EUROPEAN PUBLIC SERVICE UNION

# Public Assets


## A CRITICAL READING OF

**DG ECFIN's discussion paper:**
***Public Assets: What´s at Stake? An analysis of Public Assets and their Management in the European Union***

Prepared for EPSU by
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# A CRITICAL READING OF *Public Assets: What´s at Stake? An analysis of Public Assets and their Management in the European Union* (European Economy Discussion Paper 089[1], November 2018)

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## Executive Summary

In 2016, the Directorate-General for Economic and Financial Affairs of the European Commission (DG ECFIN) commissioned to KPMG, a global consultancy company, and Bocconi University, a private Italian university to carry out research on public assets across Europe. This briefing, prepared for the European Federation of Public Services Unions, provides a critical reading of the summary report based on the research that was published as a discussion paper by DG ECFIN in November 2018.

After analysing the main claims made, approach and structure deployed, it examines the key assumptions embedded in the report. It argues, first, that the financial accounting perspective taken by DG ECFIN is over-reductionist and fails to capture realistically the role of public assets in society and the economy. Second, it finds bias in the report, since its "valuable examples" of government ownership and management of public assets tend to be those associated with "reigning in" government. Methodological flaws in the report are highlighted, such as its seemingly random selection of case studies.

While the discussion paper report concludes by calling for more transparency on the ownership and management of state-owned companies, this EPSU report goes further, and calls for more transparency on the ownership and management of both private and state-owned companies alike. To this end, it supports the development of a user-friendly open access database for all private and public companies so citizens can actually understand "who owns Europe".

# Description of the Discussion Paper, *Public Assets: What´s at Stake? An analysis of Public Assets and their Management in the European Union*

## Why was this report written?

In 2016, the Directorate-General for Economic and Financial Affairs of the European Commission (DG ECFIN) published a contract notice for a "Study on State Asset Management". The objective of the study was to provide an "overview of public assets" and to encourage "the adoption of best practices regarding their management (including their restructuring and/or privatization) of the portfolio of assets, with the aim of improving the sustainability of public finances and market functioning".[2] The initiative behind this development originated from the European Parliament, particularly via the Croatian MEP Ivana Maletíc of the European Peoples' Party, who pushed for European-wide research on the public sector. The motivation for Maletíc's petition is stated to be frustration with the perceived slowness and ineffectiveness of public sector reforms in Croatia. In particular, Maletíc wanted to know which "best practices" existed with a potential for policy transfer to Croatia.[3]

The research was commissioned to KPMG, a global consultancy company, and Bocconi University, a private Italian university. The contract was worth Euro 800,000 (but subsequently only around 600,000 was awarded) and its research output, published in 2018, is available online.[4] However, much of the "raw" data used by the researchers - as well as their calculations - are not publicly available. The research was summarised into a short Discussion Paper by DG ECFIN under Lucio Pench, Director of Fiscal Policy and Policy Mix, and Stefan Ciobanu, Head of Unit Fiscal Governance. Pench is an expert on fiscal consolidation and surveillance, Ciobanu on fiscal governance and statistics.[5]

The commissioning of this work and the subsequent publication of the EC report has alarmed a number of observers. A major concern is that the research might be biased towards the private sector, constituting, in effect, another push towards privatization.[6] Although the EC is treaty bound to maintain neutrality on questions of ownership, its activities inside the "Troika" – most dramatically in Greece 2010-2018 – showed the EC has become emboldened to take a position in favour of private ownership (Clifton, Díaz-Fuentes and Gómez, 2018). Hence, there is a concern that the conclusions of the research might be used to justify a new wave of market-oriented reform through the European Semester, whereby the EC undertakes surveillance of the budget and economy of EU Member States and provides "recommendations" (Corporate Europe Observatory, 2017).

## The Major Claims made in the Report

The Report critiqued here summarises the research project, and makes three major claims:

1. **Public assets were worth an estimated Euro 16.5 trillion in 2015**. Public assets can be classified into two bodies: "financial assets" and "non-financial assets". "Financial assets" refer here to government stakes in companies (often referred to elsewhere as "corporatization"). "Non-financial assets" refer to assets which are directly owned and controlled by government. In this study, they cover only dwellings, buildings and structures and natural resources. Following this categorization, some 40% of public assets are financial assets (valued around Euro 6 trillion), the other 60% correspond to non-financial assets (valued around Euro 10.5 trillion). This research represents one of the first attempts to classify and value all public assets in the EU.

2. **As regards management and investment decisions, governments are still very active in the EU**. Governments tend to control strategic decisions for most non-financial assets, even if ownership and operational decisions are shared with local government/private investors. Governments are continuing to invest in strategic non-financial assets, whilst financial assets are being reduced.

3. **Public assets constitute an important part of governments' fiscal risks.** However, there is insufficient data available on public assets and their management, especially as regards "non-financial assets": there is also a lack of data on how public assets are managed. The report specifically calls for policy-makers to improve this situation, by increasing information from a financial accounting perspective on this topic, with a view to monitor "fiscal risk" and increase "transparency".

## Structure of the DG ECFIN discussion paper

The DG ECFIN discussion paper is organized into six parts.

**Part One** sets out the motivations for commissioning the research. The background driver is cited as Council's recommendation of November 2015 to promote "*open and competitive product and services markets while reducing public debt in full respect of the Stability and Growth Pact*" (p. 5). In this regard, the report states that more information is needed about public ownership and management to help in turn to assess the "*operational and fiscal challenges weighting on public accounts and on national and European product and services markets*" (p.5). Hence, this report is justified by the need to assess the role of public assets as a potential fiscal risk for government from a financial accounting perspective.

The rest of the report summarises findings of the Bocconi/KMPG research. **Part Two** analyses financial assets in the EU. The main source of data on financial assets is the private database, ORBIS (Bureau van Dijck). The report states there are 37,399 companies with public sector stakes. The number and value of these financial assets per country, the extent of government ownership, sectoral distribution, and geographical scope of activity, are considered. The report finds most financial assets to be involved in either services (40%), utility providers (25%) or real estate (19%). By asset value, financial and insurance services are by far the most important, representing nearly 60% of total value (partly due to bank bailouts in the UK and Ireland). Total employees and labour costs, profitability, and contribution to GDP are described.

**Part Three** analyses "non-financial assets". It follows ESA2010 classification into "produced" (buildings and structures, machinery and equipment, computer software, R&D, precious art, metals, stone) and "non-produced" (mineral resources, energy reserves and other natural resources, contracts, leases, licenses, purchases less sales of goodwill, marketing assets). Yet, it only looks at a selection of non-financial assets. A range of different databases were used to compile information on non-financial assets, including EUROSTAT, in conjunction with data from ORBIS, OECD, GFS, EU Building Stock Observatory for Building, CIA Factbook. Where data was not available, estimates were made on their value (critiqued later).

Only some of these are considered here. If any of these assets are owned by a "PSH", they are treated as a financial asset, only where government fully owns and directly controls assets are they considered as "non-financial assets". The sectoral distribution, country distribution and estimated value are assessed.

**Part Four** describes management practices of public assets (both financial and non-financial assets). The report establishes three managerial classifications: centralised, decentralised and private sector management. Public assets in different sectors are described by managerial tendency linking ownership, operational decisions and strategic decisions. Then, six cases are reviewed which explore examples of public asset management in different EU countries.

**Part Five** briefly describes government "investment strategies", meaning sale or acquisition of assets by government and the involvement of the private sector. Data from diverse sources is collected and eight case studies are examined. Sectors and countries in which governments are reducing and increasing their portfolio are presented. Case studies examine the consequences of sale/acquisition for market share, profitability, efficiency and solvency.

The **Conclusion**, apart from restating the main findings, recognises weaknesses in the report's coverage, particularly, as regards non-financial assets, due to data non-availability and non-comparability. It makes a number of recommendations. **To improve government management of public assets**, the introduction of an "asset management entity" is advisable. In addition, the report states greater coherence between local and central government as regards operational functions should be promoted. More laws to boost the transparency of asset management is required. Another recommendation is that the government should be encouraged to share – but not fully transfer – risk to the private sector.

Further, greater attention should be paid to management with a customer-oriented focus. Privatization needs to be accompanied by competition, and checks should be made to ensure this is the case. As regards **government investment**, an independent regulator to decide on investment and expenditure should be encouraged. Finally, **more research is needed on public assets**. The report claimed in particular that there is insufficient data on non-financial assets, and work extending knowledge about the sectors not covered in this report should be performed. Methodologically, more work is needed in order to better reconcile databases on public assets, especially, EUROSTAT and ORBIS. National databases on public assets should be made more comparable. Member States should publish inventories of their assets and management practices.

## CRITICAL ANALYSIS OF THE REPORT

In what follows, the report is critically analysed for its assumptions and claims, what devices are used to convey these (methodological approaches, use of economic theory/ideology, language and so on), and alternative interpretations. Next, some observations are made about flaws in the report, including methodological and conceptual issues, and finally, what is missing from the report.

### Assumption 1
### Public assets can and should primarily be analysed from a financial accounting perspective and, on balance, they present fiscal risks to government.

The report presents a number of key assumptions which, together, form the internal logic which underline the framework it is based on. The first major assumption is that **public assets can and should primarily be analysed from a financial accounting perspective and, on balance, they present fiscal risks.** Public assets are categorized into being either "financial assets" – that is, those where the government has stakes in companies (often called "corporatization" in the literature) or "non-financial assets", those that are fully and directly owned by the public sector.[7] Second, public assets (both financial and non-financial assets) are seen as entities generating **financial gains and losses**, which affect governments' fiscal balances (financial needs and capacity to repay debt). Given this, the rest of the report over-focuses on the "risk" side of this question. The devices used in the report to analyse public assets all hinge upon the logic of this financial accounting perspective.

The public policy literature uses the very useful concept of "venue". The specific venue selected for a policy initiative will in turn influence the approach and content produced. Hence, it is unsurprising that this approach to public services is so narrow, since it was commissioned by DG ECFIN, which takes an overly narrow view of the impact on debt on public finances.

However, this financial approach is hardly suitable to analyse public assets, since their contribution cannot be reduced to an "assets and liabilities" approach. The financial approach pays insufficient attention to the financial benefits of public assets and, more importantly, to the social, political and cultural benefits generated by public assets, including social welfare concerns.[8] This approach does not take in consideration the economic and social perspectives of fiscal policy. A significant amount of "non-financial assets" is the result of public investment in public and merit goods, including schools, hospitals and other key infrastructure. If markets – including financial markets – were left to work alone, essential public and merit goods would be underprovided. This would render society below the economic and social optimum: education and health are required to guarantee social mobility and equal opportunities based on talent. Physical infrastructure networks, including transport, is required to physically facilitate mobility of people, goods and services required for better market functioning. Whilst the privatization of these non-financial assets could reduce public debt and the "fiscal burden", it would also shrink the potential of society and the economy itself. None of these essential questions are contemplated in the financial accounting perspective.

As a result of this financial accounting framework, and over-focusing on the risk side, the report assumes that, to increase the "transparency" (p.6, p. 36) of government ownership, more needs to be known about public assets, particular, non-financial public assets.

Fundamentally, **the financial accounting perspective is over-reductionist and fails to capture realistically the role of public assets in society and the economy**.

This approach is accompanied by a choice of words that helps construct a negative approach to public assets. For example, the report worries that public assets might be "weighting" (p.5) on governments, may constitute "fiscal risks" (p.5), causing "negative risks" such as "shocks" and creating "uncertainty" in the economy (p.6). This negative language is not balanced by a positive perspective, such as their contribution to fiscal balances but also to society as a whole. This renders the report biased against public assets.

## Assumption 2
## There are "valuable examples" as regards government ownership and management of public assets, and these tend to be associated with "reigning in" government.

The second major assumption in the report is that there are **"valuable examples" (p. 26) practices as regards government ownership and management of public assets, and that these are consistently associated with practices to "reign in" government ownership or management.** Despite the fact that the EC is treaty-bound to neutrality on questions of ownership, the report concerns explicit and implicit assumptions as regards what it assumes is best practice from around the EU. The main devices used here are the "case studies", which are taken as "valuable examples", however, there is a more subtle display of this assumption as seen through the presentation of visual data in graphs.

Turning first to the case studies, a methodological question is raised. In most scholarly work, cases are selected following a range of selection strategies, in order to be able to derive conclusions. In this report, no such selection strategy is mentioned. Rather, the cases seem to be chosen completely *ad hoc*. Case studies in the report present troubling examples of misinterpretation and bias. The most alarming is in Section 4, which examines management practices in public asset ownership. Here, three categories are established: centralised, decentralised and private sector management. After establishing these categories, private sector management is not explored further (suggesting perhaps the authors thought this was not necessary), whilst the report focuses on centralised and decentralised approaches. The assumption in this section is that these two approaches may lack relevant entities for their overall management. Six case studies are presented "to ensure a fair balance between centralised management and quality of service provision" (p.26).

It is shocking to find that one of the "celebrated" best practices is the Hellenic Republic Asset Development Fund (HRADF). This is a highly controversial entity imposed on Greece by the so-called "Troika" in the aftermath of the country's debt crisis, and is associated with "imposing" privatization in a humiliating fashion, top-down.[9] According to the report, the HRADF "bestowed credibility" on the privatization process, allowing the EU to represent "the possibility" to attend board meetings, thus providing "transparency" and "accountable" processes. The report shows very little sensitivity to ongoing historical contexts and social realities, and holds up a highly politicised development as if it were "apolitical" and positive as regards "financial transparency", ignoring questions of vested interests, captive regulators, and incentives promoting "revolving doors". The creation of the Troika and its intervention in Greece has widely been seen as a failure and a low point in EU democracy.[10] Is this really best practice in the eyes of the EC?

A more implicit means of setting up best practices is conveyed in the report through the use of graphs and tables. A good example is found in Section 1, which presents the number of Public Sector Holdings per country and their estimated value. The report draws attention to countries which have the most active government intervention, in the form of high degrees of "full ownership" (Estonia, Czech Republic and Latvia) and fully-owned Public Sector Holdings with large assets (Estonia, Lithuania and Bulgaria), p, 8. However, by not drawing attention to those countries with less government ownership, the report is implicitly suggesting it is these countries in Central and Eastern Europe which need assessment and report. It implicitly is making the case that more, not less, government, is the problem. An alternative perspective would be to identify those countries and sectors where Public Sector Holdings have been found to be efficient, and use this as a model for policy transfer.

## Flaws in the report

Any effort to quantitatively and qualitatively describe public assets in the European Union will inevitably come up against huge methodological and data challenges: this is indeed a significant scientific challenge for any researcher. There is no one single database that contains this information: various data sources need combining. This presents challenges. Overall, the quality of the report deteriorates as it continues. Section two is stronger than section three, and so on.

Starting with the analysis of financial assets in Section Two, one major problem is readers do not have access to the full dataset should they want to replicate the study. ORBIS is a private database, not available to all scholars but, more importantly, the calculations on financial assets made by the researchers cannot be checked by peers. ORBIS is not a complete or fully reliable database on publicly-owned financial assets and, though this is acknowledged in the report, this remains a flaw.

**It would be of real interest to make open access the researchers' calculations for replication and checking**.

Section two presents a significant methodological challenge: how can the assets, liabilities and net worth of Public Sector Holding assets be quantified? The results are displayed in Graph 2.9 on page 15, which presents several important errors. First, the graph mixes two different things. On the one hand, it states it calculates the "assets" of Public Sector Holdings as derived from ORBIS, which the report admits is not a comprehensive list. On the other hand, it derives the "liabilities" from EUROSTAT, which is also a non-comprehensive list, but in a very different way to ORBIS. EUROSTAT only includes those government-controlled entities where government ownership is over 50%. The report itself acknowledges these flaws (p.14) but, despite this, the report states "the difference between net worth and assets should in principle correspond to the outstanding liabilities of government controlled entities" (p.15). Graph 2.9 presents many questions, for example, how is it that countries such as Cyprus and Slovakia have no liabilities? There are other flaws in this section, for example, authors mix two different terms, "outstanding liabilities" (in the ledger), with "liabilities" in the title. The flaws here – most strikingly the use of data which are not comparable, means that no policy recommendations should be drawn from the research.

The main methodological challenge in Section Three, to estimate the value of "non-financial assets", is especially difficult because national accounting methodologies may differ and data is very "scarce and heterogeneous" (p. 19). In this case, researchers acknowledge they had to "estimate" (p.19, p.20) the value of a significant body of non-financial assets using different methodologies according to the sector in question (pages 21-22), since official calculations are lacking. Table 3.1 shows the country/sector where official data exists and where the researchers estimated. Notably, official data was estimated for Bulgaria, Croatia, Ireland, Romania and Spain for all three sectors, and two out of three categories for Belgium, Cyprus, Denmark, Hungary and Slovakia. The category "other natural resources" lacks official data for 20 out of 28 countries. Comparing the countries where all estimations on non-financial assets were done by the researchers to the report´s graph 3.3 on the value of non-financial assets, it is striking how very high non-financial assets as a percentage of GDP has been calculated for countries in Eastern Europe, most particularly, Bulgaria, Croatia and Romania. It is likely these estimations are over-estimating the value of many of these assets by using heterogeneous estimation tools that are more suitable for the private sector.

The weakest parts of the report are found in the qualitative studies of public asset management and investment in Sections 4 and 5. As mentioned in Assumption 2, scientific justifications for case study selection strategies are missing, so, as selection is *ad hoc*, it is highly debatable that something can be derived from case study discussion. Additionally, the fact that the authors included the HRADF alongside other examples, such as the UK's National Rail or the Finnish central government public sector holding, Finavia Oyj, reveals a significant lack of contextualization, since the establishment of the HRADF in Greece under the Troika remains especially controversial. As regards qualitative methodologies, the main approach is case studies, which are used to analyse public asset management and government investment strategies. No methodology is provided to justify case selection strategy. The choice of case studies appears random.

## Concluding remarks: open questions of concern

The first major question here is why the Commission is conducting research on a topic – the "value" and "management" of public assets, when its specific mandate is to remain neutral according to the treaties? It is obvious that the European Union faces unprecedented challenges in the contemporary period – climate change, the rise of anti-EU parties, populism, migration and economic uncertainty – and that national decisions around the composition and organization of the public sector remain largely domestic, with the exception of growing EC competition and state aid legislation. The Commission´s *White Paper on the Future of Europe*[11] suggests the EU should focus on its core principles. Attempting to value domestic public assets is not one of them.

The second question is whether the report is balanced, or whether it exhibits bias towards the private sector. This analysis points to fundamental flaws in the methodology that all tend to go in the direction of over-estimating the value of public assets, particularly, in countries in Eastern Europe, as well as the choice of words to paint public assets more negatively than private ones. Attention is placed on the negative side – public assets are presented as being a drag on public finances, while their positive role in the economy and society are ignored. The report is biased in favour of the private sector.

Third, what is the real purpose of the report? Originally, it was promoted purportedly to provide insight into public assets in the EU for Croatia through best practice policy transfer – but the conclusion of the report is that all governments should be more transparent about their public sector. No effort was made to identify "what works" in Europe, and what models could be transferred to Croatia. The original motivation seems to have shifted to a different priority – to present public assets as a "black box" which needs making transparent. But if the aim is to render economies transparent, why not start by seriously deterring tax avoidance schemes prevalent in the private sector?

Is there evidence this report lays the ground for a renewed privatization push or perhaps, more subtly, a greater "advisory" role of the EC in public sector governance? On the one hand, readers of the report might feel assured that this report will not be used to promote privatization because the authors state that privatization does not necessarily make firms more efficient. This has previously been the classic claim of privatization proponents. However, by more subtly focusing on the negative (risk) side of public assets and ignoring the positive side, and by making claims that some countries still have "too many" public assets, this report certainly could be used to promote further privatization in the EU, and more private-like public asset governance, especially in the East.

## References and notes

[1] https://ec.europa.eu/info/publications/economy-finance/public-assets-whats-stake-analysis-public-assets-and-their-management-european-union_en

2 European Commission (2016) Belgium-Brussels: Study on State asset management in the EU at https://ted.europa.eu/TED/notice/udl?uri=TED:NOTICE:440766-2016:TEXT:EN:HTML

3 Interview with Accredited Assistant Alen Halilovic, 20 January 2019.

4 https://ec.europa.eu/info/evaluation-reports-economic-and-financial-affairs-policies-and-spending-activities/analysis-public-assets-and-their-management-european-union_en

5 DG ECFIN organizational chart at https://ec.europa.eu/info/sites/info/files/organisation-chart-dg-ecfin-february2016_en.pdf

6 This concern has already been flagged by Corporate Observatory Europe in *Is the European Commission preparing a new privatisation push?* https://corporateeurope.org/power-lobbies/2017/11/european-commission-preparing-new-privatisation-push

7 Readers can be confused because the use of terminology in the report is not systematically used at times. For example, though the report establishes the category "financial assets" and "non-financial assets", within both sub-categories, are public assets in the "financial sector" or in the "non-financial sector". On occasions, the report uses "financial assets" when it means assets in the "financial sector", for example, on p.15 when describing Chart 2.9. In addition, when discussing financial assets, the report often uses the term Public Sector Holdings (PSH) and when discussing non-financial assets it often uses the term government controlled entities.

8 Massimo Florio (2014) *Network Industries and Social Welfare. The Experiment that Reshuffled European Utilities*. Oxford University Press.

9 Judith Clifton, Daniel Díaz-Fuentes & Ana Gomez (2018) "The Crisis as opportunity? On the role of the Troika in constructing the European Consolidation State", *Cambridge Journal of Regions, Economy & Society*, 11(3), 29, 587-608.

10 Charlotte Burns, Judith Clifton & Lucia Quaglia, (2018) "Explaining policy change in the EU: financial reform after the crisis", *Journal of European Public Policy*, 25(5), https://doi.org/10.1080/13501763.2017.1301535

11 European Commission (2017) *White paper on the future of Europe* https://ec.europa.eu/commission/future-europe/white-paper-future-europe_en