



Improvement of Economic Policy  
Through Think Tank Partnerships



# Partnership for Corporate Governance and Secondary Privatization in Transition

**FINAL REPORT**  
**PART A:**  
**TECHNICAL REPORT**



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in Transition**



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# 1. Program Progress Summary

## 1.1. Overall Project Goals

In this project we compare trends in secondary privatization (that is, post-privatization changes in the ownership structures of privatized enterprises) and their relationship to the quality of corporate governance in selected transition countries, with particular attention to Poland and Russia. This is a response to the pressing problems of corporate governance – not only in the transition countries but in the world as a whole – and to the recognition of new ownership patterns emerging in the transition countries which we believe give cause for rethinking their corporate governance regimes.

Under voucher privatization programs (as well as other non-equivalent privatization programs which tended to privilege employees), the state (to a greater or lesser degree) defined the ownership structures of privatized enterprises, both by giving insiders privileged access to shares and, in some cases, encouraging the creation of investment funds which serve as financial intermediaries, holding enterprise shares directly on behalf of individual citizens participating in voucher privatization programs. Following the primary privatization, often of a very administrative nature, many enterprises have entered “secondary privatization,” a stage of change in the ownership structure which has been determined more by market forces; as a result, strong ownership consolidation trends are observed in most transition countries. At the same time, in the area of corporate governance, the transition countries are facing serious problems due to extensive opportunities for abuses of shareholder rights by the most privileged insiders. One of our central questions concerns the mutual effects of such consolidation processes and the evolution of corporate governance practices.

## 1.2. Deliverables (Including Policy Recommendations)

Policy analysis is one of the main focuses of this project, and one of our chief goals was to produce a set of guidelines for corporate governance in transition countries. The relevant policy areas on which we focused were corporate law (particularly regulations governing corporate control, the membership and competence of various organs of management, and the legal responsibilities of managers) and the policies and regulations governing securities exchange.

In addition, certain implications for anti-trust law, bankruptcy legislation, and enforcement have been suggested.

The deliverables produced for purposes of dissemination of project results included (for a more detailed discussion, see section 2, Self-Assessment of Partnership Outcomes):

- *Working papers* published by CASE in both hardcopy and electronic form (the latter on the CASE web site) and presented at international conferences and two roundtable meetings (see next point). Additionally, journal publications are planned.

- *Two roundtable meetings* – Two roundtable meetings, one in Warsaw and one in Moscow, were held for dissemination and public discussion of the project results. In addition to members of the team from all three partner institutions, participants included representatives of other local think tanks, business groups, policy makers, and the media.
- *Television appearances* – During their stay in Warsaw in connection with the Warsaw roundtable meeting in December 2003, brief interviews with Alexander Radygin and Marina Turuntseva appeared on Polish television.
- *Information appearing on the web sites* of the participating institutions, including the network of institutes affiliated with CASE in Georgia, Kyrgyzstan, and Ukraine. A special page was created for the project on CASE's web site and links to this page appear on the web sites of these institutes.

### **1.3. Summary of Activities and Achievements (Including Deliverables)**

The project team kicked off its work with a meeting at Staffordshire University Business School in February 2003. At this meeting the team discussed the current state of affairs in Poland and Russia in the areas of corporate governance and the ownership structures of the economies. Plans were made with respect to how to proceed and when to organize upcoming events planned to take place in the project.

Project team members attended the Regional Think Tank Partnership Program conference held in Sestroretsk, Russia, June 7-9, 2003. This conference served as an occasion for the group to further discuss research methodology, re-formulate hypotheses, and make plans concerning papers that would be produced.

Roundtable meetings were held in Warsaw on 12 December, 2003, and Moscow on 16 January, 2004, at which the final results of the project were publicly presented and discussed with leading experts on privatization and corporate governance in Poland and Russia.

With respect to the project's research goals, materials prepared within the project (including programs of the roundtable meetings) can be found in the Annex to this Technical Report (Part B).

First, a paper was prepared in which theoretical and empirical literature on privatization and corporate governance (in general and in the transition countries in particular) was overviewed and the research questions to be addressed in this project were presented (see Chapter I in the Annex).

Second, papers presenting an overview and analysis of legislation, regulations, and institutional arrangements relevant for secondary privatization and corporate governance in Poland and Russia were prepared (see Chapters II, III, and IV, and parts 1-3 of Chapter IV in the Annex). These cover the following questions:

- The legal framework for privatization and results of the privatization process
- Corporate governance legislation embodied in company codes and other relevant legislation
- Institutional overview of the capital markets, banking sectors, investment funds and bankruptcy regulation and practices
- Description of changes in ownership structures in various types of privatized companies

Third, a questionnaire on corporate governance practices in transition countries was prepared and completed for Poland, Russia, and a number of other countries. A comparative paper analyzing the results of this questionnaire was prepared (see Chapter IV, part 4, in the Annex; the questionnaire itself can be found in Appendix 1 in the Annex). The questionnaire covered such questions as:

- Rules governing voting at annual shareholder meetings
- Membership and activities of supervisory boards and executive boards
- Rules governing minority shareholders' rights
- Transparency and reporting practices
- Other matters, such as legislation on insider trading and collusion to change share prices

Finally, the Russian and Polish team members conducted an econometric analysis of data sets containing data on corporate governance, ownership structure, and economic performance for 186 Polish companies (including 86 of the 500 largest Polish companies and 100 companies privatized by management-employee lease leveraged buyouts) and 100 Russian privatized companies. In this analysis, we conducted econometric tests of the effects of types of ownership (i.e., size of shares of different types of owners, degree of concentration, and the like) and various corporate governance variables on enterprise performance. For the Polish employee-leased companies (the only group of companies for which our data made such an analysis possible), we also tested for the endogeneity of ownership (that is, the hypothesis that economic performance and other economic characteristics on the firms determine the nature and direction of changes in ownership structure). We did this by estimating a regression of the level of concentration of shares in the hands of the single largest shareholder on a number of variables representing the economic characteristics and performance of the firms, and by testing a probit model in which the probability of the emergence of various types of dominant ownership (e.g., dominant ownership by a strategic investor, by top management, or by some combination of these) in a given firm is estimated (see Chapter V in the Annex).

Our conclusions and policy recommendations can be found in Chapter VI of the Annex.

#### **1.4. Roles of the Partner Institutions**

Each of the three partners made a crucial contribution to the project, and each benefited from participation and interaction with the others.

IET and CASE are both providing country data and analysis for Russia and Poland, respectively. SUBS is providing comparative analysis using data from other countries, as well as some guidance with respect to methodology; additionally, SUBS hosted a meeting of the team (this was the only internal meeting to take place within the project, aside from the aforementioned meeting in Sestroretsk) and provided extensive methodological advice to CASE team members concerning the ownership endogeneity analysis (similarly, the CASE team members extensively discussed the interpretation of the results of her econometric analysis with Marina Turuntseva of IET).

Among the benefits that accrued to the project partners were the deepening of old cooperative ties and the creation of new ones which allowed for broadening the scope of the partners' experience. The SUBS partner, for example, worked on Russia for the first time (previous transition economy experience has been limited to Central and Southeastern Europe). CASE and IET, on the other hand, deepened the long-standing cooperative

links between the two organizations, which had previously been largely limited to the leadership of the two organizations. The project also afforded CASE and SUBS the opportunity to extend previous cooperation on the subject of secondary privatization.

Procedurally and organizationally, IET was the partner with the most experience working in USAID projects, and as a result the other two partners frequently consulted with IET concerning such matters.

Finally, it is worth mentioning that we also followed the work of the two other Grant Cycle 2 teams working on corporate governance issues in the Think Tank Partnership Program. We exchanged interim reports with both of those teams, and one of them was represented at Moscow Roundtable in January 2004.

## **2. Self-Assessment of Partnership Outcomes**

### **2.1. Outreach and Dissemination Capacity**

The two partners responsible for the bulk of the dissemination activity in this project – IET and CASE – are already among the most influential think tanks in their respective countries, and have very well-developed dissemination capacities. However, CASE, which published the materials produced within the project, was able to increase its dissemination capacity as a result of negotiating a lower cost of publishing with its publishing house.

We expected that the greatest challenge for IET and CASE with respect to dissemination in this project would be in convincing the target audiences in Poland and Russia that the experience of the other country merits serious attention. However, the level of interest was high. While this is undoubtedly partly due to the general heightening of interest in corporate governance issues as a result of the corporate scandals in the USA (Enron, etc.) and Western Europe (Parmalat), we observed a high level of interest of experts in each of the two countries in the experiences of the others. To some extent, this is due to the increased awareness resulting from the Western corporate scandals that corporate governance problems face all countries and are not unique to the transition countries. However, we also observed a high level of interest of Poles in developments in Russia as a result of curiosity about the implications of the Yukos affair, and in Russia. Similar factors were at work in Russia.

### **2.2. Analytical Capacity**

IET and CASE have been on the forefront of improvements in economic science in their respective countries. The methodological and analytical capacities of the participating institutions are sufficient to allow them to engage in work which is on the cutting edge of research in the areas of privatization and corporate governance in the transition economies (issues such as the endogeneity of ownership changes and post-privatization ownership evolution). However, there are increasing limitations in the data which are available in both countries, as companies are less and less willing to provide various kinds of information in surveys. Thus, unfortunately, increasing refinements in the methodological capabilities of these institutions are accompanied by declines in the quality of available data in whose analysis they can employ these techniques.

For the first time, CASE conducted an analysis of the endogeneity of ownership in the transition. Very little such analysis has been conducted in the past (Iraj Hashi of SUBS was the co-author of one such study). As a result of consultation between CASE and SUBS on this subject, both institutions (and especially CASE) were able to improve their analytical approach in this area.

Finally, all three participating institutions increased their awareness of the comparative dimensions of corporate governance analysis, broadening their perspectives from concentration on a single country (in the case of IET and CASE) or narrow group of countries (Central European countries, in the case of SUBS).

### 2.3. Institutional Capacity Building and Sustainability

The separate, individual capacities of CASE and IET have been considerable in the past. In addition, both institutes have had diversified funding sources for years. However, the implementation of this project, which allowed the two institutions to cooperate and interact in ways that had not been attempted before, has led to invaluable synergies. It has also led to the deepening of contacts at both the scientific and administrative level, as well as the exploration of possible new avenues for future cooperation in the areas covered by this project and other areas. In this sense, the project has created considerable added value for both institutes.

### 2.4. Partnership and Network Building

As mentioned in Section 1, this project gave the partners the opportunity to deepen old cooperative ties and create new ones which allow for broadening of the scope of the partners' experience. The SUBS partner, for example, worked on Russia for the first time (previous transition economy experience has been limited to Central and Southeastern Europe). CASE and IET, on the other hand, deepened long-standing cooperative links between the two organizations, which had previously been largely limited to the leadership of the two organizations. The project has also afforded CASE and SUBS the opportunity to extend previous cooperation on the subject of secondary privatization.

Additionally, as discussed in Section 1, the partnership of these three institutions has borne fruit in the form of a joint expression of interest submitted to the European Union's Tacis program for a large project concerning deregulation in the Russian Federation. This consortium was shortlisted for this project and is currently in the stage of preparing a proposal. Similar cooperation is expected in the future.

### 2.5. Performance Indicators and Dissemination Measures

Performance indicators	Number reported
Number of requests for policy advice from politicians and policy makers	0
Number of mentions in the press	0
Number of articles, working papers, and books	Working papers published by CASE (in hardcopy and electronic versions): - in English: - in Polish: - in Russian:
Number of publications in professional journals	2 planned, in the Russian journals <i>Shareholders' Journal</i> and <i>Problems of the theory and practice of governance</i>
Number of international conferences participated in	3: <ul style="list-style-type: none"> <li>• 5<sup>th</sup> Annual Conference on Enterprise in Transition organized by the Faculty of Economics of the University of Split in Croatia, 22-24 May, 2003 (Richard Woodward, CASE)</li> <li>• Seminar on "Corporate governance in Russia," 19 March 2003, Finland (Alex-</li> </ul>

	<p>ander Radygin, IET)</p> <ul style="list-style-type: none"> <li>• Conference "Restructuring and Decentralization in transition economies," Italy, 14-15 November 2003 (Alexander Radygin, IET)</li> </ul>
Number of national conferences participated in	<p>2:</p> <ul style="list-style-type: none"> <li>• Conference "Modernization of Russian economy," April 2003, Moscow (Alexander Radygin, IET)</li> <li>• OECD seminar "Corporate governance in Russia", panel "Beneficiary ownership" (Alexander Radygin, IET)</li> </ul>
Number of full-time staff members	CASE has 35 employees and experts working on a full-time basis, of which three deal with corporate governance issues. All IET staff is part-time. Of that staff, numbering 37, four are working on issues related to corporate governance and corporate ownership changes.
Time of active involvement in policy analysis since the think tank's inception	Not applicable
Number of joint publications, paper collections, and special issues of journals	0
Number of policy briefs and media publications jointly prepared by partnership	0
Number of international conferences, seminars and roundtables held under the project and attendance for each event	<p>Attendance at two roundtables:</p> <ul style="list-style-type: none"> <li>- Warsaw: 25 (11 from CASE and 14 from outside)</li> <li>- Moscow: 66</li> </ul>
Number of jointly produced policy analyses	0
Number of jointly produced regional cooperation/conflict resolution studies	Not applicable

### *Internet dissemination*

A banner for the project appears on CASE's home page ([www.case.com.pl](http://www.case.com.pl)), with a link to another page:

[www.case.com.pl/strona--ID-projekty\\_rozwoj\\_sektora,projekt\\_id-75937,nlang-710.html](http://www.case.com.pl/strona--ID-projekty_rozwoj_sektora,projekt_id-75937,nlang-710.html)

This page contains general information about the project, as well as a link to a page dedicated to the Warsaw Round Table and containing downloadable versions of the papers presented at the Round Table:

[www.case.com.pl/strona--ID-seminaria\\_miedzynarodowe,seminarium\\_id-1514571,nlang-710.html](http://www.case.com.pl/strona--ID-seminaria_miedzynarodowe,seminarium_id-1514571,nlang-710.html)

Foundations affiliated with CASE in Georgia, Kyrgyzstan, and Ukraine also contain general information about the project and links to the project publications. These are as follows:

1. On the CASE-Transcaucasus site (in the "What's New" section):

[www.case-transcaucasus.org.ge/cgi-bin/news/viewnews.cgi?category=all&id=1073646013](http://www.case-transcaucasus.org.ge/cgi-bin/news/viewnews.cgi?category=all&id=1073646013)

2. On the CASE-Kyrgyzstan site (in the "Links" section):

[http://www.case.elcat.kg/Links\\_en.htm](http://www.case.elcat.kg/Links_en.htm)

3. On the CASE-Ukraine site (in the "News and Announcements" section):

<http://www.case-ukraine.kiev.ua/main.html#>

IET's web site contains a link from the home page to the following page with information on the Moscow Round Table meeting, as well as downloadable versions of the presentations:

[http://www.iet.ru/personal/sovet\\_2004\\_01\\_16.htm](http://www.iet.ru/personal/sovet_2004_01_16.htm)

#### *Dissemination to federal authorities and NGOs in Russia*

Some parts of the texts were submitted to the State Duma of the RF, the Ministry of Economic Development and Trade, and members of the Expert Council of the Federal Securities Market Commission. In addition, the following NGOs, among others, received texts: the National Council on Corporate Governance, the Association for the Protection of Shareholders' Rights, the Russian institute of directors, and the Institute of Corporate Law and Management.

#### *Hardcopy publications by CASE in its Studies & Analyses series*

Adobe Acrobat versions of the hardcopy publications by CASE can be found on its web site:

[http://www.case.com.pl/strona--ID-publikacje\\_studia\\_i\\_analizy,nlang-710.html](http://www.case.com.pl/strona--ID-publikacje_studia_i_analizy,nlang-710.html)

[http://www.case.com.pl/strona--ID-publikacje\\_studia\\_i\\_analizy,ROK-2003,TID-1421,nlang-710.html](http://www.case.com.pl/strona--ID-publikacje_studia_i_analizy,ROK-2003,TID-1421,nlang-710.html)

These include the following:

- Studies & Analyses no. 263: Piotr Kozarzewski, Corporate Governance and Secondary Privatisation in Poland: Legal Framework and Changes in Ownership Structure (in English, Polish and Russian)
- Studies & Analyses no. 264: Barbara Blaszczyk, Iraj Hashi, Alexander Radygin, Richard Woodward, Corporate Governance and Ownership Structure in the Transition: The Current State of Knowledge and Where to Go from Here (in English)
- Studies & Analyses no. 268: Iraj Hashi, The Legal Framework for Effective Corporate Governance: Comparative Analysis of Provisions in Selected Transition Economies (in English, Polish and Russian)

The content of all the papers prepared under this project have been included in the Annex to this report (Part B).