-fifths of the members are elected by employees and the election made by employees binds the general meeting (Art. 14 of the Commercialization and Privatisation Act).

Furthermore, members of supervisory boards must be qualified to sit on supervisory boards, which includes passing the exam for candidates for supervisory board members (art. 12 par. 2 of the Commercialisation and Privatisation Act) or having a license exempting them from the obligation to pass this exam, i.e. having a PhD degree in economics or in law or being listed as a legal advisor, attorney, certified auditor and/or investment advisor.

In practice, the applicable legal framework is insufficient to prevent or minimalize the political impact on SOE's hiring policy. Scholars point to a number of practices which allow politics to intervene in SOE's management.

Firstly, qualification procedure to supervisory boards is conducted only if it is recommended by the Director of a particular Department of the Ministry of Treasury and accepted by the Minister of Treasury. If the election is to be organised without a qualification procedure, then the Ministry is not obliged to announce the election to the public (§ 3 of the Ordinance No. 45 of the Minister of Treasury of 6 December 2007). Such regulation renders the election procedure non-transparent and allows for nominations and appointments to SOE's boards based not on candidate's competences and experience but rather on political support.

3 The rule does not apply to board members elected by employees under art. 19a of the Commercialization and Privatization Act.

According to press information,[4] since the last parliamentary elections around 200 new board members were appointed. According to the Supreme Audit Office report, between 2004–2008, 65% of supervisory boards' members were removed without any justification.

Recently, it turned out that Bartłomiej Misiewicz, a public relations officer in the Ministry of National Defence and a Polska Grupa Zbrojeniowa S.A. (the armaments industry) supervisory board member, did not pass the exam for candidates for supervisory board members and has no higher education. Referring to the Misiewicz case, the Minister of National Defence Antoni Macierewicz stated that: "inthe armaments industry there is no need for such a requirement [of higher education and passed exam] but there is a requirement for loyalty, cooperation, competence and decisiveness. All of these features are possessed by Mr. Misiewicz".[5] The case of Misiewicz is not an exception. In 2005, the Supreme Audit Office[6] pointed out that 46% of supervisory board members did not pass the required exams although they were bound to do so. In this case it is explicit that when it comes to political interest the law is not observed at all. Furthermore, it shall be highlighted that there are no strict legal consequences of appointing a person who does not meet the formal requirements. Especially, nobody has ever been sued or criminally accused of breach of law here.

Secondly, appointment of the Ministry of Treasury officials as board members is regarded to be a bonus for an official, paid not by the Treasury but by the SOE.[7] Previously, candidates to supervisory boards employed by the Ministry of Treasury or by other ministries were appointed without a qualification procedure. Although the law concerning this issue has been amended, officials are still appointed outside of the public qualification process, as the qualification process is not obligatory. Furthermore, the Ministry of Treasury provided neither code of ethics for state officials serving as supervisory board members, nor conflict of interest rules. The problem was raised by the Supreme Audit Office in 2009, which stated: "it should be highlighted that participation of state officials in supervisory boards may lead to conflicts of interest. The reason for that is that one person merges work in the entity's supervisory board with supervision over the entity in the ministry".[8]

4 Cieśla, Wojciech – Krzymowski, Michał (2016): *Dwustu ludzi dobrej zmiany*. Source: www.newsweek.pl/polska/lista-nominacji-pis-w-spolkach-skarbu-panstwa-i-instytucjach-panstwowych,artykuly,381794,1.html (26 September 2016)

5 Skarżyński, Stanisław (2016): *Afera misiewiczowa. Macierewicz złamał prawo*. Source https://oko.press/afera-misiewiczowa-macierewicz-lamie-prawo/ (26 September 2016)

6 Najwyższa Izba Kontroli (2005): *Informacja o wynikach kontroli wykonywania obowiązków przez przedstawicieli Skarbu Państwa w spółkach prawa handlowego*. Source: file:///Users/kaja/Downloads/px_1999061%20(1).pdf (9 October 2016)

7 Postuła, Igor (2011): Problemy polityki personalnej w radach nadzorczych spółek Skarbu Państwa. *Problemy Zarządzania,* Vol. 9, No. 4 (34). 226–246. Source: http://pz.wz.uw.edu.pl/sites/default/files/artykuly/pz_4_2011-1_postula.pdf (9 October 2016); Siemiątkowski, Tomasz (2014): *Spółka Skarbu Państwa to nie przedsiębiorstwo państwowe.* In Kidyba, Andrzej ed.: *Skarb Państwa a działalność gospodarcza*. Warszawa, Wolters Kluwer S.A. Source: https://sip.lex.pl/#/monografia/369301832/66 (9 October 2016)

8 Najwyższa Izba Kontroli (2009): *Informacja o wynikach kontroli sprawowania nadzoru właścicielskiego w spółkach z większościowym udziałem skarbu państwa*. Source: www.nik.gov.pl/plik/id,1682,vp,1900.pdf (9 October 2016)

Taking into account that state officials are subordinated to the Minister of Treasury (or other minister), appointment of the State employees in SOEs' supervisory boards clearly jeopardises the boards' independence.

Considering further the issue of supervisory board members' independence, it should be explained that there are formal requirements as to the independence for members in supervisory boards in the Treasury's *sole-shareholder* companies. Art. 13 of Commercialisation and Privatisation Act provides that as long as the State Treasury remains the sole shareholder of the company, members of the supervisory board of that company shall not:

1. remain employed by the company or provide work or services for its benefit under another legal title;
2. have shares in companies set up by the company, except shares admitted to public trading under separate provisions;
3. remain employed by the companies referred to in subparagraph 2 or provide work or services for their benefit under another legal title;
4. perform work which would be contrary to their duties or might arouse suspicions of partiality or mercenaries. Furthermore, as a member of a supervisory board cannot be a person who is employed as a member of the Polish Parliament or European Parliament members' offices; or is employed by a political party or is a member of a representative body of political party.

Defects of such regulations are quite straightforward. First of all, there is no formal limit for a supervisory board candidate to be a member of political party. However, some authors argue that there is no need to introduce such limitation on candidates to supervisory boards as it does not prevent situations in which candidates would be supported by a political party.[9] Thus, possibly the only way to provide factual independence of supervisory boards' members is introducing an obligatory public qualification process and precise selection criterion.

4. CENTRALISATION OF OWNERSHIP RIGHTS (POINT D OF THE OECD GUIDELINES)

Up to now Poland was assessed by the OECD as a one of the countries with centralized organization of ownership rights in SOEs.[10] Currently, the organization of ownership function over SOEs is subject to fundamental changes.

The ownership entity in the light of point D of the OECD Guidelines is the Ministry of Treasury. The Ministry of Treasury was created in 1996, and replaced the Ministry of Ownership Transformations. The Ministry of Treasury consist of ten Departments (i.e. Department of Ownership Supervision or Department of Strategic Companies) and Offices.

9 Postuła 2011.

10 The OECD (2005): *OECD Comparative Report on Corporate Governance of State-Owned Enterprises*. Source: www.thepresidency.gov.za/electronicreport/downloads/volume_4/business_case_viability/BC1_Research_Material/OECD_Comparative_Analysis.pdf (9 October 2016)

To date, the bulk of SOEs are under the supervision of the Ministry of the Treasury. A relatively small number of SOEs is (or – taking into account the recent changes – *was*) supervised by other Ministries, in particular by the Ministry of Energy and the Ministry of Infrastructure as well as by regional authorities.

Nonetheless, the Ministry of Treasury is to be liquidated in the first quarter of 2017. When announcing liquidation of the Ministry of Treasury, the Minister of Treasury Dawid Jackiewicz stated that the Ministry of Treasury is to be replaced by an agency or holding company. It was the Minister's duty to provide government with a draft legislation on the new organisation of ownership functions over SOEs.

In the first half of 2016, a number of SOEs was transferred from the Ministry of Treasury to the Ministry of Energy, Ministry of Development, Ministry of Economy, Ministry of Maritime Economy and Inland Navigation.

Surprisingly, the Minister of Treasury was dismissed by the Prime Minister on 15 September 2016, and the final stage of liquidation of the Ministry of Treasury will be supervised by Henryk Kowalczyk – head of the government's Standing Committee. In her official statement the Prime Minister said that: "Dawid Jackiewicz met his obligation. He presented a concept and statutory solutions. Now the Government will carry on legislative procedure".[11] The Prime Minister also pointed out that the supervision over State-owned companies is to be the most efficient, transparent and free from any pathology (i.e. political impact on board nominations).[12]

During the press conference on 4th of October, 2016, the Prime Minister and Minister Kowalczyk announced that substantive supervision over the SOEs will be exercised by sector ministries, whereas the ownership supervision will be exercised by a specially constituted body within the Chancellery of the Prime Minister, and kept under direct control of the Prime Minister. Furthermore, a council for State-owned companies is to be established within the new ownership entity. The council would be responsible for nominating and appointing candidates to SOEs' boards.[13]

In the light of OECD Guidelines, such change in ownership policy is a step backwards. On the conference[14] concerning SOEs on capital market, Professor Maciej Bałtowski considered that currently the State is destroying corporate governance in SOEs rather than mending it. The consequences of establishing a decentralised model of ownership function may be different than envisaged.

The reform of ownership function is justified by the will to combine the recent model of organisation together with sector expertise. However, the tendencies among the OCED countries are the opposite, and the countries aim instead to centralise ownership function. Referring to the decentralised model the OECD noted that: "[t]he main advantages and

11 Press release, source: www.premier.gov.pl/wydarzenia/aktualnosci/likwidacja-ministerstwa-skarbu-panstwa.html (8 October 2016)

12 *Ibid.*

13 Press release, source: www.premier.gov.pl/wydarzenia/aktualnosci/nowy-nowoczesny-sposob-zarzadzania-spolkami-premier-beata-szydlo-o-nadzorze.html (8 October, 2016)

14 Conference "State-owned companies on capital market", Warsaw, 6 October, 2016.

rationale for such a decentralised organisation are sector expertise and the capacity to implement a more active industrial policy. With the shift from industry specific policies to more framework-oriented and market liberalisation policies, *the advantages of such an organisation have now vanished* (emph. added). The management of state-owned assets is shifting towards an ownership view with a focus on added value, and SOE are less perceived as instruments of industrial policy than they used to be".[15]

Furthermore, it should be highlighted that the decentralised organisation model was used in Poland prior to the transposition to market economy, and the restoration of a decentralised model carries a risk of negative connotations.

Unfortunately, at the moment of final completion of this paper (in mid-October 2016) no further official information or drafts have been presented to the public. Thus, it is impossible to address in detail other issues, such as the creation of an ownership entity within the Chancellery of the Prime Minister or council for State-owned companies. Nevertheless, it appears that the political impact on SOEs may be even stronger after the reform.

5. ACCOUNTABILITY OF THE OWNERSHIP ENTITY (POINT E OF THE OECD GUIDELINES)

Due to current centralisation of ownership rights in the Ministry of Treasury, the relationships with relevant public bodies are yet clearly defined and the Minister of Treasury is accountable for the way it carries out state ownership rights before the Parliament. The Parliament may demand the Minister resign from office or to be dismissed by Prime Minister. Furthermore, members of the Parliament have a right to ask the Ministry of Treasury questions regarding exercising of state ownership rights.

Annually, the Minister of Treasury provides the Government and the Parliament with a report on the economic and financial conditions of state assets as well as with a report on economic and financial conditions of SOEs. The reports are published in the Public Information Bulletin of the Ministry of Treasury and are available to anyone.

It should be explained that the Polish Supreme Audit Office is a constitutional body which supervises government administration as well as other entities listed in the Constitution and other acts (including SOE). The Supreme Audit Office is also empowered to provide entities with post-inspection instructions and recommendations.

The Supreme Audit Office inspected SOE a number of times (e.g. in 2005, 2009 and 2013), by its own motion as well as on request of other state bodies or members of Parliament, in terms of exercise of ownership supervision over SOE. However, the recommendations of the Supreme Audit Office are not always implemented or observed.

The autonomy of the Ministry of Treasury in terms of fulfilling its responsibilities is wide. The Ministry also enjoys some degree of budgetary autonomy that safeguards its flexibility.

Taking into account liquidation of the Ministry of Treasury in 2017, it is not yet clear how these issues will be regulated in terms of holding company or state agency.

15 The OECD 2005.

6. POLAND AS A WELL INFORMED AND ACTIVE OWNER (POINT F OF THE OECD GUIDELINES)

Previously, Poland did not act as a well informed and active owner of the SOE. This was subject to criticism and noticed by the Supreme Audit Office's reports. In reports of 2005 and 2009, the Office negatively assessed activity of the Ministry of Treasury. However, in the 2013 report the assessment was positive.

6.1. Representation at the general shareholders' meetings (point F(1) of the OECD Guidelines)

The State is represented at the general shareholders' meetings by the Department of Ownership Supervision of the Ministry of Treasury. The organizational structure of the Ministry of Treasury and competences of particular departments are governed by Ordinance No. 4 of the Minister of Treasury on establishment of organization rules and regulations of the Ministry of Treasury. It should be noted that organization rules and regulations are frequently amended and reflect political changes. Furthermore, detailed procedures of state representation and conduct of ownership supervision is subject to internal regulations of the Ministry which are not publicly available.

Certain departments of the Ministry of Treasury act as communication channels between the SOEs and the Ministry of Treasury. The SOEs provide adequate departments with periodical reports, information, draft resolutions which are further analysed and processed by state officials. Some authors point to the stabilizing role of state officials in exercising ownership rights as their work positions and duties are not dependent on any political factors.[16]

6.2. Board nomination process (point F(2) of the OECD Guidelines)

As it was considered in point 3 of the Report, nominations to the SOEs' boards are severely politically impacted, and this has not been overcome for more than 25 years. Despite the establishment of a structured qualification process, there is still a possibility for a candidate to avoid its completion and become a member of the SOEs' body. Many of the criteria for candidates are based on flexible and unclear factors, which finally make it possible to appoint any desired person.

In the SOE's which are of key importance for the Treasury, candidates are selected by an external recruiter. However, the decisive factor standing behind the appointment is still political.[17]

In 2010, the government proposed the establishment of a nomination committee which would be competent to select and nominate candidates to supervisory boards of the most

16 Postuła 2013.
17 *Ibid.*

important SOEs in the Treasury's portfolio. Unfortunately, the nomination committee was never established and the idea itself vanished from the public discussion.

It should be underlined that the existing legal framework requires candidates to SOEs' boards to have both a certain level of degree and experience. The Ministry of Treasury also provides Good Practices on the selection of boards' candidates to SOEs' of key importance for the Treasury. These regulations are not always observed in practice though.

In the line with OECD Guidelines, the Ministry of Treasury runs a database of candidates, who passed the exam for supervisory board members in the SOE. Data of persons who are exempted from completing the exam are added to the database on request. The database is not publicly accessible.

As regards the OECD Recommendation on Gender Equality in Education, Employment and Entrepreneurship, in June 2015, the Ministry of Treasury established Good Practices in terms of ensuring a balanced participation of women and men in the governing bodies of companies with state treasury shareholding. According to statistics of the Ministry of State Treasury, 29,5% of the members of the supervisory boards – representatives of the State Treasury in companies with the State Treasury shareholding listed on the Warsaw Stock Exchange – are women.[18] Thus, women are under-represented in supervisory and managerial positions in companies with State Treasury shareholding.

The Practices aimed at achieving at least 35% average participation of women among all the members of the supervisory boards selected and appointed by the Minister of State Treasury by the year 2020.

6.3. Reporting duties (point F(3) and (4) of the OECD Guidelines)

Besides annual reports required under the Companies Act, SOEs are subject to additional reporting duties.

The SOEs provide the Ministry of Treasury with detailed reports on: management board activity, report on the SOE's activity in the previous financial year and report on the examination of financial reports.

Besides the mentioned reports, the SOE provides two quarterly reports. One, giving information on financial situation, financial credibility, the remuneration of employees and potential risks, is to be accepted by the supervisory board and submitted to the Ministry of Treasury. The second report on sureties and guarantees granted is to be submitted to the Ministry of Finance.

In order to provide timely and proper exercise of SOEs' reporting duties, the Ministry of Treasury annually provides SOEs with Guidelines on financial reporting.

18 Ministerstwo Skarbu Państwa (2015): *Good practices in terms of ensuring a balanced participation of women and men in the governing bodies of companies with State Treasury shareholding*. Source: www.msp.gov.pl/en/corporate-supervision-1/good-practices/7213,Good-practices-in-terms-of-ensuring-a-balanced-participation-of-women-and-men-in.html (9 October 2016)

6.4. Transparency and disclosure (point F(5) of the OECD Guidelines)

There is no disclosure policy applicable exclusively to the SOEs. However, the SOEs are subject to generally applicable legal norms which provide for information disclosure, e.g. in case of public companies (i.e. companies listed on stock of exchange).

6.5. External auditing (point F(6) of the OECD Guidelines)

In Poland the SOEs in the form of joint-stock companies are required to be audited by a certified and independent external auditor.[19] It should be noted that such a requirement is not designed especially for the needs of SOEs, but generally applicable to all joint-stock companies. It is each supervisory board's responsibility to select an external auditor, and selection should be based on auditors' experience, independence and price. The external auditor's selection procedure is provided by Ordinance No 34 of the Minister of Treasury of 29 September, 2008.

Furthermore, the SOEs may be controlled by the Supreme Audit Office on its own motion or on third-party request.[20]

6.6. Remuneration policy

6.6.1. Regulation on boards members' remuneration between 2000–2016

Prior to the year 2000 there were no strict regulations aimed at setting any rules or limits for remunerations of the boards' members in state-owned companies in Poland. As a result of serial abuses exposed during the decade of the '90s, a new act was introduced in 2000.[21] It was primarily meant to target social expectations, thus its practical role in establishing effective limitations to excessive wages has often been questioned. The act of 2000, apart from state-owned companies also covered state agencies and other legal forms of entities owned or co-owned by the state and local governments, excluding state offices and administrative bodies. It focused on setting limits to remunerations of members of the management boards, supervisory boards and main accountants of the entities in question.

The act established numerous limitations in different areas referring to benefits received by members of the boards. It indicated a monthly wage as the base of the benefits, which could be supplemented in case of executives by an annual reward and additional benefits. The remuneration of state-owned companies was to be set by a shareholder's (state) representative. Its maximum amount was indirectly set by the act of 2000, and referred to

19 Art. 64 of the Accounting Act of 10 April, 2010 (consolidated text: Journal of Laws of 2016, item 1047).

20 Art. 2 of the Supreme Audit Office Act of 23 December, 1994 (consolidated text: Journal of Laws of 2015, item 1096 amended by Journal of Laws of 2016, item 677).

21 The act of 3 March, 2000, on remuneration of executives in certain legal entities (consolidated text: Journal of Laws of 2015, item 2099).

the index of an average monthly wage in enterprises as of the last quarter of the previous year as announced by the Central Statistical Office of Poland.[22] Thus the maximum amount of remuneration set out by the act of 2000, varied between the index level multiplied by 1 (for supervisory board members) and the index level multiplied by 6 (for management board members).

The annual reward could have been granted by the shareholder (state) if several conditions were met, mainly related to economic effects of the company during the previous year. Its maximum amount was set to the tripled monthly remuneration of the management board member who was to be granted the reward.

Additional benefits which could have been granted to management board members comprised of items such as insurance policy, bonuses to cover costs of living and commuting, etc.[23] Their total annual amount could not exceed a maximum annual amount of base remuneration for management board members. Any terms of contracts between state-owned companies and their boards' members that determined their benefits in the amounts exaggerating the maximums set out by the act of 2000, were null and void.

Summing up, according to the act of 2000, management board members had an opportunity for average monthly earnings equalled to approx. 7500 € gross (approx. 6000 € net pay),[24] excluding indirect benefits (additional insurance etc.). Compared to private companies and taking into account satisfactory economic results achieved by the company, this was rather a modest level of income, which could not be able to attract top managers and caused demands for seeking additional profits. That has led to an introduction of several practical cheats which were used to increase a total income of executives in state-owned companies. The practices including i.e. receiving additional remunerations for being boards' members in holding companies, preparing paid reports for the company or "golden parachute" contracts, revealed serious flaws in the act of 2000, thus making it ineffective towards business reality.

6.6.2. The new regulation of 2016, on boards members' remuneration

As the act of 2000, had been widely criticised, not only because of its flaws and ineffectiveness in fighting excessive wages of executives, but also for setting improper and anti-incentive pay, the new government established in fall 2015, was determined to pass an updated regulation

22 The index for Q4 2015, which is the base for setting remunerations in 2016, equalled to 4280,39 PLN, which can be roughly converted as 1000 € gross (approx. 810 € net pay). It is worth mentioning that between 2010 and 2015, the index – for the purpose of setting the remuneration limit in state-owned companies – was artificially equalled to Q4 2009 and amounted to 3454,58 PLN (approx. 800 € gross, 650 € net pay). Thus for 5 years remunerations of boards' members in state-owned companies were not linked with the economic growth in Poland and placed behind current trends in private enterprises.

23 Tomaszewska, Monika (2013): Prawo do świadczeń dodatkowych na tle przepisów ustawy o wynagradzaniu osób kierujących niektórymi osobami prawnymi (ustawy kominowej). *Gdańsko-Łódzkie Roczniki Prawa Pracy i Prawa Socjalnego,* 2013/3. page 129 and further.

24 Calculated as a maximum allowed monthly wage (6000 €) supplemented by a maximum allowed annual reward represented as a monthly average (18 000 € / 12 = 1500 €).

which was supposed to introduce a totally renewed approach. Consequently, on 9 June 2016, the act on rules of setting remunerations of executives in certain companies[25] was adopted. It was not supposed to replace nor repeal the act of 2000, however the new act sets out the rules for boards members' remuneration in all state-owned and local government-owned companies, including those with state participation at a level lower than 50%, leaving the hitherto rules determined by the act of 2000, in other state-owned entities.

The act of 2016, provides different determinants of executives' remunerations in companies. Their remuneration shall consist of two parts. The first one is fixed and depends on the operational level of the company, including its assets, incomes and employment rates. The fixed part depends on the index of an average monthly wage in enterprises as of the last quarter of the previous year announced by the Central Statistical Office of Poland, which is multiplied by 1 to 3 in small companies[26] and by 7 to 15 in the biggest companies[27] (there are 5 levels defining the company size). The exact rate of remuneration for executives is to be set by supervisory board. The board may also exempt from the rules set above under "special conditions" (certain examples have been provided by the Article 4 sec. 4 of the act), however if the remuneration granted shall be higher than the limits set out by the act, the state shareholder has to announce publicly the reasons for such ruling. In publicly traded companies (co-owned by the state) the remuneration can be set accordingly to the current levels in other publicly traded companies of a comparable size and branch of business.

The second part of remuneration (annual reward) is variable and depends on successful completion of business goals of the company in the previous fiscal year. Its amount may not be higher than 50% (not higher than 100% in publicly traded companies and in the biggest companies) of the annual fixed remuneration. The business goals are set out in resolutions of the supervisory board and may include i.e. increase of net gain or net income, change of production rate, reduction of costs, change of certain economic indexes, etc. The business goals for holdings are evaluated for the entire family of companies.

Management board members cannot be paid for acting as members of the boards of subsidiaries. They may however be granted additional profits, along with the remuneration (fixed and variable). If the supervisory board's resolution provides that, the executives may use the company's assets essential for their work, such as i.e. apartment, car, computers, mobile phones etc. Secondly, a terminal wage can be provided to an executive – replacing exaggerated "golden parachutes" –, which shall not be higher than his/her total fixed remuneration for 3 months, provided that he/she has acted as management board member for at least 12 months in the company. Thirdly, compensation rate for prohibition of competition has been severely limited and cannot exceed a 6-month fixed remuneration.

25 Journal of Laws of 2016, item 1202. The new act entered into force on 9 September 2016.

26 Having up to 10 employees or annual net turnover lower than 2 millions € or assets owned were lower than 2 millions € (at least two conditions met).

27 Having over 1251 employees or annual net turnover over 250 millions € or assets owned over 215 millions € (at least two conditions met).

Remuneration of supervisory board members is limited to the amount of an index of an average monthly wage in enterprises as of the last quarter of the previous year announced by the Central Statistical Office of Poland, which is multiplied by 0.5 in small companies and by 2.75 in the biggest companies.

In state-owned and local government-owned companies with their participation of at least 50% of shares, the resolutions setting remuneration levels and their grounds are published by the dominant shareholder and available on the internet.

7. CONCLUSION

As the Report shows, the ownership supervision in Poland still needs development and improvement. Unfortunately, the SOEs are regarded as part of a political scenery, connecting the tempting worlds of politics and business. Although a lot of time has passed during the last 25 years and many abuses have been revealed, hardly any efforts have been taken to improve transparency, efficiency and balance in SOEs. It may be argued that such an omission, although depriving and having adverse results for the State Treasury and SOEs, was comfortable for all major political parties which governed Poland.

Nevertheless, some current developments should be assessed positively, e.g. the new remuneration policy. If we compare the new remuneration rules with the old ones and then compare them with Chapter II, letter F.7 of the OECD Guidelines on Corporate Governance of State-Owned Enterprises (2015 Edition, p. 19), we can see general progress in fulfilling the goals set out by the Guidelines, especially in setting remunerations at levels than could attract and motivate qualified professionals. However if we combine it with a general unsatisfactory level of adopting Chapter II, letter F.2 rule of the OECD Guidelines (clear nomination policy), it may be questionable if this goal – of attracting well-skilled managers – can be effectively achieved, even though the remuneration levels shall not be seen as a problem. Also a link between the economic effectiveness of a company and remuneration levels has been introduced which seems to comply with fostering long- and medium-term interests of the enterprise in the OECD Guidelines. However still a clear remuneration policy is missing, allowing the levels to be adjusted in certain range in individual cases.

The new rules of 2016, can be described as more complex, apparently rather transparent and allowing to set comparable remunerations' levels with other publicly traded companies. However, the rules are not strict, allowing adjusting remuneration levels "manually" in certain cases, which may provide for justified results on one hand and help attract successful managers by setting their wages on a comparable level to private companies. On the other hand, it may lead to arbitrary decisions on remuneration, which would be based only to a minor extent on rules which are clear and common to everyone. The Ministry of State Treasury in Poland foresees savings of about 60 Millions PLN each year due to the new regulations on remuneration levels in state-owned companies.[28]

28 Press release, source: http://biznes.onet.pl/praca/ustawa-kominowa-wynagrodzenia-w-spolkach-sp-9-wrzesnia-2016/

In the authors' view the main and still unsolved problem is the political impact on SOEs' supervisory and management boards. The practice of replacing SOEs' board members after parliamentary elections seems to be a bonus for the winning party. Unfortunately, such practice is perceived as *normal* by a part of society, and SOEs are treated as the property of the governing party. Thus, it appears to be of highest importance to provide *obligatory* public qualification process and establish an independent nomination council or committee to select board's candidates to SOEs in the Treasury's portfolio. The future will show whether a council for State-owned companies by the Chancellery of the Prime Minister will be independent enough to safeguard compliance with the OECD Guidelines, Chapter II, points B and C. However, the arrangement of the council within an ownership entity, which forms part of the Chancellery of the Prime Minister raises considerable scepticism as to its independence and autonomy.

Furthermore, the reform of ownership function is contrary to recommendation covered by point D, Chapter II of the OECD Guidelines.

The general situation of corporate governance in SOEs is harmful for SOEs itself. Over the last year,[29] value of SOEs noted on the Warsaw Stock Exchange decreased 39 million PLN,[30] and significant political impact on SOEs' management (even in the minority-owned companies) renders them unattractive for private investors. Due to government's ownership policy Professor R. Czerniawski proposed to classify SOEs on the Warsaw Stock of Exchange as high-risk companies.[31]

Taking into account, that SOEs still play an important role on Polish capital market, their shaky position could have undesirable effects on the economy. Thus, regardless of recent reform, there is a need for a diametrical change in policy on corporate governance of SOEs.

29 The author compared the value of listed SOEs just before parliamentary elections in 2015, and after one year

30 Biedrzycki, Paweł (2016), *Wartość spółek Skarbu Państwa na giełdzie spadła o 39 mld zł od zwycięstwa PiS w wyborach*. Source: https://strefainwestorow.pl/artykuly/20160926/wartosc-spolek-skarbu-panstwa-na-gieldzie-spadla-o-39-mld-zl-od-zwyciestwa-pis-w (9 October 2016)

31 Conference "State-owned companies on capital market", Warsaw, 6 October 2016.

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Zóra Zsófia LEHOCZKI

REVIEW OF THE INTERNATIONAL CONFERENCE TITLED "CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES IN CENTRAL AND EASTERN EUROPE"

On 14 October 2016 an international conference – organized jointly by the Institute of Civilistics (institute of the Faculty of Political Sciences and Public Administration) and by The Societas – Central and Eastern European Research Network – took place on the Ludovika Campus of the National University of Public Service. The main topic of the event was "Corporate Governance of State-owned Enterprises in Central and Eastern Europe" and the main organizers of the conference were Prof. Dr. Tekla Papp, head of the institute and Dr. Ádám Auer, assistant professor of the Institute.

The well-known scholars, who gave a lecture were the following: Professor Martin Winner from Vienna University of Economics and Business; Kateřina Eichlerová, assistant professor from Charles University in Prague; Kaja Zaleska-Korziuk, research and teaching assistant form the University of Gdańsk; Bartłomiej Gliniecki, post-doctoral fellow from the University of Gdańsk; Edvardas Juchnevicius, associate professor from the University of Gdańsk; Professor Branislav Malagurski from Educons University, Novi Sad; Professor Emőd Veress from Sapientia University and Professor Tekla Papp and Ádám Auer assistant professor, both from National University of Public Service.

The topic of the event was special and unique because nowadays corporate governance is a very popular research field and more and more articles and treatises are written in connection with this topic but the Corporate Governance of State-owned Enterprises is still a relatively unknown area for researchers and only a few publications can be found in connection with this special matter. The legal regulations relating to state-owned companies contain only a few rules concerning the principles of corporate governance and these rules do not always succeed or it is hard or even impossible to find any information whether they come across or not. On the other hand, transparency and trustworthiness are the basic principles regarding the operation of state-owned companies, so there is a discrepancy between these rules and the above-mentioned problems concerning the lack of information. These discrepancies should be disclosed and legal experts play a very important role in finding a solution to these issues. The uniqueness of the conference was that it provided a unique opportunity to outline these inconsistencies not only in the Hungarian system but in seven different countries in Central and Eastern Europe.

The opening speech was held by Prof. Dr. Norbert Kis, Vice-Rector of the University for Continuing Education and International Affairs. After welcoming the guests, he stated that the topic of the conference is very important concerning the profile of the National University of Public Service and from the view of the required and satisfactory governance of state-owned enterprises as well. He also highlighted that the upcoming presentations contain a lot of important and useful information not only for the students but for lecturers and practicing lawyers, too.

The second part of the opening was presented by dr. Gergely Szutrély, legal director-general of the Hungarian National Asset Management Inc. (MNV Zrt.). He outlined the connection between the state and state-owned companies in Hungary and he spoke about the role of the state as an owner also mentioning that the operation of the national assets is divided between the state and local governments. He also introduced the basic principles of the activity of MNV Zrt.; he stated that the rules of national asset management are in balance with the OECD Guidelines on Corporate Governance of SOEs. He mentioned the most important state-owned enterprises in Hungary and he drew the audience's attention to the importance of providing transparency in connection with the national assets. According to Mr. Szutrély, the state should manage its assets similarly to market conditions.

One of the main points of the lecture held by Professor Martin Winner was the question of the success of the principles of autonomy and independence in connection with state-owned enterprises. He pointed out that these companies have great financial and economic influence and because of this influence it is very important to impose the same rules on each and every shareholder. He stressed the importance of the success of transparency and also emphasized that these companies must operate independently from political influence. According to Professor Winner, in spite of the fact that the most important fundamental rules are established by the government, during the everyday operation of the company the principle of autonomy should come across in connection with the decision-making progress. He also stated that it is very hard to comply with this requirement but he pointed out the difference between being passive and the prohibition of intervention. According to Professor Winner, the state should operate as an informed and active owner and the key words of its operation should be professionalism and efficiency. The Professor introduced the changes in the Austrian regulation from the last couple of years and he also analyzed the impacts of these changes. He briefly touched upon the Austrian Public Corporate Governance Code, which prescribes for greater companies to have a supervisory board; this board must approve several decisions and dealings. According to Professor Winner, the main goal is to find balance between being independent and being controlled and in his opinion, finding competent, suitable directors would be just as important as complying with legal regulations in order to achieve the proper operation of state-owned enterprises.

In her presentation Kateřina Eichlerová provided an insight into the relevant regulations of the Czech Republic. She introduced the system of companies operating with state ownership and she made a comparison between state enterprises and state-owned joint stock companies. In her lecture, she pointed out the fact that state enterprises do not own any properties, all of their fortune and assets are owned by the state and these enterprises have a director with limited liability and they also have a supervisory board, the members of this board must be

natural persons. State-owned enterprises are economically dependent on the state and this connection is the strongest between the state and the joint-stock companies.

Kaja Zaleska-Korziuk and Bartłomiej Gliniecki jointly held their presentation focusing on the important changes in the Polish legal regulation, which came into force only one month before the conference. In the first part of their lecture, Kaja Zaleska-Korziuk pointed out that politics in Poland has a great influence on state-owned enterprises. A few years ago an initiative tried to change this situation by recommending that members of the board should be appointed by an independent nominating committee but this proposal did not succeed and because of the previously mentioned problems state-owned companies are not attractive for investors. The powers and rights connecting to the owners are centralized and these tendencies usually weaken the success of corporate governance guidelines. In the second part of their presentation Bartłomiej Gliniecki introduced the normative rules for the remuneration of directors with especial regard to the recent changes in the legal regulation. The new Act regulates five categories of state-owned enterprises and it prescribes in every category that how many times must the monthly average earning be multiplied to get the remuneration of the members of the board, for example the monthly average earning must be multiplied by 1–3 times in small businesses and 7–15 times in big companies. The enterprises can exceptionally differ from these rules but they must publicly explain the reasons of the change. The lecturers pointed out that even though this wage is much higher than the average, it is still way lower than the remunerations in the competitive sector and as a result of this being a member of the board of directors is still not very attractive for well-qualified experts in Poland.

In his presentation Edvardas Juchnevicius provided a glimpse into the characteristics of the Lithuanian system of state-owned enterprises. There are around 131 SOEs in Lithuania and most of these provide public services or public transportation. These companies operate in three different forms, such as state enterprises, limited liability companies and private limited liability companies. He pointed out that since the economic crisis the regulations have become stricter and the powers of decision-making and governing are decentralized for state-owned enterprises, these companies are operated by 12 ministries and 5 other institutions and as a result of the above-mentioned structure an economic growth has started in Lithuania.

Professor Branislav Malagurski from Serbia laid the emphasis on the effectiveness of points "C" and "F" from the OECD Guidelines on Corporate Governance of State-owned Enterprises. He stated that there are too many rules for state-owned enterprises in Serbia but these laws can be found on different levels of the legal system and they change very often and fast. According to Professor Malagurski, the most important decisions are made by people appointed by the state and not by shareholders and because of this the political impact is unfavourably great. The supervisory board has most powers concerning the operation of the companies and these boards have five members, out of these five only one must be independent and another one must be employed by the enterprise. The control system is not working very well either, since the reports contain the data regarding only one year and they are usually not completely objective. The success of transparency is limited, the plans are made for only one year without any no long term planning and the realization of plans is not effectively supervised.

In his presentation, Professor Emőd Veress introduced the main points of a decree which contains the regulation of state-owned enterprises in Romania; this ordinance came into force in 2011. He pointed out that some rules of the decree were changed in the summer of 2016 and the purpose of the new regulations is to ensure transparency. This Emergency Ordinance contains obligatory rules for the operation of state-owned enterprises. Professor Veress pointed out that there are special rules for the greatest state-owned enterprises in Romania, for example the company must hire an independent HR specialist in order to name the directors and only one or two director candidates can be appointed by the state.

The last presentation of the conference was held jointly by Professor Tekla Papp and Ádám Auer; they highlighted the core points of corporate governance and after that they introduced the condition and the realization of corporate governance of state-owned enterprises in Hungary. They emphasized that in Hungary we still have a lot of unanswered questions in connection with this certain topic. Unfortunately, legal regulations contain only a few rules for the operation of state-owned companies and the other problem is the fact that in Hungary there is no special company form for state-owned enterprises. After introducing the relevant rules, the lecturers stated that because of the above-mentioned unanswered questions and because of the lack of legal regulations the principle of transparency, unfortunately, fails to be realized in some cases.

After the presentations, the lecturers gladly answered every question from members of the audience and from their colleagues as well. All in all, the international conference provided a great opportunity to discover the current state of corporate governance of state-owned enterprises in the surrounding countries. During the lectures the audience heard a lot about unanswered questions and uncertainties in the legal regulation and these issues prove the importance and the up-to-dateness of the topic of the conference. The scholars all agreed that they still have a lot to discuss and they are going to relate their experiences next time they meet because the regulations and practices are still changing very fast, so maybe in one year they are going to have more experience or, on the contrary, they are going to have a conversation about completely different matters and rules.

One of the greatest values of the conference was the fact that the acknowledged experts on company law came from seven different countries and they introduced seven different systems of corporate governance of state-owned enterprises, so they had the opportunity to exchange their views with each other and the audience had a glance into seven different legal systems and into seven similar but still different interpretations and regulations of corporate governance of SOEs.

Dr. Zóra Zsófia LEHOCZKI (zora.lehoczki@gmail.com) received her law degree at the University of Szeged in 2016 and continued her studies as a PhD student at the National University of Public Service, Faculty of Political Sciences and Public Administration. She carries on her research work in the Institute of Civilistics; her research field is company law with especial regard to the topic of the capital of companies. She pays marked attention to the capital and assets of State-owned Enterprises.

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