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**Fiscal Effects from Privatization:  
Case of Bulgaria and Poland**

**Edited by Julian Pańków**

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## Introduction

This study constitutes part of the "Support for Economic Reforms in Bulgaria" project conducted by the Center for Economic and Social Research (CASE Research Foundation), Warsaw and financed by the Open Society Institute, Budapest. The aim of the project is to assist co-operation with Bulgarian counterparts in implementing structural reforms in the Bulgarian economy. At the request of the Bulgarian authorities, this assistance involves developing and carrying out reform programs, as well as evaluating their results in priority areas of structural and institutional reform, with particular reference to the process of ownership transformation. This includes providing an overall strategy for privatization and reporting its effects, monitoring the process of enterprise privatization, post-privatization contract enforcement and the restructuring of newly privatized companies.

The purpose of this study is to:

- describe and evaluate the fiscal dimension of the privatization process in Bulgaria and Poland,
- conduct a cross-country comparison of the fiscal effects of privatization in Bulgaria and Poland, examining their respective approaches to the same,
- identify the crucial factors in the privatization strategy and policies of both countries that affect their privatization revenues,
- provide background information for the possible transfer of know-how concerning the best approach to maximizing the fiscal effects of privatization, by examining those positive and negative aspects of Poland's experience that could prove relevant to Bulgaria's economic environment.

This study includes an evaluation of the fiscal effects of privatization in both countries in the period since the very beginning of the process, i.e. in the case of Poland since 1990 and in the case of Bulgaria since 1993. The cross-

country comparison of the fiscal dimension of privatization has been contingent on the privatization models, priorities and methods applied in both countries.

The research on the fiscal effects of privatization was undertaken by the CASE Research Foundation and the Institute for Market Economy, Sofia, at the request of the Economic Policy Committee of the Bulgarian Parliament. The independent assessment of the fiscal results of privatization the Committee expects to receive will form part of an overall evaluation of the ownership transformation process in the Bulgarian economy and the effectiveness of that process.

This study is to be a follow-up to the previous CASE and IME research and consultancy activities in the area of privatization, both with regard to the Bulgarian and Polish cases and comparative studies.

The general analytical framework for these comparative studies is provided by the report from the international research project entitled "*Privatization in post-Communist countries*", that was carried out under the auspices of the CASE Research Foundation [1].

The changing priorities of the Bulgarian government's privatization strategies, reflected in the varying pace of the country's privatization process to 1998 was analyzed in the report *The Role of the Core Executive in the Privatization Process* [2]. The current study is to verify and update conjunctions between declared priorities, applied strategies and the fiscal effect of privatization.

The description of the various fiscal aspects of privatization will attempt to provide answers to the following questions:

1. To what extent have budgetary revenues been a priority of the privatization programs and strategies in Bulgaria and Poland?
2. What were dynamics of the revenues obtained from privatization in the two countries?

[1] Blaszczyk, Barbara, Richard Woodward, (1996), *Privatization in Post-Communist Countries: Experience, Problems, and Conclusions*, in: Barbara Blaszczyk, Richard Woodward (Eds.) *Privatization in Post-Communist Countries*, Warsaw, CASE, Volume I.

[2] Stanchev, Krassen, Luisa Perrotti (1999), *The Role of the Core Executive in the Privatization Process*, Country Report: Bulgaria, OECD/SIGMA - World Bank Project (Draft), Sofia.

3. What role did specific privatization methods and techniques play in providing revenues?

4. What was the level of concentration of these revenues in the two countries i.e. the share of the proceeds generated by privatization of major providers in total revenues from privatization?

5. What was the role of foreign investments in providing revenues from privatization?

6. What was the share of revenues from privatization in total budgetary income and GDP in the two countries?

7. What form do allocation procedures take?

The evaluation of the fiscal effects of privatization in Bulgaria and Poland has been undertaken in order to:

1. Outline basic privatization procedures and identify links with other fiscal issues,

2. Identify similarities and differences in approaches to the privatization issue,

3. Identify comparable privatization methods and strategies,

4. Assess the "effectiveness" of these comparable methods in providing revenues from privatization,

5. Identify the most commercial privatization schemes and to assess the share of such schemes in generating revenues,

6. Analyze limitations and the chances for increasing revenues from privatization, depending upon methods applied.

There are two factors to justify the work undertaken for this report: the final stage of the privatization process in Bulgaria and in Poland, which provides the ground for general evaluation, and diverse experience of both countries, in terms of applied approaches to privatization and their fiscal dimensions, which gives the basis for comparison and transfer of know how. We hope that the findings and conclusions will contribute in both countries to the public debate on the progress and results of privatization process as a part of structural transformation.



## Summary

Comparison of fiscal dimension of privatization process in Bulgaria and in Poland reveals both similarities and differences.

On the contrary to Poland, where privatization proceeds have been one of the highest priorities of the privatization strategy, fiscal objectives have rarely been referred to as a priority in the modeling and execution of Bulgaria's privatization policy. During the transition period privatization served in Bulgaria two important functions that directly affected fiscal affairs: a) cash inflow into the central budget and various non-budgetary accounts and b) reduction of the national debt through the use of government bonds as legal tender in privatization transactions. Since the very beginning of Bulgaria's privatization process, both these functions have been subject to strict regulation.

The major fiscal objective of Bulgarian privatization has gradually changed from support of different off-budget funds, i.e. different types of public spending, to official debt reduction. The Bulgarian government's intention to use privatization to relieve the national debt burden is strengthened by the possibility of using a variety of government bonds as payment instruments in privatization transactions. The main aim of privatization is currently the reduction of foreign debt. This should apply to the entire cash flow into the central budget, since no Brady bonds have been used as payment instruments in privatization since 1997. Since an early-1999 amendment to the Privatization Act, 90% of the cash revenues from privatization has flowed directly into the central budget (and not to 7 non-budgetary accounts).

The Polish government has adopted a "multi-track" approach to privatization, using various methods which it has been hoped will support the achievement of different objectives. Capital (or indirect) privatization is aimed at providing the greatest revenues to the budget. In analyzing the fiscal dimensions of Poland's privatization strategy for the 1990s, one cannot overestimate the importance of the privatization of the banking sector. This program of privatizing state-owned banks was adopted at the beginning of 1991.

Together with the evolution of a general privatization approaches, the allocation procedures for the revenues

obtained in both countries has been subject to subsequent changes.

Under the Polish Privatization Law of July 13, 1990, parliament passes an annual resolution setting out a privatization agenda (referred as "Directions of Privatization") for the Government to follow. Due to increasing importance of revenues from privatization for the state budget, beginning in 1993 these "Directions" were included as an appendix to the Budget Law. From 1990 to 1997, the revenues from privatization were included in the central budget and covered current budgetary needs. Since 1997 incomes from privatization began to be separated from the central budget. This was the result of the consensus that revenues from privatization should not be consumed by current budgetary needs, but should be earmarked to cover the cost of social programs and State Treasury obligations towards Polish citizens.

The Polish "Privatization Program up to 2001", adopted by the Government in 1998, for the first time ever stipulated in a detailed manner the assignment of financial revenues obtained from the privatization process. Of the social programs that are to be financed by revenues obtained from privatization, the pension system reform is the most expensive one. The second program intended to be financed through privatization incomes was the compensation program for 2.95 million employees working in the non-productive State sector at the beginning of the 1990s and 1.3 million pensioners. The restitution program is also to be covered by privatization revenues.

According to the 1999 and 2000 Budget Acts in Bulgaria, allocation of excess revenues is at the discretion of the Council of Ministers. The latter will decide on revenues allocation 'taking into account the execution of privatization programs and the financial restructuring of the real and banking sectors according to the conditions of the three-year agreement with the IMF'.

In early 1993, at the beginning of the privatization process in Bulgaria, the total volume of state-owned long-term assets was estimated to be BGN 580 million (USD 345 million). The total volume of state-owned assets subject to privatization is BGN 383 million (USD 228 million) or 66%

of the total assets under state ownership/control. Prior to 2000, enterprises in infrastructure sectors (energy, transportation, water supply and sewerage systems) were excluded from the scope of privatization. It is estimated that about 30% of long-term tangible assets are held by infrastructure companies that for the time being are not subject to privatization or would prove difficult to privatize. According to the Program for the Privatization of State-owned Companies in 2000, some of these infrastructure enterprises are scheduled for privatization.

The Polish Ministry of Ownership Transformation conducted the first official assessment of the value of State property in 1995. As of 31st December 1994, the book value of the stocks and shares of State Owned Enterprises, State financial institutions, commercialized State Enterprises and companies with partial State Treasury participation was estimated at 75 billion PLN or 30.8 billion USD. The estimated value of the State's productive sector as of 31st December 1997 was twice as much and amounted 150 billion PLN or 42.9 billion USD.

The privatization process in Bulgaria and in Poland has been uneven in terms of both contracted payments and cash revenues.

For the period 1993–1999, the total volume of cash proceeds from privatization in Bulgaria amounts to approximately USD 1 billion. Privatization revenues have registered a continual increase since 1993 along with an increase in the number of transactions and volume of assets privatized. Privatization proceeds were only 0.1% of GDP in the first year of the process, but reached 3.21% in 1997. Privatization's contribution to consolidated budget revenues became relatively significant after 1995, when it reached 1.2% of budget revenues. The contribution was highest in 1997 – 9.9%.

Privatization revenues for the period 1991–1999 in Poland amounted to 11.878 million USD. The most important from the budgetary point of view are revenues from indirect privatization and this share is increasing almost every year. In 1999, the total share of indirect privatization, enterprises plus banks, in total revenues reached 97%. Revenues from indirect privatization are also characterized by the most regular real annual growth rate. Both, the share of privatization revenues in total budget revenues and their share in GDP rises each year. The highest ratio of privatization revenues in Poland was in 1999 and amounted 9.58%.

The payments contracted by the central privatization bodies in Bulgaria have significantly exceeded cash proceeds. On average, cash proceeds were 41% of contractual payments. Since 1998, the annual programs of the privatization have included projected contractual payments. The actual payments contracted significantly exceeded the plan.

Also in Poland for the last 6 years, the government has regularly underestimated privatization revenues in any given fiscal year. The regular underestimation of revenues may

suggest that privatization was being treated as a hidden source of budget reserves.

The total share of obligations in privatization revenues in Poland is decreasing. This may be most easily observed in the case of indirect privatization, which drives the total revenues. In the case of direct privatization a prevailing number of the privatized companies have been leased to insiders, what results in deferred payments, similarly to the Bulgarian MEBO buy-outs.

Concentration on revenues by source has been in both countries significant, since almost 44% of the cash proceeds from privatization in Bulgaria have so far come from the top five transactions. Very high is also the level of concentration of privatization revenues in terms of the major revenue providers in Poland. The share of the largest privatization contracts in total privatization revenues tends to increase, especially over the last three years, i.e. 1997–1999.

The greatest number of large privatization transactions in Poland has been performed in the banking sector (6), followed by the tobacco industry (4) and the cement and pharmaceutical industries (3).

The contractual revenues from transactions with foreign investors amounted in Bulgaria to approximately USD 825 million, i.e. 36% of the payments contracted by all central privatization bodies. The volume of foreign direct investments through privatization (including direct payments and liabilities of privatized companies undertaken) was USD 1.14 billion for the period 1993–1999, i.e. 42% of the total FDI volume for the period.

The share of foreign investors in total privatization revenues in Poland has been declining: from 78.7% in 1991 up to 23.3% and 12.5% in 1997 and 1998 respectively. The ratio of revenues from transactions concluded with foreign investors to total foreign direct investments for the last three years did not exceed 10%, and in 1998 declined even below 5% of FDI volume.

The privatizing agents in Bulgaria contracted the payments using several types of payment instruments, including cash, government securities, vouchers and compensatory bonds (issued against restitution claims). The main feature of all the regulations introduced to deal with the legal, institutional and procedural aspects of the debt-equity swap mechanism in Bulgaria was debt annulment by converting government debt in state assets. The total volume of government bonds actually used as legal tender in privatization amounts to approximately USD 413 million, i.e. about 29% of actual payments (including cash and debt instruments). Almost 2/3 of the total volume of government bonds used in privatization payments has been domestic debt bonds.

The role of payment instruments other than cash would not seem to be an important factor in privatization revenues in Poland. Only at the very beginning of the privatization process, some direct privatization payments were carried out by Polish state treasury bonds.

Direct costs of privatization in both countries are relatively small and constitute a decreasing fraction of privatization revenues. The costs of privatization in Bulgaria were on average 3.7% of the total cash revenues from privatization. The greatest costs have been connected

with the implementation of the process, when the cost of the capital privatization in Poland amounted to 21% of privatization revenues, following which the cost began to fall to the level of about 2% in 1998 and 1% in 1999.

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## Part I

# Strategies and Fiscal Objectives of Privatization in Poland and Bulgaria

Privatization considered as a transfer of ownership of state owned assets to the private actors may have various economic, social and political objectives [Bornstein, 1992]. As a rule, the goal of privatization is to maximize some combination of these objectives. The combinations resulting in privatization strategy mix vary among the separate countries and could be subject to changes in each of them.

### I.1. The Case of Bulgaria

An analysis of the fiscal aspects of Bulgaria's privatization process is somewhat hampered by the changes that have occurred in the country's priorities and revenue allocation schemes over the last few years. In this period, the government amended its rhetoric and policy-vision vis a vis privatization. However, the overall organization of the institutions governing the process has never been seriously challenged, though it has undergone substantial reform and rationalization in accordance with amendments to the privatization model. The creation of new institutions and the work of existing ones have supported these new approaches.

The first major characteristic of the Bulgarian privatization process concerned its so-called *voucher privatization*. Naturally, this model had very limited fiscal effect. However, its purpose was not mass privatization. This necessitated maintaining conventional privatization as a source of budget revenue. At some point, however, this approach began to contradict the idea of auctioning vouchers for enterprises in relatively good condition. This concept had been put forward since 1990, but it wasn't until 1994 that it took shape under the cabinet of Mr. Berov. Subsequent cabinets have substantially remodeled this originally very liberal project,

which first and foremost aimed at reducing government responsibility for the process. It was applied on two occasions: the first time in 1995–1996, under a socialist government and the second time, although in an entirely revised form, under the current government, that took office in April 1997. However, the impact of voucher privatization on the disposal of State-owned assets has been relatively limited.

Preparation of the first scheme began in 1995 but was only conducted between the end of 1996 and the beginning of 1997: notably, when the socialist government then in power, already facing a crisis, was also under considerable pressure from international financial institutions. The process resulted in 85 million shares being offered to the public, over 80% of which were sold.

The second wave of mass privatization began in February 1999. To reflect the government's policy shift, the decision to resort to this method of privatization was based more on the need to accelerate the overall process than, as in the previous case, an attempt to pursue objectives of 'social fairness'.

As mentioned earlier, the second wave of mass privatization was conceived in a radically amended form. Firstly, privatization funds were excluded from the process [3] – although there are several different ways of investing the vouchers (for instance, in pension funds). Secondly, the price at which shares are acquired is not fixed but weighted against the average of all bids. A broad range of payment instruments (including cash) is allowed, vouchers may not be traded and entirely new negotiable instruments ('compensatory bonds') may be issued against claims on formerly nationalized properties, to complement the 'restitution' side of the privatization program. Furthermore, unlike the situation in 1996, there is currently no fixed list of State-owned enterprises to be privatized by this method. Instead, the

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[3] In order to participate in this wave of mass privatization, in fact, the earlier funds are required to register as investment intermediaries with the Securities and Exchange Commission.

policy provides for minority stakes (up to 5–10%) of all state-owned enterprises to be offered to the general public at centralized bidding sessions.

It is not clear how such a limited percentage of shares could actually accelerate the privatization process and thus improve overall economic and fiscal performance. Moreover, only 'unattractive' companies are likely to be included in the scheme. It is certainly too early to evaluate the effects of this second wave of mass privatization. Indeed, the government's changing vision has not facilitated the process but, compared to the first wave of mass privatization, has seriously affected economic performance.

*Management-employee buy-outs (MEBO)* have been the second major component of Bulgaria's privatization approach. The country's privatization law has introduced a special regime for management-employee buy-outs (MEBO) and cash privatization transactions. In general, MEBOs are not a typical phenomenon of any given set of governments, in particular, socialist-led governments. Under the current reform-minded government, recourse to this preferential system has been justified by the need to accelerate the disposal of State's assets [4]. However, the institutional impact has been that such transactions have in fact distributed the rights to re-sell formerly government-owned assets to managers that were appointed by the government itself [5].

It is generally considered that MEBOs fail to maximize fiscal revenues, tend to result in poor corporate management and embody politically acceptable methods of liquidating public enterprises. Indeed, MEBOs are often the solution applied when the firms involved have already accumulated losses that decrease the value of their net assets and therefore, lower the sale price and the revenues that can be expected. Furthermore, the increasing number of MEBOs tends to magnify some of the most powerful constraints on the Bulgarian privatization process: for instance the built-in collateral legislation concerning procedures for hiring and firing the management staff of State-owned enterprises, as well as that concerning the appointment of Board members. Such legislation ultimately enables the management of State-owned enterprises in various ways to obstruct or privatization or make it conditional on other issues. In June

2000, Bulgaria's Prime Minister publicly admitted for the first time that obvious conflicts of interest exist in such privatization methods. The fall in the number of MEBO transactions in 1999 to 43.5% of all privatization transactions is evidence of an awareness that these companies are likely to perform badly in terms of efficiency and competitiveness. Eventually, a market-driven economic system will take shape albeit gradually, once resale through MEBO mediation is discontinued.

The third major feature, a relatively recent innovation, has been the policy of involving so-called 'privatization intermediaries'. This selection of 'privatization intermediaries' from among internationally reputed consulting firms, to perform as 'agents' of the government in the preparation of large-scale privatization transactions constitutes an important and controversial development of the current government's policy. The government decided that the presence of such intermediaries would increase the level of foreign investment, improve privatization results and increase the transparency of sales. Between 1997 and 1999, 170 enterprises were handled by such intermediaries. The 1999 Annual Report on Privatization [6] claims that 'by the end of the year, the privatization process had gained considerable momentum thanks to the privatization transactions handled by consultants and intermediaries that began to predominate by the end of the first six months, due to the approaching contract deadlines imposed under the regulations for the financial sanitation of state-owned enterprises' [7]. However, the report provides little evidence or information that could substantiate an independent judgement.

Doubts have been cast on the procedure for selecting such intermediaries. Furthermore, the contracts binding privatization intermediaries raise doubts about the real intentions behind this policy. Particularly relevant is the fact that, with few notable exceptions, privatization intermediaries do not operate on the basis of a 'success fee'. Rather, their remuneration is in most cases fixed or mixed (partly fixed and partly success fees).

Thus, although intermediaries are constrained by deadlines for the submission of bids for the privatization transactions they are handling, they have no interest in speeding up the process if this results in any reduction of

[4] Privatization Agency, Privatization Strategy and Program, no date (1999), p. 1.

[5] According to the Bulgarian Law (Council of Ministers Decree 7/1994) line ministers are principle of state-owned enterprises; they appoint managers under no competition between management teams, there are no performance guidelines and no venture capital elements of the management itself. The tradition has been that every new cabinet appoint new managers thus benefiting its party affiliates, paying back for loyalty and past political services.

[6] This report (the full title: A report on the Result of the Program to privatize State-owned Enterprises in 1999), was compiled by the Privatization Agency and accepted by the Council of Ministers on March 28, 2000 (Decision 150/2000) is not yet publicly available, and, by the time of compilation of this draft, is still pending hearings in the Parliament.

[7] Report on the Result of the Program to Privatize State-owned Enterprises in 1999, p. 17.

their own returns [8]. On the other hand, the intermediaries that we consulted expressed concern that they were being treated as 'scapegoats' by the relevant decision-making authorities. In fact, intermediaries are charged with preparing the sale of enterprises grouped into industrial 'pools' listed by sector (i.e. metallurgy, tourism, chemicals, etc.). However, they have no authority to 'sign' agreements. These must be submitted for approval to the privatization agency and in the case of the country's 'blue chips', to the Council of Ministers.

None of the above mentioned three components constituted the major source of revenues from privatization. The major source were the negotiations and tenders and to a lesser extent the auctions and the public offers on the Stock Exchange.

The Privatization Act of May 8th 1992 outlines the possible ways of privatizing state-owned and municipal companies. There are six possible procedures for selling majority stakes in whole companies:

- Auction.
- Competitive tender.
- Direct negotiations with potential buyers.
- Public offer of stocks on the Stock Exchange.
- Centralized voucher auctions.
- Sale to insiders without tender or auction (in accordance with Article 35 of the Privatization Act).

This Act gives preference to participation by insiders, as this allows for deferred payment (up to 10 years) when the selected buyer is a management-employee company. Moreover, this allows managers and employees to buy up at preferential terms up to 20% of the shares of the company in which they are employed.

In the years under consideration, the total number of transactions increased progressively, a development that reflects the increasing commitment of the government to privatization. It is however important to point out that in spite of the above mentioned features, the privatization process has been uneven in terms of both contracted payments and cash revenues. The slowdown in the mid-1990s for example, requires a twofold explanation: on the one hand, this corresponds to a change in the administration, following the general elections of December 1994. On the other hand, whilst few cash-based privatization transactions were concluded in that year, 1995 marked the preparation of the first mass privatization program, which constituted an important turning point in policy, as described earlier.

Together with the evolution of a general privatization approach, the allocation procedure for the revenues

obtained has been subject to subsequent changes. According to the 1999 and 2000 Budget Acts, allocation of excess revenues is at the discretion of the Council of Ministers. The latter will decide on revenues allocation 'taking into account the execution of privatization programs and the financial restructuring of the real and banking sectors according to the conditions of the three-year agreement with the IMF' [9].

Finally, it is important to point out that until the end of 1996, virtually all the larger state-owned enterprises were considered 'strategic' and therefore not subject to privatization. At present, the long-postponed privatization of such firms is a high priority on the government's agenda. However, it is difficult to foresee the overall outcome of these privatization transactions. This is because some of the largest enterprises in this group (in terms of capital and manpower) are on the brink of bankruptcy and likely to be privatized at 'nominal prices', whilst others are more profitable and expected to provide the budget considerable revenue.

Fiscal objectives have rarely been referred to as a priority in the modeling and execution of Bulgaria's privatization policy. Privatization was and still is perceived as a process of politically determined property transfer that should entail the lowest possible social costs. Although this is not explicitly emphasized in the government's programs, the ultimate aim of privatization is a restructuring of former state-owned companies rather than record-breaking fiscal surpluses or a reduction of the national debt.

However, during the transition period privatization served two important functions that directly affected fiscal affairs: a) cash inflow into the central budget and various non-budgetary accounts and b) reduction of the national debt through the use of government bonds as legal tender in privatization transactions. Since the very beginning of Bulgaria's privatization process, both these functions have been subject to strict regulation and thus fiscal objectives have been an attributing, though not determining factor of Bulgarian privatization.

Although the allocation procedure lost some of its clarity following the 1999 amendment, public officials from the Ministry of Finance emphasize that (from the fiscal point of view) the main aim of privatization is currently the reduction of foreign debt. This should apply to the entire cash flow into the central budget, since no Brady bonds have been used as payment instruments in privatization since 1997. Interestingly, in planning the fiscal year Ministry of Finance the uses two methods for planning revenues from privatization:

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[8] For instance, the Privatization Agency expected to see finalized by 1999 'most part' of the first 30 companies offered for sale through privatization intermediaries in 1997 and 1998, whilst only six transactions had been concluded between 1998 and early 1999 (Privatization strategy and Program, p. 3), while the recent report (March 2000) does not disclose any specific information on this matter.

[9] However, none of the institutions we asked to share their vision (including the head of the IMF mission to Sofia) on allocation of provisional 2000 exceeding revenues could provide reliable information.

– According to the first approach, the Ministry of Finance arrives at its own estimate of how much is needed for the current covering of foreign debt and this is duly sent to the Privatization Agency.

– The second approach begins with the Privatization Agency, which presents a program (for which it has three methods of preparation) before Parliament. Since 1996, these programs include the volume of expected contractual payments and the expected cash inflow from privatization into the consolidated budget. Following its approval, the program is submitted to the Ministry of Finance.

However, it is not clear whether the Privatization Agency considers the estimate sent by the Ministry of Finance before presenting its own program to the Parliament.

The government's intention to use privatization to relieve the national debt burden is strengthened by the possibility of using a variety of government bonds as payment instruments in privatization transactions. These include two types of Brady bonds, as well as 5 types of long-term domestic debt bonds (all of which are described in detail below). The ratio of cash payments to debt instruments, to which privatization agents must adhere when negotiating payments, is announced annually in the privatization programs [10]. This ratio was 50:50 in 1996, since when it has been 30:70.

Thus, the major fiscal objective of privatization has gradually changed from support of different off-budget funds, i.e. different types of public spending, to official debt reduction. The most important events influencing this change were the following:

– In 1997, the *ratio of debt instruments to cash payments*, to which privatization agents must adhere when negotiating payments, was raised from 50:50 to 70:30.

– Since 1997, every year a certain group of companies must be privatized only against cash payments; 96% of these proceeds is used for official debt reduction.

– Since an early-1999 amendment to the Privatization Act, 90% of the cash revenues from privatization has flowed directly into the central budget (and not to 7 non-budgetary accounts).

## 1.2. The Case of Poland

The principal goal underlying Poland's privatization strategy, as declared at the very beginning of the process, was to improve resource allocation [Lewandowski, 1994]. Other objectives of privatization were to:

– distribute property rights among the Polish population,  
– develop a Stock Exchange and capital markets through initial public offers,

– improve the performance of enterprises by means of restructuring, leading to a more efficient use of equity, labor and management skills,

– reduce the size of the public sector and the burden on the public budget and administration,

– generate revenues for the state and municipal budgets [Lewandowski, 1994; Pater, 1995].

The Polish government has adopted a "multi-track" approach to privatization, using various methods which it has been hoped will support the achievement of different objectives. The Act of July 13th, 1990 on the Privatization of State Enterprises constituted a compromise between a number of different concepts [Błaszczuk and Woodward, 1997].

The first method, called capital (or indirect) privatization, which is aimed at providing the greatest revenues to the budget, is used for the privatization of larger state-owned enterprises. Capital privatization consists of two stages. In the first of these, the enterprise is 'commercialized' or incorporated (that is, transformed into a joint-stock or limited liability company). For the time being, all the company's shares remain the property of the State Treasury. In the second step, shares in the newly established companies are made available to private investors through public offers, tenders or negotiations following a public invitation.

The second method, referred to as liquidation (or direct) privatization, is applied to small and medium-sized companies in relatively good financial standing. Privatization by liquidation involves transfer of the enterprise's assets to private investors. According to the law, there are three main options for privatization of the whole or part of the company under this method: (1) sale of assets; (2) in-kind contribution of the assets to the newly created company; and (3) leasing of assets to either the company created by the management and employees of the liquidated SOE or to a third party (private individuals only).

According to the Privatization Law of July 13th, 1990, in those cases where commercial methods were used (referred to in Poland as capital, or indirect, privatization) employees had the right to acquire up to 20% of their company's shares at a preferential price (50% of the issue price). In cases of liquidation, or direct privatization in which the leasing method was used, employees had priority over all other bidders.

In August 1996, a new privatization law was adopted [Błaszczuk and Woodward, 1997]. The new law grants employees a more privileged position with respect to the acquisition of shares in companies undergoing privatization

[10] Adopted with Decisions of the National Assembly.

through an indirect method. Employees may acquire up to 15% of the shares in their companies free of charge. A further 15% is available free of charge to any farmers or fishermen that supply a given company on a permanent basis. Former employees on retirement or disability pensions also have the right to obtain shares from this pool. The shares acquired free of charge may not be sold for two years following acquisition and for three years in the case of managerial employees. The law also gives the government the right to extend these periods.

As for so-called direct privatization, the new law allows 'outsiders' to put forward privatization initiatives without the need to seek the approval of 'insiders'; however, it also reduces the number of enterprises eligible for this type of privatization by introducing very low ceilings on the size of enterprises considered eligible [11]. Additionally, while the employees of the enterprises privatized according to this method do not receive a complimentary 15% of the shares, as in the case of capital privatization, under the new law they may receive the equivalent thereof paid to their accounts in the company's social fund.

Over the entire course of privatization in Poland, the procedure for liquidation under the State Enterprise Law of 25 September, 1981 has also been used. This procedure is aimed at meeting the claims of creditors of liquidated SOEs with poor financial standing and thus its fiscal effect is only marginal.

Other privatization schemes have subsequently been added and two of these are important, although not with regard to their direct fiscal effects: (1) the Polish model of mass privatization referred to as the National Investment Funds (NIF) Program and (2) various types of debtor-creditor arrangements under the Act of 3 February, 1993 on Financial Restructuring of Enterprises and Banks, allowing for conversion of debt into equity.

The Mass Privatization Program (MPP) was developed by the Ministry of Ownership Transformation in mid-1991. The Act on National Investment Funds (NIF), which is a modified MPP, was finally adopted in April 1993. This law provides the legal basis for the Polish Government to establish National Investment Funds, to contribute to those funds the shares of the former SOEs transformed into joint stock companies, to appoint professional management for the funds and to distribute to the Polish public share certificates, allowing them to acquire a portion of national assets represented by their NIF shares for a price of 20 PLN (in late-1995, slightly over 7USD). It was intended that the NIF pro-

gram would accelerate the pace of privatization. Commenced in early 1995, the NIF Program has finally reached its implementation stage. 512 enterprises were selected for the program, in which 15 NIFs were to participate. The distribution of share certificates began in November 1995 and was completed in November 1996. According to official data, these were distributed to 25.889 million persons, constituting the vast majority of those entitled to receive the share certificates. Of all the share certificates distributed, as many as 98.68% have been cashed or exchanged for NIF shares. By the end of the distribution period, the original registration fee was seven to eight times lower than the market value of the share certificate [12].

In analyzing the fiscal dimensions of Poland's privatization strategy for the 1990s, one cannot overestimate the importance of the privatization of the banking sector. This program of privatizing state-owned banks, separated in 1989 from the National Bank of Poland (NBP), was adopted at the beginning of 1991 [Borowiec, 1996]. According to the program, two to three commercial banks were to be privatized each year starting in 1993, through the following share distributions:

- 30% - to domestic investors,
- up to 20% - to the employees of the banks under privatization, under preferential terms,
- 20 to 30% - to foreign investors,
- 30% will remain in the hands of the State Treasury, including 5% for restitution claims.

The legal framework for the program's implementation was introduced in April 1992 as an amendment to the Banking Law.

Under the Polish Privatization Law of July 13, 1990, Parliament passes an annual resolution setting out a privatization agenda (referred as "Directions of Privatization") for the Government to follow. Due to increasing importance of revenues from privatization for the state budget, beginning in 1993 these "Directions" were included as an appendix to the Budget Law.

From 1990 to 1997, the revenues from privatization were included in the central budget and covered current budgetary needs [13]. Since that time, funds obtained from privatization began to be informally partly separated from the central budget. This was the result of an "unwritten" agreement reached by the Poland's main political forces in the mid 1990s. The largest political parties agreed to the consensus that revenues from privatization [14] should not be consumed by current budgetary needs, but should be

[11] Under the new law only enterprises employing up to 500 persons the annual sales of up to ECU 6 million and own funds of up to ECU 2 million may be privatized using the direct privatization methods.

[12] Informacja o Programie Narodowych Funduszy Inwestycyjnych (Information on National Investments Program), Ministerstwo Skarbu Państwa, Październik 1999.

[13] See section on revenues in Poland.

[14] Especially from the big privatization programs such as privatization of the telecommunication or oil and energy and banking sectors.



earmarked to cover the cost of social programs and State Treasury obligations towards Polish citizens. Politicians realized that without that source of financing, the central budget would not be able to cover the long-term cost of the social programs agreed upon by the political parties (pension reform and restitution and compensation programs). On the other hand, there was no agreement between the parties on how the programs should be designed and to what extent funds obtained from privatization should support particular programs. For example, left-wing parties focused more on compensation programs, almost entirely rejecting the restitution program. This was just the opposite of the right wing parties' political preferences.

In effect, the consensus became the basis for and clearly determined the strategic goals of Poland's privatization for the years to follow.

Before that time, the strategic goals for the privatization process have yet to be clearly formulated. This was due to the fact that expectations connected with privatization were enormous. At the beginning of the transformation of Poland's economy, it was presumed that the privatization process would increase the effectiveness and competitiveness of privatized companies, assist in the formation of a capital market, cover the budgetary deficit, help in repayment of the foreign debt and lastly, meet social expectations through distribution of the shares of the privatized companies among Polish citizens and the employees of the privatized companies. This meant the lack of any coherent privatization strategy, since some of these goals were plainly contradictory and this had an adverse effect on the speed, quality and scope of the privatization process in Poland [15].

At present, one may assume that the main political forces in Poland are agreed that the main goal of privatization in Poland is the maximization of revenues. In fact, the newly formulated privatization strategy in Poland has allowed privatization of sectors that, since the beginning of

transformation, were practically excluded from the process by the politicians (e.g. the coal mining, energy, oil, chemical and transportation sectors).

The "Privatization Program up to 2001", drawn up by the Ministry of the Treasury, for the first time ever stipulated in such a detailed manner the assignment of financial sources obtained from the privatization process. According to this program, the financial resources needed to cover the cost of the social and compensation programs to 2001 were estimated at 75 billion PLN. It was planned for all these funds to be obtained from the privatization process. Table 1-1 presents the assessment of the costs of the particular social and compensation programs included in "Privatization Program up to 2001".

Of the social programs that were to be financed by funds obtained from privatization, presented in the "Privatization Program to 2001" and that are now in the process of completion, the pension reform was at that time the most expensive [17]. The main goals of Poland's pension reform were a rationalization of the current pay-as-you go system and a partial replacement with funded elements. The crisis in the Polish social security system became obvious to all in the 1990's. The difficulty that arose in assuring the financial sustainability of the system was due to the simultaneous occurrence of:

- a sudden increase in the number of new pensioners in the beginning of the 1990's,
- a decrease in the number of contributors as a result of declining employment,
- a marked growth in the real value of pensions compared to real compensations, due to an indexation mechanism favoring pensioners and a broadening of the privileges for special groups of workers.

As the result, the whole system became dependent on state budget subsidies, which rose to over 6% of GDP in 1992–1994. The prognosis for the public costs of retire-

Table 1-1. Assessment of the costs of the social and compensation programs to be financed by privatization revenues

No.	Program	Cost in PLN billions	Cost in USD [16] billions
1.	Financial support for pension reform to 2005 - to 2001	54.0 20.3	15.35 5.77
2.	Compensation program for non-productive State sector employees and pensioners	20.0	5.69
3.	Restitution (re-privatization) program	17.0	4.83
4.	Non-equivalent privatization	8.0	2.27
5.	Incomes aimed at budgetary needs in 1998	6.8	1.93
6.	Other programs (e.g.- restitution of trade union property confiscated by the communist regime in 1981)	3.1	0.88

Source: "Privatization Program to 2001", Ministry of the Treasury, 1998

[15] B. Błaszczak "Prywatyzacja w Polsce po sześciu latach – osiągnięcia, opóźnienia i pożądane kierunki", Raport CASE nr 9, CASE, 1997.

[16] The average exchange rate of the National Bank of Poland as of 31st December 1997 – 3,5180 PLN/USD.

[17] On the other hand, among the social programs, the pension reform seems to be the most needed and the most challenging one.

ment and disability benefits clearly showed that within the framework of the "old" pension system, these expenses would increase to 22% of GDP by the year 2035 [18]. As a result, the introduction of a funded system was the only solution for overburdened public finances, an aging society and the need for lifelong incomes.

The reform was implemented on January 1, 1999. According to the program, the cost of pension reform to 2001 was estimated at 20,3 billion PLN and to 2005 at 54 billion PLN.

The second program intended to be financed through privatization incomes was the **compensation program** for 2.95 million employees working in the non-productive State sector at the beginning of the 1990s and 1.3 million pensioners. This was a result of the verdict handed down by the Constitutional Court. In accordance with the agreement between the Government and the trade unions [19], in 1991 and 1992 the salaries of state-owned non-productive sector employees, the financial privileges for special working groups (e.g. soldiers) and pensions were not indexed. This was due to the economic situation (especially fiscal position) in Poland being catastrophic at the time. Finally, the trade unions put and their case to the Constitutional Court and won. In June 1998, the Ministry of the Treasury estimated the cost of the program at 19 billion PLN. The program was begun in March 2000 and will be completed by 2004. Initially, it was intended for payments to be made in the form of compensation certificates but in the end, the Government decided that payments would be made in cash [20].

The "Privatization Program up to 2001" also reserved funds for the **restitution program**. This program is also to

be covered by privatization revenues. The government decided to reserve 17 billion PLN to the year 2001 in order to meet restitution claims in the form of re-privatization certificates exchangeable for State shares or stocks in privatized companies or commercialized companies. The Government decided that the total sum of the fund set aside to meet indirect restitution claims would reach 40 billion PLN [21]. Parliament has still not decided the scope and form of the restitution program.

As a result of the above, the overall cost of the program is still unknown. However, it can safely be said that it could prove the most expensive program among all those financed by privatization revenues. The most serious disputes concern the scope of the program. There have been more than 170 thousand restitution claims. The total value of claims presented by former owners has been estimated at 198.4 billion PLN. According to the Ministry of the Treasury, the real value of all restitution claims amounted to 110–130 billion PLN. The Administration is forcing the scenario of a partial (50 percent) fulfillment of restitution claims submitted by former owners, which means that the cost of the restitution program would amount to 60–70 billion PLN. However, the unions and the associations of former owners do not wish to agree to this compromise solution. The position of the former owners is supported by European Law.

It is crucial that this issue be solved before entering the EU, in order to avoid a scenario where the central and the local budgets would be forced by European Law to meet the restitution claims in full (such a scenario would have an unimaginably catastrophic impact on public finances).

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[18] Piętka K., Petru R., "Reform of the Social Security System in Poland", Warsaw, July 1997, CASE.

[19] And what is more important voted by the Parliament.

[20] The program is serviced by the largest, State saving bank PKO BP.

[21] It concerns only the restitution claims, which wouldn't be able to meet through the return of the property taken away by the communist's regime.

## Part 2

### Evaluation of State-owned Assets

#### 2.1. The Case of Bulgaria

In early 1993, at the beginning of the privatization process in Bulgaria, the total volume of state-owned long-term assets was estimated to be BGN 580 million (USD 345 million) [22]. The total volume of state-owned assets subject to privatization is BGN 383 million (USD 228 million) or 66% of the total assets under state ownership/control.

Prior to 2000, enterprises in infrastructure sectors (energy, transportation, water supply and sewerage systems) were excluded from the scope of privatization. It is estimated that about 30% of long-term tangible assets are held by infrastructure companies that for the time being are not subject to privatization or would prove difficult to privatize, such as the National Electric Company, Bulgarian State Railways, forests, ports, etc. According to the Program for the Privatization of State-owned Companies in 2000, some of these infrastructure enterprises are scheduled for privatization [23].

There are basically two approaches to measuring privatization of state-owned assets in Bulgaria. The first one is the methodology applied by the World Bank, according to which a company or the assets of a given enterprise are considered privatized when 67% of its shares are transferred from public to private ownership [24]. The methodology of the Privatization Agency considers the company and its assets privatized when 51% of shares are in private hands.

Between 1992 and June 30, 1995, just 2.6% of total state-owned assets were transferred to private hands. By mid-1995, the total volume of state ownership in 3,510 enterprises, in terms of fixed assets, amounted to BGN 564 million. This accounts for up to 64% of the 1995 [25] GDP.

A significant acceleration in almost all forms of privatization can be observed in late-1996 and 1997. In 1996, the voucher privatization scheme was launched. Preparation for the first wave began in 1995, but was only completed between the end of 1996 and the beginning of 1997. According to the Government Program for Mass Privatization, stakes varying between 10 and 90% of shares in 1,050 state-owned enterprises were included in a list of companies to be privatized through the voucher system. 10% of every stake offered was to be transferred free to the company's workers and managers; the remaining 90% was to be offered to the public through centralized public auctions [26]. As a result of this process, some 85 million shares were offered to the public, of which over 80% were sold. However, the relative impact of mass privatization on the disposal of state-owned assets is considered to be limited. With regard to the relative effect of the first wave of mass privatization on the total value of long-term assets owned by the state, available sources provide somewhat contrasting figures: some indicate a relative impact of 7–9%, while others report a slightly higher percentage of 11–13%. In all cases, the official figures [27] on the total impact of

[22] The book value of the state-owned assets is as of 31 December 1995. Due to the galloping inflation in 1996–1997 and the brief hyperinflation period in early-1997, the figures were re-estimated in late-1997.

[23] For example, such infrastructure companies scheduled for privatization are: companies for production and distribution of electric power (hydro-electric power stations, thermo-electric power stations, regional companies for electric power distribution, etc.), coal-mining enterprises, detached manufacturing units of Bulgarian State Railways, etc.

[24] Following Bulgarian Trade Law, which proclaims that 67% are needed for full control over a company.

[25] At current prices.

[26] Three separate bidding sessions took place in late-1996 and early-1997.

[27] A report on the Result of the Program to privatize State-owned Enterprises in 1999.

**Table 2-1. The Privatization Agency's Figures for State-owned Long-term Assets at the beginning of 1999 (book value as of December 31, 1998) [28]**

	Majority stakes	Long-term assets (million BGN) as of 31.12.1995	% of the total volume of state-owned assets (BGN 580 million)
1. Cash privatization	163	55.218	9.54
2. Via intermediaries	126	103.886	17.9
2.1. Pools	73	15.167	2.6
2.2. SARA Pool	26	1.699	0.3
2.3. Consultants	27	87.020	15
3. For liquidation	19	3.263	0.6
<b>Total</b>	<b>308</b>	<b>162.367</b>	<b>28</b>

Source: Privatization Agency

**Table 2-2. The (%) share of state-owned assets privatized by years**

	1993	1994	1995	1996	1997	1998	1999	Total
Assets subject to privatization	0.56	2.47	1.62	6.19	27.81	6.80	25.79	71.24
Total state-owned assets	0.37	1.63	1.07	4.09	18.36	4.49	17.03	47.04

Source: Privatization Agency

mass privatization, including minority stakes, indicate 14.6% of the total volume of state's assets.

Indeed, 1999 saw the most significant progress in privatization since the beginning of the process. 1,225 transactions were completed, a record compared to previous years. The volume of de-nationalized assets in 1998 was about BGN 79.14 million, which is 13.63% of the total assets subject to privatization. 11.46% of them were sold by the Privatization Agency, 0.96% by Ministry of Trade and Tourism, 0.37% by the Ministry of Industry and 0.33% by the Ministry of Regional Development and Public Works.

The overall result of both cash and mass privatization in terms of long-term assets sold from the beginning of the process until the end of 1999 differs according to the two methods of measuring privatization of state-owned assets.

According to the estimates using World Bank methodology, the total volume of long-term tangible assets privatized over the period is BGN 184 million, i.e. 31.7% of the total volume of state-owned assets and 48% of the assets subject to privatization (BGN 383 m). These results are quite different from those of the Privatization Agency.

According to the Privatization Agency, the assets privatized to the end of 1999 amount to BGN 268 million, which is significantly higher than the World Bank estimate. If we accept these figures, the relative value of privatization against the total value of the long-term assets is 47%.

Respectively, the share of already privatized assets in the total assets subject to privatization is 71%.

## 2.2. The Case of Poland

The Ministry of Ownership Transformation conducted the first official assessment of the value of State property in 1995 (and at the same estimated the potential revenues to be obtained from privatization). As of 31st December 1994, the book value of the stocks and shares of State Owned Enterprises, State financial institutions, commercialized State Enterprises and companies with partial State Treasury [29] participation was estimated at 75 billion PLN or 30.8 billion USD (see Table 2-2). However, this estimate was not comprehensive as it covered only the productive sector [30]. It also did not take into consideration potential income from the sale of municipal property (this aspect is especially important when analyzing restitution claims).

Following the parliamentary election won by the Action for Solidarity Election (Akcja Wyborcza Solidarność) and the Union of Freedom (Unia Wolności) parties in September 1997, a much more comprehensive and detailed estimate of state-owned property was carried out by the Ministry of State Treasury. This study included not only the value of the

[28] Excluding 39 enterprises, which are difficult for privatization. Their long-term assets amount up to BGN 205 million, or to 35.43% of the total state-owned assets.

[29] In that case only the value of the stocks and shares in the hands of the State Treasury was taken into consideration.

[30] Productive sector includes also the financial sector.

Table 2-3. The book value of property owned by the State as of 31st December 1994

	Value in billion PLN	Value in billion USD [31]
State Owned Enterprises		
- equity	34.9	14.3
- 2/3 of profits	1.6	0.7
Commercialized State Enterprises		
- equity	21.3	8.7
- 2/3 of profits	2.3	0.9
Financial Institutions (11 banks and 3 insurance companies)		
- equity	9.6	3.9
- 2/3 of profit	0.7	0.3
Market value of stocks owned by the State Treasury and listed on the Warsaw Stock Exchange	1.8	0.7
Companies with partial State Treasury participation	1.3	0.5
25% of the value of the companies included in the MPP program	1.5	0.6
<b>TOTAL</b>	<b>75</b>	<b>30.8</b>

Source: "Directions for Privatization of State Property in 1995", Council of Ministers, Warsaw, 1996

State's productive sector but also assessed the value of the State sector's non-productive property (e.g. lands and forests, buildings and facilities of State administration and State organizational units and the property of higher education institutions). These estimates were included in the "Privatization Program up to 2001" prepared by the new Government. The Council of Ministers adopted the program on 14th July 1998. It should be emphasized that the program presented not only a schedule for the privatization activities of the new government and an assessment of the value of State property, but also allocated the revenues obtained from privatization. In fact, it was the first official government document to balance potential revenues from privati-

zation of State property with the potential cost of the social and compensation programs to be financed from the same.

According to the program, as of 31st December 1997, the value of State property (not including the value of natural resources and national cultural property) amounted to 604.3 billion PLN (almost 172 billion USD [32] – see Table 2-4). Comparing the value of the State's productive sector estimated by the Ministry of Ownership Transformation in 1995 with the figure estimated by the State Treasury in the Program, we may observe an enormous difference. The estimated value of the State's productive sector as of 31st December 1997 was twice as high as the estimate made in 1995 (respectively 150 [33] and 75 billion PLN). Analyzing the values of State proper-

Table 2-4. Value of State property as of 31st of December 1997

	Type of property	Value in billion PLN	Value in billion USD [34]
1	Lands and forests	117.8	33.5
2	River routes, canals and dams	287.2	81.6
3	Buildings and facilities of state administration and state organizational units	41.4	11.8
4	Stocks and shares of the State Treasury	81.7	23.2
5	Property of state agencies	19.3	5.5
6	Property of state-owned enterprises [35]	50.1	14.2
7	Property of higher education institutions	3.7	1.1
8	Other	3.1	0.9
9	<b>TOTAL (1-8)</b>	<b>604.3</b>	<b>171.8</b>

[31] The average exchange rate of the National Bank of Poland as of 31st December 1994 – 2,3173 PLN/USD.

[32] The average exchange rate of the National Bank of Poland as of 31st December 1997 – 3,5180 PLN/USD.

[33] Into a productive sector I included shares and stocks belonged to the State Treasury, the property of State Agencies, the property of State Owned Enterprises.

[34] The average exchange rate of the National Bank of Poland as of 31st December 1997 – 3,5180 PLN/USD.

[35] The value of the State Owned Enterprises (SOE) was estimated on the base of the net assets value of the SOE (assets minus liabilities).

ty as estimated in 1995 and 1998, the clear conclusion must be drawn that any comprehensive estimate of State property values should be treated with caution and a wide margin should be left for errors and omissions.

In its "Privatization Program up to 2001", the Ministry of the Treasury "reserved" the following components of State property to cover the cost of the compensation and restitution and social programs to be financed by privatization revenues:

- stocks and shares of the State Treasury – 81.7 billion PLN,
- property of state-owned enterprises – 50.0 billion PLN,
- property of the State Treasury that can be transferred within the restitution scheme – 31.2 billion PLN,
- municipal property that can be transferred within the restitution scheme – 69.7 billion PLN.

The total value of State property earmarked to cover the cost of the compensation and restitution and social programs was estimated by the Ministry of the Treasury in the "Privatization Program to 2001" at 232,6 billion PLN.

Many economists express the opinion that the forecasted value of State property presented in the "Privatization Program to 2001" was extremely optimistic. There are several arguments backing this view. Among these the most important are the following:

- According to the Central Statistics Office, many of the companies that are to be used as "collateral" for the restitu-

tion claims are permanent loss-making enterprises that will have to be sold at a price below their book value (some of these enterprises will even have a negative market value - e.g. companies that will be liquidated or enter bankruptcy procedures).

- In view of past and present experience in the field of ownership transformation as well as the quality of the State portfolio (the financial and competitive position of the companies to be privatized), one cannot be certain that these enterprises will be privatized even within the next ten years.

- Some enterprises considered by the "Privatization Program to 2001" as a source of potential privatization revenues have already been excluded from the privatization process ("Lasy państwowe" can be used as an example, the value of the enterprise being estimated at 12 billion PLN).

- Municipal authorities will block any attempts to use their property as a means of meeting restitution claims, especially where the property is already used as collateral for credit or bonds.

To summarize, it would seem that the potential incomes to be obtained from privatization of State property as presented in the "Privatization Program up to 2001" were overvalued. The State Treasury will probably never obtain such large revenues from any form of privatization process (or through the return of assets to former owners).

## Part 3

### Dynamics of Fiscal Effects of Privatization

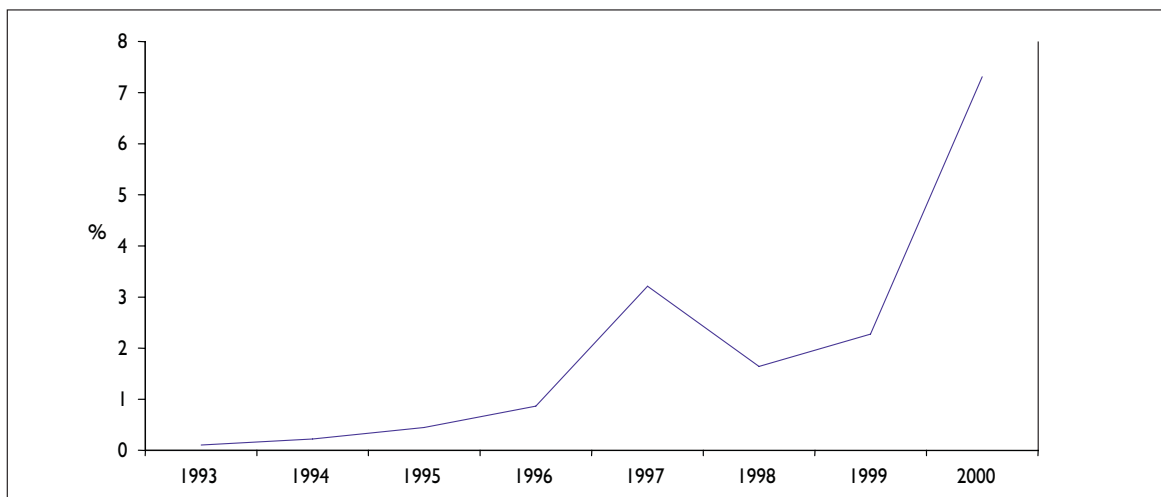
#### 3.1. The Case of Bulgaria

In analyzing the fiscal dimensions of privatization, we may distinguish three important categories of the financial effects of privatization. The first is the volume of payments contracted by the central privatization bodies, including cash and other means of payment. The second is the volume of actual payments in privatization transactions. Finally, we have cash proceeds from privatization, which represent only the flow of money into the central budget and various non-budgetary accounts. In this section, emphasis falls on cash proceeds from privatization.

For the period 1993–1999, the total volume of cash proceeds from privatization amounts to approximately USD 1 billion [36]. Privatization revenues have registered a continual increase since 1993 (with the exception of 1997, when only three transactions brought revenue of more than USD 280 million) along with an increase in the number of transactions and volume of assets privatized.

Privatization proceeds were only 0.1% of GDP in the first year of the process, but reached 3.21% in 1997. In the graph below, the expected privatization of the Bulgarian Telecommunications Company is included in the forecast for 2000 [37]. If this indeed takes place, the cash proceeds from privatization for that year will be over 7.3% of GDP.

Figure 3-1. Cash Proceeds from Privatization as a percentage of GDP



Source: Ministry of Finance, National Statistics Institute

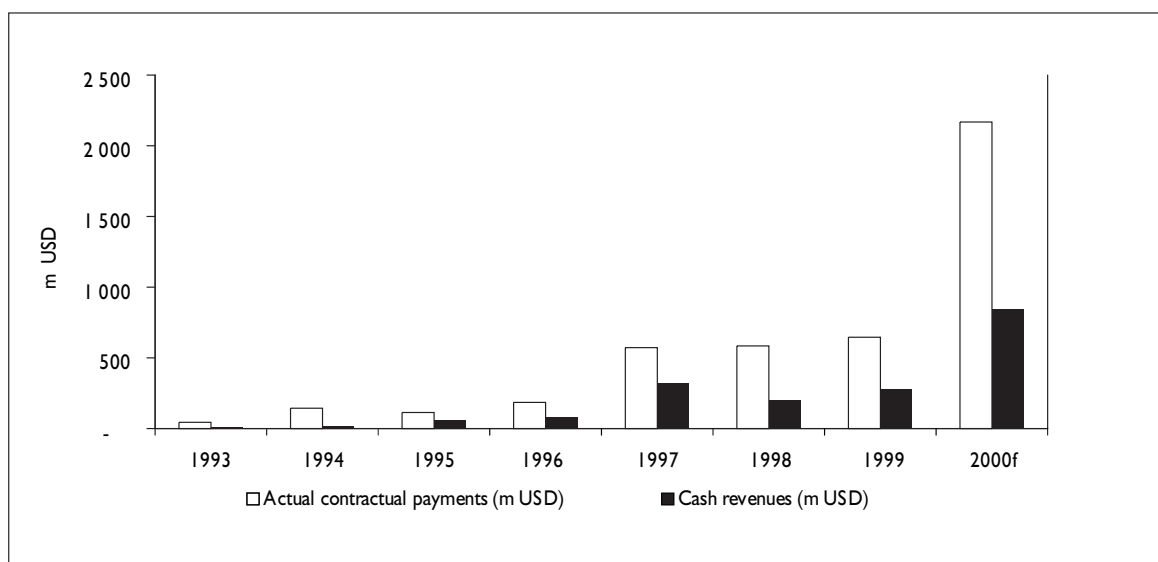
[36] Estimated through the yearly average BGN/USD exchange rates.

[37] It is most likely that BTC will be privatized in 2000 for the government has undertaken such commitment before the International Monetary Fund. The one and only offer so far was submitted by the Greek-Dutch consortium OTE/KPN, which proposed a price of USD 700 million. The price is to be paid entirely cash.

**Table 3-1. Contractual Payments vs. Cash Proceeds in Bulgarian Privatization (million USD)**

Year	1993	1994	1995	1996	1997	1998	1999	2000
Payments contracted	44	144	114	185	572	585	646	2.168
Cash proceeds	11	21	59	85	325	201	283	847

Source: Privatization Agency, Ministry of Finance

**Figure 3-2. Contractual Payments and Cash Proceeds from Privatization**

Source: Privatization Agency, Ministry of Finance

Privatization's contribution to consolidated budget revenues became relatively significant after 1995, when it reached 1.2% of budget revenues. The contribution was highest in 1997 – 9.9% – and is expected to be approximately 18% in the year 2000.

The payments contracted by the central privatization bodies have significantly exceeded cash proceeds. In the graph below, both are represented in USD in order to eliminate the effects of domestic currency depreciation. On average, cash proceeds were 41% of contractual payments. The main reasons for this were:

- extensive use of debt instruments as legal tender in privatization,
- the deferred payment schemes (up to 10 years) used in MEBOs,

– the rapid depreciation of the domestic currency, in which most of the contracts before 1998 (i.e. years of galloping and hyperinflation) were signed.

Since 1998, the annual programs of the Privatization Agency have included projected contractual payments. In both years, the actual payments contracted significantly exceeded the plan. Even in the program for the year 2000, only 663 contractual payments are envisaged although USD 700 million is being offered for BTC alone. A possible explanation for this mismatch is the government's fear of huge budget deficits due to planned but unrealized privatization proceeds. However, it is the cash proceeds that directly affect the budget rather than the contractual payments, which remain in the programs.

**Table 3-2. Planned and Actual Contractual payments**

Year	Payments contracted (million USD)	
	Planned	Actual
1998	373	585
1999	548	646
2000	663	2 168

Source: Privatization Agency



Table 3-3. Contribution by Various Privatization Bodies to payments contracted (1993 - 1999)

Body	Share (%)*
Privatization Agency	53.8
Ministry of Economy**	27.6
Ministry of Regional Development and Welfare	8.4
Ministry of Agriculture and Forests	6.1
Ministry of Transport and Communications	3.9
Ministry of Health	0.6
Ministry of Culture	0.1
Ministry of Education and Science	0.02
Energy and Energy Resources State Agency	0.1
<b>Total</b>	<b>100.0</b>

Note: \* Share of revenues in current year in BGN

\*\* Before late-1999 the Ministry of Economy was two bodies: the Ministry of Industry and the Ministry of Trade and Tourism

Source: Privatization Agency

In the majority of contractual payments, the largest share was held by the Privatization Agency, as it was responsible for the sale of the largest (in terms of long-term tangible assets) enterprises. The remaining central privatization agents altogether contracted 46% of the revenues.

The privatizing agents contracted these payments using several types of payment instruments, including cash, government securities, vouchers and compensatory bonds (issued against restitution claims). The Table 3-4 represents the share of different payment instruments in the total contractual payments for state-owned companies. The Table shows that 30.6% of the payments were negotiated in government bonds. Meanwhile, the total

volume of government bonds actually used as legal tender in privatization amounts to approximately USD 413 million, i.e. about 29% of actual payments (including cash and debt instruments). Equity-debt swaps are described separately.

Concentration on revenues by source has been significant, since almost 44% of the cash proceeds from privatization have so far come from the top five transactions (Table 3-5). Over the years, the major providers of privatization revenues have been the chemical, food, brewery and tourism industries.

All the companies listed in the Table 3-5 were purchased by foreign investors. Altogether, the Privatization Agency contracted 88 transactions with foreign

Table 3-4. Share of Means of Payment in Payments Contracted (1993-1999)

Means of payment	Share (%)*
Cash	66.3
Government bonds	30.6
Investment bonds	0.8
Compensatory bonds	1.0
Other means of payment	1.3
<b>Total</b>	<b>100.0</b>

\* Share of revenues in the current year in BGN

Source: Privatization Agency

Table 3-5. The Five Largest Privatization Deals

Company	Sector	Price (million USD)	Purchased by
Sodi – Devnya	Chemical industry	160	Solvay
Neftochim - Burgas	Chemical industry	101	Lucoil Petrol
MDK – Pirdop	Copper production	80	Union Miniere Group
Petrol – Sofia	Chemical industry	52	Yucos Petroleum, Petrol Holding and OMV
Devnya Cement	Cement production	45	Marvex
<b>Total</b>		<b>438</b>	

Source: Privatization Agency

investors. The contractual revenues from these amounted to approximately USD 825 million, i.e. 36% of the payments contracted by all central privatization bodies [38]. Meanwhile, the volume of foreign direct investments through privatization (including direct payments and liabilities of privatized companies undertaken) was USD 1.14 billion for the period 1993–1999, i.e. 42% of the total FDI volume for the period.

### 3.2. The Case of Poland

#### Revenues according to privatization method

In the Table 3-6, privatization revenues have been divided into four methods (paths) as in the "Reports on achievement of the State Budget" prepared by the Ministry of Finance. Thus we may see that capital privatization has been divided into two parts: one for enterprises and one for banks. However, it must be remembered that privatization of banks should in practice be treated as part of indirect privatization. On the other hand, in the Table 3-6 "direct privatization" means both: ordinary direct privatization of small enterprises in good economic condition, but also the liquidation of bankrupt firms.

Table 3-6 shows the very high annual growth rate of real privatization revenues each year. The biggest increase was recorded at the beginning of the process and this may be interpreted as a sign that the fiscal side of privatization has been extremely successful since the very beginning of the process. One may also claim that this is a poor statistical effect, i.e. the result of a very low base. The last sharp increase, in 1999, is the result of implementing privatization in the largest state banks and such companies as Pekao S.A., Poland's second largest bank, and TP S.A. – the national telecommunications operator.

As the table indicates, revenues from indirect privatization are the most important from the budgetary point of view and this share is increasing almost every year. In 1999, the total share of indirect privatization, enterprises plus banks, in total revenues reached 97%.

Revenues from indirect privatization are also characterized by the most regular real annual growth rate. The sharp increase in indirect privatization revenues in 1996 can be explained by the amendment of the privatization law enacted in the middle of that year. One may presume that numerous previously begun privatization processes were accelerated in order for them to be completed before the new law came into force. It may also be true that other ministries (other than MST) tried to privatize as much as possible before all state enterprises were "transferred" to voivodship authorities and the Privatization

Table 3-6. State budget revenues from various privatization methods according to State Budget Realization Reports (in millions of

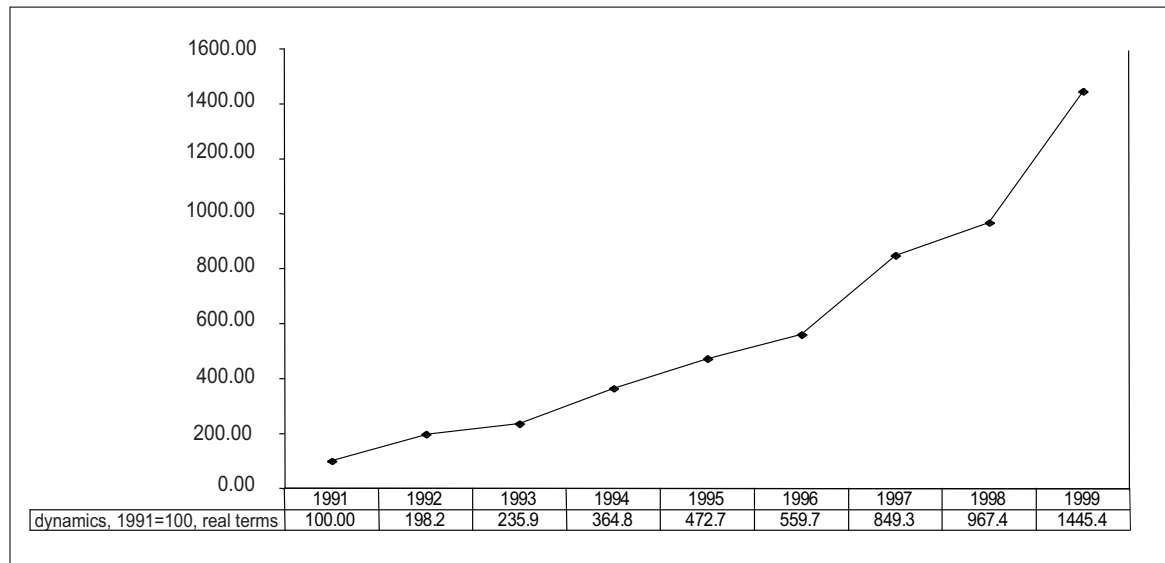
Year	1991	1992	1993	1994	1995	1996	1997	1998	1999
Total privatization revenues	170.94	484.44	780.36	1594.86	2641.58	3749.80	6537.70	8325.95	13347.5
Revenues in millions of USD	161,26	356,21	431,14	702.58	1091.56	1393.98	1993.2	2385.66	3364.21
dynamics, previous year = 100 (in real terms)		198.2	119.1	154.6	129.6	118.4	151.7	113.9	149,4
Indirect (Capital) Privatization	-	309.40	439.38	846.80	1714.20	1945.30	3254.10	6620.00	12949.7
Share of Indirect in total	-	63.9%	56.3%	53.1%	64.9%	51.9%	49.8%	79.5%	97.0%
previous year = 100 (in real terms)			105.0	145.8	158.4	94.6	145.6	182.0	182.3
Direct Privatization	-	-	287.03	322.90	406.10	973.40	359.10	429.40	388.7
Share of Direct in total	-	-	36.8%	20.2%	15.4%	26.0%	5.5%	5.2%	2,9%
previous year = 100 (in real terms)				85.1	98.4	199.9	32.1	107.0	84,4
Privatization of Banks (capital only)	-	-	53.96	425.20	521.30	831.10	2924.50	1276.55	N/A
Share of Banks in Total	-	-	6.9%	26.7%	19.7%	22.2%	44.7%	15.3%	N/A
previous year = 100 (in real terms)				596.1	95.9	133.0	306.3	39.0	N/A

Note: the data for indirect privatization in 1999 also covers the privatization of banks

Source: Report on achievement of the State Budget for the years 1991–1998, Ministry of State Treasury (data for 1999), Central Statistics Office (inflation), IFS-IMF, Own Calculations

[38] In this percentage only the PA's transactions with foreign investors are included due to the limited availability of data of the other privatizing bodies' activity.

Figure 3-3. Growth in Privatization revenues in years 1991–1999 in real terms. 1991 = 100



Source: As in Table 3-6

Agency, which in fact constitutes a department of the MST. This transfer took place in the beginning of 1997, due to a reform of the central government administration. This observation is additionally confirmed by the data on indirect privatization originating in MST, showing that no sharp increase occurred in that particular year.

Figure 3-1 also shows the real increase of annual privatization revenues from the beginning of the process. In 1999, official privatization revenues were in real terms more than 10-fold greater than at the beginning of the process (1991).

In discussing revenues from privatization, one must not forget the mass privatization program (NIF – National Investment Funds program) conducted in the years 1995–1997. Obviously, fiscal revenue was not the main objective of this privatization path and it will be considered in more detail when we come to discuss the costs of this process. However, as will be explained later, we do not consider this process privatization as such and therefore do not include either the revenues or costs related to this program as a direct fiscal effect of privatization.

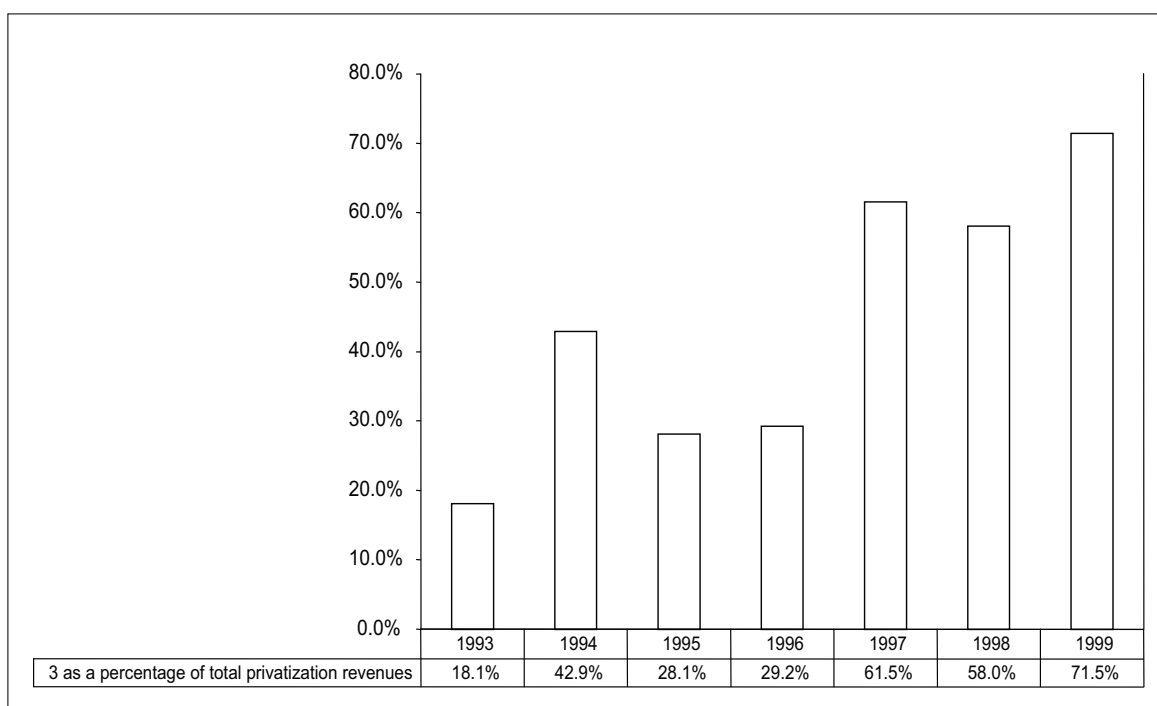
The selling of NIF "share certificates" began in November 1995 and was practically completed by November 1996. The total number of certificates sold reached 25,889,334. Since every certificate was sold for 20 PLZ, this provided revenue equal to 517.79 million PLZ during one year, of which approximately 350 million has been transferred to the budget. Therefore this revenue is comparable to the revenues from privatization of banks in 1995, or to one of the largest privatization contracts carried out in 1996 (ZPT Kraków).

### Major revenue providers

Table in Annex No 1. presents the level of concentration of privatization revenues in terms of the major revenue providers. As may be seen, the share of the largest privatization contracts in total privatization revenues tends to increase, especially over the last three years, i.e. 1997–1999. Figure 3-4 provides a very clear illustration of this process. This increase is closely linked to the growing importance of indirect privatization in total revenues, since all larger privatization contracts are performed using this path, either by a public offer on the stock market or by selling to strategic (mainly foreign) investors. The mixed path is also applied, as in the case of the Pekao SA bank or TP S.A. If we consider the enormous privatization plans for the year 2000, we may also expect the role played by large individual privatization contracts to increase in the future.

The greatest number of large privatization transactions has been performed in the banking sector (6), followed by the tobacco industry (4) and the cement and pharmaceutical industries (3). Obviously, this branch structure does not reflect the structure of the entire privatization process. The greatest number of privatized companies belongs to the food, machinery and construction sectors and this seems to mirror the structure of industry as a whole as it was inherited from the socialist economy (as far as the number of companies is concerned and excluding coal mines, steel mills and other branches that have been excluded from privatization due to their "strategic" nature).

Figure 3-4. The three largest privatization contracts as a percentage of total privatization revenues in the years 1993–1999



The growing concentration of privatization revenues presented in Table in the Annex No. 1 leads us to look more cautiously at the figures presenting a sharp increase in privatization revenues. It means that last year's privatization revenues were almost totally determined by enormous individual transactions. Obviously, the number of large state-owned companies, such as the largest banks, the national telecommunications operator or the national airline is strictly limited. Therefore one cannot expect this sharp increase in privatization revenues to last forever; eventually these revenues will begin to fall as sharply as they have been increasing. The above observation may seem trivial, but it is particularly important from the macroeconomic policy point of view.

#### Cash revenues and other financial obligations according to various privatization methods [39]

The total share of obligations in privatization revenues is decreasing. This may be most easily observed in the case of indirect privatization, which in an obvious way drives the total number of revenues.

The situation looks a little different in the case of direct privatization, where a large number of the privatized companies have been leased to insiders. About 80% of budget incomes from direct privatization for the years 1994–1997 came from this method. According to the Central Statistics Office, the share of obligations in leasing contracts increased in 1997 from about 17–25% (for the

Table 3-7. The share of other financial obligations in the total privatization revenues contracted in the years 1991–1997

	1991	1992	1993	1994	1995	1996	1997
Indirect privatization	20.2%	14.9%	14.8%	11.0%	5.1%	1.3%	0.4%
Direct privatization	since '90	30.6%	33.3%	24.1%	19.1%	19.2%	69.4%
Total	since '90	20.7%	23.8%	14.2%	7.6%	4.7%	6.2%

No data is presently available for the years 1998–1999  
Source: MST and CSO

[39] The data for this part come from the CSO and as already mentioned earlier can not be treated as complete and therefore one should take them as estimates only.

three previous years) to more the 77% of all contracted revenues. This increase explains the sharp growth of obligations in total direct privatization revenues in that year.

### Ratio of effective revenues to those planned in government programs

Table 3-8. shows that for the last 6 years, the government has regularly underestimated privatization revenues in any given fiscal year. The graph clearly illustrates both the direction and the size of this error. This time, budget plans were nearly half the effective revenues, which sets a new record. The regular underestimation of revenues may suggest that privatization was being treated as a hidden source of budget reserves.

This could be especially true for the years before 1997. Since then, privatization has not been a part of budget revenues but is counted as an additional source of government income which, according to the "Report on achievement of the state budget for 1998" was used to finance the budget deficit and therefore can no longer be a tool for decreasing the official budget deficit. This would seem to be a reasonable policy. Treating privatiza-

tion as part of budget revenues could be very dangerous, since it might lead to some form of hidden budget deficit that could explode when this kind of revenue eventually ceases [40].

Taking into account both its importance for total privatization revenues and also the size of any "mistake", it seems that bank privatization is the main cause for concern, when it comes to underestimating revenues. This seems especially strange, since privatization of any bank is normally planned a long way ahead of time and therefore revenues should also be relatively easy to plan. However, one must also remember that the final price obtained for a privatized bank (or other company) at the moment of privatization is very much dependent on the current situation of the financial markets and therefore to some extent, any poor prediction may be justified.

The serious error concerning indirect privatization in 1996 seems to have been mainly caused by the appearance of really large individual privatization contracts, for example STALEXPORT, which was sold for more than 190 million PLN. The significant error concerning direct privatization in 1996 was probably caused by the amendments to the privatization law referred to earlier in this text.

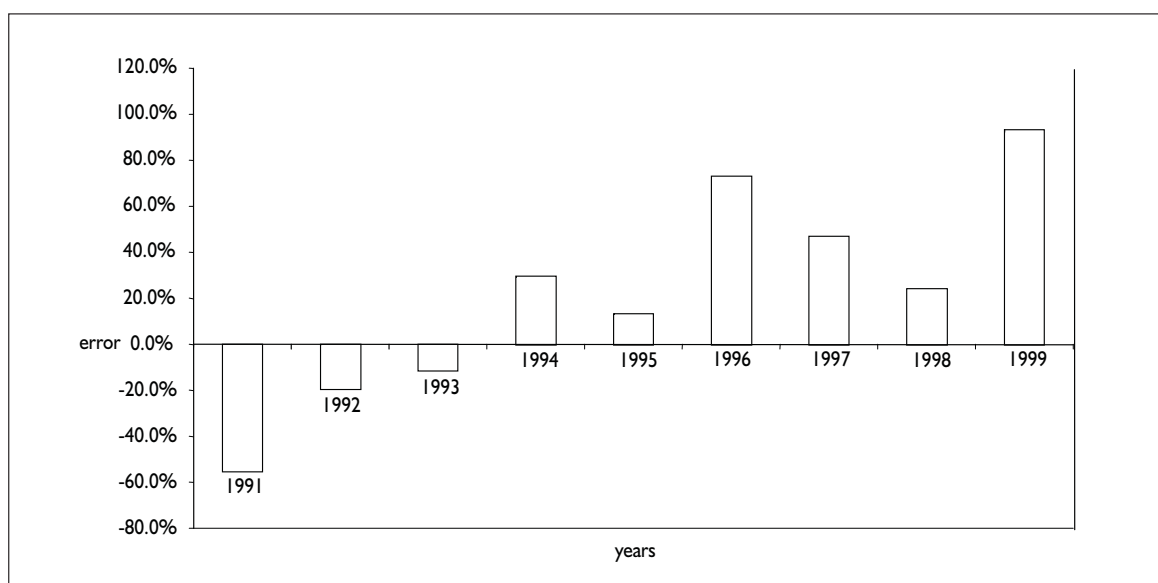
**Table 3-8. Government privatization revenues programs and revenues obtained according to privatization method in the years 1991–1999 (millions of PLN)**

	1991	1992	1993	1994	1995	1996	1997	1998	1999
Total planned priv. revenues	380	600	880	1230	2330	2165	4450	6700	6900
Obtained	170	484	780	1595	2642	3750	6538	8326	13347
Revenues obtained as a percentage of those planned	45.0%	80.7%	88.7%	129.7%	113.4%	173.2%	146.9%	124.3%	193.4%
Planned indirect priv. revenues	-	400.00	450.00	450.00	1516.00	1800.00	2510.00	6251.18	NA
Obtained	-	309.40	439.38	846.80	1714.20	1945.30	3254.10	6620.00	NA
Revenues obtained as a percentage of those planned	-	77.4%	97.6%	188.2%	113.1%	108.1%	129.6%	105.9%	NA
Planned direct priv. revenues	-	-	380.00	350.00	370.00	365.00	490.00	451.52	NA
Obtained	-	-	287.03	322.90	406.10	973.40	359.10	429.40	NA
Revenues obtained as a percentage of those planned	-	-	75.5%	92.3%	109.8%	266.7%	73.3%	95.1%	NA
Planned bank privatization revenues	-	-	-	430.00	450.00	400.00	1450.00	987.80	NA
Obtained	-	-	53.96	425.20	521.30	831.10	2924.50	1276.55	NA
Revenues obtained as a percentage of those planned	-	-	-	98.9%	115.8%	207.8%	201.7%	129.2%	NA

Source: Reports on achievement of the state budget for the years 1991–1998, own calculations

[40] The issue of the use of privatization revenues is treated in more detail in chapter 6.2 of this report.

Figure 3-5. The government's error as a percentage of planned privatization revenues



Source: As in Table 3-7

### Privatization revenues as a share of GDP and as a share of the central budget

As may be expected, both the share of privatization revenues in total budget revenues and their share in GDP rises each year. Figure 3-6 illustrates this very clearly. A similar graph for the share in GDP would be almost identical, since the share of budget revenues in GDP has remained more or less at the same level – 25–30% for the last 9 years. In 1998, privatization revenues per capita were 61.70 USD and per person gainfully employed 146.66 USD. The meaning of these figures may be better

understood if we consider that GDP per capita and per person gainfully employed in this particular year amounted to 4119.08 USD and 9791.62 USD respectively.

Comparing the figures in Table 3-9, one must remember that till 1996, privatization revenues were counted as an ordinary budget income, i.e. the officially reported budget deficits in those years were deficits after privatization had been included. Since 1997 they have been calculated separately. Therefore, in order to ensure comparability, in the Table 3-8 the last row (net budget result/GDP) shows the actual budget deficit/surplus after privatization revenues have been included in central bud-

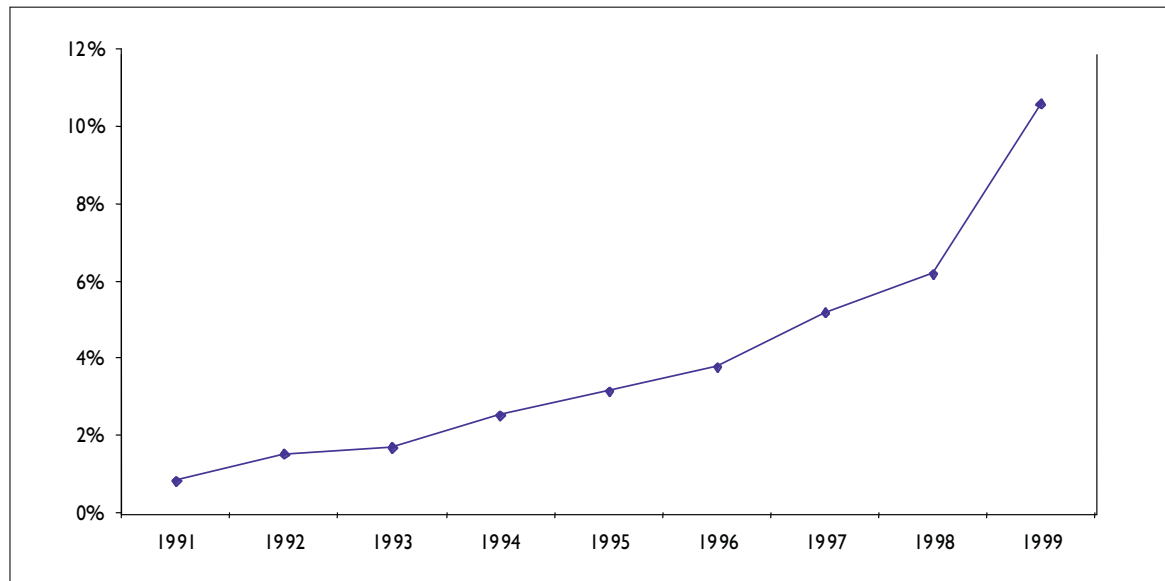
Table 3-9. Privatization revenues as a share of the central budget and as a share of GDP (millions of PLN)

Millions of PLN	1991	1992	1993	1994	1995	1996	1997	1998	1999
Total privatization revenues	170.94	484.44	780.36	1594.86	2641.58	3749.80	6537.70	8325.95	13347.50
Total central budget revenues (including privatization)	21088	31277	45900	63125	83721	99674	126309	134885	125911.5
Privatization as a percentage of budget revenues	0.81	1.55	1.70	2.53	3.16	3.76	5.18	6.17	10.60
Privatization as a percentage of budget revenues (for the period 1997-1999 increased by privatization revenues)	0.81	1.55	1.70	2.53	3.16	3.76	4.92	5.81	9.58
Central budget deficit / GDP (%)	3.8	6.0	2.8	2.7	2.4	2.4	1.3	2.4	2.05
Privatization as a percentage of GDP (%)	0.21	0.42	0.50	0.76	0.86	0.97	1.39	1.51	2.18
Net budget result */ GDP (%)	-3.8	-6.0	-2.8	-2.7	-2.4	-2.4	0.1	-0.9	-0.1

\* Central budget deficit plus privatization revenues

Source: Reports on Achievement of the State Budget for the years 1991-1999, Central Statistics Office-for GDP and own calculations

Figure 3-6. Privatization as % of Budget Revenues



Source: As Table 3-10

get revenues. In this way, the net budget result for the period 1991-1996 is equal to the central budget deficit. However, in the years 1997-1999, the net budget result is a lesser negative figure (in 1997, even a positive one) than the budget deficit.

### Revenues from foreign investors

The share of foreign investors in total privatization revenues seems to be declining.

Due to a lack of domestic capital and also underdevelopment of the Stock Exchange, at the beginning of the privatization process sales to foreign strategic investors was the best and indeed the only possible way of privatizing larger enterprises.

The situation eventually changed in 1994, when Bank Śląski was partially privatized through a public offer on the Stock Exchange. In 1998, the two largest privatization transactions were performed through the Stock Exchange

and this sharply reduced the importance of foreign investors in that year. Obviously, this does not mean no part of the shares of those companies were purchased by foreigners on the Stock Exchange. Nevertheless, it is not to be treated as the sale of a privatized company to a foreign strategic investor.

However, it seems that in 1999 the situation had changed. Shares of both the banks privatized in that year were sold to foreign direct investors. Hence the first impression one draws from Table 3-10 may be a little misleading. The largest privatization contracts planned for 2000, for example T.P. SA and Bank Handlowy SA are also to be concluded by selling part of their shares to foreign investors. Thus it seems that the sharp fall observed in 1998 was only a one year anomaly.

The data concerning the percentage share of privatization transactions in total FDI also fails to indicate any well-defined pattern. In fact, it is quite closely correlated with the percentage share of foreign investment in total privatization revenues. It seems that this share is quite

Table 3-10. Revenues from foreign strategic investors (FSI) as a share of total privatization revenues, indirect privatization and in total FDI in the years 1991-1998 (millions of PLN)

	1991	1992	1993	1994	1995	1996	1997	1998
FSI	134.6	290.9	319.4	236.20	1163.1	1139.2	1522.1	1042.4
FSI/total revenues	78.7%	60.0%	40.9%	14.8%	44.0%	30.4%	23.3%	12.5%
FSI/indirect privatization		94.0%	72.7%	27.9%	67.9%	58.6%	46.8%	15.7%
FSI/FDI				5.5%	13.1%	9.4%	9.5%	4.7%

Source: Report on the change of ownership structure in 1998. MST-1999, National Bank of Poland and own calculations

randomly determined by the occasional large privatization contracts with foreign investors in the given year. For example, in 1995 (the year with the highest share) most of the five largest privatization contracts were concluded with the participation of a foreign investor (about 70% of the value of shares sold), whereas in 1998 (the minimum share) only 19% of the shares of the five largest contracts were sold to foreign investors. It is expected that in 2000, the share of privatization transactions in total FDI will again rise, for the same reasons as referred to in the previous paragraph.

### Various payment instruments

The role of payment instruments other than cash would not seem to be an important factor in privatization revenues in Poland. At the beginning of the privatization process, some direct privatization payments were carried out by treasury obligations. The share of these kind of payments decreased very rapidly. In 1991 it was 19%, in 1992 – 2,7% and finally in 1993 – 1,5%, after which the Central Statistics Office ceased to report any transactions of this kind.

In the case of direct privatization, part of the assets of privatized companies are either contributed in kind to the company or, especially in cases of liquidation, may serve to pay off the creditors of a bankrupt company. According to the Central Statistics Office, the total share of assets contributed in kind in the years 1990 – (first half of) 1999 equaled 8.4% of the assets distributed by the direct privatization method and payments to creditors constituted 50.1% of the assets of companies liquidated during the period.

One must however take into account that these kind of transactions are not registered as privatization revenues and therefore do not affect our earlier statistics.

The other issue to be examined in this section is ownership transformation under the "Law on Financial Restructuring..." that was enacted in February 1993. Although some may consider the ownership transformations that have been conducted to be a form of privatization, this is not strictly correct. This law was developed and introduced mainly for state-owned banks and enterprises, to enable them to resolve mutual arrears problems. Therefore, even if under this law some assets of state enterprises were seized by banks or other companies, this should not be treated as privatization, since at least during the first few years, most of those banks and companies were likewise state-owned.

Obviously, this situation has gradually changed. Nevertheless, any change in ownership structure has always been a by-product of transactions conducted according to this law.

### 3.3. Comparison

Comparing the dynamics of privatization proceeds in Bulgaria and Poland one has to take into consideration various starting points for the privatization process in both countries. Privatization in Bulgaria began in practice three years later than in Poland. From this point of view comparison of the dynamics reveals an interesting coincidence: in both countries privatization revenues achieved a share close to 1% of GDP in the same year, namely in 1996, which was the third year of the initiation of the process in Bulgaria, and the sixth in the case of Poland. In both countries the revenues tend to rise systematically year by year. Comparison does not prove the hypothesis relating trade-off between budgetary incomes from privatization and speed of privatization [41].

Especially relatively significant became privatization's contribution to the countries' budget revenues in the late nineties: it reached 9.9% of budget revenues for Bulgaria (in 1997) and for Poland 9.58% (in 1999).

Comparison of revenues from privatization in Bulgaria and Poland in absolute terms reflects rather the relative size of both economies, therefore can give only a very general picture of the proportion of the privatization proceeds for each country.

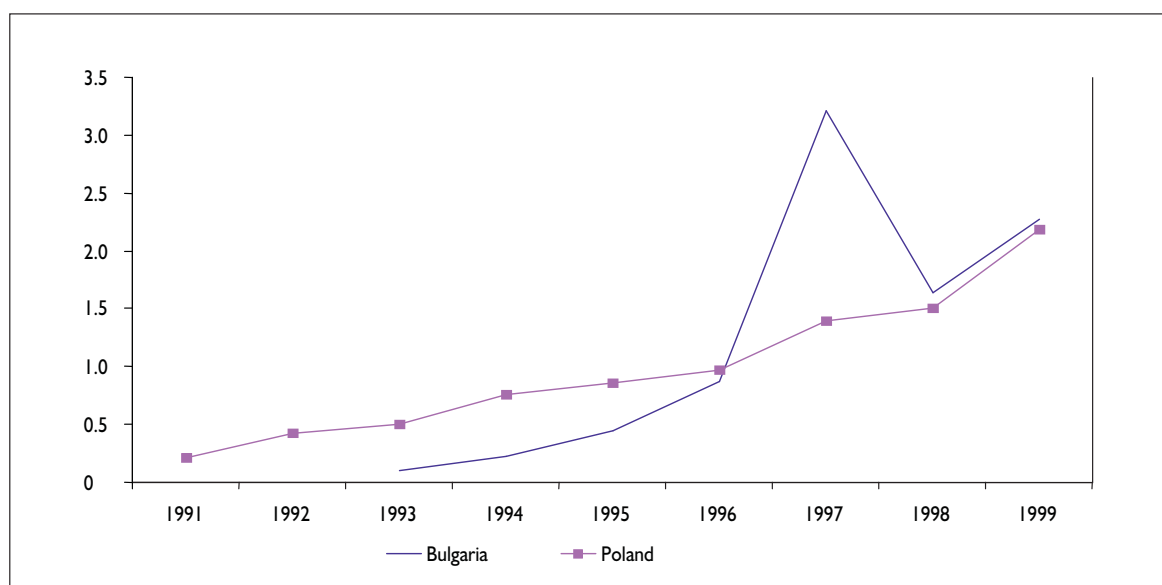
Comparison of the level of concentration of the privatization revenues for Bulgaria and Poland in terms of the biggest providers shows more differences than similarities. Relatively high concentration for Bulgaria in the first two years of the process could be explained by the very low absolute size of the privatization proceeds and the small number of privatization deals for this period. Growing and very high concentration in Poland for the last three years is caused by privatization of large companies and banks. Privatization revenues were almost totally determined by very few enormous individual transactions.

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[41] This interdependency has been formulated by B. Błaszczuk and R. Woodward and was probably valid for the first stage of privatization [Błaszczuk and Woodward, 1996, p. 17].

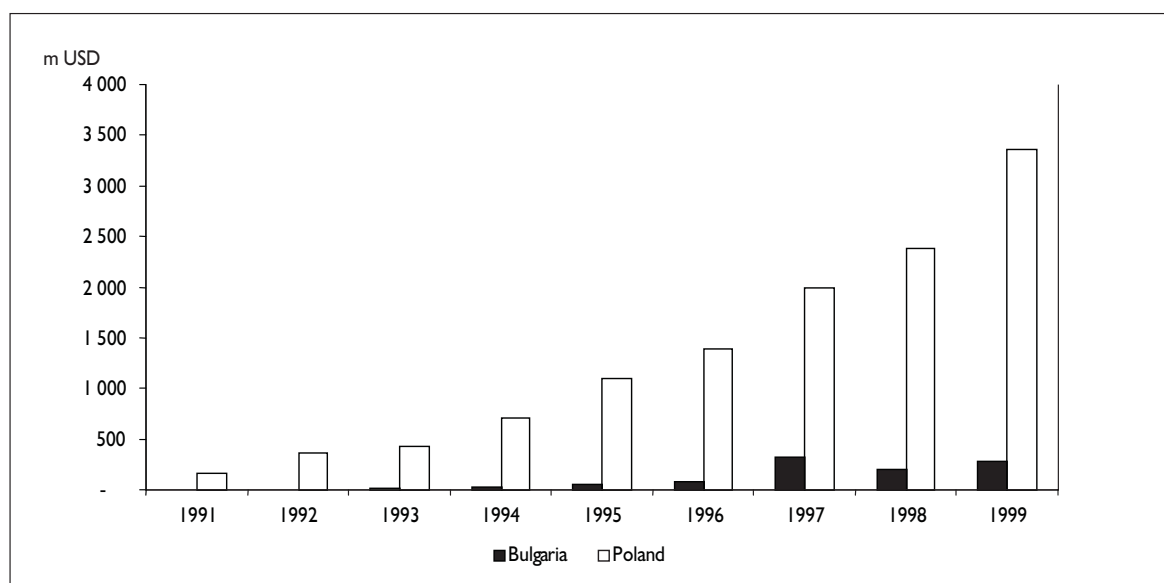


Figure 3-7. Privatization Revenues as % of GDP in Bulgaria and Poland



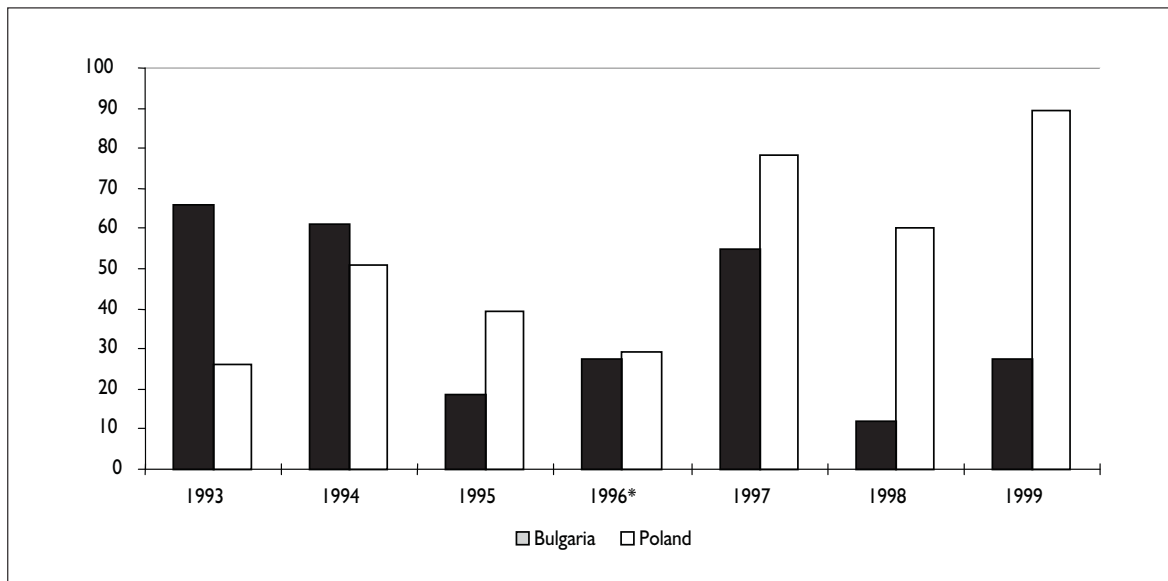
Source: As in the Figure 3-1 and the Table 3-9

Figure 3-8. Privatization Revenues in Bulgaria and Poland



Note: \* For Poland only the largest three in 1996  
 Source: Privatization Agency (Bulgaria).

Figure 3-9. Biggest Five Providers' Share (%) in the Privatization in Bulgaria and Poland



Source: As in Table 3-7

## Part 4

# Debt-Equity Swaps in the Bulgarian Approach to Privatization

### 4.1. Brady Bonds as a Payment Instrument in Privatization

Most of the measures for reducing Bulgaria's foreign debt and servicing the same by concluding Brady Bond transactions with the London Club creditors were completed by the end of 1994. Meanwhile, the bad loans of the pre-transition period, accumulated by state enterprises in state banks, were transformed into official domestic debt. As a result, by the end of 1994 Bulgaria faced a substantial domestic debt of BGN 273.7 million (USD 5.05 billion) and foreign debt amounting USD 10.3 billion. The domestic debt consisted largely – 57.2% or BGN 156.6 million (USD 2.89 billion) of government bonds issued to transform the debts of state-owned companies into official debt. At the same time, the largest share of foreign debt was in Brady Bonds – 50.1% or USD 5.1 billion.

During the same year, steps were taken towards alleviating the country's debt burden and simultaneously stimulating the privatization process. These measures involved introducing regulations to govern debt conversion. They were part of the government's general market adjustment strategy aimed at sustainable growth through private sector development and investment stimulation.

The main feature of all the regulations introduced to deal with the legal, institutional and procedural aspects of the debt-equity swap mechanism was debt annulment by converting government debt in state assets. Naturally, concluding such transactions, swapping debt against property, largely depends on the attractiveness, liquidity and quality of assets to be invested in. Another concern is the careful selection of debt instruments, based on the country's strate-

gic goals for government debt reduction and mid-term fiscal stabilization.

At first, two major types of government bonds for converting debt to property were introduced:

- government domestic debt bonds, issued under the provisions of the Law on the Settlement of Non-Performing Credits Negotiated Before 31 December 1990 [42] (These bonds are called ZUNKs, a Bulgarian abbreviation of the Law),

- Brady Bonds, issued under an Agreement with the London Club since March 1994.

The Privatization Act stipulates that government debt creditors may participate in the privatization process with their claims by following the procedures set by the Council of Ministers and which determine the CM's legal activity in this area. It also regulates all activities related to conversion of debt to property for each specific debt instrument.

The conditions and procedures for participating in privatization through foreign debt government bonds have been regulated by two successive ordinances of the CM [43]. These ordinances defined two categories of government debt bonds that may be used in privatization transactions, both in accordance with the clauses of the London Club Agreement. The first of these are Discount Bonds (DISCs), the second being Front-Loaded Interest Reduction Bonds (FLIRBs) (Bond requisites are explained in Appendix). There are no restrictions concerning the entities permitted to use such instruments in privatization transactions, i.e. they may be applied by both individuals and companies, after presenting all necessary papers in accordance with the country's currency regulations.

Several important amendments were introduced by the ordinance of 1997. Firstly, the newly adopted ordinance stipulated the procedure for acquiring and using foreign

[42] Officially published in the State Gazette No. 110 in 1994.

[43] Ordinances on the terms and conditions of participation in privatization with Bulgarian foreign debt bonds, adopted respectively with Decree of the Council of Ministers # 278 of 25 November 1994, and Decree of the Council of Ministers # 502 of 30 December 1997.

debt bonds as a payment instrument in privatization transactions, since these are considered useful both by the investors and other institutions involved in this process.

Secondly, it introduces a differentiated approach to swap quotas for various types of bonds, i.e. when concluding a privatization contract, no more than 50% of the acquired stock, shares or property value may be covered by DISCs and no more than 75% in the case of FLIRBs.

Thirdly, the practice of determining the BGN denomination on the basis of the BNB average fixed exchange rate is no longer acceptable. This is due to the accelerated dynamics of the BGN/USD exchange rate in the recent past, which in practice brought about distortions in BGN prices. For this reason, BGN values are calculated by multiplying the USD value by the BGN/USD exchange rate on the same day bonds are transferred to the account of the Ministry of Finance.

Finally, the first of these ordinances, that of 1994, specified that payment with Brady Bonds is only permitted where *the buyer undertakes not to transfer abroad the securities shares or enterprises acquired in a privatization transaction for at least 4 years, and likewise not to transfer abroad the liquidation share or price received following the sale of the securities, shares or enterprises acquired in the transaction for at least 10 years.* However, the later ordinance, that of 1997, abrogated this condition.

The accepted value of Brady Bonds was determined as follows:

- the value of DISCs is calculated in USD equal to their face value, whereas FLIRBs – are calculated with a 50% reduction in their face value,
- the BGN value of Bonds is calculated as an amount equal to the USD value using an exchange rate calculated for each specific privatization transaction, namely the average fixed exchange rate of the Bulgarian National Bank for the past six months (the period starts from the day the respective privatization transaction is signed).

According to the ordinances, Brady Bonds may not be used for:

- settling investment obligations or forfeiture under privatization contracts,
- state taxes and fees,
- other state and municipal claims,
- privatization through open sales of shares,
- participation in municipal privatization.

Experience has unearthed a whole set of problems in using foreign debt bonds and other payment instruments in privatization transactions and these have still not been

settled by the above-mentioned regulation. This has resulted in the need to amend and supplement the existing regulations. In early 1995, an amendment [44] to the ordinance governing swaps with Brady Bonds resulted in:

- The introduction of limitations for capital repatriation and exportation of profits (such a restriction is present in all debt conversion programs). In reality, profit obtained through acquired stocks, shares or enterprises cannot be transferred earlier than four years following the conclusion of the transaction. Capital transfers (the liquidation quota or price of the enterprise sold) are restricted for a 10-year period. In general, these limitations are intended to improve the country's short-term balance of payment.

- The introduction of ceilings for swap volumes - foreign debt bonds cannot be used for payment of more than 50% of stocks, shares or property acquired through privatization transactions.

- The recognition of buyers' claims from calculated but unpaid interest on interest coupons as of the day bonds are obtained. These receivables are to balance that portion of the price of shares, stocks or property acquired through a privatization transaction which is not covered by foreign debt bonds.

## 4.2. Domestic Debt Bonds as a Payment Instrument in Privatization Transactions

Five types of domestic debt bonds have been recognized as legal tender in privatization transactions. Firstly, ZUNKs were legally introduced as a privatization payment instrument in early 1994 by an ordinance of the CM [45]. Between its introduction and abrogation, slightly less than two years, this ordinance was amended and supplemented several times, in order to introduce operational improvements in the conversion process and of course, to develop the secondary bonds market. In late 1995, it was followed by another ordinance of the CM [46], which introduced three other types of long-term domestic debt bonds as legal tender in privatization transactions.

The following are most important new aspects of the above-mentioned and currently active ordinance:

- The types of long-term government bonds that may be converted to property were increased. At a later stage, this

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[44] Decree of the Council of Ministers # 41 of 20 February 1995.

[45] Ordinance on the terms and conditions of participation in privatization with ZUNKs, adopted with Decree of the Council of Ministers # 36 of 16 February 1994.

[46] Ordinance on the terms and conditions of participation in privatization with ZUNKs, bonds as per CMD # 244/1991, CMD # 186/1993, and CMD # 3/1994, adopted with Decree of the Council of Ministers # 221 of 22 November 1995.

will actually unify the statute concerning stocks originating from converting company debt to government debt according to the structural reform carried out during the period 1991–1994 (the requisites for the different bonds are quoted in Appendix).

– The ordinance abolished restrictions on using long-term government bonds whether acquired from the BNB or commercial banks and transforming bad loans into bonds, as a payment instrument in privatization transactions. This is a very important step towards establishing a real market price and free secondary trading, as well as creating incentives for investors.

– The ordinance also introduced comprehensive procedural and institutional regulations for using domestic debt bonds as a payment instrument in privatization transactions.

Of all the domestic debt securities, ZUNKs were those most often used in privatization payments. Both BGN- and USD-denominated ZUNKs may be used for purchase of stocks, shares, enterprises and/or separate units of state property, by:

- a) commercial banks which transformed bad loans into bonds and
- b) private individuals and companies that have purchased such bonds from the central bank or else commercial bank bonds from (a).

The value of ZUNKs in BGN, denominated in USD, is calculated at the BNB exchange rate on the day bonds are transferred to the Ministry of Finance [47].

The above-described participants in ZUNK transactions must adhere to the provisions of Chapters 5 and 6 of the LTPSME. The imposed restriction was intended to provide commercial banks that have transformed bad loans to long-term government bonds the opportunity to achieve rapid and effectively low-income assets, i.e. ZUNKs. This restriction is no longer in force.

Following the initial regulation of ZUNKs, these bonds were used at their face value as a payment instrument in privatization transactions. However, according to the BNB's ordinance of April 1994 [48], the market price of ZUNKs is to be calculated by commercial banks, but may not be lower than the minimum price calculated by the BNB (which is based on their discounted value plus a specific premium for using them in the privatization process). For instance, over the 1994–1996 period the minimum price for BGN-denominated bonds with a face value of 1,000 varied between BGN 665.60 and 700.00, while for

the USD-denominated bonds varied between USD 90.00 and 91.77 per USD 100 face value. Bearing in mind the need to stimulate investor interest, the CM adopted decrees, according to which the above-mentioned premiums (the incentive for using bonds in the privatization process) were set at:

- 40% till 31 December 1995 [49],
- 40% till 30 June 1996 [50],
- 30% till 31 December 1996 [51].

In regulating swaps with domestic debt bonds, the ordinance also envisages long-term bonds being accepted at their face value premium, as defined by the Council of Ministers, when they are used in privatization transactions. Actually, after 1996 this premium was "zero", i.e. there was no such premium, due to the low minimum prices of the BNB (a 350 BGN premium for a ZUNK with a face value of 1000 BGN and a USD 45 premium for a ZUNK with a face value of USD 100). These provisions do not limit free secondary trading of stocks. This means that investors may apply a reasonable reduction, formed as a spread between the face value and the present value of the securities. This Ordinance # 14 of the BNB for defining the minimum prices of ZUNKs, was later abrogated.

According to the currently active regulations on using domestic debt bonds in privatization payments, there are no limitations on capital repatriation or exportation of profits, nor with regard to the volume of domestic debt swaps. On the other hand, calculated but unpaid interest on interest coupons (as of the date bonds are acquired), is not balanced against the price of the acquired shares or privatized property. It is assumed that this interest is negligible.

### 4.3. Volume of Government Bonds Used as Legal Tender in Privatization

The total volume of debt instruments used as payment instruments in privatization transactions, including both Brady Bonds and domestic debt bonds, was USD 412.7 million (see Table 4-1). This means that equity-debt swaps account for almost 30% of the total fiscal effect (cash proceeds plus debt reduction due to swaps).

[47] According to the Ordinance on the terms and conditions of acquiring, servicing, and repaying ZUNKs, adopted with Decree of the Council of Ministers # 33 of 14 February 1994.

[48] Ordinance on the sanctioning of the commercial banks for losses from transaction with long-term government bonds under their market price, adopted with Decision of the BNB Governing Board # 125 of 12 April 1994; abolished on 12 August 1997.

[49] According to Decree of the Council of Ministers # 89 of 19 April 1995.

[50] According to Decree of the Council of Ministers # 263 of 29 December 1996.

[51] According to Decree of the Council of Ministers # 263 of 29 December 1996.

Table 4-1. Cash vs. debt instruments in privatization payments

Year	Cash proceeds (million USD)	Debt instruments used (million USD)
1993	11.3	-
1994	21.2	25.6
1995	58.7	147.3
1996	85.0	46.0
1997	325.3	52.1
1998	201.3	121.1
1999	282.6	20.7
<i>Total</i>	<i>985.4</i>	<i>412.7</i>

Source: MF, BNB, IME's, own calculations

Table 4-2. Volume of government securities used as legal tender in privatization transactions (million USD)

Year	Domestic Debt Bonds		Brady Bonds	Total
	BGN-denominated	USD-denominated		
1994	25.58	-	-	25.58
1995	27.33	7.50	112.44	147.28
1996	10.26	14.37	21.35	45.98
1997	5.81	39.64	6.62	52.06
1998	2.41	118.72	-	121.13
1999	-	20.70	-	20.70
<i>Total</i>	<i>71.39</i>	<i>200.93</i>	<i>140.41</i>	<i>412.73</i>

Note: BGN-denominated government bonds are: 1) ZUNK bonds denominated in leva; 2) bonds issued under CM Decree No. 186/1993; and 3) bonds issued under CM Decree No. 3/1994. The USD-denominated domestic debt bonds are ZUNKs denominated in USD. The figures for 1999 do not include December

Source: MF, BNB, IME's, own calculations

Almost 2/3 of the total volume of government bonds used in privatization payments has been domestic debt bonds (in the Table 4-2, both domestic and foreign debt bonds are estimated in USD for better comparison). The largest share of domestic debt bonds were USD-denominated ZUNKs – USD 201 million or 3/4 of the total volume of domestic debt bonds used.

Investors clearly preferred FLIRBs in their payments with Bulgarian Brady Bonds, since they used such bonds with a total face value of approximately USD 118 million (see Table below). Within the range of opportunities for domestic debt to property swaps, four types of government bonds were used (out of the five legally permitted). The largest share were USD-denominated ZUNKs, whereas the largest debt

Table 4-3. Volume of different bonds used and debt reduction in the period 1994–1999

Type of government bonds	Total volume used	Total debt reduction
DISCs	USD 22.8 million	1.24%
FLIRBs	USD 117.6 million	7.09%
USD-denominated ZUNKs	USD 200.9 million	10.77%
BGN-denominated ZUNKs	BGN 16.8 million	63.62%
Bonds as per CMD # 186/1993 [52]	BGN 2.3 million	36.38%
Bonds as per CMD # 3/1994 [53]	BGN 0.8 million	38.40%

Note: Total Brady Bonds debt reduction is estimated on the basis of the volume of bond issues; for domestic debt bonds, the basis is the respective outstanding debt at the time of the legal introduction of the swap mechanism

Source: Ministry of Finance, IME's, own calculations

[52] Bonds issued according to Decree of the Council of Ministers # 186 of 24 September 1993.

[53] Bonds issued according to Decree of the Council of Ministers # 3 of 18 January 1994.

reduction was by BGN-denominated ZUNKs (about 64% of the volume of debt outstanding as of late 1995).

The overall reduction of official debt through equity-debt swaps was about 2.7%, estimated on the basis of the debt at the end of 1994 (the BGN-denominated debt was converted into dollars for the purposes of the calculation).

Over the period 1995–1997, the practice whereby investors used foreign debt bonds as a payment instrument in privatization transactions was due to the income guaranteed with bonds payment, as well as the opportunity to convert debt to property. For the purpose of the present report, the value of Brady Bonds in BGN is calculated using

the average weighted BGN/USD exchange rate for the respective year, bearing in mind the fact that privatization revenues are received in BGN.

We may conclude that the mechanism for converting debt to property is not a panacea for solving the country's problems, debts and development difficulties. This mechanism should be recognized as a useful but limited tool for decreasing the nation's debts and attracting new investment. Due to its weaknesses, this mechanism should not be regarded as a universal instrument. The goals achieved should be assessed within the context of the entire macro-economic strategy for the country's development.

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## Part 5

### Costs of Privatization

#### 5.1. The Case of Bulgaria

Probably the best way to analyze the costs of Bulgaria's privatization is to examine the revenue side of the non-budgetary fund called the *Fund to cover the expenses arising from the privatization of state-owned companies*. In the period 1993–1998, this covered the expenses of all central privatization bodies, but was administered by only one of them, namely the Privatization Agency. After 1998, it was split into several funds, each of them covering the expenses of separate bodies. The tables below are based on the allocation of

privatization revenues to those funds. This allocation serves as the upper limit for the expenses of these privatization bodies. It does not allow for separation of the costs of procedures, from one side or the costs of maintaining privatization bodies, from the other.

On average, the costs of privatization were 3.7% of the total cash revenues from privatization. The percentage of spending on an annual basis is difficult to calculate, as the Table provides only the allocation of revenues, i.e. the portion of revenues that could be spent in the following years.

Although the figures in the Table above do not represent the actual spending in the years indicated, it is easy

Figure 5-1.

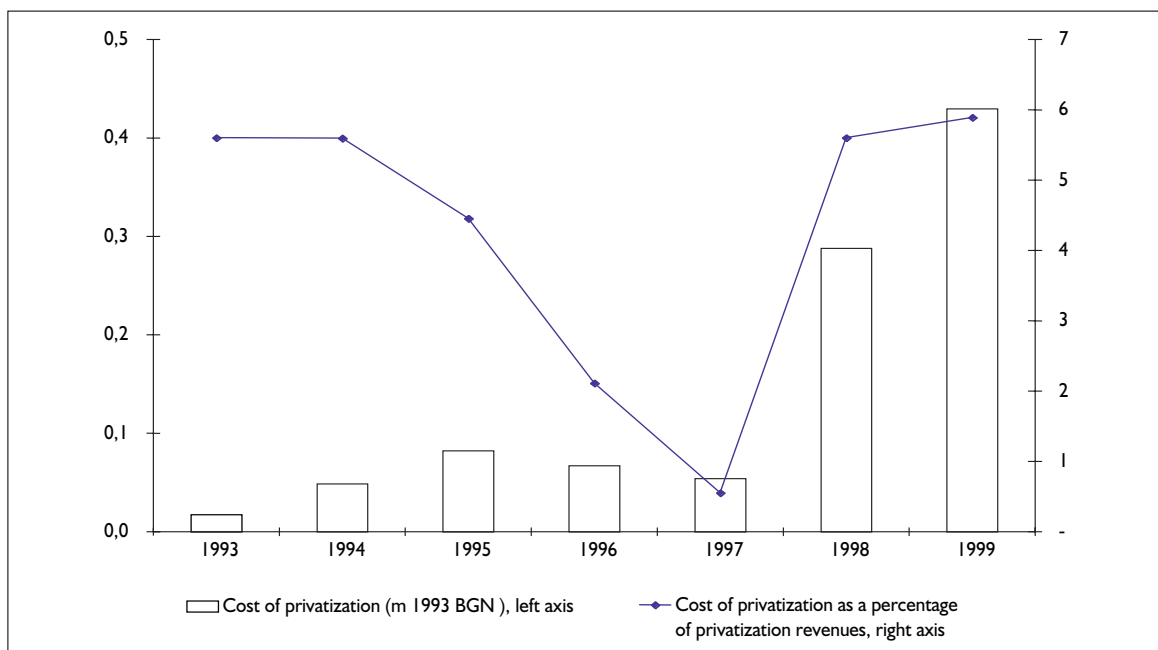




Table 5-1. Costs of privatization in Bulgaria

	1993	1994	1995	1996	1997	1998	1999	Total
Million USD	0.6	1.2	2.6	1.8	1.8	11.3	16.7	36.0
% of revenues	5.6	5.6	4.5	2.1	0.6	5.6	5.9	3.7

Source: Ministry of Finance, IME's, own calculations

Table 5-2. Costs, revenues and number of transactions

	1993	1994	1995	1996	1997	1998	1999	Total
Revenues (Million USD)	11.3	21.2	58.7	85.0	325.3	201.3	282.6	985.4
Costs (Million USD)	0.6	1.2	2.6	1.8	1.8	11.3	16.7	36.0
Transactions	62	165	309	515	590	1 110	1 224	3 975
Cost per transaction (Thousand USD)	10.2	7.2	8.5	3.5	3.1	10.2	13.6	9.1

Source: Privatization Agency, Ministry of Finance, IME's, own calculations

to follow the trend of privatization expenditure. Estimated in real terms (1993 BGN), the costs changed only slightly over the period 1993–1997, but increased dramatically in the years 1998 and 1999, with costs in 1999 being 9 times higher than in 1997.

In examining the trends for numbers of transactions and costs by years, practically no correlation may be established between the costs of privatization and the number of transactions. The same holds true for the relationship between the volume of privatization revenues and costs. However, a kind of economy-of-scale level was reached in 1997, when both total volume of costs and costs per transaction were at their lowest for the whole period.

### Opportunity cost of preferential sales to insiders

The direct expenditures in the privatization process seem to be insignificant, considering their 3.7% of cash payments. They become even more negligible if we view them as a share not only of the cash proceeds but also of total payments (including debt instruments) or total payments contracted. However, the opportunity cost of the chosen privatization model, in terms of missed cash proceeds, should be considered in order to fully appreciate privatization costs. In section 8, we stressed the opportunity cost of the prevailing use of closed procedures and the inclusion of non-price commitments in privatization contracts. Here we examine the cost of preferential sales to insiders.

Three types of preferences to insiders have been legally permitted since the very beginning of the process.

The Privatization Act of 1992 formulated these preferences in the following manner:

- Up to 20% of the shares in a company subject to privatization may be sold to insiders [54] at preferential terms; the price is 50% of their value, which is determined administratively.

- Any management-employee company, in which at least 20% of the current staff are shareholders, may buy out the company subject to privatization, without any opening tender or auction procedure; thus, the price of such a management-employee buy-out (MEBO) is the value of the company, which is assessed administratively.

- A management-employee company may use a deferred payment scheme (up to ten years) when selected as the new owner.

It has been the tradition of the privatization bodies that in most cases, a residual stake (of up to 20%) has been offered to insiders. In almost all cases, these preferential shares were sold.

The technique of sales without tender or auction, although rarely used for the privatization of whole companies (only 8.1% of all the transactions by the central privatizing agents), was prevalent in the privatization of the separate units of companies (49.1%). The price at which such buy-outs took place was based on an evaluation of the unit. Since insiders had the chance to influence these evaluations (for they submitted most of the information required by the evaluating agent), most of these companies and their separate units may safely be considered undervalued.

The privatization law (especially its amendments in 1994–1996) introduced a special regime for MEBOs. In

[54] The employees that have worked at least for two years; the employees who have been dismissed from the company no more than 14 years ago; the pensioners who retired no more than 10 years ago; managers, working not under labor contract, who have managed the company at least for one year.

**Table 5-3. Number and share of MEBOs without tender or auction in the privatization of whole companies and separate units (all central privatizing bodies) 1 Jan 1993 – 30 Nov 1999**

	Number	Share (%)
Whole companies	154	8.1
Separate units	931	49.1

Source: Privatization Agency

**Table 5-4. Consumer Price Index (1993 = 100)**

Year	1993	1994	1995	1996	1997	1998	1999	2000
CPI	100	132	214	477	5 641	6 899	7 058	7 468

Source: Statistical Yearbook 1999, own calculations

particular, a preferential payment system allows management-employee buyer companies to make a down payment amounting to 10% of the price offered, whilst scheduling the remaining 90% through installments over a period of ten years. It was not until 1999, that privatization bodies were required to discount the price offered by insider companies by the ranking of offers. In practice, this gave the management-employee companies the opportunity to outbid any competition with only a slightly higher price, but also one which was due in 10 years. A classic example of such an advantage is provided in the box below. Following the early 1999 amendment to the Privatization Act, privatizing bodies were required to apply a discount, but only a 10% discount was applicable for the whole 10-year period. The situation was amended at the beginning of 2000, since when a 10% discount is due each year of the deferred payment.

This preference was the main reason for the huge share of MEBOs – 44.3% in the period 1993–1998. However, the isolated figures for 1998 alone indicate a considerably higher percentage of 73.4% [55]. In 1999, management-employee companies won a third of all privatization contracts.

A striking illustration of the hidden cost of the deferred payment preference may be seen in a comparison between contractual payments in such MEBOs and the actual proceeds in real terms. All such transactions contracted before early 1997 (a period of hyperinflation) required new owners to pay only a ludicrous fraction (in real terms) of the sum for

which they had contracted. For instance, one such MEBO from late 1996 required the new owner to pay the first installment of the deferred payment in late 1997 (with inflation at 579%), when it was almost 7 times lower (in real terms) than the sum contracted.

The up to 20% stakes reserved for employees have probably had a insignificant hidden cost in terms of missed revenues, compared to the other two preferences - deferred payments and sales without auction or tender. Nevertheless, in the Table below, we hypothetically represent the missed revenues of the stakes reserved for insiders in some of the largest privatization transactions. In this hypothetical example, we assume that the reserved shares, if offered for competitive sale, would have had the same price as the majority stake shares.

Finally, although it is difficult to calculate, we believe that insider preferences have involved a high opportunity cost in terms of missed higher prices due to two particular effects of the preference arrangement (especially the deferred payment schemes and the sales without tender or auction), namely:

- limited demand for the companies (or their separate units);
- the incentives for insiders to influence the valuation of the companies (or their separate units).

This eventually meant the formal undervaluing of companies and more importantly, only one (price competitive) buyer, namely the management-employee company.

**Table 5-5. Opportunity Cost of Reserved Stakes**

Company	Majority Stake Sold (%)	Price of Majority Stake (Million USD)	Reserved Stake (%)	Opportunity cost of Reserved stake's (Million USD)
MDK*	56	80.0	14	20
Sheraton	67	22.3	18	6
Aroma	67	8.41	20	2.51
Eltos*	55	7.65	20	2.78
Burgasko Pivo	67	5.02	20	1.50

Note: \* In the case of these companies the reserved stake includes the reservation for restitution claims.

[55] Privatization Agency, Privatization Strategy and Programme, no date (1999), p. 1. (actually, 1998 Annual Report of the Privatization Agency).

### The Case of Rodopa

Rodopa - Shumen is one of three slaughterhouses in Bulgaria with an export license to the member countries of the EU (the other two are Mecom - Silistra and the slaughterhouse in Svishtov). In late 1998, the company had liabilities amounting to over \$7 million, due the state budget, the United Bulgarian Bank and Bank Biochim. At that time there were two main players in the privatization bid for Rodopa Shumen - Vanbouk and the management-employee company Rodopa - 97. Vanbouk's bid was for \$406,000 to be paid immediately in cash and Rodopa-97's bid was for \$700,000 to be paid in cash over a ten-year period. However, when discounted with 10% for each year of the deferred payment period, the price offered by the management-employee company amounted to just under \$300,000. Therefore the opportunity cost of the MEBO (the offer of \$406,000) would have been too high.

However, this bid was submitted before the legal introduction of the discount procedure, which would have formally meant that the MEBO offer was more competitive. Thus the Executive Director of the Privatization Agency signed the contract for the sale of 67% of Rodopa - Shumen with Rodopa - 97. It is believed the signing of the contract took place only an hour after the members of the Supervisory Council decided to review the case at their next meeting, due to uncertainty concerning the origin of the management-employee company's funds. The above concerns were aired by a company closely related to the rejected bidder - Vanbouk.

An examination of the origin of the management-employee company's funds must obviously have been necessary, because the District Attorney in the town of Shumen asked the local police chief to investigate the case. According to a letter from the Attorney General to the Privatization Agency, an investigation is necessary "because of the potential for criminal acts and unauthorized spending of Rodopa funds, when the company made a deposit to take part in the bid for 67% of Rodopa. It is believed the deposit amounting to \$39,000 was taken from the cash account of the privatized slaughterhouse.

### Trade-off between Price and Non-price Future Commitments

The concept of privatization prevalent among the staff of the privatizing bodies is of a process that aims at developing the company, i.e. their task is not only to transfer property, but also to find "good" new owners committed to "developing" the companies. This leads to the persistent use of "closed" procedures, i.e. tenders and negotiations (see Table 5-6). These techniques in turn allow for the inclusion of a variety of non-price future commitments in the privatization contracts, such as the average number of staff to be employed, investment plans, preservation of the company's previous activities, etc [56].

We believe that "closed" procedures reduce the potential amount of privatization revenues, at least for the following reasons:

- 1) the trade-off between the price and the non-price commitments,
- 2) the unclear rules of procedure reduce the number of interested investors, which means lower demand and thus a lower price for the company,
- 3) discretionary power, resulting from the unclear rules for buyer selection may, in certain cases, mean that the highest price offered is not the one selected.

Although it is difficult to estimate, there is a certain trade-off between the price offered and the promises made by the new owner. The reason is that the assessment of offers is made on the basis of both price offered and business plan submitted. This means that a buyer should have the best possible comprehensive offer rather than highest offer price. A good example is the weightings recently applied by the Ministry of Economy in the ranking of offers – 0.3 is given to the future employment program and 0.7 to the price.

However, these weightings are not always common and are almost never announced to the candidates (actually, the recent practice employed by the Ministry of Economy should be considered an exception). In practice, this makes the rules of procedure totally confusing, which in turn reduces investor interest. This reduces the demand for and the eventual price of the privatized company.

**Table 5-6. Share of "closed" and "open" procedures in the privatization of whole companies (all central privatizing bodies) 1 Jan 1993 – 30 Nov 1999**

Procedure*	Share (%)
Open	7
Closed	93

\* "Open" procedures are auctions and public offers; "closed" procedures are tenders and negotiations

Source: Privatization Agency

[56] For detailed review of privatization procedures and non-price future commitments see "Evaluation of the Post-Privatization Monitoring System in Bulgaria", CASE and IME, March 2000.

No clear rules for buyer selection are outlined in the Ordinance on tenders [57], where Art. 11 states that "the buyer selected should be the one whose offer best satisfies the tender conditions". Neither may such rules be found in the case of direct negotiations and indeed no specific regulation whatsoever governs this latter procedure. This makes it the least regulated and thus the most highly discretionary privatization technique. Therefore, the risk of losing the highest price (and even the "best" offer, where such a complex evaluation is possible) remains high.

For these reasons, we consider the prevailing use of tenders and negotiation, as well as the persistent application of non-price future commitments, to equal high opportunity costs in terms of missed inflows of cash to the budget. As it is impossible to measure the total opportunity cost of this selected privatization model, we illustrate this issue with the following two cases.

#### The Case of Chimko

Privatization of the fertilizer producer Chimko commenced in 1997 when the South Korean Daewoo and the American Stellar Global companies showed interest in the company which at that time was a profitable concern. Stellar Global offered a higher price - \$100.2 million. According to the Privatization Agency, the negotiations with Stellar Global were halted due to the fact that the company was facing financial problems, which led to a delay in the privatization process. However the procedural delay itself led to a deterioration of the plant's financial position, which resulted in a drastic fall in the selling price.

In the period 1997-1999, Chimko's liabilities increased due to higher gas prices. In 1998, new negotiations were opened, when the minimum price was \$38 million, but no buyers appeared. A year later, a new negotiation was opened. IBE - Trans of New York and BTC partners registered in the British Virgin Islands submitted their offers. The Privatization Agency chose IBE - Trans and in July last year, a privatization contract was signed. According to the contract, a price of DM 1 million had to be paid in and \$50 million had to be invested over a period of 3 years. The old liabilities of the company (mainly due the state-owned gas supplier Bulgargas) amounted to DM 70 million. The company's debt decreased to about DM 54 million after the state waived the forfeits.

Thus for a period of two years, the effective price (revenue plus liabilities) of Chimko fell from \$100.2 million to DM 55 million. At the same time the actual proceeds to the budget were only DM 1 million (down from \$100.2 million).

#### The Case of Vinex

Vinex - Preslav, one of the largest white wine producers, was privatized in late 1999 after three unsuccessful privatization procedures in a row. In the fourth procedure, two candidates appeared - a former privatization fund St. Sofia and a Bulgarian company named Perinea. The selected candidate was St. Sofia.

However, according to the rejected bidder, Perinea's offer was a higher price. According to Borislav Banchev, owner of Perinea, the company offered a price for the majority of the shares amounting to USD1.71 million and proposed a commitment to invest USD5.5 million. According to Mr. Banchev, at the beginning of the bid procedure, his company offered USD1.1 million while the price offered by St. Sofia was even lower. In the first phase of the negotiations, both companies offered higher prices but the negotiations were terminated.

The fourth privatization procedure for Vinex attracted more bidders than those previously held, probably due to the considerable reduction in the minimum price. During the first two privatization procedures, there was no investor interest and in the third bid, only one offer was submitted by a management-employee company. Two years ago, the starting price for the majority of the shares was approximately USD10 million, whereas the last procedure involved no such fixed price. Last summer, the condition imposed on the bidders was for them to pay a minimum \$1.9million and at that time, only a management-employee company submitted an offer, which later proved to be incomplete and thus the whole procedure failed.

The current buyer had good a chance from the very beginning. Since October 1998, the Executive Director of St. Sofia, Borislav Manachilov has been a member of the Vinex Board of Directors. He also figured in the management of the management-employee company that had participated in the previous procedure. Therefore, it is no surprise that St. Sofia won the bid so easily.

As in most of the cases, the delay in privatization led to deterioration in the financial performance of Vinex. After all, the plant is not such a large debtor - it owes the state budget 1.5 million BGN and if we add the dividends, corporate income tax etc. due the state, the total liabilities add up to some USD 2 million. Although Vinex has current liabilities due Reiffeisen Bank and United Bulgarian Bank, it is repaying these regularly. In the period 1997-1998, the company was in good financial standing and had a BGN 1.26 million and BGN 0.4 million profit respectively. Since the end of 1999, the financial condition of the company has deteriorated and it is now believed to have shown a loss of BGN 0.2 million.

[57] Adopted with a Decree of the Council of Ministers No. 155 of 14 August 1992.

### Liabilities connected with restitution claims

The restitution of urban property and land was the first form of privatization undertaken in Bulgaria. Eight restitution laws (adopted in 1991–1992) governed restitution of arable land and real estate where (and if) such existed in kind.

The restitution of agricultural land has been the most complicated and controversial. This was due both to the symbolic value attached to land restitution, which triggered considerable political controversy over the implementation of the policy and due to legal issues arising from the definition of ownership of restituted land. In spite of the relatively early adoption of the Ownership and Use of Agricultural Land Act [58], namely by the third quarter of 1996, only 18% of the arable land subject to restitution had actually been returned, with defined boundaries, to its owners. At the same time, actual legal titles had been issued for just 6% of the land. This, notwithstanding the fact that 54% of the claims had been processed and ruled on. A significant acceleration of the land restitution process was observed after 1997. To a great extent this progress was due to the amendments in the Land Law, which aimed at strengthening ownership rights and introducing new provisions for claiming individual property rights. As a result, by the end of 1998, 79.6% of the land subject to restitution had been returned to its owners/heirs [59]. By the end of December 1999, restitution of 96% of the land was reported completed.

In the case of the restitution of urban property, the process had a relatively faster pace. Between 1992 and 1995, over 22,000 small and medium-sized entities had been privatized under the Restoration of the Ownership of Nationalized Real Estate Act [60], thereby resolving the larger part of the claims submitted by previous owners and their heirs. Altogether however, the total value of restituted property between 1992 and 1996 amounts to some 2.5% of the country's GDP for 1996. Moreover, disputes over property arising in connection with the later disposal of state-owned assets have led observers to point out that restitution ultimately slowed down the overall privatization process in Bulgaria.

The Privatization Act reserves 10% of privatized enterprises for restitution claims (in addition to the 20% reserved for insiders).

The Compensation of Owners of Nationalized Property Act [61] adopted in 1997 was aimed at broadening the scope of restitution of formerly confiscated urban real

estate and assets. The compensation mechanisms introduced by the law were as follows:

- In the case of restitution claims against an already privatized enterprise, the claimants are compensated in the form of shares from the state-owned stake in the enterprise or in the form of compensatory bonds.

- In the case of restitution claims against an enterprise prohibited for privatization, the compensation granted is in form of compensatory bonds.

- If the enterprise has not yet been privatized, the claimants receive shares in the company. If the value of these shares is insufficient to cover all the claims, compensatory bonds are to be given for the remaining part.

If the enterprise has been privatized in full and there is no state-owned share in its capital, the compensation granted is only in the form of compensatory bonds.

The idea of this law is simple – to create a means of payment which the government grants to those eligible for restitution of their former properties, allowing those means to be used in privatization transactions, e.g. to be converted into shares. The compensation process is equal to the possible use of so-called compensatory bonds in privatization. The latter is a generic term for all three compensation means, i.e. orders as such, temporary notices (which notify possession of formerly nationalized properties) and compensatory bonds for nationalized living accommodation (houses, flats, etc.), i.e. "housing compensation orders".

District governors are entitled to register claims and claimants. Estimation of the assets subject to compensation is the obligation of the state bodies (principal) that own the remaining government share after privatization. In practice, it is difficult to estimate the exact amount of properties and owners that will be involved in the process: properties were transformed, estates were changed or vanished as physical assets and the heirs of former owners have dispersed.

## 5.2. The Case of Poland

Table 5-7. shows that direct costs of privatization constitute a decreasing fraction of total privatization revenues. The greatest costs have obviously been connected with the implementation of the process. For example, the cost of the capital privatization of the first 5 companies privatized in this way amounted to 21% [62] of privatization revenues and 13% of the value of all companies, following which, as may be observed in Table 5-7 and Figure 5-2, the cost began to

[58] Adopted 1 March 1991.

[59] Although legal titles had been issued only for 24 % of the land.

[60] Adopted 21 February 1992.

[61] Adopted 18 November 1997.

[62] Białowski, 1998.

**Table 5-7. Direct costs of privatization in the years 1991–1998 (millions of PLN)**

	1991	1992	1993	1994	1995	1996	1997	1998	1999
Costs as a percentage of privatization revenues	13.8%	7.6%	5.4%	9.7%	8.2%	3.4%	1.1%	2.0%	1.0%

Source: Reports on the achievement of the state budget in the years 1991–1998 and own calculations

fall. This reduction, as noted by Bałtowski (1998) may be linked to two factors. Firstly, since 1992 the very expensive foreign consulting companies hired to prepare and implement the privatization procedures have been systematically replaced by much cheaper domestic firms. The second reason is that in 1995, a new law on public ordering was introduced and this put much pressure and obligation on privatization agencies to economize in their selection of privatization consultants.

Likewise it is possible that the centralization of the privatization process since 1997 may also reduce the direct costs of privatization. This means that some fixed costs or quasi-fixed costs such as promotion and staff salaries may now be incurred only in one ministry as opposed to several.

However, neither the above Table nor the graph take into account the costs of the NIF program. According to the report of the Supreme Auditing Chamber (Najwyższa Izba Kontroli - NIK) the total cost of the NIF program at the end of 1995 was equal to 150.7 million PLZ. However 48.7 million PLZ of this figure was mainly covered by PHARE and USAID funds.

The other cost item in this program is the annual payment for the management of NIF assets. This payment is paid by the State Treasury to the private companies hired by the NIF boards. Between July 1995 and December 1996,

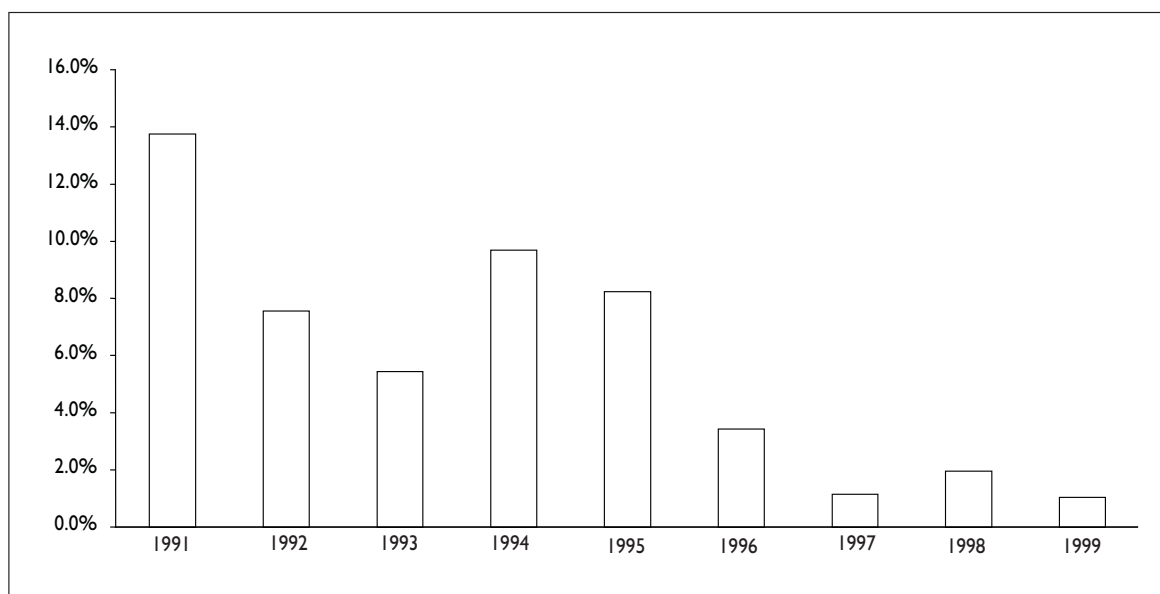
these payment amounted to more than 46 million USD, approximately 115 million zlotys. However these costs must be counted separately and for more than one reason should not be treated as direct costs of privatization: costs related to the NIF program are usually counted separately in all statistics, since this was not a program of privatization as such, but rather a non-equivalent transfer of property rights. Moreover, it was a once only action and is therefore hardly comparable to "the rest of privatization" which is spread out over a long period.

### Costs of maintaining privatization bodies

Until 1997, it is almost impossible to assess the costs of maintaining privatization bodies in Poland, since the privatization process, as already mentioned, has been performed by several ministries and all the country's voivodships. The former Ministry of Ownership Transformation was not only responsible for controlling some aspects of privatization, but also carried out other objectives such as: monitoring and subsidizing dependent enterprises.

Following the reform of 1997, the situation changed but this does not mean that any exact assessment of these kinds of costs is possible. The newly created MST is now fully

**Figure 5-2. Direct costs of privatization as a percentage of privatization revenues in years 1991–1998**



responsible for the entire privatization process, but privatization continues to be not the only task of this ministry.

### Costs of non-equivalent privatization

"The Privatization Program up to 2001" limited the analysis and projections of the cost of the non-equivalent privatization program only to the distribution of free shares to the employees of the privatized companies. It estimated the cost of this part of the program for the period from 1998 to 2005 at 8 billion PLN (see Table 6-7).

Initially, the Privatization Law passed by parliament on 13th July 1990 regulated the process of transferring free shares to employees. According to this Act, employees of commercialized State-owned Enterprises were given the right to purchase up to 20% of the shares in the privatized companies on preferential terms. The shares offered to the employees were 50% cheaper than the shares offered to Polish citizens in the form of a public offer. Under the political pressure of the left-wing parties, a new Privatization Act (the Law on Commercialization and Privatization of State Enterprises) was passed by parliament in the summer of 1996. This guaranteed even greater preferences for the employees of the privatized companies.

The new Law stipulated that employees of privatized companies could obtain free of charge up to 15% of the shares in their enterprises, but the value of such shares could not exceed the value of the 18th or 24th average monthly salaries in the productive sector. Another 15% of the shares were reserved and could be provided free to the farmers or fisherman who had acted in the past as suppliers to the privatized companies. A special stipulation also regulated the free transfer of up to 15%, of shares to the employees of the enterprises included in the National Investment Fund program. The law on NIF was passed on

30th April 1993. However, the Act concerned only 512 of the companies included in the program. It should be emphasized that these three regulations were aimed at convincing and persuading insiders to agree on commencing the ownership transformation processes in their enterprises.

According to the report of the Supreme Auditing Chamber (NIK) published in 1999 [63], under the Law on Commercialization and Privatization of State Enterprises, as of 30th of September 1998, free or preferential shares had been transferred in the case of 236 companies. The total nominal value of these stocks and shares amounted to 5.3 billion PLN (free and preferential shares were transferred to 412,000 employees of privatized companies and 33,500 farmers and fisherman. The value of these shares amounted to 5,277 and 0,23 billion PLN respectively). In order to estimate the cost of the transfer of free shares to the employees of the privatized companies, we must also take into consideration the Wholly-owned Treasury Companies included in the Mass Privatization Program (MPP). As of the end of 1996, the total book value of shares transferred to employees and farmers and fisherman under the Law on the National Investment Funds Program may be estimated at 1 billion PLN [64]. This estimate was based on the book value of 512 companies included in the program at the time when the fourth (and in fact the last) group of the companies was included in the program. As of 30th of September 1998, the total cost of free and preferential shares could be estimated at 6.3 billion PLN [65]. Additionally, according to the "Privatization Program to 2001" the value of free shares to be transferred to employees and the suppliers of the privatized companies to 2001, will amount to 8 billion PLN (see Table 6-7). However, the representatives of the Ministry of Finance estimate that this cost will also increase and will amount to 11 billion PLN [65]. If we summarize these figures, the total cost of the program will by then amount to 17.3 billion PLN (see Table 5-8) [66].

**Table 5-8. Assessment of the total cost of a non-equivalent privatization in the form of a distribution of free or preferential shares to the employees of the privatized companies**

<b>The cost of free or preferential shares transferred to the employees and suppliers of the privatized companies in billion PLN according to:</b>	<b>1990-1998</b>	<b>1999-</b>	<b>1990-</b>
- the Law on Commercialization and Privatization of State Enterprises, enacted in 1990 and 1996	5.3	11	16.3
- the Law on National Investment Funds	1	0	1
<b>TOTAL</b>	<b>6.3</b>	<b>11</b>	<b>17.3</b>

[63] "Informacja o wynikach kontroli procesu nieodpłatnego nabywania akcji przez pracowników i innych uprawnionych w procesie prywatyzacji przedsiębiorstw", NIK, Warszawa, 1999.

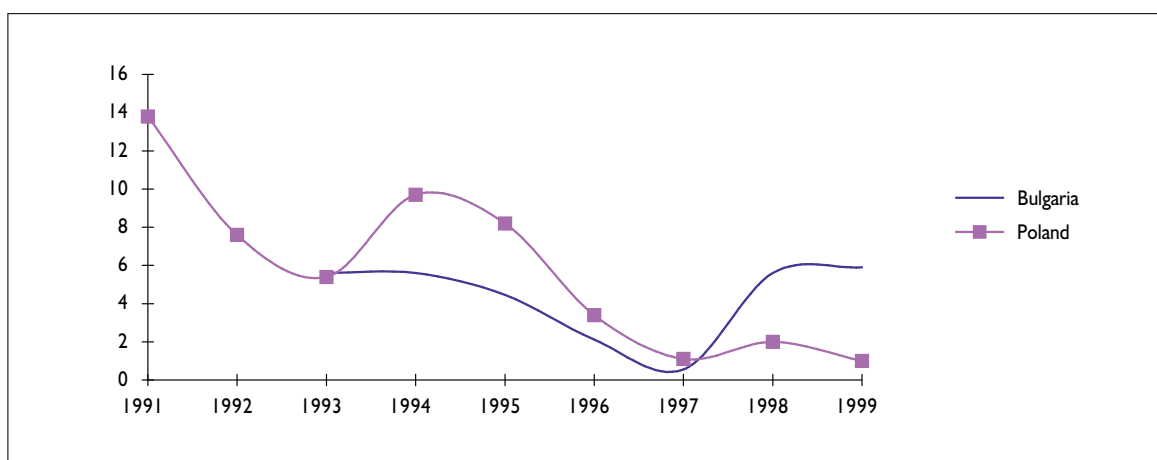
[64] Own estimate on a base of unpublished data from the Ministry of State Treasury.

[65] Not taking into consideration the fiscal impact and the cost of the lost opportunities of the companies privatized on the preferential terms under the MEBO scheme, but such a research has not been done yet.

[66] M. Psikorski, "Posłowie podzielili pieniądze", Rzeczpospolita, 1999.10.09, Warszawa.

[67] These are only the rough estimates made by the author, as there are no systematic database available on this issue.

Figure 5-3. Direct Costs of Privatization as % of Revenues in Bulgaria and Poland



Source: Tables in the text

However, this non-equivalent privatization scheme will not be limited only to the transfer of free shares to the employees and suppliers of the privatized companies. It results from a political decision finally agreed upon by the coalition parties (under the pressure of the senior coalition party) [68] in March 2000. It may have enormous impact on the overall cost of the non-equivalent privatization program. The additional costs resulting from extending this program were not taken into account in the "Privatization Program to 2001" report. This program will cater for those citizens who have not obtained any free or preferential shares. The indirect non-equivalent privatization program will be financed by the resources obtained from the privatization process.

Initially, the AWS party proposed that 25% of the shares of privatizing enterprises should finance the extended non-equivalent privatization scheme. Later AWS agreed on a figure of 9%. On the other hand, the Union of Freedom party did not agree to the extension of the non-equivalent privatization program, arguing that financing pension reform, the compensation program and the restitution program from privatization sources is a kind of non-equivalent privatization. Additionally, Union of Freedom underlined that privatization stocks are limited and it will in time become a serious problem to fully finance already existing social and compensation programs through the incomes obtained from privatization. However, after long negotiations the coalition parties agreed that up to 7% [69] of the

shares of privatizing enterprises (excluding those companies where the privatization process has already started) will finance the extended non-equivalent privatization scheme. The Minister of State Treasury, Emil Wąsacz announced that according to preliminary estimates, extending the indirect non-equivalent privatization program will cost at least 3.5 billion PLN [70]. There is no data concerning the cost of the direct non-equivalent privatization program (e.g. the free transfer of municipal flats to their present users), as no comprehensive and systemic decision has been taken.

Dynamics of share of direct costs of privatization in privatization proceeds for Bulgaria and Poland presented in Figure 5-3 reveals significant similarities. In both countries the costs systematically have been declining from the relatively high level in early stage of privatization to the level not exceeding 2% of revenues for Poland and about 5% for Bulgaria.

In the case of Bulgaria, the estimate of the costs of privatization is based on the revenue side of the Fund covering the expenses of the privatization bodies. As the share of this fund in the allocation of revenues is determined by the Privatization Act, the share of the costs in revenues has been on average approximately 5%. The sharp fall in 1996–1997 followed by another increase in 1998 was probably the result of the time lag between the moment cash proceeds were received and the moment funds were distributed to the various funds and accounts.

[68] The main explanation raised by the MP from the AWS was that all citizens should benefit from the privatization process, not only the employees of the productive sector.

[69] The Law stipulates that limit of 7 percent can be decreased if the assumed incomes from the privatization are not achieved in the previous calendar year.

[70] "7 procent akcji na uwłaszczenie", Rzeczpospolita, 08.03.2000; Figure 5-3.



## Part 6

# Allocation of Revenues from Privatization

### 6.1. The Case of Bulgaria

The original Privatization Act [71] of 1992 outlined the eventual practical use of the proceeds from privatization, listing 5 non-budgetary accounts as destinations for these revenues.

In 1994, an amendment to the Act changed the structure of allocation and determined the shares of revenue for each of the funds. Another amendment in 1995 rescheduled the allocation shares to the various funds. The share of dif-

ferent funds in the allocation procedure set by the Privatization Act for the two periods – before and after the amendment of 1995 – is given in the Table below.

In 1997, the allocation procedure for privatization revenues was amended again, when the Mutual Fund was cancelled. The same amendment introduced two more funds to the allocation procedure – the Social Security Fund and the Artists' Fund of the Ministry of Culture – as well as changing the funds' shares in the allocation of privatization revenues.

The titles of the respective funds provide a clear picture of the actual purpose of the revenues [73] allocated.

Table 6-1. Types of non-budgetary funds according to the original Privatization Act of 1992

Funds	Share (%)
Fund covering the expenses of the central privatizing bodies	Not fixed*
Mutual Fund	20
Social Security Fund	30
State Fund for Reconstruction and Development	Not fixed*
Support of the Agricultural Development Fund	10

Note: The 1993 Privatization Program fixed the allocation share of these two funds at 30% and 10% respectively.

Table 6-2. Types and (%) shares of non-budgetary funds in the allocation of privatization cash revenues according to the 1994 and 1995 amendments of the Privatization Act

Funds	1994 – 1995	1995 – 1996
Mutual Fund	20.0	20.0
Fund covering the expenses of the central privatizing bodies	5.6	5.6
National Environmental Protection Fund	4.0	4.0
Support of the Agricultural Development Fund [72]	12.0	24.0
State Fund for Reconstruction and Development	58.4	46.4

[71] The formal name is Transformation and Privatization of State-owned and Municipal Enterprises, adopted on 8 May 1992.

[72] In 1995 Support of the Agricultural Development Fund split into two separate funds: Agriculture Fund and Tobacco Fund; after 1995 they receive respectively 26% and 4% of the revenues.

[73] The greatest share held the State Fund for Reconstruction and Development (SFRD). It was created in 1991 having as main aim the support of the structural reform and the payments on the foreign debt. SFRD extended short- and medium-term credits through selected commercial banks after the necessary money for the foreign debt payments had been allocated. Besides the privatization revenues other sources of funding for the SFRD were credits, subsidies and transfers. In 1998 the Fund was closed following the arrangements in the Memorandum with IMF.

The Mutual Funds' money used to be transferred to the Social Security Funds by the end of the fiscal year.

**Table 6-3. Types and (%) shares of non-budgetary funds in the allocation of privatization cash revenues according to the 1997 amendment of the Privatization Act**

Funds	1997 – 1999
Fund covering the expenses of the central privatizing bodies	10
National Environmental Protection Fund	5
Agriculture Fund	26
Tobacco Fund	4
State Fund for Reconstruction and Development	33
Social Security Fund	20
Artists' Fund of the Ministry of Culture	2

Besides, the Budget Act of 1996 proclaimed that cash revenues from the privatization of 6 companies would go directly as subsidies to medical schools, hospitals and a special fund of the Ministry of Health (the largest of these companies was sold for USD 4.05 million).

This precise regulation of privatization proceeds (except those from "cash privatization" as described below) allocation lasted until 1999 [74], since when the revenues have been divided between the central budget (90%) and the Fund covering the expenses of the central privatizing bodies (10%). As a result, the Budget Act of 2000 contains the following truism: "Revenues from privatization of state-owned companies shall be used for budget deficit financing and official debt restructuring" [75]. Thus the clear division between the spending purposes ceased to exist in the case of privatization proceeds.

Since 1997 [76] an annual list of attractive companies that are to be privatized only against cash payments has been approved by the Council of Ministers. 96% of the proceeds from this so-called "cash privatization" goes directly to the central budget and is used for official debt reduction. The seven largest transactions for the sale of "cash privatization" companies are listed in the Table below. Altogether these have provided USD 478 million in cash revenues, which is 21% of all payments contracted and 34% of all cash proceeds from privatization to the year 2000.

### Allocation of Privatization Revenues

The cash proceeds from privatization have been allocated strictly according to the procedure provided by the Privatization Act and the annual Privatization Programs (thoroughly described in section 4). According to these regulations, privatization revenues are generally directed in two directions:

- The central budget;
- Non-budgetary funds specified in the Privatization Act.

The allocation procedure has been constantly amended throughout the whole privatization process. In practice, it has passed through 6 important amendments to the Privatization Act. Meanwhile, other regulations that affected the allocation procedure (such as the Budget Acts and the Privatization Programs), were also amended.

The Table 6-5 presents the actual share allocated to the different destinations for privatization cash proceeds. Several facts are worth noting:

- The cash proceeds gathered in the first two years of the privatization process (1993 and 1994) were allocated to non-budgetary funds at the end of 1994 in strict accordance with the already amended procedure. Thus the procedure from the original Privatization Act of 1992, supplemented by the 1993 Privatization Program, was never actually applied.

**Table 6-4. The seven largest transactions from the "cash privatization" lists**

Company	Sector	Shares sold (%)	Price (Million USD)
Sodi – Devnya	Chemical industry	60	160
Neftochim – Burgas	Chemical industry	58	101
MDK – Pirdop	Copper production	56	80
Petrol – Sofia	Chemical industry	51	52
Devnya Cement	Cement production	70	45
Interpred WTC – Sofia	Trade	70	20
Druzhiba - Plovdiv	Glass production	51	20
Total			478

Source: Privatization Agency

[74] The Privatization Act was amended in the here discussed part on 12 February 1999.

[75] The 2000 Budget Act, § 5 of the Transitory and Concluding Provisions.

[76] Amendment of the Privatization Act was made in late-1996.

Table 6-5. Actual Allocation of Privatization Revenues (Percentage share of cash proceeds)

Destination	1993-94	1995	1996	1997	1998	1999
Central Budget	-	-	-	84.2	54.0	65.7
Fund covering the expenses of the central privatization bodies	5.6	4.5	2.1	0.6	5.6	5.9
Support of the Agricultural Development Fund	-	9.2	-	-	-	-
Mutual Fund	20.0	12.2	19.5	0.4	-	-
National Environmental Protection Fund	4.0	3.2	1.5	0.4	2.8	-
Agriculture Fund	12.0	0.6	7.9	2.1	14.7	-
Tobacco Fund	-	0.1	1.2	0.3	2.3	-
State Fund for Reconstruction and Development	58.4	46.1	17.5	4.6	18.1	-
Artists' Fund of the Ministry of Culture	-	-	5.9	-	1.1	-
Social Security Fund	-	-	-	2.5	10.7	-
Universities, ministries and hospitals	-	-	-	1.7	1.2	-
Fund-raising budgetary account	-	24.1	44.4	3.2	(10.5)	28.4
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source: Ministry of Finance

– After 1995, the practice of maintaining residual funds (remaining in the fund-raising account) emerged, i.e. the money distributed to the funds was less than the actual cash proceeds. The only exception to this is the year 1998 (the negative figure for the fund-raising account is given in brackets), when just the opposite happened – the money exceeded the privatization revenues received.

– The allocation shares after 1995 do not follow the allocation procedure as described in section 4. Three major reasons for this exist:

- 1) the allocation of the cash proceed from the 4th quarter of the year takes place at the beginning of the next year (which is also the reason for the residual funds described above);
- 2) the amendments to the allocation procedure are often introduced in the middle of the year and applied directly, i.e. the percentage share resembles neither the amended or the newly applied procedure;
- 3) after 1997, "cash privatization" appeared. Meanwhile, the allocation procedure remained active for the non-cash privatization proceeds. However, in the Table above, the percentage shared is calculated on the basis of the total privatization revenues for the respective year.

Although the titles of funds provide a reasonably clear idea of the use of the cash proceeds from privatization, in the following paragraph we examine more closely the eventual allocation of the privatization money, as well as some of the important features of the allocation procedure.

The non-budgetary *Fund covering the expenses of the central privatization bodies* was administered by the Privatization Agency. It existed until 1998 when it split into separate funds for the separate bodies.

The Privatization Act established the Mutual Fund in 1992, the main idea being to use the collected funds for the Social Security Fund and the Fund for compensation of former owners. From the end of 1995, the money collected in the Mutual Fund was allocated to the Social Security Fund for pensions [77]. The Fund was canceled in 1997 [78] and the money collected so far was to be redistributed to the Social Security Fund.

Besides the Social Security Fund, another mandatory insurance fund was eligible for privatization proceeds allocation, namely the Professional Qualification and Unemployment Fund. However, no explicit data is available on distinction between their shares (thus in the Table above, they are listed as Social Security Funds). Since mid 1998, no less than 50% of the money for the social security funds was due to go to the National Health Insurance Fund.

The 1996 Budget Act [79] postulated that the revenues from the privatization of 6 specific companies should be allocated in the following special way:

– To the Ministry of Health Care Fund, to cover the cost of life-sustaining medicines already used in 1996 – up to BGN 4.5 million.

– To medical schools and university hospitals, to cover heating and electricity costs, as well as the costs of medicines – up to BGN 1.3 million.

[77] According to § 35 of the Transitory and Concluding Provisions of the Amendment of the Privatization Act of 15 December 1995.

[78] Amendment of the Privatization Act of 7 October 1997.

[79] Actually § 6 of the Transitory and Concluding Provisions of the Amendment of the Budget Act of 20 December 1996.

– To orphanages, to cover food costs – up to 0.3 million.

In 1996, the revenue from the above mentioned 6 companies barely reached BGN 0.5 million and this was in its entirety allocated to the Ministry of Health Care.

By August 1997, all the above mentioned six companies had been sold. At that time the allocation of the cash proceeds from their privatization was roughly:

- Ministry of Health Care – USD 1.5 million;
- Medical schools and university hospitals – USD 2 million;
- Orphanages – USD 0.2 million.

The funds remaining at the end of 1998 were allocated to the medical schools and the university hospitals.

In 1997 [80] a brand new article was introduced to the Privatization Act to regulate the allocation of cash proceeds from privatization-related activities, as well as the allocation of money from forfeits for breach of privatization contracts. The allocation procedure was as follows:

– To the Fund covering the expenses of the central privatization bodies – revenue from events associated with the privatization process (sale of memoranda, auction documentation, advertising, publishing and other activities) as well as any auction/tender/negotiation deposits appropriated.

– To the State Fund for Reconstruction and Development – forfeits for breach of the clauses regarding investments in privatization contracts.

– To the Social Security Fund and compensation for former owners – forfeits for breach of the clauses regarding jobs in privatization contracts.

– To the Central Budget – forfeits [81] for breach of the clauses regarding other commitments in privatization contracts.

This procedure has since been amended twice. Presently, cash proceeds from privatization-related activities go in two directions – to the Fund covering the expenses of the central privatization bodies and the Central Budget (all the forfeits for breach of privatization contracts).

Funds from the privatization of separate units and buildings under construction, undistributed since 30 June 1994, may remain at the disposal of a company after a deduction of 20% to the Mutual Fund, where approved is granted by the respective central privatizing body. On the one hand, this new regulation has limited the revenue from privatization that is allocated to supporting the agriculture industry, ecological purposes, reconstruction and development, but on the other hand, has had a positive effect by aiding these companies' rehabilitation and making them more attractive to investors. Moreover, since late 1997 the revenues from the sale of separate units have remained in the hands of the respective company [82].

## 6.2. The Case of Poland

Since the "Privatization Program up to 2001" was prepared in 1998, before the introduction of the social and compensation programs, the Ministry of Finance has had to update its estimates and prognoses of the costs of these programs. According to the new projections, the cost of the social programs to be covered by the privatization revenues will be much higher than was assumed in the "Privatization program to 2001".

First of all, the cost of the restitution program is still not known, as the agreement concerning to what extent it is to be financed has not yet been reached by the Government, the unions and the associations of former owners. If we consider the most optimistic scenario [83] (meeting a partial – 50% fulfillment of the restitution claims) and the only one considered by the Ministry of Finance, this would result in the cost of the restitution program being much higher than was planned in the "Privatization Program to 2001". The cost of the program will be at least 25–35 billion PLN more and amount to 95 billion PLN [84].

Table 6-6. The cost of pension reform in particular years

Year	1999	2000	2001	2002	2003
Cost in Billion PLN	4	11	13	16.9	18.5

Source: Ministry of Finance, 2000

[80] Amendment of the Privatization Act of 7 October 1997.

[81] For full description of forfeits procedure and practice see "Evaluation of the Post-Privatization Monitoring System in Bulgaria", CASE and IME, March 2000.

[82] Amendment of the Privatization Act of 19 December 1997.

[83] Optimistic form the public finance point of view.

[84] "Kierunki Prywatyzacji Skarbu Państwa w 2000 r.", The Ministry of State Treasury, Warsaw, 1999.

**Table 6-7. Comparison of the assumed cost of social programs financed by privatization revenues as of 1st May 2000 and that presented in the "Privatization Program up to 2001"**

No.	Program	Privatization Program to 2001 - in billion PLN	Expected cost - in billion PLN [85] <sup>1</sup>	Difference
1.	Financial support for pension reform - to 2005 - to 2001	54.0	63 [86]	9
		20.3	28	7.7
2.	Compensation program for non-productive State sector employees and pensioners	20.0	13	- 7
3.	Restitution (re-privatization) program - total cost - fund for meeting indirect claims	60-70	95	25-35
		17.0	20.1	
4.	Non-equivalent privatization program - the cost of transferring free and preferential shares - extension of the non-equivalent privatization program	8.0	11	3.0
		0	3.5	

Source: "Privatization Program to 2001", Ministry of the Treasury, 1998

Secondly, the cost of pension reform will be much higher than was initially planned (Table 6-6). This is a result of the very poor implementation of the program by the ruling parties (it being initially implemented by politicians and not economists) and the financial condition of ZUS (the State Agency of Social Insurance) being even more catastrophic than had been expected. According to the Ministry of Finance, the cost of pension reform to 2001 will amount to 28 billion PLN and will be 8 billion PLN higher during this period than was planned in 1998. At present, the Ministry of Finance estimates that the cost of pension reform will exceed 63 billion PLN by 2003 (the Privatization Program to 2001 assumed that the cost of pension reform would amount to 54 billion PLN by 2005).

Thirdly, the ruling political forces, under pressure from the senior coalition party (AWS), have reached an agreement on a more comprehensive non-equivalent privatization scheme than was expected in 1998.

Fourthly, incomes from privatization still support the current budgetary expenditures. For example, the Ministry of Finance earmarked 5.58 billion PLN to cover the budgetary deficit in 2000.

If we compare the costs of the programs included in the "Privatization Program to 2001" with the present estimates or the real cost already incurred, only the cost of the compensation program is going to be lower than was initially expected. The Ministry of Finance has explained that the most pessimistic scenario was taken into consideration. The real cost of the program will be 7 billion PLN lower than

was originally expected and will amount to 13 billion PLN.

To summarize, expectations regarding the value of State property are still enormously high, despite the fact that the transformation process began over 10 years ago. On the other hand, the cost of the programs financed by privatization revenues is going to be very high.

The value of State property was optimistically estimated in the "Privatization Program to 2001" at almost 233 billion PLN. Moreover, the State Treasury in 1998 obtained 13 billion PLN and in 1999 over 20 billion PLN from privatization. We might therefore theoretically assume that the State will obtain approximately 200 billion from privatization. In fact, as mentioned earlier, these estimates are too optimistic and there is a real threat that the potential privatization revenues will be much lower.

At present, the total cost of the major social programs alone should be estimated at 185.5 billion PLN [87]. However, these are still very rough estimates, as the organization of the restitution program has yet to be determined. The adoption of any particular plan for the restitution program may dramatically change all predictions and estimates. Moreover, we should not forget about the privatization revenues consumed by the budget. For example, this year the central budget will consume over 5 billion PLN.

More threatening is the fact that the costs of social programs are growing systematically (Table 6-7 presents a comparison of the assumed cost of social programs financed by privatization revenues as of 1st May 2000 and the cost presented in the "Privatization Program up to 2001"). Although it

[85] Estimates as of 1 May 2000. In order to make these data comparable the cost of the particular programs occurred already in 1998 and 1999 were included.

[86] The cost of the pension system reform only up to 2003.

[87] Considering the cost of the pension reform only up to 2005.

is very difficult to fully compare the cost of the programs to be financed from incomes obtained from privatization, since for some programs the time horizon of some estimates cannot be compared, the cost projections presented in the Privatization Program are much lower (more optimistic) than the present estimates of the Ministry of Finance. It is clear that the cost of pension reform will be higher. The same applies to the non-equivalent privatization program. Only the cost of the compensation program will probably be lower.

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In fact, according to the estimates presented above the real threat exists that there is already insufficient money to cover the cost of all existing social programs that were supposed to be covered by the sources obtained from privatization. As a result, there is no possibility of fully meeting the restitution claims, as the privatization revenues are already very limited and the budget will never manage to bear such a painful burden.

## Conclusions

Comparison of fiscal dimension of privatization process in Bulgaria and in Poland reveals both similarities and differences. On the contrary to Poland, where privatization proceeds have been one of the highest priorities of the privatization strategy, fiscal objectives have rarely been referred to as a priority in the modeling and execution of Bulgaria's privatization policy.

In practice, privatization revenues in Bulgaria and in Poland constitute a continuously increasing part of total budget revenues and therefore, their fiscal effects are significant in the planning of the budget and economic policy in both countries.

Indirect privatization in Poland and cash case-by-case privatization in Bulgaria are the main source of revenues. In the last three years, the share of the largest privatization contracts in total privatization revenues in Poland, to lesser extend in Bulgaria, has increased sharply. However, since the number of large and strong companies is limited, one should not treat privatization as a source of substantial budget revenues over the long term.

The privatization revenues structure in both countries is characterized by relatively high level of concentration, measured by the number of major providers of revenues. In case of Poland, especially since mid-90ties, major providers, as a rule, became the privatized banks. This is not the case of Bulgaria, where major providers have been exclusively industrial enterprises.

Governments of both countries tend to underestimate future privatization revenues. This would seem to be the result of two factors: unexpected changes on financial markets and excessive caution on the part of the government in planning revenues, which does not need to be intentional. For both the countries under discussion, this is the best way to create government reserves that could be used to cover gaps in current expenditures.

There were significant differences between Bulgaria and Poland policy with regard to the allocation of the revenues from privatization. Actually, both countries uses principally different approaches, changing over the entire period from the very beginning of the privatization

process. Formally, according to regulations, privatization revenues in Bulgaria suppose to be directed to the central budget and to strictly specified non-budgetary funds. In practice, the allocation procedure has been constantly amended throughout the whole privatization process. While the privatization revenues in Bulgaria were and still are used to cover the gap in current governmental expenditure and to reduce official debt, in Poland for the last two-three years privatization proceeds are to be used for covering costs of the implementation of large social programs.

Foreign investment constituted an important part of privatization revenues and seems to be mainly driven by occasional large privatization contracts. However, in the contrary to Bulgaria, where foreign investments amounted to 42% of the total FDI volume for the period 1993–1999, in Poland privatization proceeds from foreign investors are not a large part of total FDI, due to the relatively high total volume of foreign investments in the Polish economy.

A variety of payment instruments were used in Bulgaria in the privatization deals, including foreign and domestic debt bonds. This broadens the gap between the total financial effect reported and the actual budget revenues from privatization. However, recently there are signs of improved revenue strategy in Bulgaria, resulted in the higher cash share in the 1999 payments. A factor which supports this development is also the lower share of MEBO's in the total deals concluded. Contrary to the situation in Bulgaria, cash is the main payment instrument in the Polish privatization process.

Direct costs of privatization in both countries are relatively small and constitute a decreasing fraction of privatization revenues. The costs of privatization in Bulgaria were on average 3.7% of the total cash revenues from privatization. The greatest costs have been connected with the implementation of the process, when the cost of the capital privatization in Poland amounted to 21% of privatization revenues, following which the cost began to fall to the level of about 2% in 1998 and 1% in 1999.

## Annex No. I

Table. Major Polish revenue providers and their share in total privatization revenues in the years 1993–1999 (millions of PLN)

Year	1993			1994			1995		
	Name of company	Branch of industry	Price	Name of company	Branch of industry	Price	Name of company	Branch of industry	Price
	GÓRAŹDŹE	Cement	73.74	BSK S.A.	Banking	425.00	STOMIL OL.	Tyres	344.00
	TELETRA	Electronics	35.23	STALEXPORT	International Trade	168.30	TYTOŃ AUG.	Tobacco	220.50
	KABLE-BYD.	Cables	32.39	STOMIL-DĘB	Tyres	91.40	WINIARY KAL.	Food	178.10
	CEMENT STRZ. OP.	Cement	31.60	SAN	Food	68.40	TYTOŃ RAD.	Tobacco	153.30
	TELEKOM WA.	Electronics	30.18	JELFA	Pharmaceuticals	57.80	CEMENT. OŹ.	Cement	140.60
The largest:									
1 as a percentage of total privatization revenues	9.4%			26.6%			13.0%		
3 as a percentage of total privatization revenues	18.1%			42.9%			28.1%		
5 as a percentage of total privatization revenues	26.0%			50.8%			39.2%		
Year	1996			1997			1998		
	Name of company	Branch of industry	Price	Name of company	Branch of industry	Price	Name of company	Branch of industry	Price
	ZPT Kraków	Tobacco	579.75	HANDLOWY	Banking	1667.10	TP S.A.	Telecommunications	3146.60
	WPT Poznań	Tobacco	305.70	KGHM	Copper Mining	1348.40	Pekao S.A.	Bank	916.10
	Browary Tyskie	Brewing	211.05	PBK	Bank	1006.60	Polfa Poznań	Pharmaceuticals	770.33
	-		-	ŚWIECIE	Pulp/paper	693.30	Fabryka Łożysk "Iskra"	Metallurgy Industry/Sheaves	158.80
	-		-	POLFA KR.	Pharmaceuticals	389.00	DT Centrum	Retail trade	106,1
The largest:									
1 as a percentage of total privatization revenues	15.5%			25.5%			37.8%		
3 as a percentage of total privatization revenues	29.2%			61.5%			58.0%		
5 as a percentage of total privatization revenues	-			78.1%			60.0%		



Table. Major Polish revenue providers and their share in total privatization revenues in the years 1993–1999 (millions of PLN)

(All estimated/unofficial figures)	1999		
	Name of company	Branch of industry	Price
	Pekao S.A.	Banking	4240.00
	PZU	Insurance	3000.00
	Bank Zachodni	Banking	2300.00
	PKN	Oil and Petroleum	2082.73
The largest:			
1 as a percentage of total privatization revenues	32.6%		
3 as a percentage of total privatization revenues	73.4%		
4 as a percentage of total privatization revenues	89.4%		

Source: Report on achievement of the state budget 1991–1998, MSP – 1999, own calculations

## Annex No. 2

Table. Major Bulgarian revenue providers and their share in total privatization revenues in the years 1993–1999 (millions of USD)

<b>1993</b>		<b>m USD</b>	<b>Total contractual payments</b>	<b>44 m USD</b>	<b>%</b>
Name of the company	Branch	Price	The biggest:		
Tzarevichni Producti - Razgrad	food industry	20,00	1 as the percent of total privatization revenues		45,0
Svoboda - Kristal - Kamenovo	food industry	4,39	3 as the percent of total privatization revenues		60,0
Republika - Svoge	food industry	2,00	5 as the percent of total privatization revenues		66,0
Nektar - Silistra	food industry	1,38			
Odiana - Sofia		1,29			
<b>1994</b>			<b>Total contractual payments</b>	<b>144m USD</b>	
Name of the company	Branch	Price	The biggest:		
Hotel Vitosha-Sofia	tourism	41,80	1 as the percent of total privatization revenues		29,0
Zagorka - Stara Zagora	brewery	21,70	3 as the percent of total privatization revenues		50,6
Grand Hotel Varna	tourism	9,36	5 as the percent of total privatization revenues		61,2
SOMAT- Sofia	transport	8,22			
Chimimport	trade	7,05			
<b>1995</b>			<b>Total contractual payments</b>	<b>114m USD</b>	
Name of the company	Branch	Price	The biggest:		
Burgasko Pivo - Burgas	brewery	5,02	1 as the percent of total privatization revenues		4,4
Astika	brewery	5,00	3 as the percent of total privatization revenues		13,1
Kamenitza Plovdiv	brewery	4,88	5 as the percent of total privatization revenues		18,7
Prima Lakta-Lovech	food industry	3,48			
Kabel Komers Burgas	el.engineering	2,99			
<b>1996</b>			<b>Total contractual payments</b>	<b>185 m USD</b>	
Name of the company	Branch	Price	The biggest:		
Sheraton - Sofia	tourism	22,30	1 as the percent of total privatization revenues		12,1
Aroma	cosmetics	8,41	3 as the percent of total privatization revenues		20,7
Eltos - Lovech	el.engineering	7,65	5 as the percent of total privatization revenues		27,6
Energokabel	el.engineering	7,23			
Vidima Sevlievo	sanitary fittings	5,40			
<b>1997</b>			<b>Total contractual payments</b>	<b>572 m USD</b>	
Name of the company	Branch	Price	The biggest:		
Sody Devnya	chemical ind.	160,00	1 as the percent of total privatization revenues		28,0
MDK - Pirdop	copper prod.	80,00	3 as the percent of total privatization revenues		49,7
Devnya Cement-Devnya	cement prod.	44,55	5 as the percent of total privatization revenues		55,0
Interpret WTC - Sofia	trade	20,00			
Albena resort - Balchik	tourism	10,11			

Table. Major Bulgarian revenue providers and their share in total privatization revenues in the years 1993–1999 (millions of USD)

<b>1998</b>			<b>Total contractual payments</b>	<b>585 m USD</b>
Name of the company	Branch	Price	The biggest:	
Druzha JSCo.-Plovdiv	glass	20,00	1 as the percent of total privatization revenues	3,4
Somat -Sofia	transport	13,70	3 as the percent of total privatization revenues	8,0
Polimeri - Devnia	chemical ind.	12,95	5 as the percent of total privatization revenues	11,9
Novotel Evropa-Sofia	tourism	12,05		
Riviera - Varna	tourism	11,00		
<b>1999</b>			<b>Total contractual payments</b>	<b>646 m USD</b>
Name of the company	Branch	Price	The biggest:	
Neftochim JSCo. Bourgas	chemical ind.	101,00	1 as the percent of total privatization revenues	15,6
Petrol JSCo.-sofia	Chemical ind.	52,00	3 as the percent of total privatization revenues	25,4
Pharmacia - Dupnica	pharmaceutical	11,00	5 as the percent of total privatization revenues	27,6
Troyapharm JSCo-Troyan	pharmaceutical	7,35		
Svilozha - Svistov	chemical ind.	7,00		

## Annex No 3

Table. Brady Bonds, to be used in privatization deals in Bulgaria, issued under an Agreement with the London Club since March 1994

Front Loaded Interest Reduction Bonds (FLIRB)	
Issuing date	28 July 1994
Maturity date	28 July 2012
Volume of emission	USD 1 658 million
Interest coupon:	Floating
- tranche ?	1 - 2-year: 2%; 3 - 4-year: 2.25%; 5-year: 2.5%; 6-year: 2.75%; 7-year: 3%; from 8-year to date of payment: 6-month LIBOR (USD) + 13/16
- tranche ?	The same scheme as tranche A + additional 0.5% for each separate payment
Basis	30 / 360 for fixed interest payments and actual days number / 360 for payments with floating interest rate
Interest payment dates	28 January and 28 July
Principal payment	8-year grace period, followed by payment scheme with 21 equal 6-month installments, starting since 29 July 2002
Interest payment collateral	Allowed are investments in securities, which are denominated in USD and cover the value of interest payments from 1 to 7-year altogether. Volume of collateral is 2.6% of initial principal value and the incomes are on behalf of creditors for covering one-year interests, which are based on 3% of principal.
Collateral institution	Federal Reserve Bank of New York
Face value of one bond	USD 250 000
Type	Global. Transferable on installments not less than USD 1 000 or divisible to USD 1 000.
In form of	Payable to bearer or book entry
Place of registration	Luxembourg Stock Exchange
Settlement	Euroclear, Cedel or presenting sovereign bonds; Citibank for collateral securities

Discount Bonds (DISC)	
Issuing date	28 July 1994
Maturity date	28 July 2024
Volume of emission	USD 1 850 million
Total volume of tranche ?	USD 1 685 million
Total volume of tranche ?	USD 165 million
Interest coupon:	Floating
- tranche ?	6-month LIBOR (USD) + 13/16
- tranche ?	6-month LIBOR (USD) + 13/16 + 0.5%
Basis	Actual days number for the period / 360
Interest payment date	28 January and 28 July
Principal payment	Single at the date of payment
Collateral:	
- on principal	U.S. Treasury Bonds with zero coupon and 30-year maturity.
- on interest	Annually reinvested U.S. Treasury Bills with 1-year maturity, which cover the-yearly interest payments based on 7 % of residual principal.
Collateral institution	Federal Reserve Bank of New York
Face value of one bond	USD 250 000
Type	Global. Transferable on installments not less than USD 1 000 or divisible to USD 1 000.
In form of:	Book entry
Place of registration	Luxembourg Stock Exchange
Settlement	Euroclear, Cedel or presenting sovereign bonds; Citibank for collateral securities.

## Annex No 4

Table. Domestic bonds, to be used in privatization deals in Bulgaria

Regulation	CMDecree N 244/91	CMDecree N 186/93	Article 4 ZUNK/93	Article 5 ZUNK/93	CMDecree N 3/94
Emission number	BG 2000192224	BG 2009993226	BG 2009893228	BG 2009794228	BG 2009693222
Date of issuing	01.1.1992	01.7.1993	01.10.1993	01.1.1994	01.12.1993
Date of payment	01.1.2011	01.7.2017	01.10.2018	01.1.2019	01.12.2018
Maturity in years	19	24	25	25	25
Grace period in years	4	4	5	5	5
Period of payment in years	15	20	20	20	20
Installments	15 equal annual installments	20 equal annual installments	20 equal annual installments	20 equal annual installments	20 equal annual installments
Principal value in thousands	BGL 3 302.08	BGL 2 301.90	BGL 8 346.69	USD 494.91	BGL 884.77
Interest payment	6-month	6-month	6-month	6-month	12-month
Interest rate in 1999	Basic Interest Rate + 1	2/3 Basic Interest Rate	2/3 Basic Interest Rate	LIBOR	2/3 Basic Interest Rate

\* Principal value is according to actual data of 31 December 1999

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The Restoration of Ownership of Nationalized Real Estate Act (adopted 21 February 1992).

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