

## **PUBLIC-PRIVATE PARTNERSHIP AS A MODEL OF PUBLIC SECTOR REFORM IN REPUBLIC OF SERBIA**

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**Abstract:** The purpose of this work is to point out the close connection between economic development, public sector and competitiveness of enterprises in Serbia and also a necessary change of the structure of service provider in the aspect of influence on the quality and price of services from the aspect of legal possibilities of the new way of establishing relations between citizens as users of services, state (local self-government) and provider of service-products. Basic stand is that there is no economic environment which will incite entrepreneurial spirit, investments and more quality services for citizens without overall reform of public sector and changing property-legal relationships. With this paper, we want to draw attention especially to finding solutions, which will link reform undertakings in the field of public companies and services through public- private partnership.

**Key words:** Privatization, public sector, reform, publicly private partnership

### **1. Introduction**

Increasing competitiveness of economic entities should be searched in frameworks of different developmental models of Serbian economy. Changing the previous model is necessary, concerning the changed circumstances in which state, society and economy have found themselves after economic crisis arised. It would be more difficult for the state to pay off even its current obligations and there are no funds for capital investments, social tensions will be more and more present, and economy more and more burdened. Which steps the state, in such circumstances, can make to help the economy? The only possible response is – reform of public sector.

Public sector influences affairs of overall economy of the Republic of Serbia in many ways. This economy sector, for its monopolistic position which arises from the nature of production process and a way of transferring the products to buyers (service user), has a strong influence on total expenditures of economy's affairs and other fields as well as population standard. Through its low efficiency and high costs of operations in general, public and (state) sector transfers negative influence through a relatively higher price of its products, onto the economy as a whole [4]. Keeping this sector on current level of efficiency and property status, will endanger the effects of social sector privatization, developmental and competitive ability of private sector. Hence, the privatization of public sector is a condition for successful privatization. Privatization is not finished until public sector of economy is privatized. Partial privatization, i.e. privatization of social sector only, loses its sense and if privatization of public sector is omitted, the positive effects of social sector privatization will be omitted. With privatization of public sector of economy, there are new conditions of successful and final transition onto market economy. As a result, cheaper and more efficient state should appear and significantly better environment for promoting competitiveness of Serbian enterprises.

### **2. Previous economic growth and competitiveness**

Facts indicate that public sector will not be able, in the future, to respond to developmental needs of overall economy and society, from the aspect of quality of products and services as well as from the aspect of their volume. Continuously creating losses, redistribution of capital through bigger growth of income of current factor work productivity, rapid depreciation of equipment and other means of work, higher indebtedness and lacking of

own funds for development inevitably leads to the state which will endanger current reproduction. Hence, permanent eliminating of irrationalities and inefficiencies in this sector is not possible without privatization. With private sector privatization, the efficiency of affairs of the sector itself will be increased but also the efficiency of affairs of whole economy and its competitive ability on world market. Integration processes towards EU imply including public sector also, especially great infrastructural systems; hence its privatization is a precondition for joining the process and successful remaining in it. Hence, the started reconstruction job of public enterprises should be accelerated and it passes through several steps and those are:

- The first step is separating secondary activities from primary one, which had a negative influence on expenditures of primary activity affairs out of which, in previous period, funds for development have been separated and invested in secondary activity. This process is almost over and 66 enterprises have been chosen, out of which for 41 the privatization procedure has been initiated. These enterprises will be privatized according to basic provisions of the Law on Privatization; by the same procedure as the enterprises with social capital, concerning that they come from different activities of social economy.
- The second step is reduction of the number of employees, which is in progress with an appropriate social program, which is being financed from Serbian budget.
- The third step, which goes simultaneously with the second, is financial reconstruction and consolidation. This is a condition for financial stabilization, repairing financial structure of enterprise and providing space for bigger investments in development and modernization. Here it should not be expected for the technical and technological reconstruction to be finished from its own sources. Huge funds are needed for that, which is impossible to provide neither from the current results of affairs nor from the budget of the Republic of Serbia.
- The fourth step is organizational and business reconstruction of enterprise as an important phase in preparation for privatization.
- The fifth step is adjustment of prices with the prices on the world market.
- The sixth step is privatization of primary activity. Linked to this phase, amendments to the Law on Public Enterprises by which it is provided for the 15% of the privatization subject to be given to employees and ex workers for free in the process of selling state capital of the subject of privatization regardless of the privatization method (tender or auction), 15% to privatization register, and the rest of state capital of privatization subjects will be the subject of selling to strategic investors.

In public sector, we have illogical occurrences, which are not happening in ownership economy. Total number of employees is increasing and when production is not growing, incomes really grow and when the losses are acquired, the same grow faster than the average real growth of incomes in overall economy. That indicates that there is no strong motivation for preserving capital from eating (overflow into current spending) as well as for rational combination of production factors (means of production and work force) in this property sector. The only strong dam for such irrational behavior is privatization, i.e. existence of private property in this sector. Administrative control of salaries in public sector is always giving in under pressure of compromise policy at the expense of capital and development. Because of the absence of ownership motivation in enterprise, pressures on the incomes growth are constant and they escalate from time to time up to the level of general demand for their increasing, behind which all the employees of enterprise stand.

With no ownership motivation, there is no efficient managing of enterprise, bringing rapid and quality services as well as rapid and timely changes of the enterprise management. Irrational combination of production factors, low work productivity, irrational distribution and

business with losses as frequent occurrence in public enterprises are the basic causes of low efficiency and competitive ability of this economic sector. With the existing level of efficiency, public sector in Serbia is not capable of joining EU integration process, going out to world market or enduring the pressure of external competition on domestic market. It is, as such, a great burden for the whole economy and citizens of Serbia because it transfers its inefficiency onto all the activities which use products i.e. services of this economy sector.

From the Serbian government, it is expected, in foreseeable period, to adopt strategy of reconstruction of key public enterprises, whose founder is the state, as well as the local public-communal enterprises. From the elements of that strategy, to a good extent, the future of 600 enterprises and 150,000 employees in this sector will directly depend and the effects will be indirectly transferred to Serbian economy as a whole. We must rely on the practice and experience of developed countries of European Union, and it will give the answers to questions:

- how to protect public interest in the process of privatization of public utility companies;
- what is the role of local self-government as a partner and protector of public (general) interest in the aspect of quality and continuity of performance of utilities, as well as in the aspect of monopoly control and successful creation (stimulation) of competence as basic way of antimonopoly struggle;
- in case of which utility services we can go into privatization immediately, and in case of which we should go in more steps;
- which forms of stimulating private capital's entering into existing utility enterprises should be applied;
- how to make rules in performing utilities and obligations and responsibilities of the owner of enterprise and local self-government;
- in which direction we should upgrade the existing legal regulations, and to the other questions which might be of significance for successful privatization in this sector of economy and development of private sector initiative.

In the process of transformation of whole public sector, it is necessary for the public utilities to be considered as a separate unit, because of their complexity in the sense of providing public-utility services, hence it is necessary to define special models for each activity, which is especially important in case of orientation to one of the forms of partnership with private sector or foreign partners.

### **3. Goals of the public reform sector**

Public services sector shows below average efficiency of business and engagement (usage) of capital. In this sector of economy, above average participation of constant (fixed) capital (83.3%) is present, while this participation on the level of Serbian economy is also high and it is 65.1%. Participation of floating capital (assets) below average of economy which is 16.7% against 34.9% in the economy of republic. This high engagement of fixed assets influences the high participation of fixed expenditures and low efficiency (productivity) of fixed capital. Within the scope of fixed assets, extremely high participation have different real estates, facilities, equipment and other assets in fixed assets with 89.5%.

Although the losses and below average work productivity are realized, net incomes in all public enterprises are higher than the average in economy and really acquire higher growth than work productivity. By this the assuming of work productivity of technical factor and the overflow of capital from production into personal spending is performed. [1] The facts point out that public sector will not, in the future, be able to respond to developmental needs of the whole economy and society, from the aspect of products and

services quality as well as from the aspect of their volume. Continuous creation of losses, redistribution of capital through higher growth of incomes from work productivity of current factor, rapid obsolescence of equipment and other means of work, high indebtedness and lacking own assets necessarily leads to the state which will endanger current reproduction. [3] Hence, permanent removal of irrationalities and inefficiencies in this sector is not possible without privatization. Without ownership motivation, there is no efficient managing the enterprise either, bringing rapid and quality services as well as rapid and timely changes of the enterprise management. Irrational combination of production factors, low work productivity, irrational distribution and business with losses as a constant occurrence in public enterprises are the basic causes of low efficiency and competitive ability of this economy sector. With the existent efficiency level, public sector in Serbia is not able to join the integration process of EU, enter the world market nor to endure the pressure of external competitiveness on domestic market. It is, as such, a big burden to the whole economy and citizens of Serbia because it transfers its inefficiency on all the activities which use the products i.e. services of this economy sector. Thanks to the specificity of products and services of public sector, this sector has a disproportionately big influence on conditions, and also the expenditures of business of each economic activity because:

- products of this economic sector are necessary for performing the process of production of goods and services in all economic activities, out of the economy and for the life of population;
- specific technological processes of production and services and their distribution to the consumers because of which it is not possible, in all public sector activities, to develop the competition as it is present in other branches and fields of economy
- technological monopoly with one number of public sector activities (electric power engineering, railways, post, water power engineering), which, in a particular sense, limitedly influence the development of competitiveness, especially in national borders. That additionally obligates the privatization to be more decisively implemented and competitiveness to be created in this field in order to disable monopolistic redistribution and thus transfer the negative effects from the possible growth onto the slower growth of whole economy. The most drastic is the example of New Zealand, in which because of the high participation of state in public sector, whole economy has entered in phase of long term delay and fallen out of the developed circle of the economy. Delaying the process of public sector privatization will endanger the effects of economy's public sector privatization and business successfulness and development of economy's public sector in general. One big part of production potential of economy would not be rationally used, which will besides his low efficiency issue above average business expenditures onto private sector and in that way make Serbian economy uncompetitive with economies of EU countries. Highly developed countries make maximal efforts to increase the efficiency of overall economy by strengthening private initiative in public sector through further privatization of public sector of the economy to its complete privatization wherever that is possible; maximal reduction of state's services through completing regulation in the field of prices; introducing and stimulating competition wherever that is possible; reduction of budget burden and subvention of the inefficient. Social policy is separated from the prices of utility services and the services of public sector of economy in general, because it disables market competition to which the prices give right signals for development of initiative freedom and efficient mobilization (location) of free capital. [2]

Problems in functioning of public utility companies in the Republic of Serbia are numerous,

(some of them are, in some parts of RS , the only ones which do business and are of a great influence for the belonging region) which appear as a consequence of inherited and emerging circumstances in the last 15 years: technical and technological obsolescence; enterprise over-dimensioning; tendency towards irrational spending; high indebtedness; high level of loss; high budget dependence; inadequate solution of ownership issue; fragmentation of activity; drop of volume and quality of services etc. In the same way, basic obstacle for long-term satisfying public interest for quality utility service is the lack of sufficient funds for modernization and expanding utility infrastructure, because most public utility companies are not able to finance the participation in necessary investments of a bigger volume by its own funds. In that sense, they will have to rely on the donations from various sources and credits.

It is expected that with the strategy of privatization 618 JP (and that of republic significance –founder republic 27, and of communal significance 591-JKP, founders municipalities) there will be determined different privatization options, such as for example PPP concept (public private partnership, i.e. concept which implies interaction between private and public sector), concessions and such, in accordance with positive experiences from European practice.

#### **4. Public private partnership**

Public private partnership (PPP) is a long-term contractual partner relationship between public and private sector which may include financing, projecting, building, governing, maintaining infrastructure and providing services from the part of private sector, which traditionally procures and provides public sector. When it comes to application of PPP, it is about a model which brings benefits for both sides, which requires a more successful combination of public and private sector goals. It is important to recognize the circumstances in which PPP is a better method of service delivery or infrastructure building in relation to other traditional methods of public procurement.

Public private partnership (PPP) is a mutual, cooperative acting of public sector with private sector in the production of public products or providing public services. Goal of the public private partnership is more economical, more effective, more successful production of public products or services in relation to traditional way of providing public services. Public private partnership may be described as cooperation between public and private sector in the field of planning, production, providing, financing, business or charging of public affairs. Public sector appears in that case as manufacturer and supplier of such cooperation – as a partner who contractually defines the types and volume of affairs and services which it plans to transfer onto the private sector and which offers the performing of public affairs to private sector. Private sector arises as a partner which requires such a cooperation, if business interest (profit) may be obtained and who is obliged to quality perform affairs received and defined by the contract.

Characteristics of PPP projects are:

- ◆ long-term contractual cooperation (20-50 years) between public and private sector,
- ◆ real redistribution of business risk (improving the quality of service) and
- ◆ overall responsibility on the side of private sector.

From the above description of public private partnership arises that PPP is a sort of privatization, but according to definition does not belong in the field of privatization after all. Public affairs may be performed by public administration in its own direction, i.e. by its own funds and staff. However, in some cases public administration is not in the position to indirectly perform public affairs in its own direction, most frequently for two reasons:

- ◆ because of insufficient competence of public administration staff, when it comes to specifically professional activities (e.g. medicine, oil, communal waste and such);



- ◆ because of big expenditures of performing public affairs in its own direction (e.g. procurement of construction machinery, incineration plants for communal waste).

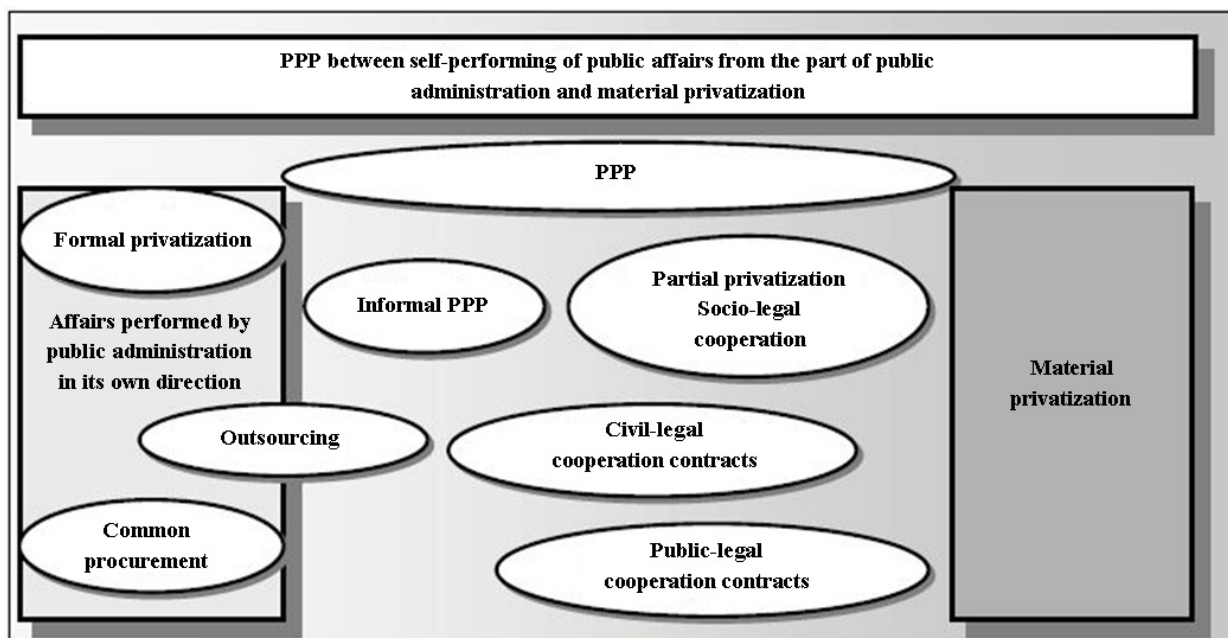
Public administration then uses traditional models of performing public affairs:

- ◆ public bidding, when a commercial agreement between public administration and private sector is made, and which is considered a model of common procurement (model of common procurement can not be considered a public private cooperation unless a long-term cooperation is present and there is no distribution of business risk between public and private sector);
- ◆ formal or organizational privatization, when public administration arises as a founder of economic society with the aim of performing specific professional public affairs (e.g. water-works, utility companies, and such).

Outsourcing is a model in which public administration gives away particular internal affairs to private sector. Those are mostly the affairs of accompanying and service character, such as cleaning public buildings, canteen jobs and such, thus this model might be considered as borderline case of public private cooperation.

On the other hand, there are different forms of privatization:

- ◆ material privatization, when public administration completely leaves performing of public affairs to private sector, waiving the majority ownership rights, with keeping supervisory functions (through supervision boards);
- ◆ complete privatization, when public sector waives all ownership rights or founding shares and all supervisory functions;
- ◆ functional privatization or *Contracting out*, when private sector arises as assistance in performing particular public function i.e. public affair (e.g. building insurance).



Source: Prozessleitfaden Public Private Partnership ([www.initiatived21.de](http://www.initiatived21.de)), p.11

Public private partnership is positioned between traditional forms of performing public affairs and privatization, hence it can appear in the following forms:

- ◆ informal cooperation, as a form of cooperation between public and private sector, exclusively on the level of information exchange and as preliminary forms of future cooperation;
- ◆ public-legal cooperation contract, i.e. concessions, when private sector gets concession for building and using specific public good through public bidding, hence private sector has a right to perform the charging of certain fees i.e. acquiring incomes, with paying concession to public sector;
- ◆ civil-legal cooperation contracts, i.e. long-term lease contracts, leasing contracts, procurement and service delivery contracts, with cooperative elements, and which are referred to planning, building, financing, doing business and managing public affairs or a public good;
- ◆ partial privatization, when public sector gives away a part of its founding right to private sector in a way in which it keeps majority ownership, by which a basis for a long-term structural cooperation between public and private sector and mutual providing of public services is created;
- ◆ socio-legal cooperation or joining public sector with private sector in mutual project company, hence private sector provides public service or manages a public good, and public sector for performing such public affairs pays to the private sector a monthly fee, with the public sector's control of performing public affairs.

Goals of all forms of public private partnership are mutual: more economic, more effective and more successful production of public products or services in relation to conventional way of providing public services, because of which models of public private partnership have often been used in practice as instruments of public sector reform. [5]

## **5. Conclusion**

Necessity of raising competitiveness of public sector certainly is a priority of economic policy of each country. The state will best support this goal if it is reforming itself. Urgent approaching to detailed reform of public sector is necessary. What is worrying is that so far the solutions were oriented to a small number of questions and that essential problems remain unsolved. There are numerous approaches, but it is necessary to observe the necessity of linking more parts of economic system, which are not mutually connected only at the first sight. By linking problems and solutions in the field of public enterprises, it is possible to build an efficient and fair economic system.

The way of solving problems so far has brought to deepening of the problems, and thus an unstable and expensive economic environment with the low level of provided services for the citizens as the users of services.

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