

2.Laurentiu Gheorghe

“Privatisation, Institutional Culture and Corruption in Romania”

Introduction

Discussing privatisation in connection with corruption is neither easy nor very original. Especially in Eastern Europe where for the last decade were written very pertinent and documented studies concerning this issue.

In almost all of them the link between communist mentality, the difficulties of transition from a centralised economy to a market economy, the inevitable corruption connected to almost any transfer of propriety from the state to private actors were made and there is not much room left for other explanations.

The aim of this paper is to study the link between the deficient institutional culture and corruption in the privatisation process in Romania. Even though the institutional culture is a factor mentioned in the studies concerning corrupt practices in privatisation, the authors tend to blame the communist system for almost all the wrongs of the emerging post communist institutions (Ceobanu 1998, Miklos, Rus).

But not all the countries from Eastern Europe enjoyed the same communist legacy, in some of them the communist regime was more permissive and criticised (The Czech Republic, Poland) whereas in others the communist regime was tighter (Romania, Bulgaria, Former Soviet Union). Nevertheless the general weaknesses of the institutions in those countries as presented by a World Bank Report¹ were: the lack of accountability and of civil liberties, the iron fisted control of the Party, the hyper centralised bureaucracy, the culture of state intervention, the existence of parallel informal norms.

Some of the countries though managed to overcome those weaknesses faster than others. Political will played an important role in this respect, but there were other factors involved as well, institutional tradition before communism was one of them.

In choosing how to privatize and in handling the actual privatisation state institutions played an important role. My task is to show how in Romania the institutional culture played an important role in the hijacking of privatisation by corruption. By corruption I understand a behavioral failure to exercise the invested authority in terms of public good, often in a form of clandestine exchange in return for some profit. (Ceobanu)

2.The Institutions

In the World Bank Report² about state capture there is a very interesting distinction made between countries with a long tradition of sovereignty and a sound institutional legacy (i.e. countries formerly part of the Habsburg monarchy) and countries who didn't benefit from this legacy.

Romania 's case is complex because part of the country was under the Habsburg ruling, but since the privatisation process was centralised and decided at the national level, this fact is not particularly relevant for this study, though if we have in mind the post privatisation corruption and the performances of privatised enterprises, the part of Romania belonging to the Habsburg Empire has a lower rate of corruption then the rest of the country.

Taking into account only the 20th century Romania had a policy of centralisation of power in the administration. Partly due to the national unification process, which ended politically speaking in 1918, partly because of a strong tradition of centralised governing

¹ “Anticorruption in Transition”

² “Anti corruption in transition “

dating from the 19th century. Apart from a short period of time between 1923 and 1938, when some kind of feeble but promising democracy was in place, Romania experienced several dictatorial regimes until 1989.

The arrival of communism only ideologically changed the nature of the institutions, leaving in place almost the same bureaucratic and centralised system. To have an idea: the functioning scheme of the police remained roughly the same from 1936 to 1989 despite the change of four political regimes and the change of the name from police to militia.

This history of centralisation combined with the almost omnipotence of the government was the basis on which the communist regime laid its foundations. The particular nature of communist institutions blended with the existing practices give birth to the most centralised administrative system in Eastern Europe.

During communism several features came to define the practice of public institutions: inefficiency; lack of internal authority (almost complete inability to implement rules within the institution); internal precariousness (reduced capacity of satisfying legitimate interests of the employees and thus assuring their loyalty); corruption; passiveness (low capacity of independent action, without pressure from the exterior); lack of external autonomy (low capacity of resisting abuses or manipulation from external institutions , persons) ; lack of internal autonomy (low capacity of resisting to the manipulation and abuses of its own leaders)³ .

Another very important feature acquired during communism was the arbitrary ways of justice. Like in the Stalinist years justice had nothing to do with formal laws, but was concerned with short time punitive campaigns against “certain” members of the administrative apparatus. That was a powerful incentive to create informal networks which parasitised official structures and offered protection to those public officials who “contributed” to the welfare of those networks.

The fall of communism had but a minor impact on these institutional practices. For members of state institutions, democracy meant lack of accountability and freedom to seek their own interests.

Since they had access to information and benefited of the help of the informal networks, some of them emerged as the new businessmen. But nevertheless maintained the same institutional practices even at the level of their own private firms.

3. Privatisation

In 1990 Romania together with all the Eastern European countries started the inevitable road to market economy. For this privatisation was essential. In the majority of cases this privatisation was done by state agencies, apart for so called spontaneous privatisations done by almost illegal means by the managers of state owned enterprises.

There are standard and non-standard means of privatisation: the standard means currently used in Eastern Europe were public auction, public tender and direct sell. The non-standard means are in general mass privatisation schemes like the voucher scheme applied in the Czech Republic or the manager employee buyout scheme applied in Romania. The difference between those two methods is that in the later preference is given to the insiders, the employees having a preferential treatment over the foreign investors

In Romania the preferred method of mass privatisation was the manager employee buyouts method (MEBO) for small and medium sized enterprises combined with standard methods for big size industrial giants.

³ A.P. Iliescu “ Transition failure and institutional flaws”

The mass privatisation process included the creation of five “Private Ownership Funds” POF (FPP)s and one “State Ownership Fund” SOF(FPS). The function of the POFs was to administrate the private owned vouchers distributed by the state to the population, though the population was free to invest their vouchers directly in state owned enterprises subjected to the privatisation process. The function of SOF was double: to administrate the state owned enterprises until they are privatised and the shares that the state kept for itself after partially privatizing some enterprises, selling the control pack of shares to private investors; and to privatize by direct sale, or public auctions state owned enterprises under its administration.

The pace of the privatising process wasn’t very encouraging, in 1990 the private sector output was 15% of the Gross Domestic product, as compared to the Czech Republic’s 5%; in 1997 it was only 55% compared to the 75% of the Czech Republic.

Even though from 1996 to 2000 the government adopted a more aggressive strategy of privatisation the consequences of the stagnation between 1990 and 1995 are still felt by the Romanian economy.

The slow pace of the privatisation problems was furthermore slowed by a number of trials in which the public auctions that were organised for the privatisation of certain enterprises were contested either by the attorney general’s office or by unsatisfied contenders.

This slow pace wasn’t particularly generated by a political unwillingness to privatise. The political factors weren’t opposed to privatisation in itself but were reluctant to undertake such privatisations that didn’t bring them or their interest groups certain benefits. More than that they opposed such privatisations as long as there weren’t illegal incentives for them. It is interesting that in the 1990s one of the government’s supporters slogans was “We’re not selling our country”, but as soon as the government secured its power and the financial interests of its members, it started a campaign to attract foreign investors.

4. Corruption

Everywhere in the world privatisation is inextricable linked with powerful vested interests and consequently with corruption, especially in transition economies where usually there is no specific interest and respect for the public good.

Particularly in Romania the environment in which the privatisation process took place was one perverted by massive administrative corruption at all levels.

In the Transparency International Corruption index in 1997 Romania was on the 37th position with a score of 3.44 in 2001 Romania reached the 69th position with 2.8 points*.

In the same time Romania has the highest level of administrative corruption in Central and Eastern Europe excluding former soviet states⁴.

This combined with the most wide spread method of privatisation applied in Romania, MEBO, favored furthermore corruption.

Certainly there are ways in which you can avoid being overwhelmed by corruption in the privatisation process, for instance the safest way to privatise is the voucher method, which doesn’t allow the intervention of the state officials in the privatisation process and is fast and transparent. Compared to the MEBO method proves to be more efficient and reliable.

Corruption Potential in Two Privatisation Methods*

<i>Method</i>	<i>Indicators of Privatisation</i>
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* on a scale from 1 to 10 1 being the most corrupt , 10 being the least corrupt

⁴ “Anti corruption in transition”

	<i>Timing</i>	<i>Transparency and Access to Information</i>	<i>Administrative Discretion</i>
Voucher-Based Mass Privatisation	--	--	--
Management-Employee Buyout Privatisation	+	++	++

* Note: "-" and "--" equal low and very low corruption potential, respectively.

"+" And "++" equal high and very high corruption potential, respectively.

Source: (Compiled from Daniel Kaufmann and Paul Siegelbaum, "Privatisation in Transition Economies," *Journal of International Affairs*, 1996, Vol. 50, p. 434).⁵

For political reasons the MEBO method was adopted. And that was the most important method of privatisation until 1995, when the government concentrated on big industrial enterprises, trying to privatise them either by selling them directly to so called "strategic investors" or by public auctions organised by eminent international firms.

The central institution involved in those privatisations was the SOP (FPS). Because of the power of this institution in the privatisation process it became a major source of corruption. In the World Bank Report on Corruption in Romania in 2001 SOP was ranked as the third most corrupted institution after the customs authorities and judicial and prosecution authorities. It was perceived as corrupt by 57% of enterprises, 52% public officials and 44% households⁶.

It isn't very difficult to understand why; first of all the decision to put the privatisation process under the control of a state institution suffering from the general weaknesses of all Romanian institutions wasn't very fortunate; in the second place the privatisation agency only dealt with the privatisation process leaving the investor afterwards alone in a jungle of bureaucratic institutions that asked for all sorts of permits and authorisations. During 1999 a typical firm had to obtain between 23 and 29 different approvals, authorisations, licenses, permits etc. To complete the paper work it needed 42 to 102 working days, to have the results furthermore 34 to 101 working days⁷. The natural response of the investor was to use informal networks to speed up this process and to protect his business interest.

5. Conclusions

The combination between the weaknesses of a public institution, the slowness of the privatisation process and the method of privatisation led to a large-scale corruption that hijacked the privatisation process to the benefit of a certain high officials of the state institutions.

In my opinion, given the nature of the Romanian institutions and the risks that are naturally involved in privatisation, the most fortunate solution to deal with that process would have been a speedy mass privatisation done without a specialised agency. The fact that SOP (FPS), had both the administrative powers and the mandate to sell the companies led inherently to a series of abuses such as devaluating on purpose the value of an enterprise to allow the take over by a preferred investor.

⁵ Ciobanu

⁶ "Diagnostic Surveys of Corruption in Romania"

⁷ "Red tape Analysis Regulation And Bureaucracy in Romania"

By assigning a state institution to handle privatisation the state simply offered the informal networks an opportunity that they couldn't miss. Unfortunately it takes a long time to change well established institutional behaviors, that's why in Romania's case, the lesser state institutions are involved the lesser corruption is. A new strategy for privatisation must be developed that involves international firms with limited powers and a very tight schedule.

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