



CONTEXT

PUBLIC-OWNED ENTERPRISES: DEFINITION, EVOLUTION, AND EVALUATION

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Public-Owned Enterprises (POEs): definition, evolution, and evaluation / Context

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Abstract

The second Chapter gives an overview of the main analytical approaches adopted in the rest of the analysis, providing also a brief historical reconstruction of the role of Public Owned Enterprises (POEs). The examination shows how, within a general pathway characterized by several stops and goes and changes of course, POEs have more recently become a widespread and specific way to manage public functions with respect to both internal management and full outsourcing. This phenomenon, often called satellization or corporatization, has thus attracted increasing interest by scientific studies, emphasizing at the same time positive aspects and pitfalls. Furthermore, the peculiarities of the links and inter-relationships among POEs, governance and corruption are presented, focusing on the guidelines and operative instructions elaborated by many international organizations and institutions to enhance anti-corruption and integrity in POEs.

Keywords: Public Owned Enterprises (POEs), Hybrid organizations, Corporatization, Historical evolution, Corruption, Accountability

JEL-Codes: D23, D73, G38, H11, K23, K42, L32

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1. Definitions and main characteristics

Public Owned Enterprises (POEs) are usually defined as enterprises where public authorities have significant control through full, majority, or qualified minority ownership (European Commission, 2016¹; Bertocchi, 2017; Baum et al., 2019; OECD, 2019a). In some cases, also companies where public authorities have a minority share and no special powers are included as POEs². We will keep in this paper a flexible and inclusive definition, focusing mainly on entities controlled by the public sector³.

A certain degree of autonomy with respect to the ownership entity is a key feature of POEs, even if with arrangements and structures varying across countries and sectors. On one extreme, there are organizations sheltered from direct constraints and more intrusive political insights, enjoying a high degree of financial, managerial, and organizational autonomy (European Commission, 2016; Sorrentino, 2020). On the other side of the range, companies fully owned by the public sector, characterized by a more direct and detailed regulatory, financial, and organizational environment implemented by the public ownership entity. From this point of view, it has been observed that, when public entities become more independent, the fulfilment of public goals is no longer (or to a lesser extent) directly embedded within the firm's boundaries, becoming often implicit and therefore less immediately visible (Sorrentino, 2020).

POEs are commonly considered as one means of the public action to address market failures such as natural monopolies, correction of externalities, provision of public goods and redistributive issues, both interpersonal and territorial (European Commission, 2016; Baum et al., 2019; Sorrentino, 2020). Other reasons in terms of national interest and macroeconomic (counter-cyclical) stabilization can justify their presence in the economy (Sorrentino, 2020). With respect to alternative means of public intervention (public subsidies, light regulation, contractualization and external regulation) public owned enterprises represent a specific organizational solution where the 'public', 'social' or 'general' interest is pursued (also) through ownership rights and other forms of control mechanisms (Saussier & Klein, 2014). The extent

¹ According to the Institutional Paper of the European Commission (2016), POEs can include the following categories:

- companies fully owned by public authorities;
- companies where public authorities have a majority share;
- companies where public authorities retain a minority share but have special statutory powers. Also companies where public authorities have a minority share and no special powers, although not formally included as POEs, can be taken into consideration in order to have a more complete picture of governments' stake in the economy.

² See the Italian case below.

³ Even if, according to the established definition, the ownership control can be exercised also with minority share through legal stipulations or corporate articles of association, to be addressed on a case-by case basis, the ownership condition most commonly assumed in empirical investigations is that the public authorities, central or subnational governments, must have the controlling share of more than 50% (Bergh et al., 2018; Baum et al., 2019).

to which a POE pursues social goals should be set by the mandate from the public owner expressed through different possible regulatory tools: statutes, strategic planning documents, public service obligations, operative guidelines, hierarchical and procedural controls and ex-post reporting requirements.

These characteristics clearly disclose within POEs a distinctive mix/dichotomy of faces, with, on the one hand, organizational autonomy, managerial independence, output-based measurement and market-driven approach, and, on the other, public mission and values, political influences, regulatory power and the need to hold POEs accountable with respect to the broader general interest (Voorn et al., 2018; Bergh et al., 2019). Specifically, in POEs, as hybrid organizations, market-oriented transactions and characteristics of hierarchies coexist, with real situations falling between the two alternatives (Bruton et al., 2015). Hybridity can be viewed as an intrinsic strength, in terms of flexibility and adaptability, but also as a weakness, bringing about both a departure from public goals⁴ and a risk of economic inefficiency and commercial failures⁵ (Bruton et al., 2015; Wilkinson, 2018; Sorrentino, 2020).

As far as their legal status is concerned, the POE's definition includes both private law corporations (joint stock companies, limited liability companies, partnerships limited by shares) and public law entities, above all when their activities, at least in part, are of a largely economic/commercial nature (OECD, 2019a)⁶. In what follows we will keep an inclusive approach, also because anti-corruption policies, principles and recommendations are extensively directed to a wide range of public controlled entities (Wilkinson, 2018). At the same time, we will focus specific attention on private-law organizations (so-called corporatized public enterprises) considering that they have assumed a considerable relevance in the last decades⁷ and that they can impact significantly on the conditions for political accountability and control (Previtali et al., 2018; Bergh et al., 2019; Sorrentino, 2020). A further distinction is generally done between listed POEs, more commonly operating in liberalized, often cross-border, markets and according to an almost private-oriented approach; and non-listed POEs, operating in non-competitive market and more influenced by social and noncommercial objectives and obligations set by the public ownership entity.

From a fiscal (public budgeting) point of view, according to the rules defined in the European System of national and regional accounts (ESA 2010), POEs are classified

⁴ In the words of McDonald (2014, p. 13): *"The emphasis on monetary performance in neoliberal corporatization has had particularly corrosive effects on the publicness of services"*.

⁵ In this second direction, for example, Wilkinson (2018, p. 16): *"SOEs are often less profitable, heavily loss-making and debt-laden. Their effectiveness can be impaired when objectives are ill-defined or clash when social objectives are prioritized at the expense of economic objectives"*.

⁶ The same approach can be found in Wilkinson (2018, p. 7): *"There is no universal definition of an SOE but commonly they are considered to be commercially active enterprises owned fully or partially by the State, and they can also include agency set up by the State, such as health services or museums"*.

⁷ In Wilkinson (2018, p. 16) it is observed that *"the OECD, in a 2017 report, found that 92 per cent of the SOEs surveyed were incorporated and the other eight per cent were statutory corporations governed by law"*.

as part of general government if they are involved in non-market activities⁸, while they are classified as enterprises/corporations if they are involved in market activities (European Commission, 2016). If a publicly controlled unit is included within the general government perimeter, its revenues, expenditures, and debt directly affect the government's balance and debt. This is not the case, at least in the short run, for units outside general government, while in the long-run the impact is expected to be similar, considering that surpluses are distributed as dividends and occasional losses are borne by owners (*ibidem*). General government's potential losses due to the participation in public corporations (market nature) may be interpreted as contingent liabilities, representing a relevant challenge of the intertemporal scenario of public budgets.

From a spatial perspective, we include POEs which are owned by the central State S-POEs and those owned by regional and local governments L-POEs. While S-POEs include some of the largest companies in the world, L-POEs are generally smaller-scale enterprises providing core public services to local communities or instrumental assets and goods to local but also regional governments. L-POEs need to be addressed with attention both because they are becoming increasingly numerous (European Commission, 2016; Voorn et al., 2018; Wilkinson, 2018⁹) and because they are characterized by specific features and flaws. In particular, they are supposed to impact negatively on the conditions for accountability of the public action (Bergh et al., 2018), facing higher corruption risks due to the application of lower transparency standards, the lack of skills and competences, and the close existing ties between the political decision makers and the senior executives (European Commission, 2016; Wilkinson, 2018¹⁰).

Finally, POEs are operating in a wide range of sectors, from traditional network services (like water, local transport, and waste management) to extractive and natural resources industries, from housing and social services to infrastructure management. Public enterprises/agencies play also a role in the production of goods and services for public administrations (web master assistances, design services, public works, green areas maintenance, research services etc.) up to the exercise of administrative functions (regional and local development planning; public tender management and awarding; regulatory and control tasks in public service provision). It is not infrequent to find POEs active also within other miscellaneous area where the identification of the public mission/market failure is more questionable and where potential competition conflicts with private firms clearly emerge (Bergh et al., 2019). The evaluation of POEs should take into consideration this wide context of the sectors and markets where they are active (European Commission, 2016; Voorn et al., 2018).

⁸ Non-market activities are those where producers provide all or most of their output to third parties free of charge or at prices that are not economically significant (European Commission, 2016).

⁹ This author underlines (p. 4) how "*while large SOEs have high profiles and attract widespread attention, most countries' SOEs exist at the regional and municipal levels*".

¹⁰ "*Large SOEs grab the headlines but smaller SOEs, mostly in the utilities sectors, represent the bulk of the world's needed to counter corruption*" (p. 19).

In fact, when POEs operate in competitive market, according to a commercial logic, they should be (mainly) assessed relying on output measures of performance (productivity, cost-effectiveness, profitability), while a level playing field with competing firms needs also to be granted. Where the POE is entrusted with a public mission, publicness measures of performance become more important together with the implementation of special principles and strict regulatory environment (European Commission, 2016).

2. Historical evolution

Historically, the spread of public entrepreneurship in Europe from the end of the 19th century has been largely explained as a process of reacting to market failures, through which public administrations progressively supplanted the market and behaved as an entrepreneur in designing and managing services (Millward, 2005; Clò et al., 2015; European Commission, 2016; McDonald, 2016; Previtali et al., 2018; Boggetti, 2020). The disillusionment with private initiated regimes gave way in most countries to direct self-production as the dominant form of regulation, where public authorities governed the whole process of service provision both through internal departments or organizing entities strictly organic to state and local authorities¹¹. In these entities local authorities kept the responsibility to define aims and strategic goals, to directly appoint the administrative organs, to approve fundamental acts and to supervise the management.

In the concept and terminology of principal agent theory the term “internal agencification” has been coined to describe this last organizational option (Torsteinsen & van Genugten, 2016; Wollmann, 2020). This quasi-monopoly of the public sector was grounded in the conviction that services were provided best under the direct guidance and oversight of elected public authorities (‘government’) as advocate and guardian of the general interest (Klein, 2012; Wollmann, 2020).

Starting from this almost generalized background, new organizational models progressively came out in the last decades of the 20th century, following the impact of New Public Management (NPM) principles and of the EU driven market liberalisation approach (Zatti, 2013; Alexius & Cisneros Ornberg, 2015; McDonald, 2016; Wollmann, 2018; Bergh et al., 2019). Bureaucratic failures, together with other technological, political, and economic forces triggered de-integration and decentralization, bringing about a changing regulatory environment. This trend led, in some cases, to the

¹¹ In the same direction (Wollmann, 2020, p. x): *“During this period the majority of public services was provided by MOE’s – mostly in an organizational ‘quasi-in house’ form in which, lacking legal, operational and financial autonomy, they remained practically integrated into local administration and politically under the sway of local government and its “common good” mandate. Exemplar of this quasi in-house organisational form were the Stadtwerke in Germany as Eigenbetriebe”.*

complete liberalisation of significant market segments of public services where private initiative and commercial interests become predominant. In other cases, the public services have been outsourced/contracted out to outside providers (both public and private) bringing about a market-organization form often termed 'functional privatization' or 'French-style privatization' (Wollmann, 2020). In many other cases, the NPM-inspired search for organisational flexibility and economic efficiency has triggered the expansion of more independent organizations and companies (both S-POEs or L-POEs). While remaining in public (municipal or State) ownership, they were given increasing legal, operational ('entrepreneurial') and financial autonomy¹². The terms 'external agencification' or 'satellization' has been exploited to describe this situation where the competent public administration acts as a hub of a multitude of increasingly independent spokes/units (Torsteinsen & van Genugten, 2016; Wollmann, 2020).

Following the economic crisis of 2007/2008, the evolution over time has been more ambiguous. On the one hand, in fact, in many European countries there has been a reduction in the scope of public ownership, driven by specific targets for privatization and the reorganization of specific sectors (transport, water and sewage, non-core sectors), but also by the need of containing public expenditures (spending review approach). On the other, a renewed interest in government ownership emerged (McDonald, 2014; European Commission, 2016; Wilkinson, 2018). Some firms become POEs after governments intervened to save private companies from bankruptcy, others justified by governments' aims to develop global markets and/or safeguard strategic sectors (European Commission, 2016¹³). This trend has been fueled also by several studies suggesting that, as far as the provision of public services is concerned, public enterprises can be on a plane or even superior level to private sector providers, above all when the transaction costs of outsourcing are considered (Wollmann, 2018). In this perspective, it is interesting to underline that, while initially POEs have been often seen as a transitional step towards full contracting out and privatizations (McDonald, 2014; Bruton et al., 2015), more recently these organizations have become a specific and alternative way to manage public functions (Klein, 2012; McDonald, 2014)¹⁴. Re-centralization, return to hierarchies and post-new public management era have been terms and concepts evoked to describe this evolving tendency (Grossi et al., 2015).

¹² According to Saussier & Klein, 2014 (p. 4): *"Instead of real privatization, most municipalities have separated enterprise operations from the administrative body, either remaining sole owner of the enterprise or bringing in a partner. In the former case, i.e. corporatization, governments simply spin off tasks or whole departments into a publicly owned company"*.

¹³ *With the outbreak of the financial crisis, the public sentiment also turned in favour of SOEs and public control"* (p. 80).

¹⁴ In the same way, Grossi & Reichard (2008, p. 604): *"Like in other EU countries, in Germany and in Italy the opening up of the capital to private investors was sometimes presented as a first step towards a full privatization but was rarely completed"*; (European Commission, 2016, p. 20): *"While it is an essential preparatory step for the (full or partial) privatization of a SOE, it can be carried out as a self-standing reform measure"*.

As already mentioned, within the ‘agencification’ or ‘satellization’ process, a particular and predominant role has been acquired almost everywhere by private-law entities, (Grossi & Reichard, 2008; Zatti, 2012; McDonald, 2014; Wilkinson, 2018; Bergh et al., 2019; Wollmann, 2020): that’s what we specifically label as ‘corporatisation’. This solution furtherly increases the hybridity of the organisational and regulatory environment. In fact, with respect to direct public management (internal department), corporatized enterprises bring about vertical de-integration and reduction of hierarchical control. Corporatization goes also further compared with simple “agencification”, as a corporatized company is a unit with its own legal status (ruled by the private law), its own budget, its own staff and an increasing organizational and management autonomy (Grossi & Reichard, 2008)¹⁵. At the same time corporatisation is not a market-oriented solution (McDonald, 2016), as it is still deeply rooted in the public initiative perspective and envisages none or negligible involvement of private and/or external actors.¹⁶ That is why corporatisation can be seen as an alternative to both self-production, on the one hand, and external regulation and privatization, on the other¹⁷. “Formal or organizational privatization”, “legal privatization”, “formal outsourcing” are terms frequently exploited to label this evolutionary model of shaping the public sector (Zatti, 2013; Wollmann, 2020).

In terms of ownership rights, the above assumptions make corporatized publicly controlled enterprises not much dissimilar to directly managed agency, seeing that private ownership is merely ancillary and public influence turns out to be dominant in the shareholders’ assembly. The main difference is commonly found in the allocation of decision rights, as control rights over business decision are, at least partially, handed over from politicians to managers (Osculati & Zatti, 2005; Klein, 2012; Saussier & Klein, 2014). In other words, if a certain degree of managerial and operative independence always existed in direct management and public agencies, corporatization decision rights are delegated at a higher stage of the decisional chain, leading to a decrease in control intensity and political intrusion. In its classical and ideal typical form (arm’s length control) the government principal (ministry, region, municipality, etc.) sets the public mission agenda, appoints managers (board of directors and, eventually, CEO) and avoids interference in their discretionary decisions (Florio, 2014). In reality, many other levers can be (and are) adopted to steer the behavior of the enterprise (Table 1).

¹⁵ Similarly, corporatisation changes the status and nature of SOEs and brings the organisation/modus operandi closer to that of private companies, notably in terms of management and financial reporting practices (European Commission, 2016).

¹⁶ If the private influence becomes non negligible, we have a mixed enterprise and no longer a corporatized public enterprise.

¹⁷ The same approach can be found in Wollmann (2020): *“This article aims at mapping the providers of public services between public/municipal sector (“in house”), corporatized (State/municipally owned enterprise) and contracted out private actors in European countries”*.

Table 1. Possible control mechanisms in corporatized enterprises

Political levers	Statute, strategic and planning documents, social and policy agenda, appointing rules and criteria.
Managerial levers	Control and authorizations on inputs, approval of the main operative decision (budgets, contracts financial report, investments, human resources, organizational structure, service levels), codes of conduct.
Structural levers	Supervisory and control boards, anti-corruption devices, hierarchical and accountability lines.
Financial levers	Level of budget, pricing policies and influence, guarantees on debt.
Reporting levers	Financial, environmental, ethical reporting, minimum transparency and data access requirements.

Source: elaborations and adaptation on Saussier & Klein, 2014.

The intensity of the control is to be very strong, in particular, to meet the so called “in house” rules established by the EU law¹⁸ where it is required that the contracting public authority has the same control over the in-house company than it has over its departments. In this perspective, the control that, according to private law, the shareholders exert over management is not enough, and other steering mechanisms, as those described in Table 1, must be implemented and, in concrete, verified (Osculati & Zatti, 2005). Alternatively, the company may be, at least partially, separated from the organizing authority, having a wider discretion in relation to the main management levers (innovation, tactical or operative decisions, budget, enrolments criteria, etc.). In this case, since a direct and strict administrative control is not established, legally enforceable contractual agreements, together with open awarding procedures are important tools for disciplining the performance of the operator, also guaranteeing the respect of the non-discrimination rules.

3. Potential and pitfalls

The hybrid nature of corporatized enterprises has been subject to diverse, in some cases opposite, evaluations (Zatti, 2012; Previtali et al., 2018; Voorn et al., 2018¹⁹; Sorrentino, 2020).

On the one hand, following the influence of the New Public Management reform wave, corporatization has been seen as a positive opportunity, bringing about efficiency and effectiveness in the public sector through organizational specialization, results-based management and performance measurement (Grossi & Reichard, 2008; OECD, 2015; Alexius & Cisneros Ornberg, 2015; McDonald, 2016; Bergh et al., 2019; Mocetti & Roma, 2020). A strong emphasis has been put on the strict separation of roles between the public authority as an owner and the management of POEs

¹⁸ See for example: Cause 258/03 Parking Brixen, Judgement 13 October 2005.

¹⁹ For these authors (p. 4): “There is no consensus in the empirical literature if autonomy is in the end harmful or beneficial”.

(OECD, 2019a). In particular, managerial autonomy and professionalization are expected to favor de-politicization, shielding directors and professional bureaucrats from the day-by-day pressure of politicians, the short term vision of election cycles and interferences from other government agencies (Klein, 2012; OECD, 2015; McDonald, 2016; Voorn et al., 2018²⁰). In this perspective, the amphibious nature of public controlled enterprises has been considered a valuable vehicle to keep critical decisions, at least partially, within the public sphere, escaping at the same time from the rigid and bureaucratic framework (budgeting and accounting rules, recruiting mechanisms, public works awarding regulations) of public administrations (Grossi & Reichard, 2008; Sorrentino, 2020²¹).

On the other hand, de-integration and reduced political control can be cause of unintended critical effects (European Commission, 2016²²), mainly due to the creation of entities that behave like private companies without the political and financial risks associated with direct private sector participation (McDonald, 2014). As observed by Alexius & Cisneros Ornberg (2015), hybridity in public enterprises, attempting to reconcile potentially conflicting logics and values, risks to be not a straight forward tool for the simultaneous creation of social and commercial value, but rather often *“sites of confusion and criticism for failing to do so”* (p. 288). Mission drift, reduced accountability, market distortions, and increasing transaction costs are commonly considered as the main pitfalls emerging from this governance option.

Firstly, the emphasis on commercial results and economic rationality may have counterproductive effects on the public missions and general interest of services, leading to short-termism and the commodification of the public approach (McDonald, 2016; Wollmann, 2020). The rhetoric of “customers” instead of “citizens” and cost-reflecting pricing are supposed to weaken the attainment of broader public goals, with values not expressed in monetary or quantitative terms that risk being penalized in decision making. Furthermore, the lack, or in any case lower, presence of synergistic planning and the diverging interests of ring-fenced corporations develop centrifugal dynamics (Grossi & Reichard, 2008; Wollmann, 2020) and isolationism (McDonald, 2016), undermining economies of scale and a more holistic execution of the public mandate. This ‘centrifugal dynamics’ can be expected to become stronger the more distanced and autonomous from ‘core’ administration these outside actors are positioned and also the more explicit their economic and market-oriented profiles are established (Wollmann, 2020).

²⁰ *“One of the key reasons to engage in ‘governance at arm’s length’ is to allow (non-political) delivery of public services”* (p. 4).

²¹ She remarks that (p. 85) *“the state-owned enterprise is characterized by its hybridity, by its mixed character, and that, far from reproaching it for its lack of purity, we should regard this as the quality from which it can derive its strength, especially if it shows itself to be sufficiently “plastic” to adapt to variable, changing and constantly evolving situations. ... Finally, its capacity for autonomy from the public authorities, its long-term vision, not subject to short-term political imperatives, and the expertise that it can amass, may certainly have some disadvantages, but these are vital qualities if it is to serve the general interest”*.

²² *“Recent experience has shown that SOEs can be an important source of concerns”* (p. 1).

Secondly, the presence of a more complex principal-agent chain (general public, public sector administrators, supervisory board and board of directors, CEO and professional management) can be cause of unclear lines of responsibility, lack of accountability and reduced democratic transparency (Osculati & Zatti, 2005; Klein, 2012; Saussier & Klein, 2014; Tönurist & Karo, 2016; Curci et al., 2017; Bergh et al., 2019). Actually, in the case of a corporatized company there is (at least) a third party that intervenes between the principal and the agent (Osculati & Zatti, 2005; Bergh et al., 2019²³): the company board of directors and top management, often made up of members with a political background and/or directly appointed by the political shareholder. Every link in the chain brings about a transfer of powers and therefore contains a risk of deviation (agency loss) from the ultimate outcome in terms of citizens' welfare (European Commission, 2016²⁴; Bauby, 2019; Bergh et al., 2019). Moreover, it is thus possible that this organizational structure complicates control, since the electors are uncertain whether to entrust voice and compulsion to the elected administrators or to the company's appointed and professional administrators (Bishop, 1990). The agency problem raises the likelihood of self-serving behavior by corporate insiders and managers (OECD, 2015, 2019a). At the same time, governance ambiguity can allow politicians to influence, also through informal practices, managerial decisions and operational choices according to their self-interest (on budget, on employees recruitment, on input provisions) shifting, at least partially, the responsibility (and the eventual blame) to the outside entity (Klein, 2012).

A third difficulty relates to accountability and evaluation. The presence of multiple missions and a broader concept of performance, where more quantitative goals are blended with more intangible/qualitative ones, makes benchmarking and ex-post evaluation more difficult since the indices of effective operations are likely to be less precise and potentially ambiguous (Tönurist & Karo, 2016²⁵; Voorn et al., 2018; Bauby, 2019; Sorrentino, 2020). These factors may boost informational asymmetries and the agency problem, rendering governance and proper accountability of POEs an intricate matter. The risk of governance opacity turns out to be particularly severe in relation to financial integrity²⁶. Public ownership, in fact, is typically associated with soft budget constraint (Grossi & Reichard, 2008; Bruton et al., 2015), creating the opportunity to have loss making corporations and debt accumulation not reflected, at least in the short period, in the public budget (Osculati & Zatti, 2005; Saussier & Klein, 2014; European Commission, 2016²⁷). In a phase of tight fiscal constraints for

²³ "In MOEs, chains of delegations, and hence accountability, become more complex processes than in ordinary firms since they are one additional step farther away from their ultimate stakeholders- the citizens" (p. 324).

²⁴ "The 'organizational distance between the managers and the owners of SOEs may create a situation of both incomplete and asymmetric information leading to mission drift and X-inefficiencies" (p. 22).

²⁵ "Due to political meddling multiple, vague and sometimes inconsistent objectives (e.g. profit maximization vs welfare concerns) can become serious problem for the companies" (p. 626).

²⁶ In the Italian case the Court of Auditor has recently observed that: "The focus on public owned companies has been increasing, both at the central and local level, due to the belief that corporatization may represent an elusive device with respect to public budget constraints" (Corte dei Conti, 2017, p. 2, our translation).

²⁷ This is the case for units classified outside the general government (p. 12) "participation in the capital of public corporations can represent a potential liability for the government...when the corporation is experiencing

central and local governments, this opportunity favors corporatization as a device to reduce budget pressure and to buy consensus through lower tariffs and better services. Similar considerations can be done if corporatization is exploited to circumvent public sector employment regulations, becoming a mean to expand the workforce without creating a direct impact (at least in the short time) on government expenditures²⁸.

Fourthly, these effects are exacerbated by the fact that declining hierarchical controls and administrative constraints are not adequately compensated by a stronger market influence. In fact, the main disciplining factors that are considered essential for policing management in private sector corporations, i.e. the possibility of takeover and bankruptcy and the pressure exerted by other market competitors are not (or only in some cases) concretely active (Mocetti & Roma, 2020), with the eventual risk that *“corporatized firms represent an institutional configuration which has both weak economic and political incentives”* (Klein, 2012 p. 4). Furthermore, even when POEs operate in a market-driven environment (open entry or regulated competition context), competition disciplining effects may be weakened if they are not kept independent from the competent regulatory authority or they can rely on ‘special treatments’ in terms of softer budget constraints or lower level of profitability with respect of the rest of market participants (European Commission, 2016).

It is finally to be observed that the proliferation of independent public owned enterprises may increase transaction and administrative costs, mainly due to service complexity and to the checks and balances to be adopted by the ownership entity to regularly and effectively monitor, audit and assess corporate performance and compliance with required standards (appointing rules and procedures, salient contract design, disclosure standards, service standards, supervising devices, code of conducts, external auditing procedures, etc.). More complex services and organizational structures rely crucially on the institutional capacity of the competent authority to govern them and can be strongly jeopardized by the impoverishment of service expertise within core public administrations frequently brought about by agencification and corporatisation (Bauby, 2019).

The above review points out the difficulty to reconcile two potentially conflicting institutional logic: the public and the commercial one (Alexius & Cisneros Ornberg, 2015). Hybrid organization as POEs, and even more corporatized ones, create confusion and/or complexity, requiring active management and multifaceted

temporary difficulties or in the case the corporation is failing, the government as a controlling entity or a majority owner may need to step in. This intervention need cannot in most cases be quantified in advance, however, as the probability of occurrence and its impact are not known. The liability is thus contingent, i.e. it may develop into an actual liability if some specific event occurs”.

²⁸ This is the so called ‘escaping’ argument, through which POEs ‘tried to escape from the rigid and bureaucratic legal framework of public administration into the relative ‘freedom’ of the business sector’ (Grossi & Reichard, 2008 p. 607). Civil servant regulation, budgeting and accounting systems and restrictions to the salaries of managers in public-law-based entities are deemed the main constraints to be bypassed.

corporate governance. The main source of confusion and ambiguity, in this perspective, is related to the ‘mantra’ of autonomy. In the OECD approach (OECD, 2019a, b), a strict separation of roles between the state as an owner and the management of the SOEs is recommended: the state allowing SOEs full operational autonomy and deriving its authority from the law, that, in this case, is the private-company law. This approach is basically coherent with POEs operating in a competitive environment, where the main concern is related to avoid unfair advantages due to the proximity to the public owner and, at the same time, to avoid they are overburdened with regulations and controls compared to private firms (ibidem). That can be also the case of corporatized public enterprises when they represent an intermediate step towards privatization and liberalization. But where POEs are established mainly or exclusively to pursue the general interest and to correct market failures, (full) autonomy and the organizational distance between the managers and the owner can have controversial effects, weakening the incentives of management to perform in the best interest of the general public (European Commission, 2016²⁹; Bertocchi, 2017). The role of autonomy is maximally debatable in those cases, not so infrequent, of private law status entities holding regulatory and administrative powers, becoming de facto partners in policy making (European Commission, 2016). This concept is lucidly recognized by Sorrentino (2020, p. 84): *“although some public status organizations lack public powers, a number of private law status organisations do hold such powers. The bigger problem affects the latter type of organisations, which, while endowed with public powers, have accountability structures that pertain solely to their membership. Their autonomous sources of authority allow them to operate with significant independence from the authorizing body. In such conditions, it is hard to ensure effective regulative action though rigorous and detailed guidelines, which may not be enough”*³⁰.

Consequently, an important prerequisite to be considered should be that to better clarify in advance the scope and the role of POEs and, accordingly, define an adequate accountability framework able to monitor financial performance as well as effectiveness vis-à-vis non-financial targets (European Commission, 2016).

²⁹ “Where SOEs operate in competitive markets, a level playing field with competing firms is necessary, also as regards access to finance. Where the SOE has a de facto monopoly, a strong regulatory monitoring and oversight is required” (p. 17).

³⁰ The difficulty to find an equilibrium between autonomy and accountability can be found also in the G20 High level principles for preventing corruption and ensuring integrity in State-owned enterprises (2018, p. 1-2) for which *‘the state should act as an active and informed owner of enterprises, but should abstain from intervening in their daily management....minimizing opportunities for inappropriate ad-hoc interventions and other undue influence by the state in SOEs’*.

4. POEs and corruption

In the public sector corruption is defined as the ‘abuse of public office for private gains’ (IMF, 2019). The private/particular/related-party enrichment may be financial, non-financial (favors, gifts, etc.) or even political (votes and consensus). Corruption is deemed to weaken key functions of the public sector such as the ability to collect taxes, to make expenditures allocation genuinely targeted to the general interest, or, again, to ensure the high quality and cost-effectiveness of public services and infrastructures. When systemic (real or perceived) corruption erodes trust in public institutions³¹, strongly jeopardizing confidence in the government (IMF, 2019). These effects tend to be persistent and strongly path-dependent, with improvement to be gained with perseverance and strong political commitment over many years or even decades (ibidem).

In the field of enterprises, corruption may acquire a more complex pattern, with both passive and active behaviors. In the first case, individuals or groups of individual demand or accept money, gifts, or other undue advantages to act or to refrain to act in the correct exercise of their function, thus penalizing the interest of the company. In the second, managers and directors try to gain contracts and benefits for the enterprise, being mainly active bribe payer. POEs faces both kinds of risks, generally depending on their prevalent nature³². Large commercial operators, in fact, can be committed (also) to expand their market share, getting privileged access to contracts and concession³³, or to obtain a relaxed regulatory oversight in markets in which they operate. For non-commercial POEs, directly entrusted of public policy objectives, passive bribery is likely to be predominant, being a concrete threat for the general interest pursued. Many operative areas and items can be involved: administrative acts and authorization, contracts awarding procedures, grants and other donations policy, workforce recruitment and career progression, tariff definition, appointment and nomination rules, control, and inspections, lobbying and political party financing. In this perspective, passive and active corruption, certainly related and equally deplorable from an ethical point of view, are to be kept distinct so as commonly separated/complementary are policies aiming to their prevention and control (Previtali et al., 2018).

³¹ “Trust in government is strongly correlated with citizens approval of their country’s leadership and perceived spread of corruption in government in OECD countries. Where governments are perceived to have high moral integrity, more people trust government” (OECD, 2017, p. 214).

³² This dichotomy is clearly stated by the OECD (2018, p. 5): “On the one hand, SOEs with public policy objectives may be more able to justify illicit activity to compensate for financial losses or reduced profit margins that can be associated with delivering on policy objectives. On the other hand, SOEs (and other firms) with entirely commercial objectives may try to justify corruption because of the pressure to remain competitive or to perform”.

³³ For example, Telia, a Sweden-based telecommunication company owned in part by the Swedish and Finnish governments, obtained contracts in Uzbekistan that generated over US\$2.5 billion through bribery from at least 2007 to 2010 (Baum et al., 2019).

Corruption and other irregular practice are acknowledged as a major obstacle to good corporate governance in POEs (OECD, 2019a). The consequences of such corruption can be serious and variegated (Wilkinson, 2018): raising input costs, labor force overexpansion, lower profitability, financial losses, diversion of managerial attention and time, reduced quality of projects and services, substantial costs for legal and other advices, loss of reputation and brand deterioration. Due to the power entrusted by public authorities, corruption in POEs is not only detrimental for internal operations but causes negative externalities and systemic effects, contributing to weakening the general trust in public institutions.

According to many observers and reports (World Bank, 2014; Wilkinson, 2018; Baum et al., 2019; OECD, 2019a) POEs are prone to greater corruption and mismanagement risks than private sector due to some specific characteristics and challenges.

Firstly, the proximity to the government can favor political opportunism, undue influence, and conflict of interest, especially when board and chief executives are politicized and directly influenced by elected organs. For example, corrupt politicians and civil servants can use political pressure and favoritism to influence the choice of management, or to distort procurement processes and hiring policies. Several studies (Auriol & Blanc, 2009; Nguyen & Van Dijk, 2012; Previtalli et al., 2018; IMF, 2019) have explored the connection between firms and politicians, finding corporate political connections to be relatively widespread, more evident among larger firms and particularly common in countries that are perceived as being highly corrupt. Accordingly, a recent OECD report (2018) brings evidences that POEs with fewer politicians and more independent members on their boards are associated with lower risks of corruption.

Secondly, the room for bribes and corruption is favored, with respect to private entities, by the presence of less informed principals (citizens) and more opaque financial relationships with the ownership authority. A lack of transparency regarding financial support and other transactions between the public owner and the POE, also due to cross subsidization among different public owned units or among different activities managed by the same unit, could result in large hidden costs, making easier to veil bribes and other forms of mismanagement.

Thirdly, POEs, when characterized by a mix of commercial and more public-oriented objectives – whether well-defined or more implicit – are thought to be affected by more risks of corruption or other irregularities not only with respect to private entities, but also to POEs with entirely commercial objectives (OECD, 2018). Mission drifts, multiple mandates or goals vagueness make control and reporting activities based on objective indicators more difficult, potentially increasing the room for mismanagement and maladministration.

Finally, POEs, often originating from markets with large economic rents and monopolistic power, are usually associated with institutional weaknesses

(Baum et al., 2019). Lack of professional boards and management, lack of a consolidated culture in terms of risk assessment, weak transparency and regulatory oversight are the most commonly vulnerabilities emphasized in case studies³⁴. Bergh et al. (2019) reports evidences that incompetent board members may explain the high incidence of municipally owned enterprises occurring in Swedish corruption scandals. Baum et al. (2019) observe that many POEs have traditionally less developed and formalized internal controls and procedures or inadequate accounting and audit methods. For the same authors, even reporting on POEs operations, both to the ultimate owner and to the general public, are less developed and rarely in line with international standard, with the risk of preventing the uncovering of financial and operative distortions³⁵.

Following this view, many international organizations and institutions have elaborated guidelines and operative instructions to enhance anti-corruption and integrity in POEs (OECD, 2018, 2019a, b; G20, 2018; Wilkinson, 2018³⁶; IMF, 2019). Even if the full contents of these efforts are beyond the scope of this contribution, we briefly sum-up in Box 1 the key elements addressed.

Box 1. Principles and operative recommendation for corruption prevention and control in POEs

- Exercise the state ownership in a rules-based economic environment, where each actor derives its authority from, and behaves in line with, applicable laws (OECD, 2019a).
- Adopt a strict separation of roles between the state as an owner and the management of the SOE, the state allowing full operational autonomy to POEs' decision-making bodies (OECD, 2019a, 2018).
- SOEs should not receive unfair advantages due to their proximity to the state, nor they should be overburdened with regulations and controls compared to private firms (OECD, 2019a).
- Clearly specify POE objectives, making publicly available information about the ownership structure, ownership rights, financial transactions and public support (OECD, 2019a, 2018; G20, 2018).
- Ensure that the state (public owner) acts as an active and informed owner with regards POEs (OECD, 2019a; IMF, 2019; G20, 2018).
- Establish accountability and review mechanism for state-owned enterprises (OECD, 2019a).
- Operate to the highest standard of ethics and integrity (OECD, 2019a; G20, 2018).
- Include SOEs in government-wide anti-corruption initiatives (OECD, 2018).
- Ensure that SOEs are overseen by effective and competent board of directors that are empowered to oversee company management and to act autonomously from the state (OECD, 2019a; IMF, 2019; G20, 2018; Wilkinson, 2018).
- Ensure that an appropriate number of independent members – non-politicians and non-executives – is on each board and sit on specialized board committees (OECD, 2019a).
- Develop mechanisms to manage conflicts of interest and to guarantee disclosure on remuneration and personal ownership of board members (OECD, 2019a).
- Be accountable to stakeholders through transparency and public reporting (OECD, 2019; IMF, 2019; G20, 2018; Wilkinson, 2018).

³⁴ For the OECD (2019a, p. 3): *'many lack the sophisticated risk-management and compliance mechanisms found in best-practice private firms'*.

³⁵ In the same direction, Wilkinson (2018) states that SOEs are less transparent than business, mainly because there is not yet a consistent level of good practice in SOE transparency.

³⁶ Peter Wilkinson is the author of the report by Transparency International setting out 10 anti-corruption principles for POEs.

- Monitor SOEs' corruption risks, integrity and anti-corruption efforts as part of risk analysis and performance (G20, 2018).
- Design the anticorruption programme based on thorough risk assessment and ensure best governance and oversight (OECD, 2019a, 2018; IMF, 2019; G20, 2018; Wilkinson, 2018).
- Ensure human resources policies and procedures support the anti-corruption programme (OECD, 2019a, 2018; Wilkinson, 2018).
- Implement detailed policies and procedures to counter key corruption risks (Wilkinson, 2018).
- Use communication and training programmes on ethics, anti-corruption, compliance or similar (OECD, 2018; Wilkinson, 2018).
- Encourage stakeholder engagement to promote accountability and the public interest (OECD, 2019a, 2018; G20, 2018).
- Provide secure and accessible advice and whistleblowing channels (OECD, 2019a; G20, 2018; Wilkinson, 2018).
- Ensure transparency of contracting process, including bidding, awarding and delivery (Wilkinson, 2018).
- Develop e-procurement and public registers of approved third parties (Wilkinson, 2018).
- Encourage that anti-corruption and integrity standards are made applicable to all levels of the corporate hierarchy and to third parties (OECD, 2019a; Wilkinson, 2018).
- Monitor, assess and continuously improve the implementation of the anti-corruption programme (Wilkinson, 2018).
- Establish accountability and review mechanisms carried out by external control bodies and/or supreme audit institutions (OECD, 2019a, b).

Principles, recommendations and actions are mainly directed to three, mutually reinforcing, pillars: i) to improve the integrity of the public authorities and their execution of the ownership responsibilities (clear specification of objectives, reporting systems, accountability and review systems, setting of high standards anti-corruption and integrity principles and practices; disclosure of all financial support by the state, risk assessment of the overall risk exposure of the state, etc.); ii) to improve corporate governance and promote integrity and prevention of corruption at the enterprise level (risk management systems; procurement and contracting processes, high standards of transparency and disclosure, professionalized boards and management structures, presence of an appropriate number of independent members in internal boards and committee, selection criteria for board members, etc.); iii) to enhance, horizontally, a culture of integrity to counter pressure and undue influence (code of conducts, ethical training and communication programmes, integrity pacts).

This array of measures represents an important steering tool to improve the management of POEs and to overcome deficiencies and pitfalls in terms of accountability and deviated behaviors, with one main potential weakness/bias. The approach adopted is mainly focused on large SOEs, operating in competitive markets and following a commercial logic³⁷, while its extensibility to smaller entities, operating

³⁷ This is implicitly recognized by the OECD Recommendation when '*recognizing the important role that state owned enterprises play in many economies, their increasing participation in international markets and the large benefits resulting from corporate governance in state-owned enterprises*' (OECD, 2019b, p. 13). The ACI (Anti-corruption and Integrity) guidelines of the OECD (OECD, 2019a) are deemed to be applicable to all SOEs

at the local scale and with an almost exclusive interface with their ownership authorities can result, at least partially, being misleading or inappropriate. The OECD and G20 principles, for example, explicitly aim to insulate SOEs from politics, requiring them to adopt corporate governance structures that guarantee transparent relationships with the shareholder as well as financial equilibria, i.e a level playing field with private competitors for financing, taxes and subsidies. The underpinning idea is that POEs operate as an alternative to private companies and that these governance principles and operative reforms are key element to make *“SOEs operate with similar efficiency, transparency, and accountability as best-practice private companies”* (OECD, 2019a, p. 10). Therefore, even evaluation criteria and indicators are usually those used for private enterprises. For example, Curci et al. (2017) evaluate the performance of Italian local public enterprises in terms of operational efficiency (total factor productivity) and profitability (return on asset-ROA, equity-ROE and investments-ROI); Baum et al. (2019) assess corruption effects on the performance of POEs considering as key performance indicators profitability (return on equity and operating profit per sales) and productivity and efficiency (sales per worker and labor costs). A similar approach can be found in Mocetti & Roma (2020) who evaluate the effect of the presence of politicians in the board of directors of POEs on their performance, measured through return on sales and the incidence of labor costs on sales.

In the real world, however, *“smaller SOEs form the bulk of the world SOEs, and the corruption risks for them should not be overlooked”* (Wilkinson, 2018, p. 23). These POEs, above when established through what we have previously called corporatization, have been mainly an alternative to self-production rather than to external regulation and/or full privatization. If it is true that the corporatized entity has lower interests and margins to corrupt public officials (active bribery), the new entity itself buys services, works and other inputs from outside, becoming the possible target of distortive offers and promises (passive bribery). Under this scheme, it has been observed that the increased decentralization of responsibilities may increase the risk of corruption and of other ethical problem (Grossi & Reichard, 2008, p. 611): *“The risk of corruption and of other ethical problems may grow. Managers have more opportunities and temptations to bribe other actors, for instance, in purchasing processes”*.³⁸

pursuing economic activities, either exclusively or together with the pursuit of public policy objectives and the exercise of governmental authority or a governmental function.

³⁸ Similarly, Ye & Hu (2019, p. 266): *“Many existing studies also show that with the enhancement of executives’ real power, they are more likely to carry out connected transactions, seek for excess compensation, and implicit money for extravagant consumption. Therefore, in order to fundamentally curb executive corruption, it is necessary to improve the internal supervision mechanism and strengthen the restriction and supervision of executive power”*.

More independent managers have additional opportunities and instruments to influence other actors in purchasing processes and in the recruiting of the workforce. At the same time, the public shareholder has lower incentive to exert control since the monetary effects of mismanagement do not immediately affect public budgets, as it happens with direct internal provision. These opaque and karstic financial relations may be also exploited by elected officials to influence operative choices to gain political consensus (lowering prices for public services, increasing the staff, etc.) without being directly responsible of the negative impacts in terms of costs and revenues. The overall treat, even in terms of corruption prevention, is that the ambiguous nature of public controlled enterprises weakens the checks normally operating in the public sector (hierarchical control, more formalized awarding procedures, direct voice from the public, ethic control) without (or only partially) being guided by the discipling effects of market pressure.

The criterion of autonomy and separation of the owner and the management³⁹, largely recommended in the market-oriented approach, in this setting runs the risk of becoming a dogmatic cul-de-sac.

On the one hand, in fact, it looks to be based on a supposed 'ethical superiority' of professional managers with respect to elected politicians and public officials. Why should an independent manager always act more honestly and in an impartial way? It could have been the case in some specific circumstances, but the generalization sounds in many respects ideological⁴⁰. The main challenge turns out to be that of the incidence of adequate checks and balances along the principal-agent chain able to influence and guide all the involved actors. In corporatized public owned enterprises these mechanisms tend to be weak on both sides, because corrupt managers can benefit of weaker controls and financial constraints, while for corrupt politicians may be easier to intervene in publicly-owned firms as they will benefit from the rents without directly bearing the costs (Baum et al., 2019).

Moreover, if compared to other forms of external regulation, corporatized public enterprises are justified not only by the presence of market failures, but also by the fact that the construction of extensive and complete contracts and other extrinsic mechanisms is difficult, when not impossible. In this context, principal-steward agent and network theorists emphasize the role of interdependence between the principal and the agent, together with the importance of relational contracting, intrinsic motivation, and trust (Voorn et al., 2018). The weight given to autonomy, separation

³⁹ In the most recent OECD recommendation (2019b) it is explicitly stated that (p. 7). '*Adherents should ensure that SOEs are overseen by effective and competent boards of directors that are empowered to oversee company management and to act autonomously from the state as a whole*'.

⁴⁰ In this direction Ye & Hu (2019) observe that: "*Although the phenomenon of corporate executive corruption is a universal reality in the society, it is extremely harmful, but scholars at home and abroad pay little attention to this aspect. At present, academic and corruption-related research results are mainly concentrated in the field of government officials' corruption*".

of roles, ex post-steering, private-shaped management and organization can be misleading⁴¹, crowding out intrinsic motivation and downplaying values hard to quantify and measure (Alexius & Cisneros Ornberg, 2015). In the extreme (but not residual) case of the in-house option, autonomy and separation of roles are openly conflictual and cannot be requested or suggested as viable organizational options.

In this perspective, many of the externally imposed/suggested standards for the prevention of criminal misconduct, while being certainly important, are not resolute. It is in fact argued (Previtali, 2017) that stressing (mainly) the role of symbolic structures, compliance standards, audit and enforcing procedures, there is a strong risk of creating a compliance system that is merely formal and paper-based and that has no real impact on traditional managerial procedures and approaches. Extra monitoring and bureaucracy may also increase compliance costs, while making managers less innovative and more defensive. POEs, or at least many of them, should contribute to the realization of non-economic missions and their underlying values (Alexius & Cisneros Ornberg, 2015; Bauby, 2019), requiring different and probably more articulated interpretative and regulatory approaches.

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⁴¹ The difficulty to find an equilibrium between political influence and managerial independence is clarified by Bergh et al. (2019, p. 327): "While having politicians represented in the MOEs boards could serve an important purpose as an information channel between MOEs and the council/municipal board, having local elite players represented on MOE boards is associated with risks".

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