

Extended Country Report

**Financial Participation of Employees
in Romania***

Lucian-Liviu Albu
and
Axel Bormann

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1. Background

The idea of employee participation is relatively new, apart from some inadequate schemes tried under the communist regime. The concept of financial participation emerged during the privatization process. Like in other transitional countries of Central and Eastern Europe, a share-ownership system and not profit-sharing schemes were predominant. In the transition period, the development of such schemes did not necessarily positively influence the payment system or work organisation.

a) History

The most significant form of employee financial participation in Romania, like in other post-communist economies, is employee ownership. Employee participation was initially introduced during the last decade of the communist rule for propagandistic reasons in the form of so-called social parts (shares) held by workers from the total amount of the 'national capital'. According to the scheme, the employees had to purchase a number of 'social parts' with a total nominal value between 10,000 ROL and 100,000 ROL (since 1st July 2005 the official national currency is RON: 1 RON = 10,000 ROL). The nominal value of each social part was of 1,000 ROL. The communist government decided that 30% of the development fund of each socialist enterprise had to be constituted by the contribution of employees. The return of each social part was put at 6% per year if the socialist enterprise fulfilled the benefit target (similar to the net profit target), 8% per year if the benefit was larger than the plan, and a minimum return of 5% per year if the socialist enterprise did not achieve its benefit target. The above rates of return remained in force until they were changed by the Communist State Decision from 1987 from 6% to 4%, from 8% to 6% and respectively from 5% to 3.5 % per year. At least theoretically, the social part owner had the right to participate in the general meeting of employees and to vote on strategic and daily business issues of the enterprise. In practice, employees were forced to contribute to the compulsory growth of the national capital stock by paying for the share of their own monthly wages. At the end of the communist regime, each employee, depending of his or her contribution period, held a small part of the registered stock of national capital. At the beginning of 1990, the total value of 'social parts' was estimated at around 1-1.5 billion USD. After December 1989, one of the first measures of the new government (already criticized by some authors) was to return these accumulated assets ('social parts') to each employee as an amount of money; the remaining part of the capital, held by state enterprises, was to be privatized during the transition period. Then, employee ownership has been created on a new base mainly during the privatization process where citizens obtained shares in the course of mass privatization and insiders in firms privatized by the MEBO method. Some employees also obtained shares in the course of minority interest sales. Finally, workers' co-operatives established before 1989 are still present in the Romanian economy.

The co-operatives have been part of national economy since the second part of 19th century. First co-operatives emerged in urban area in the 1860s, being organized as private associations of savings and loans or as loan co-operatives. After 1903, special co-operative laws were adopted in order to regulate the organization of various types of co-operatives. After the First World War, a new co-operative law was introduced which strengthened state control of the co-operative system. In 1935, the government established several central control institutions. The development of workers' co-operatives represented a central element in the platform of some traditional political forces, such as National Peasant Party (renamed after 1989 as National Peasant Christian Democrat Party - *Partidul Național Țărănesc Creștin Democrat* and recently as Popular Christian Democrat Party – *Partidul Popular Creștin Democrat*), or utopian socialist forces. In 1948, when the Stalinist government came into power, new national co-operative associations were established in order to integrate the co-operatives into the planning apparatus of the communist state. Formally, the old co-operatives remained in place, but many of their fundamental principles were altered. The co-operative system was organised in large centralised associations, such as the National Union of Agricultural Production Co-operatives (*UNCAP*), the National Union of Consumer Co-operatives (*CENTROCOOP*), the National Union of Loan Co-operatives (*CREDITCOOP*), and the National Union of Handicraft Co-operative (*UCECOM*). These co-operative associations became the essential link within the planning chain between the central ministries and individual co-operatives. So, the compulsory planning directives altered dramatically even the essence of co-operatives by suppressing their democratic decision-making rights. In any case, the artificial growth in number of individual co-operatives during communist regime has no significance in matter of genuine co-operative movement in the Romanian economy. In the first years of transition in Romania there was no important change in the co-operative system except the liquidation of the National Union of Agricultural Production Co-operatives, especially under the pressure from former small landowners and from the two major historical parties (National Peasant Christian Democrat Party and respectively National Liberal Party). Several co-operative associations e.g. *CENTROCOOP* and credit co-operatives were involved in financial scandals related to bankruptcies of banks and investment funds.

During the first years of transition, in Romania the method of MEBO was one of the major forms of privatization originated from the old movement supporting employee self-management in state-owned enterprises and the related collection of the 'social parts' during the 1980s. The employee self-management implemented by the Communist Party included a financial contribution by employees to the own funds of state enterprises. Consequently, the employees were formally included in the collective management committees. The total contribution of employees in the framework was estimated in 1990 at around 40 billion ROL (USD 1.5 billion). As in other Central and East European countries, some policy-makers argued that in a market economy with a dominant private sector, the transition to employee ownership was the adequate method for transforming employee control conforming to the institutional requirements of the new order.

The Romanian Privatization Law adopted in 1991 was a compromise between various ideas on privatization: those supporting the employee ownership, commercial methods focused on the capital market development and foreign investment, and the neutral voucher privatization solution benefitting the population as a whole with no privileges for any particular social group. In order to reinforce the MEBO privatization method, a special Law (77/1994) regarding employees' associations and management of companies to be privatized was adopted in 1994.

After 1989, the most widespread scheme of profit-sharing in Romania was the so-called gain sharing, in which the employees receive a bonus at the end of each year depending on their performance and on the general company performance. As a rule, the basis of calculation was the net profit of company. The scheme has its roots in the former communist regime when the employees received a bonus each year. Generally the scheme is applied to all employees. The bonuses are usually paid in addition to the basic fixed wage and provide a variable source of income.

b) Social Partners

At present, employees are represented by a number of large trade union confederations, such as *Confederation of the Democratic Trade Unions from Romania*, *The National Trade Union Confederation 'Meridian'*, *The National Trade Union Confederation 'Cartel ALFA'*, *The National Trade Union Block*, *The National Confederation of the Free Trade Unions from Romania 'Fratia'*. The employers' associations are still more dispersed as trade union movement. At present, eleven employers' associations are registered: *Employers' Confederation from Romanian Industry* ('Confederația Patronala din Industria României' – CONPIROM), *National Confederation of the Romanian Employers* ('Confederația Națională a Patronatului Roman' – C.N.P.R.), *National Council of the Private SME* ('Consiliul Național al Întreprinderilor Private Mici și Mijlocii' – C.N.I.P.M.M.R.), *General Union of the Romanian Manufacturers* ('Uniunea Generală a Industriașilor din România' – UGIR), *General Union of the Romanian Manufacturers 1903* ('Uniunea Generală a Industriașilor din România 1903' – UGIR 1903), *National Council of the Romanian Employers* ('Consiliul Național al Patronilor din România' – C.N.P.R.), *Romanian National Employers' Association* ('Patronatul Național Roman' – PNR), *Romanian Employers' Association* ('Patronatul Roman' – PR), *National Union of the Romanian Employers* ('Uniunea Națională a Patronatului Roman' – UNPR), *Romanian Association of the Contractors* ('Asociația Română a Antreprenorilor de Construcții' – ARACO), and *Employers' Confederation from Industry, Services and Trade* ('Confederația Patronala a Industriei, Serviciilor și Comerțului' – CPISC).

The general framework for discussions among the social partners is represented by an institutionalised structure 'The National Social and Economic Council', which is functioning on the base of the Law 109/1997, amended by the Laws 492/2001 and 58/2003 and is comprised of representatives of the government, of trade unions and employers' associations. The consultations and negotiations with trade unions are important for the employers because the unions still hold a very strong position within the National Social and Economic Council. Moreover, in many cases of privatization

of utilities and oil and gas industry, employees purchase shares through trade unions because the unions are very strong and have substantial influence in these sectors and they have the right to appoint at least one member in the board of administration in these industries. In some cases (e.g. sale of 8% from the social capital of the PETROM Company representing a total value of about 200 million EUR) the trade unions tried to achieve an amendment of the relevant law, so that not individual employees, but employees' associations controlled by the trade unions become purchasers of offered shares. Such cases show that the interests of trade unions and of their legal representatives are sometimes contrary to the interests of individual employees and that trade unions also tend to achieve their goals at the expense of employees' rights.

Neither trade unions nor employers' associations have addressed the issue of financial participation of employees as yet.

c) Current National Policy

At present, the problem of the financial participation of employees is not given priority by the government or political parties because other problems, affecting big parts of the population, are more urgent, such as reforming the pension system, social system, and agriculture. Moreover, taking into account the actual stage of economic restructuring and the evidently weak corporate governance in Romania, the problem of the financial participation of employees is rather approached punctually by managers within multinational or national companies that were better adapted to the rigours of the global market. The only aspect of financial participation of employees addressed by the government is the sale of minority shares to the employees in public enterprises where privatization is underway in such sectors as utilities (or the so-called *Régies autonomes*), oil and gas and banking, but also such state companies as National Lottery (*Loteria Națională*) and the National Printing House (*Imprimeria Națională*), which emits fiscal stamps, fiscal documents, etc. Since, in some of these privatization cases, trade unionists and representatives of political parties are suspected of insider deals and corruptive practices at the expense of employees, the credibility of the governmental support of financial participation of employees is relatively low for the general public.

2. Types of Schemes and their Legal Foundations

Currently, the Romanian law does not contain a systematic legal framework regulating employee's financial participation. However, several laws linked with the privatization process were passed, which had an impact on the extent to which the concept of employee's participation has been spread. Share ownership is by far the most popular form of employees' financial participation, while the concept of employee profit-sharing is still scarcely used in practice. Respectively, there are more legal regulations concerning share ownership than profit-sharing.

a) Employee Share Ownership and its Legal Foundations

(1) Privatization Issues

Privatization laws encouraged the development of employee share ownership strongly by implementing the idea of a broad re-distribution of state-owned funds to the population. While at the beginning of the 1990s policy-makers favoured a more abstract participation scheme by issuing privatization vouchers, the new Laws 55/1995 on the Acceleration of the Privatization Process and 77/1994 on the Associations of Employees and Members of the Management in Companies in the Privatization Process promoted a different approach, by which the shares of individual enterprises were to be distributed directly to the employees and the management of the respective companies.

As in most transition economies, the Law 58/1991 on Privatization contains various methods of privatization, namely direct sale to investors, recapitalization by foreign or national investors, management buy-out and share sales to other investors. Besides, Law 58/1991 regulates a voucher privatization scheme which evolved into a first sub-structure for spreading shares among a larger part of the population. However, the main regulative intention of this legal act was not the specific encouragement of employee participation, but rather the arrangement for a general financial participation of the population in the assets of the former socialist patrimony as a part of national wealth¹. The law set up a quota of 30% of shares to be transferred² applying different methods mentioned above. Voucher privatization was the main focus of the Law 58/1991 on Privatization.

As shown in this study, voucher privatization did not lead to a significant spread of employee ownership among the population. The main reason from a legal perspective is the absence of any incentive to promote employee participation in the Law 58/1991 on Privatization. The voucher privatization was implemented by allocating property

¹ Art. 1 Law 58/1991 on Privatization defines the aim of the law: 'The Law on Privatization stabilizes the legal framework for the transfer of state property into private property of physical persons and legal entities.'

² See the introduction of the Law 58/1991 on Privatization.

vouchers to the resident population. As regulated by Art. 3 of the Law 58/1991 on Privatization, there are two main opportunities to use the property vouchers. One is to swap the vouchers for shares of privatized companies within a period of five years, the other is selling the vouchers to somebody else, as they are freely tradable according to Art. 3 lit. a) of Law 58/1991 on Privatization. This last opportunity was extensively used by the population, which, to a large extent, rather used the proceeds for consumption than for company shares of enterprises with uncertain business perspectives; besides, this practice led to a significant concentration of vouchers in the hands of interested persons. Voucher privatization rules did not contain any preferential conditions for employees to buy shares of the firm they were employed by, so the interest of share buyers centred around companies with allegedly good business perspectives. Additionally, the law comprised no mechanism which provided the companies whose shares were exchanged for privatization vouchers with fresh financial means, so the interest of the company to convince their own employees to trade their vouchers into shares of the company was also quite limited. As a result, one could rather speak of legal incentives to avoid share ownership by employees than to support it.

By means of Law 55/1995 on the Acceleration of the Privatization Process, the aim of a 30%-quota of free of charge privatization was reemphasized³. For this purpose, the privatization agency established a list of suitable enterprises and issued the so called 'nominal value vouchers for privatization' (*cupoane nominative de privatizare*) to be spread among the resident population. Only persons who had not made full use of their property vouchers received according to Law 58/1991 were granted the new vouchers for privatization. The main difference to the system used by Law 58/1991 on Privatization was that the new⁴ vouchers were not tradable⁵; if the vouchers are sold in spite of the non-tradability, they shall become void. According to Art. 4 Abs. 2 of Law 55/1995 on the Acceleration of the Privatization Process, the new vouchers could only be exchanged for the shares of just one company while the property vouchers emitted according to Law 58/1991 on Privatization could still be used for the purchase of shares of one or more different companies.

For the first time, the new law contained a real incentive for employee financial participation. While the general public owning the afore mentioned nominal value vouchers for privatization could trade their vouchers only for shares of companies to be chosen from a list of suitable enterprises issued by the privatization agency, Art. 5 of the Law 55/1995 on the Acceleration of the Privatization Process offered the opportunity for certain persons to acquire shares of non-listed companies in exchange for their vouchers. This was possible for employees and the management of state companies who were interested in exchanging their vouchers for shares of the company they were employed by⁶. The same privilege was granted to former employees (pensioners or un-

³ Art. 1 para. I of Law 55/1995 on the Acceleration of the Privatization Process.

⁴ Art. 2 para. II of Law 55/1995 on the Acceleration of the Privatization Process.

⁵ For the property vouchers emitted according to Law 58/1991 only the sale to foreigners was prohibited, Art. 22 Law 58/1991 on Privatization.

⁶ Art. 5 lit. a) and b) of Law 55/1995 on the Acceleration of the Privatization Process.

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employed) who had their last employment contract with the respective firm. Besides, this opportunity was open to farmers with continuous economic relationships with companies of the agricultural sector (dairies, slaughter houses and other agricultural processing enterprises) without being actually employed by these companies⁷. This last provision accounts for the economic situation of farmers which is in some respects similar to that of employees (e.g. strong dependency on certain regional processing enterprises with regard to their respective production focus).

As shown above, the first Law on Privatization (58/1991) did not provide for incentives for MEBO privatization in the process of voucher (mass) privatization. Nevertheless, the Law on Privatization contains regulations on preferential treatment for employees and management with regard to the sale of shares through the national Privatization Agency (*Fondul Proprietii de Stat*). Besides the general right to participate in the privatization of companies⁸, Art. 48 of Law 58/1991 on Privatization regulated the details to be observed by the Privatization Agency when selling shares in the privatization process. According to this provision, employees (including management) of the respective enterprise had a pre-emptive right to purchase the offered shares on advantageous conditions. In case of a fixed price sale the MEBO share price had to be 10% lower than the public price; in case of a sale by means of competitive bidding sale the MEBO offer has to be accepted by the Privatization Agency as long as the offered price is not lower than 90% of the highest public bid. This preferential treatment was extended also to the direct sale procedure where the MEBO offer had to be accepted by the Privatization Agency in the case of an equal negotiation result with other interested parties.

A second step for promoting MEBO privatization models came with the Rule 1/1992 on the Standard Procedure for the Privatization of Small Enterprises by the Sale of Shares which came into force in January 1993. Although focused on the privatization of so-called ‘small enterprises’⁹, this regulation defines the MEBO method as the standard privatization procedure. The MEBO privatization had to be implemented by means of direct negotiations with interested employees and management staff, having priority over the second method which is defined as a more or less public tender procedure. The procedure is aimed at selling either all or at least a majority part of the shares to the employees. However, the shares were not acquired directly by the participating employees but by an incorporated association of share owners¹⁰.

⁷ Art. 5 lit. e) of Law 55/1995 on the Acceleration of the Privatization Process.

⁸ This is regulated by Art. 47 of Law 58/1991 on Privatization.

⁹ The maximum size of these enterprises is determined by the number of persons employed on average within the reporting year which is set to 50 employees; see annex 2 of Government Decision 10/1992 on the Approbation of the Statute of the Privatization Agency, published in M. Of. 208/1992.

¹⁰ This association is called ‘*Programul acțiunilor salariaților*’ [Employee’s Share Program]. When the law came into force there was no special legislation governing this specific kind of associations, therefore the old Law 21/1924 on Legal Entities has been effective until Law 77/1994 on Associations

With some delay the Parliament passed special legislation. The Law 77/1994 on Associations of Employees and Members of the Management in Companies in the Privatization Process provided specific regulations required for a widespread use of this MEBO privatization model. It allowed employees and management of partly or fully state-owned enterprises which were to be (fully or partially) privatized to establish the so-called 'management and employee associations'¹¹. The number of associations was limited to one for each enterprise to be privatized, so any competition between associations between the purchase of one specific enterprise was excluded by law. The membership in the association is voluntary, but it is also a precondition for making use of the advantages and exclusive rights with the result that every employee seriously considering the purchase of shares has to become member of the respective association. The law states that a minimum of 30% of the total employees and management staff has to participate in establishing the association. Associations can only perform activities listed in the Law 77/1994. As mentioned above, the associations were granted specific rights in the privatization process which offer advantages to insiders. So the enterprise has to disclose all relevant commercial and financial information to the founding committee of the association; also the costs for a feasibility study in the preliminary stages of the buy-out have to be borne by the enterprise. The association buys and administers the shares for the members. The membership is open to employees with unlimited labour contracts with at least half-time employment and to members of the management of the respective enterprise. Furthermore, former employees, both unemployed and pensioners, belong to this privileged group¹². The main decision-making body of the association is the general meeting in which each member of the association has one vote. The general meeting decides on the association statute which must contain strict rules with regard to the distribution of the shares purchased by the association. The association purchases the shares as a representative of individual members as far as the members pay for the shares with cash or offer privatization vouchers in exchange for them.

The shares obtained this way are distributed directly to the members and administered by themselves. Yet the main advantage of the association scheme in comparison to the individual purchase of shares is to be found in the use of credit facilities offered either by the Privatization Agency itself or by external banks. In this case the shares are not bought in representation of individual members but in the name of the entire association; the shares are not distributed directly to the individual members, but kept by the association as long as the shares are not entirely paid off serving as credit securities during this period. The shares are distributed offering pre-emptive rights to the mem-

of Employees and Members of the Management in Companies in the Privatization Process containing special regulations came into force.

¹¹ The Romanian term is '*asociații salariaților și membrilor conducerii*'.

¹² For details see also Art. 3 of Law 77/1994. Besides the above mentioned category of farmers and agricultural workers (persons with continuous economic relationships with companies of the agricultural sector - dairies, slaughter houses and other agricultural processing enterprises - without being actually employed by these companies) may become members of the employee's association.

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bers taking in consideration criteria like employment duration, the position in the firm and the salary. In case the right of pre-emption is not exercised by members, the respective shares may be distributed to new employees of the enterprise. As soon as all shares are distributed to the members, the association has to be dissolved.

The Law 77/1994 additionally offers quite advantageous instalment options¹³ for shares purchased by the employees and management associations. This starts with a low advance payment and is complemented by a minimum repayment period of five years and a maximum interest rate of 10% per year. Against the background of a high inflation rate during the 90ties especially the interest rate limit turned out to be remarkably advantageous.

Law 58/1991, 77/1994 and 55/1995 have been merged into a single privatization law by Emergency Ordinance 88/1997 which came into force on the 1 January 1998 which itself has been modified several times (the last significant modifications brought by Ordinance 36/2004¹⁴). While the voucher privatization came to an end at this time (no more new vouchers being issued while the tradability of the old vouchers was restricted by several legal deadlines), the legislation on MEBO privatization remained in force for the most part. Emergency Ordinance 88/1997 only defines a rough legal framework for the employee shareholder associations and refers for the details to the general legal provisions governing associations and foundations.

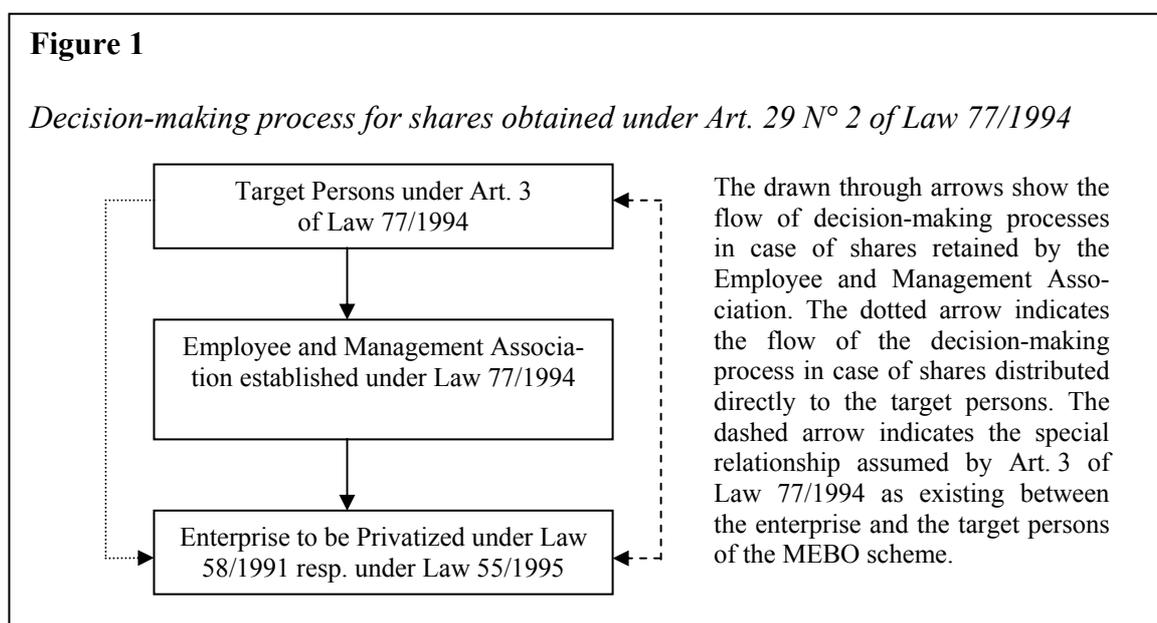
As shown in this study, voucher privatization did not lead to a significant spread of employee ownership among the population. The main reason from a legal perspective is the absence of any incentive to promote employee participation in the Law 58/1991 on Privatization. The voucher privatization was implemented by allocating property vouchers to the resident population. As regulated by Art. 3 of the Law 58/1991 on Privatization, there are two main opportunities to use the property vouchers. One is to swap the vouchers for shares of privatized companies within a period of five years, the other is selling the vouchers to somebody else, as they are freely tradable according to Art. 3 lit. a) of Law 58/1991 on Privatization. This last opportunity was extensively used by the population, which, to a large extent, rather used the proceeds for consumption than for company shares of enterprises with uncertain business perspectives; besides, this practice led to a significant concentration of vouchers in the hands of interested persons. Voucher privatization rules did not contain any preferential conditions for employees to buy shares of the firm they were employed by, so the interest of share buyers centred around companies with allegedly good business perspectives. Additionally, the law comprised no mechanism which provided the companies whose shares were exchanged for privatization vouchers with fresh financial means, so the interest of the company to convince their own employees to trade their vouchers into

¹³ Regarding to Art. 52 of Law 77/1994 the Privatization Agency is bound by these conditions. Furthermore, the Agency has to accept a certain amount of privatization vouchers (property vouchers) in exchange for the shares to be transferred.

¹⁴ M. Of. No. 90/2004.

shares of the company was also quite limited. As a result, one could rather speak of legal incentives to avoid share ownership by employees than to support it.

For the first time, Law 55/1995 contained a real incentive for employee financial participation. While the general public owning the afore mentioned nominal value vouchers for privatization could trade their vouchers only for shares of companies to be chosen from a list of suitable enterprises issued by the privatization agency, Art. 5 of the Law 55/1995 on the Acceleration of the Privatization Process offered the opportunity for certain persons to acquire shares of non-listed companies in exchange for their vouchers. This was possible for employees and the management of state companies who were interested in exchanging their vouchers for shares of the company they were employed by¹⁵. The same privilege was granted to former employees (pensioners or unemployed) who had their last employment contract with the respective firm. Besides, this opportunity was open to farmers with continuous economic relationships with companies of the agricultural sector (dairies, slaughter houses and other agricultural processing enterprises) without being actually employed by these companies¹⁶. This last provision accounts for the economic situation of farmers which is in some respects similar to that of employees (e.g. strong dependency on certain regional processing enterprises with regard to their respective production focus).



Law 77/1994 on Associations of Employees and Members of the Management in Companies in the Privatization Process finally provided specific regulations required for a widespread use of the MEBO privatization model by establishing a legal framework for this kind of specific-purpose-associations, offering privileged access to com-

¹⁵ Art. 5 lit. a) and b) of Law 55/1995 on the Acceleration of the Privatization Process.

¹⁶ Art. 5 lit. e) of Law 55/1995 on the Acceleration of the Privatization Process.

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pany information as a means of financing the purchase of shares, While Law 77/1994 itself was replaced by Emergency Ordinance 88/1997, most of the incentive regulations for MEBO privatization has been transferred to this new law which is still in force today.

As shown above, the privatization procedure for small enterprises was aimed at selling all or at least a majority part of the shares by means of the MEBO method. The result of a successful privatization under this regulation was also the acquisition of the majority voting rights for the benefit of the participating employees. However, as the shares obtained via instalment options are not acquired directly by the employees and the management staff but by the interposition of an association with autonomous legal personality, also the voting rights have to be exercised by this association. The extent of participation in decision-making therefore depends on the decision-making procedure inside this association and the way the member decisions are transferred to the general meeting.

(2) Company and securities law

(a) Corporations

The legal framework with regard to the Romanian company law is defined by Law 31/1990¹⁷ on companies, republished in November 2004 and recently modified (October 2005)¹⁸. The Law contains some specific regulations regarding employee share ownership and the distribution of shares to the employees which will be dealt with subsequently. However, it provides no legal means for a privileged participation of employees in decision-making. There are various provisions protecting the interests of minority shareholders.

Romania has only partially made use of the tools/exceptions offered by the Second Council Directive 77/91/EEC of 13 December 1976 to promote employee financial participation by means of corporate law. Regarding the permission to acquire the companies' own shares for its employees (Art. 19 III Council Directive 77/91/EEC) Art. Art. 104 lit. b) Law on Companies offers an exception with respect to the acquisition of shares for the personnel of the company; this regulation contrasting to the restrictive general regulation of this kind of transfers in Art. 103 Law on Companies, which requires an extraordinary shareholder's meeting in case the company intends to acquire its own shares. The second exception the Romanian legislator made use of is Art. 105 para. III Law on Companies modeled after Art. 23 Council Directive 77/91/EEC (encouragement of share acquisitions by employees by the permission to advance funds, make loans or provide security, with a view to acquisitions). While Art. 105 Law on Companies specifically prohibits any advancement of funds, the issu-

¹⁷ M. Of. No. 33/1990.

¹⁸ The most recent amendment/modification incorporated here was done by Law 302/2005, published in M. Of. No. 953/2005.

ing of loan schemes or the providing of securities with the purpose of encouraging the acquisition of shares by any third party, para. III of this article provides an exception to this rule in case the shares are purchased by employees of the company.

Additionally, there are some provisions protecting the rights of minority shareholders: preference shares without voting right are limited to 25% of the total share capital; the number of votes attached to one share may be limited only for the holders of more than one share; a shareholders' meeting has to be called on request of the shareholders representing a minimum of 10% of the total share capital; various information rights with regard to accounting issues; right to apply to the court for a detailed financial audit by shareholders representing a minimum of 10% of the total share capital. Currently, there is no squeeze-out or sell-out regulation in Romanian company law.

As the preceding paragraph shows, there are some incentives to stimulate employee share ownership on company shares in Romania. These incentives comprise primarily simplifications of the redemption process of company shares by the respective company itself as far as the repurchase operation is directed at the acquisition of shares for the companies' employees. Further, we find some opportunities to provide for some financing facilities for the target group of the share acquisition. However, Romania did not make use of all instruments offered by Council Directive 77/91/EEC, as there is the opportunity to increase the share capital and the use of profits given to employees to buy new shares, no derogation with regard to Art. 41 para. I Council Directive 77/91/EEC designed to encourage participation of employees and also no suspension for companies to issue collectively held workers' shares as offered by Art. 41 para. II Council Directive 77/91/EEC.

While the old legislation before 1990 emphasized employees' participation in decision-making in an almost redundant way¹⁹, the privatization laws passed since 1990 contain no special regulations concerning this issue. Also the notion of employee's co-determination, like in German law, was not introduced. The new Labour Code from 2003²⁰ as well as the nation-wide collective agreement with the trade unions from 2005²¹ contain regulations for some kinds of compulsory consultation procedures to be carried out if changes to the labour conditions are intended by the management.

As shown above, the privatization procedure for small enterprises was aimed at selling all or at least a majority part of the shares by means of the MEBO method. The result of a successful privatization under this regulation was also the acquisition of the majority voting rights for the benefit of the participating employees. However, as the shares obtained via instalment options are not acquired directly by the employees and the management staff but by interposition of an association with an autonomous legal per-

¹⁹ The old Labour Code from 1972 alone mentions this concept in more than 20 articles, admittedly with virtually no implications to the practice.

²⁰ Law 541/2003 on the Labour Code, M. Of. No. 913/2003.

²¹ The validity period for the current agreement is the year 2005 and 2006; the content is accessible via the website of the Ministry for Labour, Social Security and Family issues (<http://www.mmssf.ro/>).

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sonality, the voting rights have also to be exercised by this association. The extent of participation in decision-making therefore depends on the decision-making procedure inside this association and the way the member decisions are transferred to the shareholders' meeting.

(b) Co-operatives

As mentioned above, Romania has a strong tradition of co-operatives which dates back to the 19th century. This is still so with regard to specific economic sectors, like agriculture, trade and crafts enterprises. The recently revised Law on Co-operatives²² reiterates the important role of co-operatives in the Romanian economy. According to the new Law on Co-operatives, there are now two types of co-operatives. While the so called 'type I'-co-operatives consist exclusively of physical persons, 'type II'-co-operatives provide a legal structure for the merger of 'type I'-co-operatives into larger legal entities. The Law determines that every member has one vote at the general meeting irrespective of the number of co-operative shares actually held by the respective member. For the newly introduced 'type II'-co-operatives²³ the Law even limits the maximum share hold by one co-operative member to 20%. Both measures are aimed at limiting the economic influence of single co-operative members preserving democratic decision-making structures inside the co-operatives. Liability is generally limited to the co-operative capital; this may be exceeded in certain cases of civil or penal liability. Profits are distributed in accordance with the participation structure under consideration of the labour contribution of the respective member.

With the new legal framework implemented in 2005 the Law on Co-operatives has been freed of bureaucratic limitations, the newly introduced 'type II'-co-operatives offering a legal structure for the establishment of larger economic units governed by the co-operative decision-making process and thus supporting co-operatives which should play a more significant role in the Romanian economy. The decision-making process in Romanian co-operatives is particularly characterised by the one 'one member one vote'-principle, which ensures a member based decision-making process in co-operatives in contrast to the decision-making process in corporations which is primarily linked to the fraction of the share capital owned by the respective participant.

²² Law 1/2005 on Co-operatives, M. Of. No. 172/2005.

²³ This new type is designed as a sort of parent co-operative which has several type-1 co-operatives as members and is aimed at increasing economic significance of co-operatives in certain trade environments.

(c) Partnerships

'Partnerships' are not represented by a specific legal concept in Romania. Practically, only partnerships under civil law and the so called 'family associations' can be considered to represent a similar business form. Both are basically governed by the Civil Code, supplemented by special laws which stipulate this legal structure as compulsory for certain types of businesses, as there are lawyers or accountants. E.g., Art. 5 of Law 51/1995 on Attorneys-at-law stipulates this legal structure as the only possible business form for an association of two or more lawyers. In 2004, the Law was modified, so that a limited liability partnership is also a permissible business form²⁴. By choosing this form of organization the partners are still jointly liable but may limit this liability to the amount of 10,000 Euros which is the minimum capital required by law.

Incentives are mainly provided by the regulations which declare the legal form of association mentioned above as compulsory; on the other hand, this is the legal structure typically governing small-scale economic activity, as formal requirements of establishing, e.g. a family association are virtually non-existent. As in other legal surroundings outside Romania partnerships work well as long as the partners do not seriously disagree on fundamental issues with regard to the partnership. If this occurs, a split-up of the partnership is often inevitable.

b) Profit-Sharing

There is no special regulation on profit-sharing, with the exception of profit-sharing in state or municipal enterprises which are either constituted in the legal forms provided for by Law 31/1990 on Trading Companies with the state as single or majority owner or in a specific legal structure which is still widely in use with regard to public utilities²⁵. In 2001 the government passed the Ordinance 64/2001 on the Repartition of Profits Obtained by State and Municipal Companies with the State as Single or Majority Owner²⁶. The ordinance regulates the details of profit distribution, such as reserve funds, payouts to the owners and the coverage of losses from previous years. In Art. 1 lit. e), the ordinance also contains a provision which sets the maximum payout rate for employee profit-sharing to 10% of the overall profit of the enterprise. There is currently no provision regarding a minimum rate, also it should be noted that the number of state firms actually making profit is still low. Nevertheless, the Ordinance 64/2001 is one of the few laws expressly dealing with the issue of employee profit-sharing. Against the background of the pronounced encouragement of MEBO privatization schemes, profit-sharing in these companies should be widespread as a side effect of share ownership. As the MEBO privatization policy favoured particularly the sale of

²⁴ The details are governed by the newly introduced Art. 51 of Law 51/1995.

²⁵ This form is called *regie autonoma* and is governed by specific regulations.

²⁶ Ordinance 64/2001 on the Repartition of Profits Obtained by State and Municipal Companies with the State as Single or Majority Owner, published in M. Of. No. 536/2001; the regulation abrogated earlier regulations, e.g. Ordinance 23/1996 on the same issue.

smaller enterprises, profit-sharing schemes should be overrepresented in the sector of small- and medium-sized firms.

c) Taxation Issues

With the new Tax Code from 2003²⁷ and several amendments introduced by the new centre-right government in 2004²⁸, taxation has become an area not only of rapid changes, but also of some thorough simplification and reduction of the applicable tax rates. As a part of this policy the number of tax quotas has been reduced, while a general tendency of convergence was developed²⁹. As a side effect of this policy the applicable quotas are less different from each other. The actual rate for the taxation of income from dividends is 10%³⁰ while the general income tax rate is 16%. The uniform rate is also applicable to every form of income from profit-sharing schemes. This also implies that there is less space for the promotion of specific investment forms by means of a different design of tax quotas.

3. Incidence Now and Over Time

Comparing to other Central and East European countries, Romania experimented with various alternatives of privatization that took long time to develop and today still remained a large remaining privatization agenda. After more than ten years of transition, only 40% of the total number of large enterprises and around two-thirds of its medium-sized enterprises are privatized. According to the last available data, at the end of 2003 there were about 1,300 state-owned enterprises and another 600 enterprises de facto under state control. This number is larger than the total number in the rest of Central and Eastern European countries combined (World Bank, 2004).

a) Mass Privatization

Mass privatization is characterised by the distribution of vouchers of ownership to citizens, held in private funds representing 30% of the privatized company's capital stock. As the initial privatization process was not a success and some people accumulated a significant part of the total number of vouchers issued, the next Law (55/1995) introduced a new form of mass privatization. Only in a limited number of cases when they

²⁷ The Tax Code from 2003 covers about 95% of all taxes in Romania, M. Of. No. 571/2003.

²⁸ Emergency Ordinance of the Government 123/2004 on the Modification of the Tax Code, M. Of. No. 1154/2004, which came into force on the 1 January 2005.

²⁹ So a flat income tax rate of 16% has been established, which covers almost all kinds of income with very limited facilities for deduction.

³⁰ The same rate applies to income from investment funds.

were organised within a strong employees' association the employees used their vouchers/vouchers to buy a large amount of shares and became important shareholders.

b) MEBO Method

In a classification provided by EBRD (2002), in case of Romania MEBO is noted as the primary method of privatization. This method of privatization has been used most frequently since the start of transition (World Bank, 2004). Privatization by MEBO started even before the mass privatization programme, its heyday registered in 1995-1996 and developed into 1997, when the practice largely ceased. It is estimated that, by the end of 1998, over a third of all industrial firms in the State Ownership Fund had undergone MEBO privatization (with average employee ownership of 65%). In addition, MEBO participants were the largest owner group in one-fourth of the Romanian privatized firms, which makes this method the most important tool of state ownership divestiture in the country (Earle and Telegdy, 2002, p. 8). However, when the Romanian legislative adopted regulations on MEBO in 1994, it also introduced legislation encouraging mass privatization with more favourable taxation. This drastically reduced new opportunities for employee ownership through MEBOs. Two features of the process made it unique in the region (Earle and Telegdy, 2002; World Bank, 2004): 1) The ownership share that went to insiders (MEBO privatization) was very large – 65% on average, with a median employee ownership of 71%. To the extent that there was any outside ownership, mostly through residual mass-privatization shares, it could play no role in corporate governance; and 2) Usually, the entire stake was transferred to employees, so the method should really be considered employee buy-outs. The role of MEBO method within the general privatization process in Romania is highlighted in the following three tables:

Table 1. Management-employee buyout privatizations in Romania, 1992-2000:II

	1992	1993	1994	1995	1996	1997	1998	1999	2000:II	Total
# of firms	19	249	565	479	509	378	267	336	46	2,632
Mean % privatized	87.5	98.9	97.1	79.8	43.7	37.3	49.0	57.3	57.5	70.8
Median % privatized	100.0	100.0	100.0	95.0	40.0	40.0	42.0	52.0	66.0	73.0
#majority privatized	16	247	553	376	113	21	105	183	27	1,652

Source: Labour Project privatization database; Earle and Telegdy (2002) - Privatization Methods and Ownership Outcomes in Romania.

3. Incidence Now and Over Time

Table 2. The post-privatization ownership structure, by year

(average % of shares weighted by employment)

	1992	1993	1994	1995	1996	1997	1998	1999	2000:II
MEBO participants	0.4	4.0	10.8	21.2	25.3	26.2	27.5	29.8	30.4
MPP participants	0.0	0.0	0.0	0.0	17.6	17.6	17.6	17.6	17.6
Outside investors, of which:	0.3	0.5	0.8	1.9	2.7	5.1	9.2	16.3	20.1
- Domestic individuals	0.1	0.1	0.1	0.1	0.2	0.4	0.8	1.8	3.4
- Domestic institutions	0.2	0.2	0.4	1.1	2.1	3.3	5.0	8.8	11.0
- Foreign investors	0.0	0.2	0.3	0.4	0.4	1.4	3.4	5.7	6.7
Others	0.0	0.4	0.8	1.2	1.6	2.0	2.6	3.2	3.3
Total Private	0.8	4.9	12.4	24.0	47.3	50.8	56.9	66.8	72.3
State	69.5	66.8	61.7	53.5	43.5	40.2	34.5	25.1	19.7
POF/SIF	29.8	28.3	25.9	22.5	9.2	9.0	8.6	8.1	8.0

Notes: Number of firms: 7,307. 'Others' refers to privatization transactions with non-identified owners. Employment figures from 2000. 'MPP' means Mass Privatization Program. Source: Labor Project privatization database; Earle and Telegdy (2002) - Privatization Methods and Ownership Outcomes in Romania.

Table 3. The post-privatization ownership structure, by year

(average % of shares weighted by book value)

	1992	1993	1994	1995	1996	1997	1998	1999	2000:II
MEBO participants	0.0	0.3	1.1	4.7	6.9	7.3	8.1	10.0	10.5
MPP participants	0.0	0.0	0.0	0.0	15.1	15.1	15.1	15.1	15.1
Outside investors, of which:	0.0	0.0	0.1	0.6	1.8	4.4	8.5	18.4	24.2
- Domestic individuals	0.0	0.0	0.0	0.0	0.0	0.1	0.3	1.7	3.2
- Domestic institutions	0.0	0.0	0.1	0.5	1.7	2.9	5.0	9.7	12.5
- Foreign investors	0.0	0.0	0.0	0.1	0.1	1.4	3.2	7.0	8.5
Others	0.0	0.3	0.7	1.0	1.4	2.0	2.6	3.3	3.3
Total Private	0.0	0.7	1.9	6.4	25.2	28.9	34.4	46.8	53.2
State	70.0	69.7	69.1	66.1	61.5	58.2	53.3	41.5	35.2
POF/SIF	30.0	29.6	29.0	27.6	13.3	12.9	12.3	11.7	11.6

Notes: Number of firms: 7,418. 'Others' refers to privatization transactions with non-identified owners. Book value from 2000. 'MPP' means Mass Privatization Program. Source: Labor Project privatization database. Earle and Telegdy (2002) - Privatization Methods and Ownership Outcomes in Romania.

In case of Romania, more recent data are difficult to be obtained because after 2001 the control over the privatization process was divided between several ministries: the Ministry of Tourism (today: the National Authority for Tourism) already privatized the whole patrimony from tourism either by selling of assets or by selling of shares; a large part of companies in industrial sector are under the administration of the Ministry of Economy and Commerce – Office for the privatization of industrial enterprises (gas, petrol, electric power, main companies from industry, former and actual companies from military industry, research institutes, etc.); the Ministry of Transport (companies of air, naval, rail and road transport and infrastructure – harbours, railways, air-

ports, etc.); Ministry of Communications (Romanian Post, Society of Radiocommunications, etc.). Around hundred commercialized companies remained within jurisdiction of the Authority for Privatization and Management of State Ownership – AVAS (*Autoritatea pentru Valorificarea Activelor Statului*), former the State Privatization Agency – APAPS (*Autoritatea pentru Privatizare si Administrarea Participatiilor Statului*), many of them being in a process of judicial liquidation.

c) Minority Interest Sales

After 1999, the method of selling minority interest to employees was introduced in order to involve the employees in the privatization process of major companies; often there were some schemes of preferential treatment for the employees in individual enterprises. The stake size is between 8% and 10% of the total number of shares issued at the time of privatization. This method was used especially in the privatization process of banking system where it covers about 12-18 thousand employees that paid about EUR 50-70 million. In the case of banking system, the employees purchase the shares as individual persons and not as employees association. The Privatization Law did not offer to employees an instrument for their participation in the decision-making process. In addition, the current privatization legislation favours strategic investors because the State Ownership Fund is aiming at increasing the share capital with the value of investment engaged. It resulted in a continued and irreversible reduction in the importance of minority shares held by employees or other small shareholders. In these circumstances, the majority of employees were encouraged to sell their own shares.

d) Co-operatives

After 1989 co-operatives (especially handicraft co-operatives) registered an accelerated decline, as number of their members, as fixed assets, and as volume of economic activity. For instance, in the period 1991-1997 the share of co-operative ownership in total tangible fixed assets declined from 1.2% to 0.3% (after 1998 published data included coops in 'private sector'). As the official published data show, only between 2000 and 2003, the share of co-operatives in total employment decreased from 0.4% to 0.2%. According to the Household Labour Force Survey 2003, agricultural holdings and co-operatives had approx. 17,000 members in the reporting year.

Today, the co-operative system in Romania includes three National Co-operative Unions: The National Union of Consumer Co-operatives comprises a number of 1,405 co-operative members with over 0.8 million persons. The Union operates in the wholesale and retail trading, hotels, public food supply, etc. The National Union of Handicraft Co-operatives (*UCECOM*) produces a large variety of products and services delivered in 21 industrial branches and over 140 fields of activity and are spread all over the country. Also, *UCECOM*, as an apex association, is the representative organization for the whole system of handicraft co-operatives in relation with Romanian authorities, other national bodies and international co-operative organizations.

CREDITCOOP is the Central House of credit co-operative system. This system includes 16 county branches and 133 co-operative members. At the end of December 2004 the co-operative equity was 970 billion ROL (24 million EUR) and the total of assets was evaluated at 3,688 billion ROL (93 million EUR).

Table 4. Number of co-operative societies

Year	Registered with Trade Register		of which: Active economic units	
	Total	of which: New economic units	Total	of which: Newly created economic units
1993	4,042	424	899	334
1994	4,176	134	967	235
1995	4,357	181	1,230	447
1996	4,505	148	1,621	394
1997	4,652	147	2,094	464
1998	4,160	492	2,236	88
1999	5,037	732	2,400	198
2000	5,093	54	2,503	10
2001	5,208	105	2,488	88
2002	5,294	37	2,322	-
2003	5,347	53	2,236	-

Notes: A co-operative enterprise includes one or several companies with co-operative capital. Source: National Institute of Statistics.

Within the co-operative system in Romania, only those from the second group (Handicraft Co-operatives) are proper workers' co-operatives (including the mentioned number of about 17,000 members in 2003, according to the Household Labour Force Survey).

e) Profit-Sharing

The most commonly used scheme of profit-sharing is the direct payment of bonuses to the workers in cash, which is usually referred to as 'cash-based profit-sharing' arrangements. This scheme in case of public sector is used in the case of the 'Fund of Employee Profit Participation'. This method is applied in state-owned companies and consists of the allocation of 5%-10% of the net profit for distribution to employees depending on their performance and contribution to the final financial result of companies. The scheme is used in the banking and insurance systems, mining industry, aluminium industry, etc. The scheme and its derivative versions may cover more than one million employees.

4. Empirical Evidence of Economic and Social Effects

During the first decade of transition the predominant methods of privatization were insider privatization and mass privatization. As a consequence, the ownership was highly fragmented, the management was inadequately qualified, and enterprises had no sufficient fresh capital for restructuring and investment. This led to inefficient corporate governance and, as a general characteristic, to a significant delay in promoting a decisive privatization process. This was accompanied by soft budget constraints, large arrears to the government, the utilities, and the financial sector. Many inefficient enterprises were kept in function and even efficient enterprises were indirectly encouraged to accumulate arrears, blocking their incentives to restructure. Moreover, the insider methods often lead to informal ties between politicians and managers. The powerful insiders such as trade unions not only influenced the choice of privatization tools but also blocked the divestiture of state enterprises.

In Romania, as in other Central and Eastern European countries, outsider privatization generally made a more efficient restructuring possible. Especially enterprises privatized by foreign investors showed higher capital intensity, labour productivity and profitability than insider-owned enterprises. Unfortunately, in Romania, there are no statistics, surveys or case studies regarding the economic performance of different ownership structures. Only at the level of the whole private sector there are available statistical data. Due to the extension of privatization process, the share of private enterprises in national economy increased continuously. In 2003, the share of the private sector in GDP was 70.4% and in the total number of employees of 63.2%. Private enterprises showed a higher productivity than state enterprises.

5. Conclusions

The current level of financial participation of employees is relatively low due to the recent change of orientation in economic policy towards sale to strategic outside investors, including foreign investors. The prevailing form is employee share ownership which emerged in the course of privatization, mainly by the MEBO method. Presently, there are only few cases of profit-sharing, but their number increases gradually.

Mass privatization and MEBO were the major privatization methods at first stages of transition, but, in the last years, the focus changed to strategic foreign investors. Mass privatization had an indirect impact on the growth of employees' share ownership. MEBO method had a direct impact both on the growth of employees' share ownership and on that of profit-sharing. Its impact on participation of employees in decision-making and management was significant mainly in the early period. Before 1997, privatization legislation supported employees' participation within the scope of mass priva-

tization and MEBO method. Afterwards, privatization legislation introduced regulations on the sale of minority shares to employees. Cash-based profit-sharing (referred to as 'The Fund of Employee Profit Participation') must be applied in companies and in autonomous bodies, to which National Labour Collective Agreements are applicable (10% from the net profit in the case of companies, or 5%, in the case of autonomous bodies can be distributed to employees depending on their performance and contribution to financial result); in fact, due to various causes, it covers probably only a small proportion of employees. As average proportion in labour cost, at national level, the net profit directly paid to employees in 2003 was about 2.2%, while 70.3% were distributed from salary funds, including premiums and benefits. Until the end of 2004, self-employment instead of wage-earner position predominated for tax reasons, but under the provisions of the new Fiscal Code (in force since 2005) an opposite trend developed.

Until now, the influence of the EU legislation on the development of employee participation in Romania has been weak. However, several European companies in such branches as cement industry, town-cars industry, steel industry, software industry, and banking introduced practices of financial participation of employees, in most cases profit-sharing.

Although the financial participation of employees is presently relatively low, new schemes both of employee share ownership and profit-sharing have been introduced recently. Discussions on employee participation are taking place among policy-makers, trade unions and the general public. The EU accession might give an additional impulse to the development of employee participation.

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