

EXPLORING THE IDIOSYNCRASIES OF STATE-OWNED ENTERPRISES IN THE WHOLE OF GOVERNMENT PICTURE

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Abstract

State-owned enterprises, as controlled entities by governments, are present all over the world as a result of privation, nationalization or on the strength of financial and social issues, representing an important part of the governmental financial situations. The purpose of the paper is to illustrate the complexity surrounding the meaning of the term SOE as controlled entity since this term is crucial for the aim of governments to increase its accountability and transparency.

A content analysis of responses to the IPSASB Consultation Paper (CP) concerning SOEs has been used. Based on our study, we conclude that a definition is necessary as emerging countries need to have clearly established boundaries of their financial statements and, most of the time they do not have the necessary resources as professional bodies, qualified personnel, to fulfil their obligations as regulators.

Keywords: *State-Owned Enterprises, Public Entities, International Public Sector Accounting Standards, Consultation Paper*

JEL classification: *M41, M48, H71*

1. Introduction

Reforms in public management represent a global trend (Ongaro and Valotti, 2008), being frequent the situation when regulations are not correlated with the business world reality or instructions regarding their implementation are missing. Unfortunately, in most countries the current legislation referring to state-owned enterprises (SOE) is inadequate, adjustment and restructuring

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of SOEs a necessity determined by market and technological changes (Kloviene and Gimzauskiene, 2014).

The importance of SOEs strongly increased in the recent period of time due to a stringent need for effective, efficient and high quality public services (Papenfuss and Schmidt, 2015). Recently, both researchers and practitioners focus on aspects regarding good governance, as a way of increasing organisational efficiency.

In this context, the topic approached concerning SOEs is considered to be of great interest based on their role of key economic players that aim fulfilling certain needs of societies and complement activities of private organizations and public institutions, instruments of their holders to meet their political objectives and in the same time the subject of much policy making concern (Machura, 1993).

The significant role of SOEs is demonstrated by studies made at country level, mentioned in their research by several authors (Papenfuss and Schmidt, 2015). Christiansen (2011) underlines the importance of SOEs by presenting statistical data that create an overview of the Organisation for Economic Co-Operation and Development (OECD) reporting countries' situation in the year 2008/2009: a number of 2,057 enterprises, employing over 4 million people and with an estimated value exceeding 1.3 trillion US dollars.

In financial reporting area, SOEs represent an issue for consolidation. Being part of the controlled entities they will be included in the consolidated financial statements of the controller governments. In practice there is a huge diversity of entities which are more or less SOEs, or are included in this category without having the SOEs characteristics. In this context, the first issue who arises is what are state-owned enterprises and their characteristics.

The research presented in this article is qualitative oriented, aiming to search for meanings and understandings on how SOEs are defined. Our conclusion is the fact that, clearly defined concepts should contribute to a better understanding of the SOEs concept and by this, to contribute to good governance through enhancing the quality, consistency, and transparency of public sector financial reporting (IPSASB, 2012). The following sections of this paper present methodological aspects, followed by results highlighting aspects concerning SOEs definition. The conclusions of our study are drawn in the final section.

2. Methodology approach and research question

The challenge of applied accounting research is to improve practice by analysing and discussing different views and accounting policies. The purpose of the paper is to illustrate the complexity surrounding the meaning of the term SOE as controlled entity since this term is crucial for the aim of governments to increase its accountability and transparency.

The methodology is in line with the interpretative perspective and pays particular attention to meanings behind SOE. The data collection is based on content analysis of responses to the IPSASB Consultation Paper (CP) concerning SOEs. The paper is qualitative oriented, the primary goal being to search for meanings and understandings on how SOEs are defined.

In order to solve the definitional issue, IPSASB developed a Consultation Paper (CP) in August 2014, named The applicability of IPSASs to Government Business Enterprises and Other Public Sector Entities, with the objective to identify the public opinion regarding the application of the IPSAS for SOEs and Other Public Sector Entities. The CP was published on the IPSASB official website and practitioners were invited to submit their comments.

A number of 28 comment letters were submitted in the period 15th October 2014 - 14th January 2015 and made public. In order to analyse respondents' point of view related to the CP, an in-depth content analysis of the comment letters was conducted. The analysis criteria are the approach chosen by respondents, respondents' function and geographical location. The research question of the study is: What are the SOEs definitions from an academic and a professional point of view? How are SOEs defined by experts?

3. Definitional issues: IPSASB's Consultation Paper concerning SOEs definition - respondents points of views

3.1. Consultation Paper Description

Taking into account that SOEs are present all over the world being part of different jurisdictions, IPSASB developed some projects aiming to set the conceptual delimitation of the term. The first CP idea arises in 2008, but IPSASB discussed and approved a brief project on SOEs in March 2012, and in December 2012 the project started. A broader strategic approach was proposed, in which a formal definition of a SOE would not be retained. The IPSASB considered four approaches to SOEs (IPSASB, 2012): "(a) Do not specifically define SOEs but provide the high level characteristics of entities for which the IPSASB is developing standards; (b) Clarify the existing

definition of SOEs so that it is easier to apply; (c) Narrow the existing definition of SOEs; or (d) Redefine SOEs using a different approach e.g. based on services provided by entities or the objectives of entities. But, because it received little support it was decided not to further develop approach (d)".

In the final CP developed in 2014, IPSASB suggests two main approaches. The first approach does not define the term, it develops a list of characteristics for public sector entities, while the second approach is modifying or narrowing the current definition presented in IPSAS 1- Presentation of financial statements. Both approaches have two sub-options, the differentiating criteria among them being the use of statistical terminology (IPSASB, 2014).

Option 1a relies on current and developing IPSASB literature to describe the characteristics of public sector entities. Option 1b involves importing a number of terms and explanations from GFS reporting guidelines into IPSASB's literature. Options 2a and 2b are not mutually exclusive. Option 2a could be adopted in conjunction with Option 2b so that the existing definition of a SOE is both clarified and narrowed.

The IPSASB's preliminary view is that Approach 1 is the best way forward. A majority of IPSASB members have expressed their support for the preliminary view presented through Option 1a. IPSASB requested the respondents to provide answers, reasons and their point of view about IPSAS's PV and what option they prefer. All the respondents welcome the opportunity to respond to the CP and they congratulated IPSASB for this initiative.

3.2. The structure of the sample by options

At the level of the two approaches (Approach 1 and Approach 2), choices are predominantly oriented towards Approach 1 (89.28%) while only 3.57% mention Approach 2. Two of the respondents do not support any of the approaches proposed by CP. One of them is not sufficiently clear when expressing the opinion (3.57%) while the other one proposes a different approach (3.57%).

Among the supporters of Approach 1, 80% agree with one of the options (76% agree with Option 1a, 4% agree with Option 1b) and the remaining 20% are partially supporters (they support partially Option 1a). The only respondent that supports Option 1b is the International Consortium on Governmental Financial Management - ICGFM from USA.

Regarding Approach 2, just one of the respondents totally supports of one of the options proposed, more precisely, the Institute of Chartered Accountants from Ghana supports Option 2b. In conclusion, the majority of the respondents support the definition of SOEs using the characteristics of public entities, presented through Approach 1, respectively Option 1a.

3.3. The structure of the sample by function and country

The structure of the sample of respondents considering the function criteria is: 36% members or regional bodies, 25% preparers, 18% standard setters or Standards Advisory Bodies and a percentage of 7% for audit offices, accountancy companies, and others.

Over 50% of analysed answers are from countries with high interest on the topic, in top of them Australia with 14.3%, Canada with 10.71%, followed by UK, South Africa, France and Malaysia, each of them with a percentage of 7.14 %. The level of interest in these countries can be justified, on one hand by the existence of national regulations for SOEs, and, on the other hand, by problems identified in their national regulations.

In Australia, according to Public Governance, Performance and Accountability Act 2013 (PGPA), a SOE is a company controlled by the Commonwealth. The Commonwealth controls a company if it: controls the composition of the company's board; or is in a position to cast, or control the casting of, more than one half of the maximum number of votes that might be cast at a general meeting of the company; or holds more than one half of the issued share capital of the company (Australian Government, 2013). Their interest for the CP is justified by the acknowledgment that in Australia, only those entities which are wholly owned are recognized as a SOEs.

In Canada, the government periodically develops guidance for SOEs to support sound governance and management practices. Public Sector Accounting Board (PSAB) issued a separate guideline referring to Investments in Government Business Enterprises (Section PS 3070). PSAB defines SOEs as "a government organization that has all of the following characteristics: it is a separate legal entity with the power to contract in its own name and that can sue and be sued; it has been delegated the financial and operational authority to carry on a business; it sells goods and services to individuals and organizations outside of the government reporting entity as its principal activity; it can, in the normal course of its operations, maintain its operations and meet its liabilities from revenues received from sources outside of the government reporting entity" (PSAB, 2014).

The interest of PSAB for the CP is due to the fact that in their jurisdictions were identified entities that are wholly owned by the provincial government (acting like SOEs) and are not defined as SOEs directly. In the same line is the lack of South Africa jurisdiction (Act 1996 - Government Business Enterprises (Competition)) which recognizes and defines as SOEs just “government agencies that carry on commercial operations”.

In determining the boundary for the WGA (whole of government accounts), the UK Treasury has adopted the classifications of public bodies used by the Office for National Statistics (ONS). As a consequence of the Treasury adopting statistical, rather than accounting standards, when it comes to defining ‘control’, the WGA excludes an important SOE (Network Rail Ltd) with net assets of £8 billion at 31 March 2014) (HM Treasury, 2015). The alternative recognized by the Treasury is applying IPSAS, which require the inclusion of bodies that are subject to Government control and define control as “the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities” (IPSAS, 2014).

The responses to the CP proposed by IPSASB received from countries like Ghana, Kenya, Zambia, Nigeria, Puerto Rico, Israel, and Brazil represent about 25% of the total number of responses. Also, responses from developed countries like New Zealand, Japan, Sweden, Swiss, Germany, and Belgium were received, in a proportion of over 20%.

In conclusion, many responses were sent by accounting professional organisations that promote specific regulations, standards, guidelines for SOEs accounting treatments and definitions from developed or emerged countries with high interest on the SOEs issue.

4. Findings and discussions

Concerning the IPSASB CP, twenty-four respondents are supporting the IPSASB option that wants to define SOEs using characteristics of public sector entities, based on IPSAS terminology (Option 1a). The table below presents a synthesis of the responses using the criteria option and continent (Table 1).

Table 1: A synthesis of the responses using the criteria option and continent

		Continent											
		Asia		Australia		Europe		America		Africa		Total	
		No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
A 1	Favorable 1a	4	100	4	100	8	100	4	80	4	57.14	24	85.71
	Favorable 1b	0	-	0	-	0	-	1	20	0	-	1	3.57
	Total A1	4	100	4	100	8	100	5	100	4	57.14	25	89.29
A 2	Favorable 2a	0	-	0	-	0	-	0	-	0	-	0	-
	Favorable 2b	0	-	0	-	0	-	0	-	1	14.29	1	3.57
	Total A2	0	0	0	0	0	0	0	0	1	14.29	1	3.57
Other	Other approaches	0	-	0	-	0	-	0	-	1	14.29	1	3.57
	No clear view	0	-	0	-	0	-	0	-	1	14.29	1	3.57
	Total other options	0	0	0	0	0	0	0	0	2	28.57	2	7.14
Total		4	100	4	100	8	100	5	100	7	100	28	100

Source: Author's projection

All respondents that support Option 1a argue clearly their choice listing a series of arguments. The most common arguments are: “it is a principle-based approach”, “it acknowledges the role of regulators and other relevant authorities in determining which entities should apply IPSASs”, it helps “educate” regulators and other relevant authorities and assist preparers. The respondents which support option 1a mention that the alignment with GFS terminology can cause mismatches between Conceptual Framework for Accounting and the terms used in GFS and, also, a systematic alignment between IPSAS (based only on the control criteria) and GFS does not make sense because of their divergent scopes and objectives. Moreover, the

inclusion of statistical terminology, which is more difficult to understand, requires an average level of statistical knowledge for the users.

On the basis of an in-depth analysis of the responses, we extract the main benefits related to the implementation of the Option 1a: is principle-based rather than rules-oriented; uses principles that focus on fundamental characteristics of public sector entities; is relatively easy to understand and apply; does not create issues with further defining additional terms; allows the exercise of judgement and acknowledges the role of regulators; addresses the interpretation and lack of flexibility issues that lead to the start of this project.

From the total number of 25 respondents that support Approach 1, just one of them argues in favour of Option 1b. The respondent representing the International Consortium on Governmental Financial Management (ICGFM) from USA agrees that IPSAS should limit its review to describing the characteristics of public sector entities (Approach 1), but this should be done using GFS terminology since IMF classification is well laid out and does not need further classification. They state that Option 1b should be implemented easier considering the fact that GFS terminology is being applied by countries throughout the world.

We consider that the choice is influenced by the nature of their activity. Taking into account the fact that ICGFM is dedicated to improving financial management by providing opportunities for professional development and information exchange, the introduction of statistical terms it is a key factor for increasing the market demand for services provided by them.

At the level of Approach 2, the justification made by IPSASB regarding the definitional issue of SOEs was approved indirectly by each of the respondents through the fact that no one chose Option 2a. Only the respondent representing the Institute of Chartered Accountants from Ghana believes that the problems with the current definition of SOEs can be solved by narrowing the existing definition. Their reason was argued as follows: “We believe that option 2b has the following advantages: (a) benchmark for deciding whether an entity applies IPSAS or IFRS; (b) limited definition of SOE to focus on profit-oriented entities”. Also, the respondent states that “through Options 1a and 1b characteristics like comparability, capacity of regulators, convergence and international harmonisation should be affected”. We consider that, in this case, the decision is influenced by the fact that Ghana is an emerging country with a governmental system that cannot handle the issue of regulators' power.

The respondent representing the Association of National Accountants of Nigeria is the only one that proposes another approach, by compiling Option 2a and Option 2b. Going on the idea that defining one term or characterising it does not determine the nature of an approach (principle-based or rules-based) and considering the particularities of public sector, they consider that Approach 2 is the most appropriate. In their opinion, under Approach 1 the qualitative characteristic of comparability can be affected by the power of regulators (different practices across jurisdictions) and financial analysis replaced with an economic focus. The third approach proposed by them is a compilation of the definitions presented through the two options included in Approach 2. Under this approach, a SOE is an entity that: “has been assigned the financial and operational authority in legislation or governance documentation to carry on a business (Option 2a and b); delivers services, in the normal course of its business, to individuals and non-government organizations as well as other public sector entities outside the reporting entity at a profit or to achieve recovery of all fixed and variable costs of the reporting period (Option 2a); can prepare its financial statements on a going concern basis without being reliant on any continuing government funding or other forms of direct or indirect financial support from government (other than purchases of outputs at arm’s length). Such funding or financial support includes concessionary loans, government guarantees and grants for meeting community service obligations (Option 2b); and is controlled by a public sector entity (Option 2a and b)” (IPSASB, 2014).

5. Conclusions

SOEs, as controlled entities by governments, are present all over the world as a result of privation, nationalization or on the strength of financial and social issues, representing an important part of the governmental financial situations. There are several different approaches about what types of entities are covered by SOE’s definition.

IPSASB decided to describe the characteristics of public sector entities for which IPSASs are intended (Approach 1), the definition of SOEs being excluded from their standards. In this situation, professional judgment is needed to decide whether an organisation is classified as a SOE (IPSASB, 2014).

Based on our study, we conclude that a definition is necessary, and as we saw, significant national professional bodies are considering necessary to use a definition, to present the characteristics, to provide a guideline for SOE

recognition. Emerging countries need to have clearly established boundaries of their financial statements and, most of the time they do not have the necessary resources as professional bodies, qualified personnel, to fulfil their obligations as regulators. Even though IPSASB decides to adopt Option 1a and to not define what a SOE is, they should develop some Guidelines in order to clarify sensitive aspects.

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