3 Conclusions and recommendations

The Romanian Government has undertaken important reform efforts over the past decade to improve the governance and performance its state-owned enterprises. Yet, significant implementation shortcomings exist. This chapter sets forth policy recommendations to help the Romanian authorities undertake further reforms as well as designing adequate mechanisms to ensure the implementation of the already existent rules for the exercise of state ownership and governance of SOEs.

The Romanian Government has undertaken important reform efforts over the past decade to improve the governance and performance of its SOEs. In particular, the adoption of GEO no. 109/2011, later amended and approved by Law no. 111/2016, provides a strong legal framework for the corporate governance of SOEs. It established, *inter alia*, transparent selection procedures for board and executive members, a clear objective-setting and performance monitoring framework for SOEs and streamlined ownership arrangements with a co-ordination function attributed to the Ministry of Finance.

However, significant implementation shortcomings exist. As both legislations were adopted under the influence of international financial institutions in 2011 and 2016, implementation efforts seem to have stalled once the respective reform projects were terminated, which may signal a lack of sufficient political will to ensure continued implementation of the provisions of the legal framework. In some cases, ownership practices seem to have regressed towards earlier practices of excessive political influence in the more economically important companies.

The ownership framework remains widely decentralised across line ministries, with SOE ownership being exercised by individual corporate governance structures established across line ministries. The co-ordination functions vested in the Ministry of Finance are not extensive and sanctioning powers, while frequently employed, are not strong enough to deter widespread cases of non-compliance with corporate governance provisions. Moreover, corporate governance structures of line ministries are sometimes lacking resources and expertise to effectively exercise their ownership rights and are not effectively insulated from ministerial regulatory and policy making functions in some instances.

The professionalism and autonomy of boards of directors of Romanian SOEs are of particular concern. This is due to actual selection practices of board members, which in most cases depart significantly from the letter of the law. At present, the legislative framework allows for the appointment – and reappointment – of 'interim directors' at the discretion of the state if no adequate directors can be identified via the prescribed nomination procedures. Currently, a majority of SOEs operate with such interim boards, which may be inferred to be politically connected. This is also detrimental for the objective-setting framework for SOEs, as key performance indicators are intertwined with the directors' employment terms, which in turn materially weakens the exercise of financial and non-financial controls over individual companies. In addition, although a state ownership policy was issued at the same time as important amendments to the legal framework on SOEs in 2016, it appears that it is not well known among the main stakeholders and is not actively implemented.

The maintenance of a level playing field between SOEs and private companies is another potential area of concern. Although Romania abides by the state aids provisions of the EU Single Market, several areas of concern remain. These include the existence of "autonomous administrations" (i.e. SOEs with non-standard forms of incorporatisation); low and non-market consistent profitability requirements of a number of companies; and the exemption from insolvency procedures of debt owed by distressed SOEs to the state. Moreover, while Romania's practice of listing minority stakes in SOEs in stock markets should be considered as a good practice, questions remain about the treatment of minority investors in companies that retain important public policy objectives.

Going forward, Romania should seek to design adequate mechanisms to ensure and oversee the continued implementation of existing corporate governance provisions applicable to SOEs. This may entail the assistance of third parties, including in the context of the upcoming OECD accession negotiations with Romania as well as commitments undertaken by the Romanian authorities in the context of the European Union's Recovery and Resilience Plan. The main recommended actions are the following.

3.1. Strengthening the state ownership function

- *Further centralisation of the state ownership function*. There is an apparent need to establish either a central state ownership entity or a co-ordination entity with enhanced powers. Such a body would take the form of an independent public agency, or it could be hosted within a central government institution not otherwise involved in the ownership and regulation of SOEs. Its mandate should be set by law, its executive management should be employed by a term unrelated to the political cycle and it should be granted with adequate resources to perform its responsibilities. This institutional set-up would help ensure that the exercise of the state ownership function is effectively insulated from other regulatory and policy making functions, and that it has sufficient powers with regard to the enforcement of corporate governance provisions.
- *Define clear financial and non-financial performance objectives for individual SOEs*. Currently, for the majority of centrally-owned SOEs with interim appointees on their boards and in their executive positions, financial objectives are set on a quarterly basis, without regard to other non-financial objectives. Going forward, clear financial and non-financial performance objectives should be established for all SOEs along with clear reporting requirements to monitor their performance. The objectives should be communicated to each SOE as a legal entity and be unrelated to the appointment terms of individual board members and executive directors.

3.2. Maintaining a level playing field with other companies

- *Standardise the legal and corporate form of SOEs*. Consideration could be given to incorporate autonomous administrations ("regii autonome") that undertake commercial activities as joint-stock companies (excluding those that are solely policy-oriented or mainly undertake administrative functions) in order to standardise the legal form of SOEs that operate on the basis of GEO no. 109/2011. However, any change in the legal form of SOEs should be based on an informed assessment of individual SOEs' objectives and commercial orientation. A number of "non-commercial" autonomous administrations should normally not retain a corporate form.
- *Remove legal exemptions applicable to SOEs*. Legal provisions protecting SOEs subject to Law no. 137/2002 from insolvency proceedings should be amended in order to ensure that all SOEs operate on a level playing field with private companies.

3.3. Strengthening board autonomy and independence

- *Ensure the establishment of professional and independent boards of directors*. There is an urgent need to address a loophole in the legislative framework allowing for the appointment of interim board (and executive) members at the full discretion of the state owner. Alternative procedures may have to be established with regard to appointing directors in case the ownership ministries fail to do so within the prescribed timeframe. If, as has been asserted, part of the problem is a lack of applicants for board vacancies, alternative means of keeping track of available candidates should be considered.[1] Consideration should also be given to designing a competitive remuneration scheme for board members in order to attract competent professionals, including from the private sector.
- *Empower boards to carry out functions of setting strategy and supervising management.* While the boards' role in this respect is already provided by law, the combination of weak boards and politically affiliated CEOs leave much to be desired. The new ownership or co-ordination entity should be empowered to oversee board appointment procedures in order to ensure a minimal

political interference, and boards should have full discretion to nominate executive managers. Recurrent shareholder meetings to influence corporate decision processes should be avoided.

3.4. Improving transparency and disclosure practices

- *Improve financial and non-financial disclosure by SOEs*. Non-compliance with disclosure requirements remains high across SOEs, with regard to the disclosure of annual financial statements, audit reports, directors' reports, board and executive remuneration, and the resolutions of general meetings. The state owner needs to act decisively to ensure that SOEs effectively disclose financial and non-financial information as prescribed by the existent laws. In the longer term, the SOEs should aspire to similar levels of transparency as listed-company best practices with regard to the accessibility and quality of information disclosed.
- *Expand the coverage of annual aggregate reporting*. The current practice of disclosure by individual ownership ministries could be improved, including by ensuring greater consistency over time and across ministries. More importantly, consideration should also be given to expanding the coverage of the annual aggregate reports prepared by the Ministry of Finance. In addition to the current coverage, annual aggregate reports should also include: (i) key non-financial performance of SOEs (e.g. risk disclosure and mitigation measures; employee and stakeholder relations); (ii) an overview of the SOE portfolio (scope and size) and sectoral distribution; (iii) implementation of public policy objectives; (iv) appointment of SOE board and board composition with regard to independence criteria; and (v) detailed reporting on individual SOEs' performance and targets (by sector or for the most economically important SOEs).

3.5. Strengthening internal control systems

- *Improve the monitoring and implementation of risk management and integrity measures*. Internal controls, risk management, anti-corruption and integrity measures currently exist, but they tend to operate in isolation and to a large extent reflect off-the-shelf mechanisms. Care should be taken to ensure a whole-of-company approach and ensure that all the relevant procedures are effectively monitored. For this purpose, ownership entities should take measures to ensure the independence, qualifications and powers of SOEs' board audit committees.

Note

[1] In some countries, this has been done by establishing pools of directors, sometimes maintained with the help of professional head hunters.