THE STATE IN BUSINESS

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New Zealand Planning Council
State Services Commission

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PUBLIC ENTERPRISE IN NEW ZEALAND

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FOREWORD

This authored paper is one of several published or to be published by the Planning Council on the public sector. Public enterprise has been and will remain important in New Zealand's development. The authors' main aim, in which we believe they have succeeded, was to present a framework for exploring questions prevalent in current public debate, such as the justification for government involvement in enterprise, the scope for private sector provision, and efficiency, effectiveness and accountability in public enterprise.

While the authors emphasise the special characteristics of individual agencies, they have been able nevertheless to draw some general propositions about possible future directions in the role and management of public enterprise from their analysis.

The suggestion is made that further work is necessary on specific aspects of public enterprise, where the information presently available proved to be insufficient for analysing some important questions to the depth the authors would have desired.

The study was undertaken as a joint exercise between the Planning Council and the State Services Commission. The Commission assigned two officers to the study and provided administrative support. The Commission was represented on a Steering Committee set up to coordinate the various papers within the public sector series, the membership of which comprised: Mrs Kerrin Vautier (Chair), Mr Graham Ansell, Sir Frank Holmes, Mr Don Hunn (who replaced Mr Murdoch Taylor), Professor Henry Lang and Dr Mervyn Probine.

Frank Holmes

Frank Holmes
Chairman

The views expressed in this paper are those of the authors, and do not purport to represent views held either by the Planning Council or by the State Services Commission.

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INTRODUCTION

It is commonplace that New Zealand, along with other mixed welfare economies, has experienced, over the long term, progressive developments in the scope, scale and direction of state intervention; and that especially since the Second World War has undergone considerable change in the Government's role in economic affairs. The choice about public sector involvement is heavily dominated by the concerns of economic management, in particular by the responses required in public policy decisions to encourage economic growth without at the same time increasing perceived tax burdens. From the standpoint of the 1980s when in New Zealand as elsewhere the problems of economic management have become acute, and the financing of public expenditure faces major constraints, a reappraisal of traditional approaches to government intervention is essential. It is clear from public discussion, including the views expressed by the main political parties, that as in other countries there is a strong presumption in New Zealand in favour of taking stock of the public sector as it now stands, and in particular of revising the traditional social preference for state provision of a wide range of goods and services.

The government is involved in the production and distribution of goods and services in two ways. Some are provided 'free', or at prices not related to market factors, as in the education and health services. How much is produced, and for whom, is determined by the interaction of public expenditure and tax considerations, government policy, and public demands, in the context of longer-term social, economic and technological developments. Other goods and services provided by the state are sold in the market at prices which, subject to the government's policy on pricing, reflects costs of production and factors of supply and demand. These market goods and services are produced predominantly by means of public enterprises, i.e. by agencies to some degree owned, and in most cases financed and controlled, by the state.

The influence of public enterprise in the economy, in terms of resource use and scope of activity, has become a much debated issue. A statistical analysis of the dimensions of public enterprise will appear in a forthcoming Planning Council publication, by Mr Mervyn Pope. In the present paper attention is directed not twards the size of the public enterprise *per se*, but to the recurring issues in the public debate:

(a) the purpose of and justification for government involvement in the production of market goods and services, and

(b) where government is involved, the appropriate nature and form of participation, and the effectiveness and efficiency of the agencies concerned.

Recently in New Zealand, as in other countries, the debate has been largely preoccupied with the possibilities for transferring to the private sector activities presently carried out by government. The advocacy of 'privatisation' rests on the contention that 'less' government and 'more' private enterprise in the market would result in a more effective use of national resources, on the assumption that the private sector is relatively more efficient in the commercial field.

To an extent, the arguments for or against state-owned enterprise are based on ideological differences of view. These will continue to evoke legitimate open debate. It is important, however, that the debate should be as well-informed as possible, especially in the light of new prospects for public enterprise which raise questions about the proper role of government, and its responsibility for the planning and management of overall resource use. Established public enterprise are being required, for example, to meet technological advances which have created new products, as in the telecommunications area; while in new areas of commercial activity, innovative forms of government intervention are being adopted (as with the growing number of joint ventures between the public and private sectors in the major energy projects).

The analysis of public enterprise issues in this paper suggests there is a need for evolving some basic principles for the establishment of public enterprises and for their continuing management. Part I deals with broad characteristics and trends. Part III examines aspects of the role and performance of public enterprise in New Zealand, by reference to the experience of individual public enterprises. The conclusions which emerge from the study are presented in Part II, and a number of general propositions put forward as indications of future directions for public enterprise, in the perspective of the 1980s. These are not intended to be definitive, or prescriptive, but rather to further public discussion. The usefulness of this study depends upon its adding sufficiently to knowledge of the special circumstances and characteristics of public enterprise in New Zealand to enlighten the discussion.

As the paper set out to address general issues, it has left numerous points of detail and qualification unanswered. There is a need to know more about the implications of public enterprise activity, particularly its precise economic effects, for example in terms of financing, investment and pricing. It is for this reason that the paper proposes a programme of further study. This would include considering public enterprises individually, to take account of their distinct characteristics.

Method of Study

1. The background for Part II was derived from the study of individual agencies, initially those which had already been the subject of review by the State Services Commission and subsequently extended to agencies beyond the Commission's direct responsibility. The selection of agencies was necessarily limited, but an attempt was made to cover a range of activity (finance and insurance, tourism, energy, transport and housing) and of organisation (government trading departments, and government corporations of different forms) The studies were undertaken to elicit from the experience of various public enterprises the significant and recurring features which appeared relevant to the role and performance of the public enterprise sector as a whole. Senior managers in each of the agencies concerned were consulted.

2. Assistance was provided by representatives of the management of private enterprises, and by officials within the Treasury and State Services Commission.

3. In the course of the study the authors had access to departmental background papers, as well as using the annual reports and other published material of the agencies themselves, and the reports of such authorities as the Controller and Auditor-General and the Public Expenditure Committee. A selective canvassing of the large volume of available literature on the public sector, and specifically on public enterprise, was undertaken. Besides published books and articles, the authors found useful the following official documents on public enterprise in other countries, which are not referenced in footnotes: Commonwealth Secretariat Reports on a series of seminars on public enterprise (The Role and Management of Public Enterprises (Jamaica, 1976), Issues in Public Enterprise Development (New Delhi, 1978), Performance Evaluation of Public Enterprises (Botswana, 1978)); Canadian Privy Council Office Report on Crown Corporations: Direction, Control, Accountability (1977); and the British National Economic Development Office Study of United Kingdom Nationalised Industries (1976).

4. A surprising lack of basic data about and analysis of public enterprise in New Zealand suggested that the subject is greatly underresearched compared with, for example, the United Kingdom where the nationalised industries have been the subject of numerous official investigations and public reports. The abovementioned proposal for further studies in this ara would help fill this gap.

5. Work on the present paper coincided with the preparation of a study of public enterprise in New Zealand by Dr Mascarenhas of Victoria University, published in August (R C Mascarenhas, Public Enterprise in New Zealand, N.Z. Institute of Public Administration, Wellington, 1982). His book adopts a systems approach to the examination of public enterprise, focusing on government policies, in the context of the general socio-economic and political environment. Although inevitably the issues discussed, and the sources of background information, are the same in many respects as in this paper, the two studies were undertaken from different perspectives and serve different purposes.

PART I

THE CHARACTERISTICS OF PUBLIC ENTERPRISE

Public enterprises broadly may be defined as those agencies owned or managed predominantly by the government, engaged primarily in commercial activity (financial, economic and industrial), where the costs of the activity are expected to be financed in whole or part by market sales.[1]

The role and characteristics of public enterprise in New Zealand can be better appreciated by looking at the path of its development and its present day conditions.

HISTORICAL BACKGROUND

From the early stages of colonisation when governments in New Zealand played a large role in the acquisition and distribution of land, public sector economic activity has continuously expanded in areas where the private sector has operated, as well as in areas which were considered to be, or in practical terms were, appropriate for government ownership. While no single factor can be isolated to explain this characteristic, history suggests that government intervention was seen from the outset as a response to the needs of economic development[2]. In a region of recent settlement, where conflicts of interest needed to be resolved and where large concentrations of capital were required to provide the economic 'infrastructure' (especially transport and communications), the state assumed a role of direct involvement in many commercial fields.

Land being the most important source of income, the early colonial governments intervened to ensure its development in the interests of economic growth. By 1900 the range of activities undertaken by the state included ownership and operation of the Post Office (with the Post Office Savings Bank), the telegraph system, railways and coal mining; the Public Trust, Government Life Insurance, State Fire Insurance and State Advances Offices had been established; the government had obtained shares in the Bank of New Zealand; and was directly involved in overseas financing for projects in New Zealand. In terms of capital formation the government's share was large, contributing possibly as much as half of all capital formation in the 30 years before the turn of the century. A substantial regulatory role for government also emerged, first in the form of restraints on private enterprise to effect public policy, and later of direct controls, for example on prices. State provision of a wide variety of goods and services had become a tradition.

Behind this substantial public sector activity lay the advantage the government had over the private sector in obtaining loan funds, and the government's capacity to undertake long term, large scale investment projects where the benefits were mainly external. Over and above these factors was an

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1 The defining of public enterprise is discussed by Mascarenhas (see reference on page 3), who draws attention to the variety of possible definitions.

2 The role of government in the New Zealand economy is examined historically in G.R. Hawke, Government in the New Zealand Economy, New Zealand Planning Council Planning Paper No.13 (June 1982).

apparent willingness to see the state directly involved in economic development, based on a pragmatic belief that where the apparatus of government was likely to be useful to development it should be used rather than not.

During this century pragmatic responsiveness to public needs and pressures has remained characteristic of government intervention which, while following a path somewhere between overseas ideologies preferring nationalisation of economic activity on the one hand, and private enterprise dominance on the other, has resulted in the state steadily extending its part in the national economy. Apart from the state having continued to assume responsibility for economic development (remaining an active participant in capital formation even after the basic economic infrastructure had been built up), two further underlying factors have been evident: first, the profound influence on government intervention of the welfare state, a concept with early beginnings in New Zealand, leading to progressive state involvement in economic and social affairs to promote equality and achieve other social purposes; and second, the emergence of two dominating macroeconomic objectives - full employment and growth - in pursuit of which governments have acted directly (participating in appropriate activities) and indirectly (supervising and introducing controls on private sector activity).

No consistent philosophy towards public enterprise in New Zealand emerges from its history. Nevertheless, history has left its mark on the public enterprise sector as it is presently characterised.

PRESENT CONDITIONS

Range and Diversity

Rather than the state having a diminishing role in the field of enterprise as the economy has developed, it has continued as an active and willing participant, extending its activity to include broadcasting, telecommunications, hotels and tourism, printing and publishing, air and sea transport, primary produce marketing, development finance, and production and distribution of energy. The contribution of central government market operations to gross domestic product now is just over 10 percent.[3] In relation to other countries, New Zealand occupies a middle position on the scale of public ownership of market activity, comparable with mixed, developed economies such as Britain and France, each of which has a major public enterprise sector.

Despite their number, public enterprises in New Zealand have not been acquired or established as a conscious process of nationalisation. The same broad reasons as have applied in the past have continued to lead government into the ownership and control of market activities:

(a) the promotion of economic growth through the provision of infrastructure, and essential services;

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3 For detailed statistical evidence of the scope of government's participation in the market see M.J. Pope, forthcoming N.Z. Planning Council Planning Paper No. 16, (1982).

(b) exploitation of natural resources, or development of sectors of the economy which the government regards as necessary for the economic and social good, where

(i) the private sector has not the capacity, or is unwilling, to invest because of the degree or type of risk, the size of the investment required, or the length of time before return on investment can be expected, and because a substantial proportion of the benefits are external to the enterprise, and not represented in the financial return to the investor; and

(ii) the government wishes to avoid the possibility of excessive foreign ownership of enterprise;

(c) the regulation of the market, including the redistribution of resources, production and income.

The use of the term 'public enterprise' suggests a formal, regularised system of agencies capable of being grouped according to uniform sets of characteristics. No such generalisation in fact is possible. Public enterprises in New Zealand, as elsewhere, occur in a great variety of circumstances. They differ widely not only in range of activity and purpose as indicated above, but also in organisation, financial structure, position in the market and commercial emphasis; and in their relationships with central government, the public, and the private business sector.[4] This variety is illustrated by the following descriptive list of the forms in which public enterprise currently is found in New Zealand: [5]

(i) wholly government-owned, operated, financed and controlled departments set up by statute and covered in the Public Accounts (e.g. Ministry of Works and Development, Ministry of Energy, Government Printing Office);

(ii) as above, with similar ministerial accountability, but operating outside the Public Accounts (e.g. Post Office);

(iii) wholly government-owned public corporations, with or without specific limitations on the powers of the Minister, and with other organisational and financial variations (e.g. Railways Corporation, New Zealand Broadcasting Corporation, Housing Corporation, Government Life Insurance Office and State Insurance Office);

(iv) primary products marketing and producer boards: corporations established by statute or regulation to provide for the marketing of primary products and to enable producers to control the marketing of their products, and funded by levies or, on occasion, by government grant or loan;

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4 In order to establish the main characteristics of public enterprise in New Zealand, in this section of the paper no attempt is made to illustrate from actual experience. This is the task undertaken in Part II, based on the study of particular public enterprises.

5 See also Appendix I, Selected Characteristics of Some Public Enterprises.

(v) wholly government-owned companies which derive their status from general legal powers, having no unique establishing legislation (e.g. the New Zealand Petroleum Corporation (Petrocorp), a limited liability company);

(vi) joint-venture enterprises with private sector interests whose status derives from specific legal instruments such as participation deeds (e.g. the New Zealand Synthetic Fuels Corporation);

(vii) public and joint-venture companies in which the government has only an indirect interest or only indirect ownership rights (e.g. Petralgas, a subsidiary of Petrocorp);

(viii) major government shareholding in private companies (e.g. New Zealand Steel Development Limited).

Public enterprises occur in a range of monopoly and competitive market situations. State monopolies usually are regarded as 'natural' monopolies because the minimum scale of investment required is so large that not only is it beyond the capacity of private enterprise, but competition would be prohibitively wasteful: for example, rail transport and major public utilities. At the other end of the scale public enterprises operate in open competition with the private sector, for example, insurance, and also with other public enterprises, as with rail and sea cargo freighting. An important feature of the 1970s and 1980s has been the co-operative market arrangement where the government and private enterprise operate in partnership, through joint ventures.

Convergence of Public and Private Enterprise

As these forms of public enterprise suggest, there are many points at which the public and private sectors overlap. Indeed, government participation in commercial areas of the economy has become a link between central government and private enterprise, creating a continuum of public and private activity without fixed or easily defined boundaries. A dominant feature of the New Zealand economy, this reflects a significant trend towards convergence of state and private sector interests, found also in other mixed economies.

In New Zealand, this convergence is manifested in a number of ways. At the general consultative level, co-operative links between the public and private sectors have been created through institutionalised planning processes, the setting up of ad hoc bodies to carry out advisory and regulatory functions, the emergence of units within and special appointments to ministerial offices, and widespread informal contacts between policymakers and private sector representatives. The effect has been one of increasing co-operation between the state and the private sector in the market.

In public enterprise, there have been changes in two significant directions: in the characteristics of government intervention in commercial activity; and in the traditional operating patterns of public enterprises. The important features of these changes are as follows.

(i) Joint ventures, involving partnerships between government and private enterprise, to establish and manage commercial activities. The joint venture usually is adopted as a mechanism for promoting and accelerating industrial development, sometimes in high risk areas, drawing on the advantages of government support and direction, private sector management and technological expertise, and shared financing. One of two forms may be taken - equity joint ventures or contractual joint ventures. They may include investment by public enterprise agencies in private commercial developments; and joint public and private enterprise promotional and marketing arrangements.

(ii) Adoption of private enterprise corporate models of organisational form and decision-making, as, for example, in the use of advisory boards, the emphasis on self-financing operations, and the interest in business techniques which are based on the profit concept. This trend has been most noticeable in the apparently increasing preference for the public corporation and the state-owned private company as a means for organising public enterprise activities, which offer a way of approximating the 'ideal' commercial environment.

(iii) Interchange of management and technical personnel. This is another dimension of joint participation by government and private business in commercial activities. Where the government's role is an active one, as compared with financing only, joint arrangements naturally will include a personnel input from each party. The move towards the corporation as a form and principle of public enterprise organisation has also led to the merging of public and private sector management expertise, appointments to the boards of public sector corporations deliberately reflecting a mixture of government and private sector representatives. The trend has been reinforced by the growth of professionalism in management in both sectors. Increasingly, graduates of public and business administration courses are entering public and private sector employment, bringing a disposition towards and expertise in rational decision techniques developed from common organisational principles, which cut across institutional distinctions.

(iv) Direct and indirect support of private sector activity. Restructuring and development of key areas of production have involved the government in financial and other forms of direct assistance. The government also is involved indirectly in numerous ways with developments in private enterprise - through regulations, special tax provisions, subsidy programmes, loan guarantees, preferential 'New Zealand content' provisions, general research, industry development and training. The private sector, therefore, to a significant extent is dependent upon the state for assistance in the development and consolidation of new ventures, and for successful performance in existing businesses. The government, for its part, is able to influence private market activity through these forms of indirect participation.

As a result of these directions, the reasonably clear lines which traditionally could be drawn between commercial activity in the public and private sectors have become blurred, so much so that it is sometimes difficult to be precise about the notion of 'public' in public enterprise; and, conversely, difficult to isolate 'private' activity, when increasingly, private enterprise is a participant in the administration of public functions.[6]

The trend to convergence, in other words, means that there may be less that is unique to public enterprise than commonly is supposed. As distinctions often are drawn between state and private enterprise to explain differences of performance, and as well provide the case for or against the state having a role in the enterprise field, they need further exploration.

Comparisons Between Public and Private Enterprise

While the characteristics of public enterprises vary widely, the private enterprise sector contains an even greater diversity of size, form, financial structure, product orientation and so on. It is difficult therefore to establish a basis for valid comparisons. The contrasts between a large public monopoly and a small private company are obvious. At the other end of the scale, when the joint venture form of public enterprise is compared with the privately-owned conglomerate, the similarities are more apparent than the differences. To confine the comparisons to the counterparts in each sector, the following discussion relates mainly to public enterprises fully owned, and in some manner financed by, the government, contrasted with the larger private business corporation or commercial firm.[7]

The distinctions which can be made between public and private enterprise rest mainly on the relationship which the state-owned agencies have with central government. This relationship, though not appearing in any consistent form, by convention requires these agencies in some way or another:

(i) to fulfil non-commercial (economic, political and social) objectives as well as purely commercial objectives;

(ii) to conform to some manner of government supervision or control;

(iii) to be publicly accountable.

Objectives in Public and Private Enterprises

The objectives of most public enterprises are numerous, often complex, and not always easily identified. An enterprise owned by the state is an instrument of public policy, and by definition will be required to fulfil, as well as its purely commercial role, a range of duties and obligations which may be laid down by Parliament in the establishing legislation, or conveyed by direction

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6 In a speech to the Institute of Public Administration Conference in August 1981, the Hon. George Gair aptly described the boundary between the public and private sectors as a 'paper curtain'. Public Sector, Vol. 4, No.1 (1982), 3.

7 The discussion here is limited by a lack of detailed information about private sector business practices. Obtaining this information was regarded as being beyond the bounds of the present study. The general observations about private enterprise are based on comments given by representatives of the management of a selection of private firms.

from the Minister concerned. A public enterprise may have non-commercial objectives which are economic (promotion of growth or stability, nationally or regionally); social (the achievement of allocational or distributional goals); and political (reflecting priorities expressed in public demands). These sorts of objectives are assumed not to be satisfied by the private market, and are the justification for government intervention. They may not be compatible with the achievement of the commercial objectives of the enterprise, and where this leads to losses on overall operations the enterprise will need to be subsidised from public funds to cover losses on its overall operations.

The mixed objectives of public enterprise are in marked contrast with the traditional, single objective of private enterprise, that is, profit maximisation, which provides a clear simple guide to decision making, and a yardstick to measure results. There are, however, qualifications to be made to this distinction.

(a) There is a discernible trend in at least the larger private business firms towards the adoption of objectives other than profit maximisation which reduce profitability: for example, the objective of long term growth or survival, which requires in turn strategies for obtaining or holding a place in the market, retaining labour for future expansion, or safeguarding sources of supply. The interaction of a mixture of such objectives may be regarded as representing the 'best use' of resources, replacing the sufficiency of profit as an end in itself. Unlike enterprises in the public sector, however, the private sector is not obliged to maintain uneconomic services for non-commercial reasons, and may always choose to place financial performance ahead of other considerations. Growth still depends on achieving high enough rates of return in the short term to attract funds from outside sources, including shareholders. Furthermore, while a particular decision may be taken on grounds other than short term financial gain, the effect overall may simply be one of shifting the emphasis from current to future profitability.

(b) The private business sector is becoming more acutely aware of the need to consider not only the financial environment, but also the broad economic, political and social environment. This is due partly to the benefits to the organisation's own interests, and partly to the formal and informal obligations and constraints increasingly placed on the private sector. The private sector is governed by a framework of law under which its activities are extensively regulated by government; and, like public enterprise, often is required to make decisions in accordance with the government's policy objectives such as employment, and the use of domestic materials and components for production. Another development apparent in New Zealand is increasing responsiveness to the economic and social plans of government on the part of private businesses, some of which now take explicit account of these plans when formulating their own development strategies.

To an extent, the emergence of non-profit goals is a result of restricted competition where the pressure to maximise profit, the traditional economic assumption under full competition, is lessened. If the emphasis on profit in the private enterprise sector shows signs of changing,[8] the need for profit in public enterprise is being increasingly stressed in recognition of the importance of public sector financial viability to economic growth. The role of the profit objective in public enterprise, however, still is accompanied by debatable issues:

(a) how appropriate is the concept of profit in the public sector

(i) as compared with the aim simply of 'breaking even' which ensures on the one hand that the enterprise does not require public funding to remain commercially viable, and on the other that is not seen to be 'taxing'consumers through unnecessarily high prices, and

(ii) in the sense of being the explicit purpose of the enterprise, the benefits of wealth-producing assets under public ownership thus being available for the common good, instead of accruing to private owners and shareholders;

(b) how far should the aim be to maximise profit, at the possible expense of non-financial objectives, i.e. what is the appropriate relationship between commercial and 'developmental' roles (especially given that the generation of a surplus is a condition for the provision of new capital to finance development activities, if funding from public resources is to be avoided);

(c) if profits are to be sought, what provisions should be made

(i) for taxing the enterprise,

(ii) for utilising surpluses generated from profitable activities, e.g. to finance the uneconomic activities of the enterprise (in which case the higher the level of profits, the greater the capacity of the agency to provide benefits to the public);

(d) if profit is not the only objective of the enterprise, how do other objectives modify performance and decision making - in particular, what concepts and techniques can be applied to substitute for the role of profit as a motivator for effective and efficient performance, and as a ready means of measuring performance outcomes.

Because of these special considerations, and despite modifications in the practices of both public and private sector business agencies, the profit objective still presents a means of distinguishing public and private enterprise.

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8 In a recent study of corporations in the United States of America it is argued that the maximisation of profits has remained the basic objective, despite a general assumption that private sector corporations have had to become more responsive to outside controls and influences. Edward S. Herman, <u>Corporate Control, Corporate Power</u> (New York, 1981).

Public enterprise objectives are influenced by changes in government policy through the issue of ministerial directives. Ministerial direction is an outcome not only of public ownership, but also of the strategic position in the economy occupied by most public enterprises. Through written or unwritten directives, ministers may seek to influence the general exercise and performance by the enterprise of its functions, or to direct the agency specifically on matters affecting the national interest, such as on regional investment and pricing levels. Where a public enterprise is established by legislation, statutory provision for ministerial direction may be made, and its scope defined, as with the Broadcasting Corporation of New Zealand. In other areas, for example the Bank of New Zealand, the prospect of ministerial direction is taken for granted as a condition of state ownership, even if it is used only rarely. The private sector, however, has not been immune from this form of government influence, as illustrated by the recent issue of 'instructions' to the finance industry on interest rate constraints which the government wished to see adopted.

Supervision and Control in Public Enterprises

Conventional government departments are subject to systems for the detailed supervision and control by central government of all matters of policy administration, expenditure and staffing. The resulting checks and balances impose on management an outside requirement for consistency and conformity which has no counterpart in the private sector.

The normal processes of administrative government however, even with varying degrees of modification have not in the past been found to be entirely appropriate for public enterprise. A preference has developed for forms of organisation tending towards the greater freedom from central government control which a successful commercial operation is seen to require.[9] In effect this means more closely approximating private sector models of business organisation and style.

Management processes and styles represent one of the more difficult areas for comparison, because certain differences and similarities depend more on factors such as size and the level of management concerned than on whether the enterprise is publicly or privately owned. For example, when compared with their counterparts in the private sector, public enterprises may not suffer any more from the inflexible forms and procedures usually associated with 'bureaucracy': bureaucratic tendencies are easily identified in larger private sector corporations, and with the same inherent limitations; and relatively small, flexible organisations have been set up by Government in certain areas of commercial activity, e.g. Petrocorp, for precisely the purpose of avoiding the disadvantages of the conventional bureaucratic style and form.

Where the conditions and attitudes of the state services do apply in public enterprise agencies, however, there are contrasts with the private business sector, particularly in personnel policies, management functions, and motivation for effective, efficient performance.[10]

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9 See Pope, op.cit.

10 A detailed and enlightening analysis of this topic is to be found in David Howells, Marks and Spencer and the Civil Service: A Comparison on Culture and Methods, in Public Administration (Autumn 1981), Vol.59, 337-352.

In personnel management, most public enterprises traditionally have conformed to the career provisions of the public service, which have been developed to preserve the integrity of the service. Standardised occupational structures and appointment procedures determine promotion and remuneration. Appointment procedures (particularly at senior levels), methods of advertising positions, and the existence of appeal rights, limit opportunities for employing people from outside the service. In the selection of top level personnel, emphasis is placed on intellectual capacity, writing ability and tactical judgment. Business acumen is not necessarily counted among the prerequisites of top management.[11] Private organisations have more scope for and flexibility in hiring and firing, and in providing rewards for performance through pay and promotion strategies. Selection of executives is likely to take account of direct, practical experience gained by working in the basic levels of the organisation. Indeed, executive training is likely to include ground level experience in the operations of the enterprise.

The traditional recruitment and career patterns, training, and experience of senior managers in the public sector reflect particular management functions:

(i) in terms of the nature of the decision processes of government, the main tasks are policy formulation and the critical appraisal of options, as compared with the execution of concrete tasks which characterises the decisions of a private business;

(ii) decision processes are characterised by the extensive use of committees, the complexity of official procedures and existence of detailed codes of practice, and by the importance placed on written analysis, which contrast with the less formal and less deliberative style of private enterprise where speed of communication and intuitiveness are important features of management. In the public sector generally, Ministers of the Crown are responsible ultimately for decisions taken within their portfolios, and there is a general presumption that public sector decisions will be well-documented.

Motivation in the private sector is based on identification of personnel with company interests. A private sector manager is motivated to perform well by the expectation that the market success of the company will ultimately benefit him or her. In most public enterprises there is no such immediate relationship between the achievement of the agency's objectives and the individual contribution of the employee, and no personal responsibility for the outcome of the agency's resource allocation decisions. Effort is less likely to be oriented specifically to the achievement of the objectives of the enterprise. Nor do the objectives of the public enterprise, when complicated by combined commercial and non-commercial purposes, offer the strong motivating force with which profit conventionally is credited. A range of motivational factors, not all easily defined, apply in government agencies. To the extent that this is true also of private sector organisations, motivation is still overlaid by the profit objective.

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11 Note however the editorial observation in Public Sector, Vol.4, No.1 (1982), 1, that "It would be erroneous to believe that all hard nosed business men reside in the private sector. There are many such characters in the public service who could and would produce a profitable return on departmental activities if this were permitted by, or were the objective of, the system."

The areas of contrast which result from the relationship of public enterprises to central Government are closely related to differences in the accountability requirements of public and private enterprise.

Accountability in Public Enterprise

The constitutional requirement to be publicly, or externally, accountable for its actions must be regarded as a major distinguishing feature of public enterprise. It is clear that where an agency is in receipt of public funds, and a public purpose provides the justification for its establishment and continued existence, the agency must be accountable to the public, through the elected Government, for effective and efficient use of funds and achievement of objectives. This means being able to demonstrate how, and how well, objectives are being fulfilled.

Full public accountability involves scrutiny by Parliament, and supervision by the executive and administrative arms of Government. In turn, these processes involve the justification of policy decisions and official actions, the public reporting of the agency's operations, and compliance with the financial formalities of the budgetary process.

These features do not apply uniformly to all public enterprises - not unexpectedly, given the significant variations in the characteristics of individual enterprises discussed in Part II. Still, external accountability, and especially the unique role of Parliament, is not paralleled in the private enterprise sector where businesses are accountable only to their private owners (shareholders), through the board of directors.

Being accountable to the public for their performance works positively for public enterprises in so far as it provides an incentive (if accountability is effective) for the successful achievement of objectives, i.e. a counterpart for the profit incentive of private enterprise. A disadvantage, in comparison with the private business sector, is the possible effect on commercial confidentiality which is claimed to be essential for competing effectively in the market.[12] There is an inherent conflict between the public's right to the disclosure of information about an enterprise's operations, and the need of the enterprise to preserve its competitiveness and the confidence of its clients. (This problem will require resolution in the legislation on official information at present before Parliament.)

While private enterprises are not publicly accountable in the same manner as public enterprises, it is in their interests to be responsive to public criticism and to have regard for the preferences of government. Businesses of all kinds are devoting increasing attention, and sometimes significant resources, to handling these. They are still left with the discretion to decide what information is made public, and what interpretation it is given.

The same clear distinction does not arise in respect of internal accountability which, as an aspect of management, is of equal relevance in both private and public sectors. Internal accountability involves the exercise of delegated responsibilities for the management of resources and achievement of goals within the organisation. Its main elements are: defined

12 This claim has been made in submissions to the Select Committee on the Official Information Bill by producer boards and other public enterprise agencies, e.g., Petrocorp, Air New Zealand and the Bank of New Zealand.

objectives; systems for generating information on resource use, costs and outcomes; methods for measuring actual performance; and means for reporting this information within the organisation. The principles are the same in any enterprise. The differences between public and private enterprise lie in procedures and practices. For those enterprises within the public service, the procedures are laid down and the practices monitored by the central government control agencies. Other public enterprises have scope to develop their own methods for accountability. In both cases, the difficulty of setting clear, measurable objectives, and of developing performance measures to deal with non-commercial (social, economic and political) considerations, complicates the development of accountability systems in a manner not encountered by the private business organisation.

It is largely because of the requirements to fulfil non-commercial objectives, comply with central government supervision and control procedures and meet public accountability that there is a tendency to assume that public enterprise copes less well with market activities than the private business sector. The more these requirements apply, the less responsive the agency is likely to be to changing market situations, and hence the less commercially effective. This assumption rests on two premises, but is subject to two important qualifications. The premises are that:

(a) private enterprises need to be flexible and adaptive to survive, or face liquidation or takeover. Public enterprises can remain in existence irrespective of performance. Losses can be met from public funds, (financial guarantees sometimes being provided in the legislation establishing the enterprise);

(b) private enterprise is subject to direct, periodic catalysts for change through the impact of the market, as with the trend to takeovers which has prompted businesses to make themselves less vulnerable by, for example, strengthening their management systems and utilising their assets more effectively. In the absence of such catalysts there is less pressure on public enterprise to keep pace with modern management demands. It may be noted, however, that in coping with market change private enterprises have the option not usually available to the public enterprise, of diversifying into new, possibly unrelated activities, allowing existing activities to diminish in importance or be phased out.

The qualifications are that:

(a) where private businesses implicitly serve policy purposes, such as regional development or employment, they may be regarded by the government as justifying temporary financial assistance to prevent the enterprise closing down because of unprofitability;

(b) commercial sections in the private sector are active in seeking from government ongoing assistance in such forms as tax concessions, subsidies and protected markets. These are provided at public expense, and lessen the impact of market forces.

THE CONTEXT FOR CHANGE

The changing implications of state ownership place new perspectives on the role and performance of public enterprise. In respect of role, it makes the question of what are the proper areas for government intervention more complex, involving wider public concerns. In respect of performance, it highlights the question of whether resources used by the public sector for producing goods and services are applied:

(i) effectively, i.e., in accordance with the intended purposes of the enterprise; and

(ii) efficiently, i.e., at least cost for the achievement of desired outcomes.

Part II addresses in some detail aspects of public enterprise role and performance in New Zealand. The two broad areas which provide the context for this discussion are:

(i) why has performance become so important a dimension of the debate about government in the market, and

(ii) what need is there for a new approach to public enterprise?

The Importance of Performance

Critics of government involvement in public enterprise:

- attribute low economic growth in part to the 'drag' on the economy of a public enterprise sector which not only is regarded as too dominant but also as an inefficient user of resources; or

- are concerned that the apparently unsatisfactory performance of at least some public enterprises is at variance with the principle of responsible government, which requires publicly owned agencies to function efficiently and effectively.

The performance of the public enterprise sector has particular significance in the current situation of sustained economic difficulty and restraint in public expenditure. Leaving aside the impact of non-commercial objectives on financial performance, it is, first, more important than ever that public enterprises be capable of generating sufficient net revenue both to provide a return on investment to contribute to public sector capital formation generally; and to allow for the self-financing of expansion, avoiding a drain on public funds. Even if, because of the implications of non-commercial objectives, the enterprise cannot be entirely self-financing, the higher the proportion of capital expenditure financed from internal sources through surpluses generated by efficient performance, the better the prospects for attracting required finance from non-government sources (if this is permitted). Second, an inefficient enterprise may resort to increasing prices or reducing services to meet high costs, which runs counter to government's obligation to apply public funds for the best allocation of resources. Third, insofar as the transfer of public enterprise activity to the private sector is considered a possible means of restraining public expenditure growth, the marketability of an enterprise will be dependent upon the strength of its performance. Losses, high debt ratios and weak market shares will not be conducive to finding ready buyers.

Apart from current economic pressures, accelerating demands of modern management, which affect the public and private sectors equally, bring the performance aspect to the fore. The increased pace of technological advance, rapidly changing market conditions, and the impact of economic, environmental and other broad public interests outside the field of the individual enterprise, all require a high degree of responsiveness and adaptability.

The Need for a New Approach

In the past, dealing with public enterprise role and performance by ad hoc means has been accepted. For a number of reasons, the need for a more considered and consistent approach has become increasingly evident.

The first and most obvious reason is found in the increasing range and complexity of government, reflecting developments in the social and economic life of the community as a whole. It is now harder to reach a consensus on where and how the state should intervene, and more than ever necessary that there should be means for informing decisions about future directions for new and existing public sector activities. In the public enterprise field, this means that defining public needs for goods and services, and deciding how these needs should be met, require closer analysis. While public enterprises may have served valid purposes when established, they have not always continued to do so; nor have they always justified their existence as tools of effective national economic management, or as models of administrative efficiency.

A second reason lies in the current advocacy of greater independence of public enterprise activity from the processes of central government, to allow the enterprises to pursue their commercial objectives in the same way as would a private sector business. Whatever the advantages may be in terms of financial viability and effective resource use, however, important constitutional and administrative issues are raised concerning the roles of the minister, Parliament, public sector managers and the public, which will not resolve themselves.

(a) Reduction of ministerial responsibility gives greater power to an enterprise's managers without commensurate increased responsibility.

(b) Public enterprises are instruments of public policy and must therefore be subject to scrutiny and control by the minister and Parliament as representatives of the public. This limits the degree of independence which is practicable.

(c) The kind of independence widely regarded as appropriate is based on a distinction between policy-making on the one hand, and the management and operation of the enterprise on the other. This distinction often is difficult to draw in practice.

(d) Current moves towards more open government and public participation in decision-making raise problems for some public enterprises, as in the potential conflict with commercial confidentiality. The extent of freedom from central control granted to a particular enterprise will also influence the extent to which public participation in decision making is possible. Relative freedom from central control may diminish an enterprise's obligation to be responsive to public pressures of various kinds, although this is not a conclusive factor: in some cases a public enterprise with relative freedom from central government control may be more responsive and communicative towards its clients and the public than an enterprise which is more closely tied to government bureaucracy.

These broad reasons for seeking a more systematic approach to public enterprise are reinforced by:

(i) the emergence of new opportunities for government intervention in commercial fields, which has intensified the debate centred on the role and performance of government in the market;

(ii) the requirement for major adjustments to public expenditure priorities in present economic conditions, which emphasises the importance of improving the capacity for making systematic assessments of the options for government involvement.

Such new challenges cannot be adequately met in the fragmented framework in which public enterprise currently operates, and they add weight to the argument for a set of consistent principles and guidelines for public enterprise, in place of the ad hoc approach of the past.

PART II

THE CASE FOR PUBLIC PROVISION:

AN EXAMINATION OF THE ROLE OF PUBLIC ENTERPRISE

The role of public enterprise is justified by the existence of a public purpose connected with the market, and by the efficiency with which this purpose is carried out. There is at present strong support, from various sections of the community, for devolving to the private sector activities which private business is presumed to be capable of taking up, or which it should be left to carry out without competition from a state agency. The support for what is generally referred to as 'privatisation'[1] is based on a number of expected gains: reduced government influence over the disposal of productive resources; the generation of a 'one-off' capital sum from the sale of assets for alternative investment[2]; an immediate and long term reduction in the public expenditure required for funding the activities of state programmes; the possibility of implementing new government programmes which, as substitutes for former activities, could be undertaken without necessarily a net increase in the size and cost of government; and finally, the prospect of enhancing overall economic performance. Whether privatisation can produce these benefits depends on:

(i) whether matters of public interest exist which warrant government intervention;

(ii) if (i) does apply, whether on grounds of relative efficiency the intervention is best carried out by public or private enterprise, within the range of options presented by government provision, government financing of private production, and government control or supervision of total private provision.

Ultimately, the choice between public and private ownership of enterprise is a political one. It is a matter of philosophical belief as to whether it is in the common good to have state ownership and control of enterprise. The philosophical ground shifts as much in New Zealand as elsewhere, and is reflected in the different attitudes and actions of successive governments. Nevertheless, there are non-political issues involved in this choice which are of considerable current importance. In this section, these issues are explored by reference to individual public enterprises in New Zealand under the following general headings: justification for market intervention; the efficiency of public enterprise; and the scope for private provision: considering the options.

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1 Because this expression is in current use, and its meaning is commonly understood, it is used in this paper as a convenient shorthand for the transfer of public sector activities to the private sector by means, for example, of: the sale of the whole or part of an enterprise; the sale of assets; putting work out to private contract. See Pope, op.cit., for a discussion of the forms privatisation may take.

2 This will not apply in all instances. Where state enterprises do not enjoy direct subsidy from government then there will be no reduction in public expenditure or substitution possibility.

JUSTIFICATION FOR MARKET INTERVENTION

The relationship between the reasons for government's involvement in public enterprise and the current objectives of the enterprise is not always evident in practice. Objectives may not be stated clearly and comprehensively.[3] Furthermore, the relationship is affected and obscured by the existence of mixed, sometimes conflicting, objectives, changes in market structure, and variations in government's market role.

Multiple Objectives

Public enterprises are characterised by a mixture of commercial and non-commercial objectives. These will not always be compatible. In the case of DFC, for example, the establishing legislation limited its role to a 'lender of last resort'. This provision was intended to allay private sector criticism that DFC would compete with private business. It proved to be too much of a constraint on DFC's performance and was removed after criticism by the 1969 National Development Conference and a World Bank investigation.

The DFC has evolved since then from a lender of last resort to a leading financier in its own right, though some conflict is still evident in the government's objectives for the corporation. Government's current policy is for DFC to 'stand on its own two feet' financially. This led to withdrawal of concessional lending to DFC (in the mid 1970's) which ironically has forced it to compete with, as well as complement, the private sector. The corporation has coped with this change most successfully, and is now self-funding[4], but the necessity to compete has the potential to interfere with DFC's developmental role in several ways.

(a) The DFC's capacity to fund high risk developmental projects is limited by the requirement now placed on it to finance its own operations. The 1981 Annual Report draws attention to the economic importance of technological innovation and the financial risks involved in the commercial development of these innovations. At present finance is available through the government-funded programmes administered by DFC, such as the Venture Capital Fund and the Applied Technology Programme, but although DFC does not regard this capital as adequate, it considers that it cannot fund the development it perceives as necessary from its usual sources because of the risk entailed.

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3 G. Corti, 'Perspectives on Public Corporations in Five Nations', Annals of Public and Co-operative Economy 47 (Jan/March 1976). This study concludes that 'the need for clarity stems from three desiderata. First the management of the enterprise must know what its aims are and the broad limits within which it can formulate these aims for itself. Second all people engaged in the enterprise need some indication of these aims and the extent to which they derive from management; the extent to which they have been occasioned by broader social, economic or political considerations; and the degree to which they can influence the goals having regard to their differing origins. Third, because by their nature the enterprises are public, the clarification of objectives is a necessary condition of public accountability which seems a prudent matter to ensure in a democracy'.

4 See the discussion of DFC's funding and productivity in National Business Review (9 August, 1982).

(b) The need to compete may lead DFC into market areas which conflict with its developmental objectives. The 1981 Annual Report draws attention to DFC's conformity with its developmental functions, but DFC sees itself effectively competing, and proving its status, in a commercial context. This is illustrated by the existence of DFC's annual report in two different forms - the standard black and white, 'no frills' report to Parliament produced by the Government Printer, and the glossy, 'up-market' version for investors and clients. The DFC was recently reorganised into a Small Business Development Division, and a Corporate Finance Division which 'has the role of directing resources into medium and large sized development-oriented companies, and major resources based projects'.[5] This suggests that assistance at the higher end of the scale has been accepted in principle and in practice. The DFC's results for the year ending 31 March 1982 show that 'larger clients' received assistance to the value of $181 million for 190 projects compared with $53 million for 699 projects handled by the Small Business Development Division.

DFC regards the number of approvals as the significant factor, with the Small Business Development Division representing 79% of total project approvals. Besides, the money spent on large businesses is spent in pursuit of developmental aims, and has not been 'diverted' from assistance to smaller businesses - no application has been turned down for lack of funds. Nevertheless, DFC's involvement in corporate financing brings it into competition with other financial institutions and, although DFC argues that this involvement has encouraged the private sector to follow DFC's lead, this does not necessarily justify continued operation in areas which become competitive. DFC's legislation undeniably emphasises assistance to smaller businesses, so to the extent that a substantial amount of money and resources is devoted to large firms (39% of the combined staff of the two divisions and 77% of the funds provided), or there is an increase in the corporate finance share of project approvals, questioning of DFC's objectives is likely to be provoked. Should DFC's ability to raise funds be constrained (and there are indications that this is happening), competition between corporate finance and small business development could occur.

Extension of DFC's equity participation (total equity investments increased from $6 million at 31 March 1979 to $31.6 million at 31 March 1982), including partnership in a joint venture with foreign interests (the Saudi-New Zealand Capital Corporation Ltd), shows that DFC is developing a closer relationship with the private sector and leads to the question of whether this relationship is appropriate given DFC's developmental role.

Equity participation by a public agency is a sensitive area. In the past, DFC showed little enthusiasm for this role and eschewed a controlling interest. However difficulties experienced by high risk ventures and some small to medium-sized enterprises in obtaining equity capital from the private market encouraged DFC to increase its involvement in this form of financing industrial development.

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5 Report of Development Finance Corporation of New Zealand, B.26, (1981), 4.

During 1981 there was concern over DFC's involvement in Polycorp, a joint public and private sector venture to produce and market a brand of educational microcomputer. DFC had a majority shareholding and provided a general manager from its staff. The General Manager of DFC admitted that the DFC's continued involvement was 'probably one of the highest of any scheme funded by the DFC' but rejected the suggestion of conflict of interest if DFC were asked to finance a rival product. However the more extensive DFC's control of and active involvement with a company (eg lobbying government to buy the company's products), the more embarrassing the probable conflict of interest will be. There was also concern from computer importers and manufacturers over the Minister of Education's proposal to purchase the machines without consulting the industry and without calling tenders.[6] If DFC equity participation in private enterprise is used to give marketing advantages to these companies, this would create hostility in the private sector and interfere with pursuit of DFC's developmental, complementary role.

DFC's partnership in joint ventures with overseas-owned companies is equally sensitive. DFC regards joint ventures such as the Saudi-New Zealand Capital Corporation Limited as an appropriate means of obtaining foreign investment for new developments while ensuring effective New Zealand control. DFC has reduced its 37.5% original interest to 25%, and 25% of the shares are now held jointly by the Goodman Group (100% New Zealand-owned) and Rothman Industries (80% New Zealand-owned). Careful selection of partners and allocation of shares is necessary to allay any public suspicion over whether effective New Zealand control can and does operate. The extent to which DFC can participate in similar ventures is limited because if DFC were involved in managing several such funds, conflict of interest could occur.

Some incompatibility between commercial and non-commercial objectives has been apparent with the Tourist Hotel Corporation, established by the 1955 Tourist Hotel Corporation Act to assume control and operation of the government-owned hotels from the Department of Tourist and Publicity, and to encourage the development of the tourist hotel industry in New Zealand with a view to promoting and increasing tourist traffic from overseas and within New Zealand. Although the THC's primary function is commercial, it has broader statutory functions which include: encouraging the full and proper use of the scenic attractions and recreational facilities for which it is responsible; advising or assisting other persons in the provision of services or amenities for tourists e.g. assistance with several South Pacific hotel developments; and control of scenic attractions and recreational facilities

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6 See National Business Review (27 July 1981).

7 The most recent reported policy directive of any substance described THC's role as: 'to administer its facilities efficiently and economically so as to maintain profitability, earn overseas exchange, and participate in tourist development; to recommend to Government the development of necessary facilities not catered for by private enterprise; and to co-operate with other State agencies in implementing the Government's tourist policies' (Report of the Tourist Hotel Corporation of New Zealand, G.24 (1978), 4).

on land it owns or administers. It is required to implement Government policy. This policy, reflected in successive policy directives and decisions requires the THC to operate profitably, but does not allow it to establish or operate hotels in metropolitan areas which would assist it to make a profit. The Cabinet has, however, recognised that losses may have to be offset from time to time because of restrictions on operations. Present government restrictions on commercial activities affect profitability. The THC warned in its 1978 Annual Report (p.4) that 'unless the terms of such directives remain closely related to current circumstances they could isolate the Corporation from the opportunities and the needs of the market and the industry'.[8]

In recent years, possibly to compensate for restrictions on its commercial activity, the THC has entered into separate marketing and representation agreements with major enterprises in the Australasian accommodation sector. Although such partnerships benefit the THC and the development of the accommodation industry in New Zealand, the element of foreign ownership in some of these partnerships, and their size and influence (see the THC's 1979 Annual Report, which notes that the THC/Flag Inns/Travelodge association is now the largest hotel/motel referral chain in the South Pacific), suggest a potential for conflict of interest, because THC's obligations to private sector partners might not always be compatible with its broader responsibilities to tourism development in New Zealand.

Market Structure

(a) Variation in Market Role

Decisions to establish public enterprise in New Zealand show no consistent perception of the objectives of market intervention. The market role of public enterprises varies widely, from virtual monopoly such as electricity generation and distribution to full competition such as the two insurance offices and the Bank of New Zealand, to joint partnerships with private enterprise. Historical considerations had a strong influence on agencies established in earlier periods of New Zealand history, when the private capital market was deemed to be unable to provide for the range of goods and services needed to develop important components of the New Zealand economy, or its social life; but political preference also has been a central factor.

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8 The THC's General Manager included withdrawal from 'politically and financially difficult hotel management contracts' in the Pacific as one reason for this year's improved financial results (see Evening Post, 26 May, 1982). On 6 April 1982, The Dominion reported that the THC appeared to have Cabinet approval to negotiate a management contract for a Wellington hotel being built by a Hong Kong-Wellington consortium, though the THC was recently prohibited from entering a similar management contract with the New Zealand-owned James Cook hotel.

The lack of any consistent principle in respect of the market role of public enterprise is illustrated by the contrast in the way that gas and electricity are produced and distributed. In the case of gas, the finite nature of the resource puts it in the category of a natural monopoly. Natural monopolies in New Zealand tend to be state-owned and operated. Yet, gas processing and distribution runs on a commercial and competitive basis with private ownership, although in the case of Maui gas (the predominant source of gas supply) the government exercises control over uses and prices. Hydro-generated electricity, although a renewable resource, has been retained as a nationalised industry.

In the financial sector, the market roles of the Government Life Insurance Office and the Post Office Savings Bank again show variation of approach. Both were established to provide secure investment opportunities for the lower income earner, but the Government Life Insurance Office competed with other life insurance companies from the outset, while in the first few years of the POSB's operation (from the late 1860s to the mid 1870s) there were several attempts to have the trustee savings banks compulsorily taken over by the POSB, which would have created a monopoly. As a result of the restrictions on the operations of trustee savings banks, the POSB was protected until 1964, when the restrictions prohibiting the TSBs to have branches further than 25 miles from their head offices were replaced by regional divisions enabling coverage of the whole country. At this point trading banks were also permitted to establish savings banks in competition with the POSB and the TSBs.

The complementary role of government in the market is illustrated by the Development Finance Corporation and the Tourist Hotel Corporation. The earlier discussion, however, shows the different extent to which these two agencies are permitted to diverge from their complementary roles.

Competition between two different public enterprises, where it leads to duplication of goods and services, or where it becomes controversial, also calls into question government's broad policy on the objectives of intervention.

Because of changes in the life insurance market, as the effects of inflation make life and endowment insurance less attractive as a form of long term saving, the GLIO has been forced, along with other life insurance companies, to put more emphasis on less developed areas such as superannuation, a service already provided by government through the National Provident Fund.

The recent controversy over price cutting between the Railways Corporation and the Shipping Corporation[9] adds another dimension to the question. The General Manager of Railways has argued that anyone taking business from Railways just makes Railways less profitable thus increasing the cost to the taxpayer of subsidising the operation. This ignores the fact that Railways' gains achieved at the expense of the Shipping Corporation equally will be at the expense of the taxpayer. The advent of the Railways Corporation, with taxpayer subsidy confined to specific 'social services' (and the end, therefore, of access to open-ended taxpayer subsidy) should mean that the pricing practices of Railways will have to meet normal commercial criteria.

9 See National Business Review (29 March, 1982), 3.

These inconsistencies make it difficult to defend the validity of public enterprise's role, particularly in terms of market domination, against the present emphasis in many quarters on encouraging more competition between public and private sectors and increasing the opportunities for private provision of goods and services.

(b) Relative market strength

Some of the main reasons for establishing public enterprise arise from perceived inadequacies in the private market at the time. Developments in the private market, however, have strengthened the capacity of private enterprise to play an effective competitive role and to enter areas presently operated as government monopolies or quasi-monopolies. The increased competitive strength of private enterprise:

- has reduced the justification for government participation in some areas of the market;

- is challenging the existence of special advantages presently enjoyed by public enterprises which artificially strengthen and protect their market position relative to private competitors.

(i) The strength of the life insurance market, in terms of competitiveness and security of assets is now far greater than it was when GLIO was established to provide small investors with security and regulate the industry by competition. As well, the potential dangers of foreign ownership are no longer as relevant as they were then; the Overseas Investment Commission, established by statute in 1973, supervises and controls the extent of overseas ownership. The private life insurance market is directly controlled by the provisions of the Life Insurance Act 1908, and by the functions and powers of the Government Actuary. A recent State Services Commission review of the role of the Government Actuary commented on the need to improve the regulation and control of the industry as the legislation is out of date. In this context, the trend overseas towards using insurance commissions was touched on. These changes in the market and the way it is controlled indicate that means of regulation other than direct participation are available to government to ensure the probity of modern market conditions. GLIO regards itself as a competitive life insurance company and is eager to increase its independence from government. As GLIO is neither directly financed by government (it is funded entirely by the policy holders), nor serving any significant non-commercial purpose, the arguments for it to retain its connections with government are not strong.

In the case of SIO, the need for direct government involvement in order to regulate the insurance industry could also be questioned, although SIO still has an acknowledged regulatory role in keeping premiums low. However, the large number of competitors should be sufficient to keep prices at a realistic level, unless the Insurance Council (to which private accident and general insurance companies belong) exercises so much influence over its members that it creates an effective monopoly. The usefulness of other methods (statutory regulation and by insurance commission control) has not been properly explored. In addition to regulation of the industry, SIO has since the 1960s also taken on public functions such as providing export guarantees and acting as claims agent for the Accident Compensation Commission. Without a government guarantee against losses arising from political causes, the private sector was not interested in providing export credit insurance, and because of perceived practical difficulties, private sector companies accepted SIO taking on the ACC agency, so long as this was not taken as an opportunity for SIO to canvass other business[10].

In the last decade the importance of tourism to New Zealand has increased substantially and there are numerous indications that the tourist industry in New Zealand is maturing rapidly (e.g. an increased number of travel agents in New Zealand and overseas, a proliferation of organisations to represent interests within the industry, private sector capacity to regulate standards and provide training, and increased co-operation between the department and the rivate sector). There is consequently criticism by some parts of the private sector of the industry concerning Tourist and Publicity's involvement in commercial activities that are profitable or otherwise attractive to private industry. This applies particularly to the department's operation of programmed tours (Tiki Tours), sale of outbound travel and overseas sales.

Tiki Tours ranks fourth largest among the published coach tours of New Zealand, and their past success has given rise to speculation that the Government Tourist Bureau favours Tiki Tours when presenting and promoting New Zealand tours. Recently, the presence of private New Zealand agents in Australia and USA has increased, creating pressure to review the need for Government Tourist Bureau sales facilities in overseas markets.[11] Sale of outbound travel is profitable and the industry is particularly critical of the Government Tourist Bureau's monopoly under Treasury regulations of Government-sponsored travel. This captive market accounts for 15% of New Zealand Government Tourist Bureau turnover. What some

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10 See A Manning, <u>Cover Story : The History of the State Insurance Office</u> (Wellington, 1980).

11 Note, however, the industry's reaction to the closure of the Toronto diplomatic post and reduction in the number of travel officers at some other posts, reported in the <u>Evening Post</u>, March 18, 1982. The president of the National Travel Association wants more government funds for tourist promotion as, for the first time since 1968, the tourist industry would not reach its growth target. Despite the fact that the Minister has promised no effect on tourist promotion from the three percent cuts, the industry is critical of the decision to close the Toronto post and transfer the travel commissioner to Vancouver, as New Zealand is not now represented in the east which 'has the industry, money, and is the market with the bigger potential'.

sectors of the tourist industry seem to want is withdrawal of the department from profitable commercial activities but continuing provision of a domestic travel sales service and arrangement of special interest tours and itineraries for individual travellers - activities which are not directly profitable but which are convenient for the industry and help give New Zealand a competitive edge in overseas markets.

Reduction of Tourist & Publicity's commercial activities has been suggested in the past, for example by the 1962 Royal Commission on the State Services, which saw these activities as diverting energies from the department's major purpose of tourism promotion and development, and by recent State Services Commission review. As with the insurance industry, the pattern overseas is indirect state involvement by means of an independent tourist authority or commission (e.g. Australia and Britain). Direct market participation through Tiki Tours and the Government Tourist Bureau does, however, provide some consistency and stability in a volatile market by supplying an outlet for small operators. To regulate private market activity usefully, GTB must be able to prevent monopoly in the private sector, which it does by assisting small operators not affiliated to major tour operators.

The insurance offices and the Department of Tourist and Publicity are competitive enterprises. Even where the public enterprise is a monopoly or quasi-monopoly, the ability of the private sector to enter the market has grown. As a result there is growing local and international interest in competition for public works contracts, in such areas as energy development and dam construction, which creates pressure to review how far the continued dominance of the Ministry of Works and Development in these market areas is necessary in the public interest.[12] Interest in competing need not to mean unnecessary and uneconomic duplication of, for example, postal services, rail transport and electricity distribution networks, but it is a reaction against limitations on competition in newer areas, such as courier services and viewdata systems, and inappropriate retention of state market power in existing areas. There is a tendency to apply monopoly power more widely than pure

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12 Though note the comments of the Commissioner of Works reported in The Evening Post, August 17, 1981: of 349 civil engineering contracts let by MWD in the past year, in 43 cases only one bid was received and the contracting industry did not appear to be as entrepreneurial or as competitive as the taxpayer was being told. This contrasts with the Minister of Works' statement to the Contractors' Federation with regard to the Clyde dam contract: 'there has been an assurance that true competition will be forthcoming from the New Zealand industry ... that New Zealand contractors can do the job I have no doubt'. The Minister gave the total number of contracts let to private enterprise, worth more than $20,000 each as 698 in 1980-81 (with a total value of over $128.8 million) c.f.562 in 1979-80 (total value $73.9 million) (Evening Post, August 11, 1981).

efficiency considerations warrant i.e. outside the boundaries of the 'natural monopoly'. For example, it could be questioned whether, on grounds of efficiency, the Post Office's monopoly of telecommunications needs to extend beyond the basic network system to cover such services as telephone installation.

When public enterprises are established, it appears that the strength and capability of the market is not always taken into account. For example, when DFC was established the potential of existing organisations to provide development finance may not have been adequately considered.[13]

Debate is presently occurring over the role of DFC in a strong private market as a result of the submission by the trading banks and Development Finance Corporation of separate proposals to operate a resource development bank. The need for direct government involvement in this area has been questioned[14] and assistance by way of a subsidy or rebate advocated, which can be defined and measured in the government accounts. Mr R Parker comments in the National Business Review[15] that similar banks overseas are non-governmental, although some began by being entirely government-owned, and he favours joint state-public financial involvement in the major development projects about to get underway, to ensure some local control over the massive investments.

(ii) In a number of ways, public enterprises are insulated from competition by means of special advantages, for example: the GLIO's exclusive canvassing rights in government departments and a government guarantee; DFC's exemption from the reserve asset ratio; the GTB monopoly over official travel; and the Railways Corporation monopoly on long distance freight haulage. Changes in private sector market strength raise the question of whether such advantages are still appropriate, though the private sector also enjoys protection from open competition, through government measures such as the issue of licences, and through the practices of individual private market groups.

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13 This view is based on unpublished research on the Development Finance Corporation.

14 See D. Johnson 'Should the "fifth bank" start from scratch?', The New Zealand Economist (July 1981)

15 December 7, 1981.

The Government Life Insurance Office has been criticised by the industry for its exclusive canvassing rights in Government departments, and also has the protection of a Government guarantee. The GLIO is unwilling to give up its advantages despite its interest in developing greater independence from government as a commercial operation.

The growth of DFC's power in the market raises the question of whether its special advantages are still appropriate, or whether these should be removed in response to criticism from DFC's competitors. The government-funded schemes the DFC administers (e.g. the Applied Technology Scheme and the Venture Capital Fund) attract clients who are then likely to use those other financial services which DFC provides in competition with privately-owned financial institutions. DFC is exempt from the regulations which require other financial insitutions to hold a specified proportion of their funds in government securities or other defined reserve assets. The reserve asset ratio affects an institution in two ways: it has to attract a high number of deposits to maintain its private lending; and its overall return is lowered because of the investment required in relatively low yielding government stock. The origin of DFC's exemption appears to have been in the nature of DFC when the regulations were introduced. Unlike the financial institutions to which the regulations do apply, DFC's activities were funded entirely by government (although initially part of its equity capital was subscribed by private enterprise), and were restricted by the lender of last resort provision to non-competitive areas. Now that DFC obtains most of its funds from non-government sources and is able to compete with other financial intermediaries for the public's deposits and for lending opportunities, there appears to be little justification for special advantages.

The 150 kilometre limit on road freight haulage prevents competition with Railways from road transport. This gives Railways a monopoly on long distance land transport and allows pricing strategies to be used to reduce competition from sea transport as well. Even with protection, rail has achieved a very low rate of return on its 'commercial' operations.

Further pressure to remove the protective advantages of public enterprise comes from:

- the recent proposal to remove BCNZ's competitive advantage of a monopoly over programme information;

- current scrutiny of protectionism in the private sector for example, producer subsidies and trade protection (prompted by CER), and Industries Development Commission studies aimed at restructuring the private sector to increase competitiveness and efficiency;

- use of subsidies for non-commercial elements of public enterprise activities (e.g. Railways Corporation and Air New Zealand) instead of special advantages to compensate for involvement in unprofitable activities, or for restrictions on market operation for various political or social reasons, to allow public enterprise to compete on the same commercial basis as the private sector (see below, pages 53-54).

Discussion of the three issues relating to the justification of market interventions through public enterprise - the effects of multiple objectives, the variations in government's approach to market role, and the changes in the relative strengths of public and private markets - show that there is not always a strong case for public enterprises to continue in their present form, if at all. The case for public enterprise would be more convincing if the reasons for their establishment or continued existence were exposed to full public debate.

There is, in general little public discussion of government's objectives for a particular enterprise and whether public enterprise is the most suitable means to pursue these objectives, because of the tendency to establish public enterprises without full public definition at the time of their establishment of:

- the reasons for selecting this particular form of intervention, and the costs involved;

- where the Government intended their financial and commercial activities to take them;

- the extent to which it was anticipated that they would compete, or dominate a particular market sector; and

- how far private participation (or exclusion) was built in to the original terms of reference.

THE EFFICIENCY OF PUBLIC ENTERPRISE

A central issue in examining the case for public provision is whether the Government is a more efficient producer than the private sector.

The Problems of Measuring Performance

No clear evidence of a general kind exists in New Zealand of the relative efficiency of public and private enterprise, despite the readiness with which it is assumed that the private sector is managerially and technically more efficient than the public. Furthermore, there is a potential contradiction between this argument for private provision of goods and services and the argument that public enterprise should withdraw from profitable activities in favour of the private sector. The general impression gained from overseas literature, however, tends to support the common view that in general public enterprises are less efficient in producing a given output than private sector counterparts.[16] While it is unlikely that comparative studies of public and private enterprise performance would show New Zealand to differ markedly from the experience of other countries, the performance of public enterprise in New Zealand is not uniformly bad. Recent work in New Zealand has shown that some public enterprises have demonstrated declining unit costs relative to the economy as a whole, and in that sense were not a drag on resources. Others, for example postal services, have shown rising relative unit costs.[17]

On the basis of financial performance, not all state enterprises perform 'badly'[18] and not all private enterprises perform well. As shown in Appendix II financial performance,[19] measured by rate of return on capital and reserves, varies from 0.9% to 21.6% in the private industry groups selected and the state enterprises selected show substantially more variation. As argued below (pages 33-34) however, any conclusions to be drawn from the use of such broad measures of performance need to take account of the environment in which particular enterprises may be constrained to operate, and are subject to major qualifications.

On the basis of comparisons within individual industry groups some state enterprises appear to perform creditably.

In 1981 a team representing MWD, Treasury and the Contractors Federation reported its findings of a comparative study into the costs of work undertaken by the MWD and private contractors on the Upper Waitaki Power Development Project over the period 1972 to 1979. Firm conclusions on the relative efficiency of MWD plant operators and private contractors were not possible because of the significant, but unqualified, effect on costs of Government purchasing advantages and the pricing practices adopted by the MWD. Treasury accordingly attached a disclaimer to the report.[20]

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16 P.S. Bevin, The Rising Cost of Public Services, MPP Research Paper, Victoria University of Wellington (February, 1981), 40-41, refers to relevant comparative studies.

17 Bevin op. cit. measured increases in unit costs of production for NZ Railways, NZ Electricity, NZ Post Office, the Police, Hospital and Education services relative to unit costs in the economy as a whole.

18 Examples of agencies which have reported a substantial profit for 1981-82 include the BNZ, the BCNZ, the SIO and DFC.

19 See also D.F. Quigley, 'Economic Restructuring and State Enterprises', The Manufacturer (20 October, 1980), for a comparison of private and public enterprise on this basis.

20 See The National Business Review (August 31, 1981).

In the life insurance industry the performance of the Government Life Insurance Office in terms of market significance is declining. Market share has been falling steadily (26.3% of policies issued in 1959 to 12.4% in 1979[21], and still declining according to the Insurance Commissioner) and GLIO's assets as a proportion of the total assets of the life insurance companies in New Zealand has decreased from 20% for the year ending 31 December 1970 to 17% for the year ending 31 December 1980[22] At the same time there has been an increasing expense ratio (management expenses as a percentage of total revenue have increased from 9.85% in 1972 to 12.4% in 1980). The effective rate of interest earned on the funds was a record 10.55% for the year ending December 1980,[23] but the yield on funds is still negative because it is below inflation. Nevertheless, the GLIO's results compare well with those of its competitors. The GLIO's expense ratio of 12.4% in 1980 is below the industry average of 17.1%[24] (though the Commissioner notes that management expenses vary with the type of business). The GLIO's bonus rates are currently the best in the market according to the Insurance Commissioner.[25]

In the general insurance industry, the State Insurance Office's share of premium income has gradually increased (16% in 1969-70, 18% in 1975-6 and 22% in 1978-9). The ratio of expenses to premium income has fluctuated little in recent years (15.3% in 1975, 13.26% in 1979 and 14.59% in 1980), and is substantially lower than the average ratios for all accident insurance companies (1977-78 26.4%; 1979-80 27.8%).[26] Profits fluctuate, because of the unpredictability of the insurance business, but the SIO compares well with its competitors. The SIO's 1980 annual report notes that a number of companies sustained losses for that financial year while the SIO made a small profit, and the State Insurance Office's Annual Report for 1981 shows a net profit before tax of $10.5 million ($4.5 million after tax and other deductions), which the SIO indicated was substantially higher than the profits of some of its major competitors. (Straightforward comparisons like this do not take account of difference in size. The SIO, in terms of total assets, is bigger than its New Zealand-based competitors, and amongst the biggest of all the non-life insurance companies operating in New Zealand.[27])

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21 Figures from a 1979 SSC review.

22 Figures derived from GLIO Annual Reports and the <u>Reserve Bank Bulletin,</u> July 1971, November 1981.

23 But see <u>Insurance Statistics 1979-80,</u> Department of Statistics (Wellington, 1981), Table 5 where the GLIO's effective rate of interest returned on life assurance and annuity funds is given as 8.72% compared with the industry average of 9.9%.

24 See <u>Insurance Statistics,</u> 5.

25 See the 1980 Annual Report for details of the GLIO's bonus payment.

26 See <u>The New Zealand Official Yearbook 1981,</u> Department of Statistics (Wellington, 1981), 776.

27 Compare the SIO's total assets of $140.7 million with the total New Zealand assets of fire and accident insurance companies, see <u>Insurance Statistics,</u> Table 13.

It should be stressed, however, that in general the conclusions drawn from data comparing public and private enterprise performance are subject to important qualifications.

(a) Public enterprise commercial objectives are complicated by the inclusion of non-commercial objectives which can have significant effects on the financial performance of some enterprises. Comparisons which take no account of these effects are misleading. For some enterprises the public purpose they serve has little or no impact on commercial performance. State Insurance for example is expected to regulate the industry by being efficient and successful, DFC needs to make a profit to fund its developmental activities, and electricity is required to make a profit to finance capital development. For other enterprises, the effects may be considerable. The cost of operating unprofitable social services contributes to the losses made by the Railways. The THC's potential profitability has been restricted, because its loss-making hotels have to be cross-subsidised by the few which do make a profit and government policy directives have prevented expansion into profitable metropolitan areas. The BCNZ is required to operate many social services, and licence fees are not determined in relation to the cost of services provided. The Government Printing Office is required to keep stock levels higher than would normally be held by private sector counterparts to ensure continuing availability, and the office's service function requires the operation of some programmes on a break-even basis as opposed to returning a profit. The financial results of the POSB and the Rural Banking and Finance Corporation are affected by government's lending and investment policies.

(b) There are cases (e.g. the MWD and the Railways) where protection of a public enterprise from competition distorts the results of comparison, and the effects of such protection on performance need to be determined before a decision on relative efficiency can be reached. However it is also true that private enterprise enjoys substantial insulation from the effects of competition, through tax concessions, subsidies and protective regulation, just as many state enterprises are presumed to. The comparison of public and private enterprise performance is complicated by these provisions for market protection because it is not possible to assess what effect the absence of market discipline in either sector has on relative efficiency.

(c) Some of the larger state enterprises are monopolistic in certain areas of operation (e.g. Railways, Post Office, Electricity and to some extent Air New Zealand) so there are no private sector counterparts with which they can be compared; neither are profitability or rates of return of themselves indications of efficiency in either sector, because they may simply result from high prices which can be charged in monopoly situations.

(d) For some other enterprises, it is not possible to compare like with like. For example, because the Housing Corporation's surplus is the arbitrary result of the difference between the budget allocation for the year and the actual operating costs (see notes to Appendix II), because both borrowing and lending rates are not market-related, and because private lending institutions conduct a wider range of business, comparison of the Housing Corporation's results with those of private sector lenders of mortgage finance is invalid. The operations of the Commercial Division of the New Zealand Forest Service are confined to wholesaling solid wood products, unlike those of its private sector counterparts, and it is not adequate to compare insurance institutions on the basis that they produce the same generic product as different returns and costs are likely from different types of insurance cover. The usefulness of rate of return data for comparing public and private enterprise is affected: because recorded asset values of public enterprises can be significantly different from their market values; and because of the method of funding of some state enterprises e.g. where loans have been written off and where outstanding loans have been converted to equity capital.

Measuring the costs of, and effective attainment of, economic and social objectives is much more difficult than measuring the financial dimension of performance. For this reason, these elements are not adequately reflected in information showing the return to government from its investment in public enterprise. The assessment of the performance of any public enterprise depends on a complex configuration of financial, economic, social and political factors, either not found, or found to a much lesser degree, in private enterprises, which limits the validity of comparisons.

Given the difficulties of measuring public enterprise performance in relation to the private sector it is beyond the scope of this study to resolve the question of relative efficiency. The available literature does tend to suggest that most public enterprises are relatively inefficient in the narrow sense of minimising resource use for production of a given unit of output but this general impression is qualified by the multiple objectives of public enterprises and the difficulty of defining and measuring public sector outputs. A more detailed and comprehensive study of individual enterprises relative to private sector counterparts than is undertaken here is required before the debate on public or private provision can be placed on a sound quantitative footing.

The question of relative efficiency can, however, be further explored by examining how far the performance of public enterprise is affected by political and administrative control. As discussed in Part I, public enterprises are subject to ministerial direction in the pursuit of their objectives and, to varying degrees, are also subject to the processes of central government supervision and control, as a result of government's legitimate concern with pay policies, major investment decisions and general financing of public enterprises, given government ownership and responsibility for the use of public funds.

Factors Affecting Performance

(a) Ministerial Direction

The fact that public enterprises are generally required to fulfil both commercial and non-commercial purposes and are thus subject to a greater or lesser degree of political control, complicates the achievement of those purposes. The extent and nature of ministerial control is an important aspect of public enterprise performance because: it can have negative effects on overall enterprise performance; in some cases, it may be used as an excuse for poor overall performance; and some agencies have become less willing to accept consistently reduced performance results where they consider themselves to be capable of success in commercial terms. Ways in which various public enterprises have been affected by policy interventions are illustrated below.

Interest rates are one area where public enterprises have been subject to control for reasons of economic and fiscal policy. The effect is to diminish financial performance. In the case of the GLIO, financed entirely by the policy-holders, this is against the interests of the policy holders whose funds are being invested. In 1974 DFC sought a general rise of approximately 1 percent in lending rates. This was opposed by the Government, though to protect DFC's financial viability (given its involvement in high-risk lending) an increase in the lending rate for high risk projects was allowed. Restrictions on the rates of interest POSB can charge on lending and pay to depositors reduce its competitiveness, along with various other controls e.g. restricting the provision of new client services and holding a larger proportion of depositors' funds in low interest bearing securities than other savings banks. Government also influences the investment policy of public enterprise. THC's expansion into profitable, and withdrawal from unprofitable, locations is restricted as a result of ongoing government policy, as discussed earlier in Part II. DFC was requested by government to step in when Matai Industries (set up on the West Coast in 1973 under regional development policies) got into financial difficulties.

The effect of government intervention on the competitiveness and profitability of public enterprises is currently being debated in the case of the BCNZ. Proposed legislation would give the Government greater power of direction over the operations of the corporation, for example, requiring the corporation to make available programme information presently the monopoly of The Listener, which may reduce The Listener's profitability. The legislative amendments to the Broadcasting Act also raise the question of the demarcation between policy areas, where government intervention is appropriate, and day to day management, where it is not.

The potentially negative effects of intervention by means of ministerial directive are mitigated when the following conditions apply.

(i) Provision for written directions and reporting these before Parliament is made, for example in the establishing legislation of individual public enterprises.

(ii) When the extent and nature of the responsibility of the enterprise's board and chief executive, and the policy areas in which it is appropriate for the Minister to exercise control, are clearly defined and agreed between the enterprise and the Minister.

(iii) When the extent to which commercial objectives are to be modified by considerations of government policy are negotiated and agreed between the enterprise and government.

(iv) When contractual arrangements are made between central government and public enterprises to provide services which government policy requires, but which cannot by their nature be commercially viable.[28]

It must be accepted, however, that the government retains the option to amend any arrangements made with a public enterprise where it considers it necessary to do so. Where legislation is affected, the alterations then become open to parliamentary debate.

(b) Administrative Control

Central government supervision and control is commonly thought to limit the capacity of public enterprise to respond to market forces and operate successfully in commercial terms. Public enterprises in fact show considerable variation in the form and degree of supervision and control which applies to them,[29] and the extent to which performance is affected.

GLIO for example attributes its poor performance and declining market share of the last 20 years to the lack of independence from central control in financial and staffing matters, which had produced an inflexible bureaucratic management style and structure unsuited to commercial operation and had failed to make managers sufficiently responsible and accountable for results.

The State Insurance Office takes a more conservative and positive approach to central control and is not seeking a change in its present mode of operation. It regards the process of annual appropriation of its operating expenses by Parliament and review by the Public Expenditure Committee as a useful discipline, and cannot see that its commercial performance would be enhanced by greater independence.

Thus, generalisations about the relationship between performance and independence from central control are not possible. The main areas of management where the effect on performance of central government control is most apparent are: organisational structure; financial management; and personnel management.

(i) Organisational Structure

Different organisational forms (e.g. departments, corporations and limited liability companies) are distinct in the formal nature of their relationship to central government. This formal distinction breaks down in practice because administrative characteristics vary so widely and cut across formal organisational structures.[30] On the one hand, freedom

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28 See below, p. 53.

29 See Appendix 1.

30 See The State Services in New Zealand, Report of the Royal Commission of Inquiry (Wellington, 1982).

from central control at the operational level may enhance the organisation's ability to respond to the market and encourage a more flexible, entrepreneurial management style, hence improving performance. On the other hand, the effective pursuit of public purposes requires that an enterprise be subject to enough control to ensure that it is a responsive instrument of policy, and that it can account for the non-commercial as well as the commercial aspects of its performance.

To achieve a desirable balance between independence and control in these terms, some public enterprises have been restructured and change is presently being contemplated for others. In restructuring, as in the establishment of new enterprises, there has been an increasing preference for non-departmental organisational forms which involve, supposedly, less central government control. Paradoxically, this preference has been accompanied by a reluctance to relinquish the elements of central control and also a desire to increase political control over existing non-departmental agencies to protect government's right as 'owner' to intervene.

In general, a change of any substance will require changes in organisational form, but it does not follow that a change of form will alone be sufficient to bring about substantial improvement.

First there does not appear to be a consistent correlation between structure and performance. The THC and DFC are both statutory corporations outside the public and state services with similar provisions for ministerial control and similar financial structures. The THC's profitability, however, is substantially constrained by government policy restricting competition while DFC is able to compete freely with other financial companies in profitable market areas with consequent effect on the return on shareholders' funds (see Appendix II).

The structure of Railways has been changed ten times during its history. It has been controlled by boards for five separate periods of its history (including the most recent phase of the New Zealand Railways Corporation which came into being on April 1, 1982). The rest of the time it has been run as a department under a single permanent head accountable to a Minister. These changes seem to have made little difference to the efficient and effective operation of Railways.[31]

The experiences of the State Insurance Office and Government Life Insurance Office, which are both departments of State, show that contrary to popular belief, flexibility and adaptability are possible within a departmental structure. In 1980, the SIO introduced a new structure for branches which improves cost-effectiveness by reducing the numbers of intermediate supervisors. The new Riccarton branch, instead of dealing directly with the public in the usual way, now administers three satellite district offices which deal directly with clients[32].

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31 See R. J. Polaschek, Government Administration in New Zealand (London, 1958), 56.

32 See Report of the State Insurance Office, B.21 (1980), 4.

The GLIO is presently re-organising its sales operation in line with private sector methods. A pilot scheme now operating in Auckland will replace the standard district offices, run by salaried personnel, with sales centres in the suburbs run by managers, who are paid on a commission basis and subject to only a month's notice.

The second, and related issue, is that the advantages of structural change may not be realised in practice, either because: in the process of designing and implementing the restructuring modifications creep in which inadvertently may thwart the original intention; or because existing procedures and controls are not sufficiently modified in accordance with the change.

In 1980 an advisory board was introduced to the GLIO to advise the Minister and Commissioner on the development and progress of the GLIO, to advise the Commissioner on all aspects of the office's operations and management and to report to the Minister periodically on the operations of the office. The reason for its introduction was to improve managerial performance, but the extent to which an advisory board, which has no statutory authority and responsibility nor power to hire and fire the chief executive, can bring about the intended improvement may be limited.

The possibility of changing the GLIO into a body corporate with a statutory board, while remaining in the public service, has recently been considered. But while the GLIO remains within the Public Service the Minister of necessity will have more direct and detailed responsibility for (and therefore control over) the GLIO than if it were outside the public service; and exemption from other forms of control could not be extensive.

The 1952-7 Railways Commission was identical with the former Railways Department in terms of financial controls and government control of policy and capital development. The only difference was the interposition of a board between the Minister and the permanent head, and the only effect of the change was 'an unnecessary and undesirable diffusion of responsibility'[33]. Under the new legislation establishing the Railways Corporation the Minister of Railways retains considerable powers which give him or her access to the affairs of the Corporation, particularly with regard to the extension or reduction of services and boards of enquiry. There should, however, be a positive effect from the greater freedom of commercial operation under the Act e.g. separate funding of non-commercial services, increased responsibility for capital investment decisions and the requirement to run its competitive services on a fully commercial basis. It is too early to ascertain the difference the new structure and legal status will make to commercial performance.

The third issue is reliance on inherent properties of the form itself, without sufficient thought for what is needed for the form to be effective in its particular context. In Canada, the Glassco Report of 1962 on Crown Corporations, which recommended that most of the corporations should be brought back into the departmental system, has been criticised for assuming that 'once the corporations were brought into the departmental fold, their accountability to the political level would be clear, and activities formerly carried out at an unseemly

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33 Polaschek, op. cit., 65.

distance from political control would be handled responsively and responsibly'.[34] The period of time which elapsed before GLIO's long-term decline was recognised and was acted on shows that such assumptions about departmental forms are untenable in New Zealand too. Organisational form per se will not result in responsible and responsive management.

Similarly, the adoption of private sector models may have limitations, as in the case of boards. Business acumen is essential given the commercial objectives of public enterprise, but as this is only one dimension of public enterprise performance board membership will always have to reflect the wider responsibilities and mixed objectives of public enterprise. The role and responsibilities of government directors have recently been the subject of discussion, because of the potential for conflict of interest between corporate concerns and those of the government. A Treasury survey[35] on this subject commented that written law denies a director the right to have regard to the special interest to which he owed his appointment. Hence a civil servant may be in 'an invidious position; failure to act in the interest of the company may render him liable to action for breach of duty while failure to promote government interests may imperil his position on the board and within the civil service'. The survey also identified the need for a policy on the nature of an official director's responsibilities with respect to the company and government. Whether the private sector model works well in its own context is a consideration that is sometimes overlooked. The effectiveness of private sector boards in New Zealand has been the subject of recent criticism which has emphasised the need for professionalism in board direction to match increasing professionalism in management[36] - an emphasis which has particular implications for the way in which directors are selected. With regard to public enterprise, the power of Ministers to appoint, or recommend the appointment of, directors sometimes gives rise to concern that political considerations play too much of a part, with consequent effects on enterprise performance.

(ii) Financial Management

In the financial management of public enterprises the operating rules are determined to varying degrees by the government, and consequently the rules differ from those imposed by market discipline which apply in the private sector. Departures from market norms affect the financial returns of public enterprise and can enable public enterprises to continue in the market with consistently poorer returns than their private sector counterparts. Where this happens, the share of the market and resources within a particular sector is not determined by relative efficiency, and overall performance of the economy is reduced.

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34 W A Baker, 'Accountability, responsiveness and public sector productivity', Canadian Public Administration (1980), vol. 23, No 4, 543.

35 Irene Taylor, Treasury Discussion Paper, 'The Responsibilities of Government Directors'. Quotation from P R Kyle, 'The Government Director and his Conflicting Duties'.

36 See R F Chandler, 'Directors' Responsibilities', Management (March 1982).

Central government control requires public enterprise to operate under different rules and conditions specifically in the areas of funding, pricing, investment, disposal of profit and tax liability, with corresponding effects on performance.[37]

(a) Method of Financing

The standard method of financing for government departments, including trading departments, is by annual appropriation through the central government budgetary process. This system, involving detailed expenditure procedures administered by the Treasury, over a 3-year budget cycle, has disadvantages for commercial operations, notably, reducing the ability to adjust financial requirements in response to market changes, and inhibiting the application of long term strategic planning.

In fact, various alternative financing methods occur in the public enterprise sector, including private sector forms of financing which are suited to business management: meeting current expenditure from current revenue; borrowing in the market to fund capital expenditure; covering losses by increasing equity finance.

The method of funding can have a significant effect on the financial performance of an enterprise. Private enterprise debt/equity ratios are determined by market norms which reflect, among other things, investors' perceptions of risks, the cost of different forms of financing and tax conventions. Financing of state enterprises not constrained by such market considerations may depart significantly from comparable private enterprises.

In public enterprises reliant on debt financing, interest charges can inhibit commercial performance,[38] particularly in the early stages of establishment when little revenue may be generated, because these charges must be met regardless of the enterprise's financial position. Equity

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37 The Controller and Auditor General has recently criticised the lack of flexibility permanent heads have to operate more efficiently: 'it is ... disappointing to record that they are still subject to very detailed and often restrictive rules and instructions applied by the control agencies of government', Report of the Controller and Auditor-General, B.1 (Pt. III) (1982), 8.

38 Recently the Shipping Corporation has endeavoured to improve financial performance, by reducing the costs of interest on loans and the levels of depreciation on capital assets, for example by arranging to lease the 'New Zealand Pacific' and the 'Container'. As a result, a reported loss of $7 m for the year ending 31 August 1980 was replaced by a net profit of $17.7 million in the following financial year. (See the Report of the Shipping Corporation of New Zealand Ltd., F.13 (1981)).

financing, with variable declared dividends, makes it easier for an enterprise to become commercially viable, because the true cost of equity capital, including the opportunity cost, may not be reflected in the organisation's financial statements. One example of this was the restructuring of the THC's capital in 1971[39] which resulted in a change from consistent operating losses to a published net profit in 1973.[40] The recently announced loan to Air New Zealand is potentially convertible to equity capital (see Appendix I), and the New Zealand Railways Corporation Act 1981 provides for the capital restructuring of the Railways by converting its debts to government, currently costing Railways around $30 million in interest charges, to share capital. Publicly provided equity in some cases is regarded essentially as a grant, with no immediate expectation that dividends will be paid on it. Without the discipline of a market-related dividend objective, the effective pursuit of commercial objectives by public enterprises requires objectives for return on funds employed and criteria for appraisal of investments.

The extent to which the government expects enterprises to be self-financing after the initial capital is supplied varies, as does the way in which enterprises are able to obtain funds. The GLIO and the SIO have paid back the initial capital sums and are now entirely self-financing. Since the mid-1970s, the government has reduced its concessional lending to DFC to the point where the Corporation is now self-financing. The agency has developed other sources of finance, both domestic and foreign, and with increasing confidence is able to enter such commitments without seeking or requiring a government-backed guarantee, although the Corporation is still constrained by the requirement for ministerial approval of its borrowing.

Where public agencies have freedom to raise money from non-government sources this raises the possibility of public participation in the form of equity investment, particularly if the trend towards joint public and private enterprise activity increases. This has obvious advantages, as it costs government less to achieve the objectives of market intervention and can bring in overseas as well as private domestic capital.

Government subsidy of an enterprise's debt financing, whether by lending money at below market interest rates or by guaranteeing borrowing from non-government sources, implies acceptance of a lower overall return compared with the private sector and that resources are not necessarily allocated to the most efficient producers.

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39 See THC's 1971 Annual Report.

40 $54,000, see 1973 Annual Report.

(b) Pricing

Though market considerations largely dictate pricing policy in competitive enterprises (eg the GLIO, the SIO, the Public Trust, the BNZ, the THC and the Government Tourist Bureau) there is sometimes criticism that public enterprises can undercut their competitors because of failure to build all costs into prices (eg Tiki Tours, MWD) or because the government will provide support in the event of an operating loss (a criticism levelled at Railways by its competitors in coastal shipping (see above p. 24). In other cases prices are determined by government policy. The Housing Corporation for example is the main vehicle for implementing Government housing policy, and the Government sets interest rates, loan terms and funding levels in accordance with government policy.

Where enterprises have a market monopoly, an efficient social outcome is achieved when prices are determined in accordance with long run marginal costs. Public enterprise monopolies (indeed all monopolies) are often suspected of using price increases to disguise inefficiency instead of dealing with inefficiency by improving productivity, and to that extent public enterprise pricing policy can act as a disincentive to good performance. Railways' use of pricing strategies, made possible by monopoly provisions and access to government subsidy, illustrate the effect on efficiency of departure from market norms (see pages 24 and 29).

(c) Investment

Private enterprise investment decisions are subject to some government control (e.g. reserve asset ratios) but the balance of their investment is determined by market forces (and corporate policy). In public enterprise, however, control is more pervasive, whether by means of ministerial directives as already discussed, or by means of general pressure (formal and informal) to take account of government policy, because of possible political ramifications of public enterprises dealing in open markets and investing assets which represent a major potential leverage on the economy. For these reasons the relative rates of return between state and private enterprises in similar activities may differ significantly.

(d) Disposal of Profits

Where the private sector deals with variable cash flows by reinvesting a temporary surplus in the light of economic and financial circumstances, at the discretion of the directors, there is little consistency of approach in public enterprise. Some public enterprises, such as DFC, retain their profits after payment of a dividend, which may be determined by their establishing legislation. Those which are departments usually return their operating surplus to the Consolidated Account, though this sytem gives rise to problems of financial management where cash flow is variable. In order to resolve such problems, a system of revolving funds has been introduced to part of the Government Printer's operation to allow more flexibility in the use of funds. Other enterprises, e.g. Petrocorp, because established under the Companies Act, are accountable to shareholders for dividend payments but not subject to specific directives on the disposal of surplus funds.

(e) Tax Liability

Tax liability is an externally imposed condition on the operation of private enterprises. In the 'public sector, however, non-trading organisations are exempt from income tax and have some exemptions from sales tax, while most trading organisations are liable for income tax (exceptions are the Post Office and the Railways Corporation), and government agencies which trade in or manufacture tradeable goods and services are required to pay both sales tax and customs duty. The THC also pays land tax.

Enterprises exempt from tax (e.g. Railways) have a competitive advantage. If each of these enterprises faced the same prices including tax and duty as other purchasers in the economy, this would ensure that purchasing decisions were made on a comparable basis, that inefficiencies were not disguised by special concessions, and that the true command over resources as a result of the operation of the government is publicly identified.

In conclusion, where public enterprise operates at lower levels of commercial efficiency relative to the private sector, this is at least in part a result of government varying the financial operating rules and of public enterprise being required to operate under different market conditions.

(iii) Personnel Management

In terms of government influence over personnel management, public enterprises fall into three categories.

(a) Those which are departments of the public service are subject to direct control by the State Services Commission as the central personnel authority of the public service. Pay scales and conditions of employment are determined by the Commission, in accordance with the State Services Conditions of Employment Act, 1977, and the Commission also regulates appointments, promotions, transfers and firing of employees according to the provisions of the State Services Act, 1962. The Commission also exercises control over staffing levels. The current practice (which is under review) involves fixing maximum staff levels or 'ceilings' for each department, and then applying a 1.5% annual reduction to this ceiling - a process known as the 'sinking lid'.

(b) Those enterprises classified as State Services (e.g. Post Office, Railways Corporation) are subject to the provisions of the State Services Conditions of Employment Act, but are not under the control of the State Services Commission. Each agency is its own employing authority and the Commission is jointly involved with these agencies in co-ordinating pay scales and conditions of employment. Cabinet control of staff levels applies.

(c) Those enterprises outside the State Services Conditions of Employment Act have the freedom to hire and fire staff, set pay rates and determine other conditions of employment. Their policies are influenced directly by the market and subject to the same legislative constraints and union pressures as private enterprise. In a number of cases, for example DFC, the THC and Petrocorp, this freedom is modified by the requirment to consult with the State Services Commission.

Central controls on personnel management can limit the responsiveness of public enterprises to their commercial environment[41].

If the argument advanced by the SIO can be accepted, control of staff levels may have detrimental effects on standards of service. Similarly, a State Services Commission review of the POSB noted that tight staffing in some District Post Offices has constrained the achievement of a more sophisticated banking service. The exemption in 1980 of the GLIO and the SIO from the sinking lid acknowledges that commercial operation requires more flexibility and that the market ought to create enough pressure to keep labour costs down.

An area which has been criticised for its supposed negative effects on productivity is public sector security of tenure. The GLIO, for example, has claimed that it finds it difficult to change its bureaucratic management structure and style towards a more commercial orientation because of public sector personnel policy. In the Railways low productivity has been attributed to retention of employees for social and political reasons.[42]

Criticism of security of tenure overlooks the positive reasons for its existence i.e. to ensure that the public sector operates as a career service, with appointment and promotion on merit, not influenced by political patronage. The possibility of reducing security of tenure for senior public service managers and introducing performance incentives similar to those which apply in the private sector could be considered, particularly if senior managers are granted more flexibility and independence as this implies a corresponding increase in directness of responsibility and accountability for organisational performance.[43] As the example of Railways shows, security of tenure may also reflect Railways' perceptions of government's broad employment responsibilities. Nevertheless there is a distinction between an explicit choice to spend public revenue on employment schemes and other forms of unemployment relief, and tacitly condoning or requiring high manning levels in public enterprise without specifying employment relief as an objective.

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41 In 'Broadcasting. Radio New Zealand: Running out of Licence', the New Zealand Listener (3 July 1980), the comment is made that wage and salary costs represent nearly 53% of total expenditure 'and because the BCNZ is tied to Public Service rates of pay and conditions of employment, there is no room to manoeuvre'.

42 See Bevin.

43 Issues such as these were addressed by the Royal Commission on Australian Government Administration. The Commission felt that elements of the 'career service' concept had mistakenly 'been allowed to become inflexible dogma of public service employment', and that an emphasis on equity in dealings with staff had led to 'a high measure of uniformity in the conditions of service and patterns of management in government employment'. The Commission argued that managers should be given scope to act entrepreneurially and should be held accountable for results. It also identified a need for: more flexible recruitment practices; reclassifying positions according to the performance of the incumbent; and improvements in promotion selection processes (including those for departmental heads). 'Royal Commission on Australian Government Administration. Summary of major themes of the report', Reforming Australian Government, Royal Institute of Public Administration (Canberra, 1977).

Relative freedom from state control of salaries and conditions of employment, as with DFC and Petrocorp, is intended to enable public enterprises to attract a wider range of applicants, particularly to include people with relevant overseas and private sector experience (though the salaries of senior managers of public enterprises are under High Salaries Commission Control - see Appendix I). DFC however, does not attribute its ability to attract and retain talented personnel for project analysis and managerial positions to its relative freedom from personnel control. DFC salary movements were geared to state movements until 1980 and relativity with the market place, both private and public sectors, is a major consideration. In order to maintain reasonable relativity and competitiveness with its various labour markets, DFC gathers data on salary levels and movements from sources in both sectors and uses this information to determine remuneration levels and movements for its own staff. DFC regards factors broadly described as 'job satisfaction' as more important than salaries for recruitment and retention. DFC would not want to revert to direct control because it regards the freedom to be 'professional' as important to its success. In DFC's opinion SSC control would be totally impractical in view of the extent to which it now deals in international markets.

Where salaries and conditions are not competitive with the private sector there can be costs in terms of training if the differential means that trained and experienced personnel are lost to the private sector. The SIO, the GLIO, and NZED are examples of enterprises which have tended to lose trained, skilled staff to the private sector. To an extent, high turnover is an inevitable cost in some public enterprises but if this cost becomes unacceptable, some relaxation of government control over pay, or, alternatively, some compensation for the costs of training, could be considered by government if it recognises an enterprise's contribution of personnel and expertise to national development as a legitimate and desirable function.

The discussion of the efficiency of public enterprise shows:

(a) the present limitations on making valid comparisons between the performance of public and private enterprise which would provide an adequate basis for deciding between public and private sector provision on grounds of relative efficiency;

(b) the particular factors which apply to public enterprise (ministerial direction and the influence of central government control) in varying degrees, also vary in their effects on performance. The central issue is to achieve the conditions necessary for commercial efficiency and effectiveness while retaining sufficient control to ensure that public policy objectives are achieved with equal efficiency and effectiveness.

THE SCOPE FOR PRIVATE PROVISION: CONSIDERING THE OPTIONS

Some of the considerations of government participation in enterprise raised in the foregoing discussion suggest that one advantage of less direct involvement would be that, with more reliance on private provision where this was an option, the government could withdraw, and concentrate on those functions for which there were no alternative means of provision. That is, with a reduced administrative load the government could fulfil its basic roles more effectively.

The extent to which the private sector could take over from public enterprise, however, is subject to qualification.

Qualifications to Privatisation

Important qualifications to privatisation are:

the government's need to take account of political and social considerations (for example entrenchment in the community, democratic benefits of ownership, the quantity and quality of private provision, short and long term management of the labour force); and

the small number of enterprises which qualify for immediate 'selling off' and the variable effects of 'sale' on public expenditure.

(a) Political and Social Considerations

Political and social considerations need to be weighed against the purely rational considerations favouring 'privatisation'.

(i) The extent to which established public enterprise is entrenched in a community accustomed by tradition to government involvement in a range of commercial activities influences the possible degree and rate of change. NZE and MWD, for example, because of their size, their market power, the strength of traditional attitudes and practices evolved within the organisation over time, and the extent to which they are part of the nation's economic infrastructure and social and political history, would be difficult to change substantially except over a long period of time. For example broad questions of the net impact on education systems and vocational training are raised where major competitors for industrial and professional skills such as NZE and MWD change their roles and reduce their functions.

(ii) There are benefits which accrue from public ownership, such as vested public interest in key areas of commercial enterprise, possibilities for using public enterprise for policy purposes (e.g. employment) and potential distributional benefits. It is significant whether or not the enterprise, or the activity, is presently profitable. Although the private sector appears eager to take over the profitable activities of public enterprise, it can be argued (depending on political philosophy) that profitability in itself is grounds for retaining the enterprise in the public sector for the purpose of government revenue and the consequent benefit to the public of expanded government programmes or reduced tax revenue requirements. For example, the recovery plan for Air New Zealand lays the foundation for possible privatisation of separate functions, but if performance improved to the point where the airline was no longer a financial burden there could be advantages in retaining public ownership.

(iii) A primary concern is that the social functions and responsibilities traditionally expected of public agencies in New Zealand, which are in fact the raison d'etre of public enterprise, are less likely to apply in private enterprise. A major consideration is whether the private sector has the capacity to provide the product or service at a price and standard desired in terms of government policy. This point is well illustrated by the debate over the rundown of the Housing Corporation Construction Division and contracting out the functions of Ministry of Works and Development.

The Housing Corporation was established in 1974 to amalgamate the housing-related functions of the former State Advances Corporation and the Housing Division of Ministry of Works and Development. One of the Corporation's major statutory functions is to provide publicly-owned rental housing by various means,[44] which have included provision through the corporation's own Construction Division. As a result of reduction in the demand for state rental accommodation, the government decided in 1980 to run down the Corporation's Construction Division. This decision reflected the government's preference for the private sector to assume a greater role in financing and providing for the country's housing needs. At the time, the PSA objected to what it saw as the loss of an important service to the public, and there have been recent indications that the private sector cannot meet the need for rental accommodation. The 1981 Annual Report of the National Housing Commission expresses concern at a rental shortage and concludes that 'some attention must be given to increasing stock in both the public and private sectors'[45]. However a clear distinction needs to be made between government housing policy and government provision of housing.

The question arises of whether regulation and control over private contractors is necessary to ensure their satisfactory performance, or whether market forces ensure adequate levels of self-regulation and control; and how far extensive and varied practical experience on the part of MWD staff is needed if the Ministry is to perform an effective regulatory role. The Public Expenditure Committee investigation of the Kaimai Tunnel project[46] queried the efficiency and expertise of the MWD, and suggested that too much emphasis had been placed by the Ministry on increasing its knowledge and skills. The Committee noted, however, that the Ministry's costs, and the estimates of the Contractors' Federation, were not necessarily capable of comparison, particularly given the difficulties associated with the project.

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44 Report of the Housing Corporation of New Zealand, B.13 (1981), 5.

45 Report of the National Housing Commission, G.30 (1981), 5. See also the Housing Corporation Annual Report 1981, op.cit., 6, for further reference to the increasing demand for state rental housing.

46 See Public Expenditure Committee Interim Report 1979, Kaimai Tunnel Project. Reports and Proceedings of Select Committees, Appendices to the Journals of the House of Representatives, Vol. IX (1979), I.12A.

(iv) Where any change from public to private provision is contemplated it is questions of employment which receive the most debate and publicity.

The government has responsibilities for the employees of public enterprise which mean that the process of withdrawing from the market is difficult, slow and costly. In the case of the Housing Corporation Construction Division, three years was allowed to effect only a small reduction in employee numbers, in order to minimise disruption for employees and allow time for redeployment, retraining etc. Negotiation of redundancy agreements, if these become necessary on a large scale, could be protracted and expensive. It is therefore understandable that the owners and managers of an agency such as GLIO, which is self-funding and entirely commercial in outlook and objectives, should not favour a rapid transition to independence because of the complex industrial questions such as union coverage, salary and employment conditions, security of tenure, superannuation, continuity of service and provision for those employees who wish to remain public servants, which would arise if GLIO became a mutual company or even a public corporation outside the public service. The large-scale redundancies recently announced by Air New Zealand, however, illustrate a more trenchant approach.

The government also has broader responsibilities in the field of industrial relations and for the maintenance and development of the labour force as a whole, which it can effect through ownership and control.

Other aspects of employment, raised by the decision to let the private sector compete for contracts such as construction of the Clyde dam, are the protection of the interests of small local operators and the protection of the employment interests of the workforce once a project is completed. The public tends to assume that contractors are less inclined to take such interests into account, and this area will require negotiation and development of industrial guidelines if activities currently carried out by the State are to be taken over by the private sector.

An additional problem in some cases is the retention of a viable core of skilled workers to respond to changing market demands. Can this be left to the private sector, or will reduction of Ministry of Works and Development's professional, technical and skilled labour force mean that specialist skills are 'lost' and, if required at some future stage of development, extensive retraining, and possibly recruitment from outside New Zealand, may be necessary? The cost of retaining skills for a long period, with no foreseeable demand, however, is a significant consideration.

Thus when considering the scope for privatisation, the points need to be made:

(i) that even where the government does withdraw from direct involvement in enterprise activities, this may not produce a significant reduction in public sector influence in the market, or in the level of public expenditure. This would depend on whether the privatisation of public enterprise, or breaking up of a state monopoly, is seen to require the introduction of regulatory controls, or even the creation of a public agency to monitor and regulate competition. For example in Britain the publicly owned British Telecom is being exposed to competition from private operators as a deliberate public policy, and some commentators are advocating a new government watchdog to monitor the participants and to safeguard the public's interest;[47]

(ii) indirect means of guiding private investment into the 'right' channels through selective taxation and subsidies, differential interest rates, reserve asset ratios, and other indirect means of controlling private sector activity, have their limitations. Factors such as possible resistance to change from interest groups, unintended consequences of taxes and continuing reluctance by the private sector to invest in areas of high risk and with long lead times may incline government towards direct investment as the surest way of achieving national development and social goals.[48]

(b) Limits to Selling Off

There are enterprises which would qualify immediately for 'selling off', although the number is not large.[49] One example is the Bank of New Zealand. More than other wholly government-owned agencies in the commercial field, the Bank already functions in a private enterprise manner. The impact of ownership being transferred to the private sector would be primarily in terms of the immediate capital gain to the government, although there would also be an effect in terms of the loss of potential for government direction of the institution which results from the government's position as shareholder. A similar situation applies in the case of the Development Finance Corporation, the Tourist Hotel Corporation, and the Government Tourist Bureau. For other public enterprises, the changes could be appreciable, e.g. in the effect on government spending or on services to clients.

The prospect of selling enterprises raises the question of their marketability. Where an enterprise is profitable and/or self-financing, it is likely that there will be ready private sector 'buyers'.

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47 Economist (20 March, 1982), 22, 25.

48 See T M C Menon and Prem Shankar Jha, Management of Public Enterprises in Developing Asian Countries: A Guide, Asian and Pacific Development Administration Centre, (Kuala Lumpur, 1980), 10-13.

49 C.f. Public Sector, Vol.4, No.1, 1: 'there are certainly areas of public administration which, by the stroke of a political pen, could become full competitors in the market and which have a business structure able to rise to the challenge'. See also G R Hawke, op.cit., 66-67.

If an activity is being 'sold off' because it is losing money and it is expected that private management would be more effective, then one of five courses of action probably would be required to interest private buyers:

(i) moving the enterprise first into a financially viable position, e.g. by re-organisation, cost-cutting, asset-selling, staffing changes (but once financial viability is achieved, the original grounds for selling the enterprise i.e. to avoid the continuing subsidy of sustained losses no longer exist);

(ii) as a prelude to privatisation, separating the agency's activities into distinct divisions with devolved profit centres, identifying the profitable areas which could be sold immediately, and improving performance in the rest (but the remaining activities will be the loss-makers in the enterprise, leaving the government therefore with a proportionately greater funding commitment, and greatly reducing the prospects for eventually disposing of the entire enterprise);

(iii) providing government financial assistance, e.g. writing off existing debts, and continuing the funding of capital requirements at low interest rates, as well as meeting the ongoing cost of providing goods and services as a matter of government policy (in which case there is no necessary reduction in public expenditure with the change in ownership);

(iv) providing indirect government support, e.g. the granting of rights and forms of protection (which would create new market distortions replacing any caused by government ownership of the enterprise);

(v) arranging the sale of the assets of the enterprise on terms favourable enough to the private sector buyer to compensate for existing performance problems, e.g. at an attractive price (but if this price is unreasonably low it may be more realistic to retain the enterprise in government ownership and deal with unsatisfactory performance by tackling the problem directly).

Because of these possibilities, the continuing cost to the taxpayer may still be substantial despite the transfer of a public enterprise activity to the private sector; and competition may not be enhanced. Discussions in the United Kingdom concerning the sale of British Airways illustrate some of the difficulties. To write off the airline's debts to effect a sale would require a large injection of government money, as most of the debt is to banks and is government guaranteed. Some of the profitable operations could be sold in order to reduce the debt but, once these had been sold, what remained would be of even less interest to private investors.[50]

Thus the implications of privatisation by selling off vary according to the circumstances of each enterprise. Individual propositions must be considered on their merits.

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50 See Economist (20 March, 1982), 25.

Alternatives

(a) Public Financing of Private Provision

An alternative to either full state provision (financing, production and marketing) or full private provision is state financing of private sector production of public goods. There are of course numerous examples in New Zealand of the government financing of goods and services, as compared with government provision. The pharmaceuticals industry is a case where publicly financed goods have been produced effectively through private enterprise, but where, conceivably, the government could have chosen to be producer as well as financier. The government's role in the pharmaceutical field is clear: it ensures the availability and pricing of medical drugs in accordance with health service policy, and regulates standards of safety and efficiency, both aims being achieved successfully without the government itself being involved in provision. Profit accrues to the producers, and financing is an item of public expenditure (unless the government itself charges market rates for the goods it buys from the private sector producers).

The financing option has the advantages that:

(i) the activity remains subject to government intervention so that

- the provision of desired goods and services not otherwise produced by the market is ensured;

- the level of consumption and the classes of consumers can be determined by government pricing policy (making the goods and services available free, at subsidised rates or at full cost);

- the range and quality of the goods and services can be regulated by direct controls or by the government exercising its influence as the consumer in the first instance; but

(ii) the government is not directly involved in decisions on matters affecting commercial effectiveness and profitability, such as management processes, product development and marketing strategies. The private sector producers are responsible for their own performance vis-a-vis their competitors. Assuming that the private sector at least is no less efficient than public enterprise would be, there is a clear benefit to the government in the occasion for reducing administrative loads (on the central machinery and on ministers) and for avoiding the operational costs of running an agency.

Financing privately produced goods and services to ensure supply under certain conditions, for example at less than market prices, in principle is distinct from financing as a method for government participation in a key industry, for the purpose of retaining control over resource development as is the case with the government's equity position in Petrocorp.

Examples of public enterprises where there is scope for exercising the financing option are the Department of Tourist and Publicity and the Tourist Hotel Corporation.

The Department of Tourist and Publicity's commercial interests could be sold or leased to the private sector, with those services regarded as unprofitable but necessary being subsidised by government grant. The government recently went a little farther down this track by leasing its Waimangu thermal valley tour operation to a private company, and the private sector has recently shown a short-lived interest in purchasing the Government Tourist Bureau chain. Reduction of departmental involvement in commercial activities would however create employment problems for existing staff; sale and lease of services would provoke reactions from various interest groups (as in the case of Waimangu); and inability to determine the market value of a particular activity would be an obstacle (possibly overcome by calling tenders) because of present non-separation from other departmental activities.

Now that the THC has developed the remote scenic resorts and provided a service infrastructure, greater interest is likely from the private sector. Conditions could be imposed on a sale or lease requiring the maintenance of standards, protection of scenic attractions and national parks and specifying other operating procedures. The New Zealand Railways Corporation Act, for example, has provision for imposing conditions on the working and maintenance of the railways system in the event of privatisation.

(b) Joint Ventures

Another option to full privatisation is joint public and private enterprise provision and/or financing. Greater co-operation between the public and private sectors, by way of joint ventures, joint promotion and marketing (examples include THC and the Department of Tourist and Publicity) and the introduction of private sector expertise through advisory boards (as in the GLIO and Government Printing Office), extends the role of private enterprise, with all the benefits that is assumed to bring: a wider range of technical skills and commercial expertise; overseas investment capital; and a more competitive commercial approach.

Partnership arrangements, however, entail certain dangers. Joint ventures may lessen public accountability for the funds invested by the government. Only very recently has it been established as a matter of principle that the audit of companies with a majority government ownership will be the responsibility of the Controller and Auditor-General whose views on the financial management of such funds may be reported to Parliament. This new provision does not apply to companies with 50 percent or less government equity shareholding.[51] As joint venture companies for example, Petrocorp, are not established by legislation, there is no statutory obligation to report to Parliament, although such a requirement can be, and in practice is, effected by ministerial direction. The prospect that the commercial operations of joint ventures (and some other public enterprises) will be exempt from proposed legislation on disclosure of official information could also limit the extent of their accountability.

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51 Report of Controller and Auditor-General, B.1 (Pt.III) (1982), 47.

(c) Contract Financing for Public Enterprises

Where there continues to be a preference for the public provision of goods and services, a third option is to seek to combine the advantages of government ownership (power of direction, and accountability for public funding) with the operational advantages of commercial undertakings,by the separate financing of the commercial and non-commercial activities of the public enterprise. This is accomplished by distinguishing between those activities which by nature are financially viable, and those which are undertaken to effect the economic and social policy objectives of the government. The first category, of activities which can be run profitably, is expected in principle to be self-financing, and it is possible for the enterprise to finance commercially viable activities by borrowing on the open market. The second category is funded by means of direct government subsidy, which represents an agreed payment to the enterprise for the costs incurred in operating non-economic services. These costs otherwise would appear as losses in the overall financial out-turn of the enterprise.

With respect to performance, there are several possible advantages.

(i) The performance of the enterprise itself can be judged on the level of efficiency achieved in providing the goods or services, measured in financial terms and excluding the effects on overall performance of non-commercial activities. There is thus a direct incentive to management to maximise returns, (especially in competitive enterprises where the relative commercial efficiency of the enterprise and its competitors can be compared), and to respond to the opportunities and disciplines of the market. The managers of the enterprise are responsible for, and independent in, the running of the operation as a business. The government sets broad objectives, and can instruct the agency to maintain particular services, approve investment programmes and supervise such aspects as pricing.

(ii) Non-commercial objectives can be pursued through the policy machinery of government, with the exercise of administrative and budgetary controls confined to the policy aspects of the enterprise.

(iii) Public accountability is improved. A ready yardstick is available to Parliament (and the shareholder) for assessing commercial performance, in the reported financial results of the enterprise; while the government's funding of services of a social nature, effected by annual appropriation, can be examined specifically by Parliament, in the normal processing of the Estimates and the scrutiny of the Public Accounts. The separate costing of social services allows attention to be focused on the specific value of these; and allows the government, Parliament and the public to choose whether or not to support a particular service in light of its subsidy requirement.

(iv) The opportunity is provided for introducing management techniques appropriate to the particular activity. The methods of modern business management (what are termed 'private sector' techniques for decision making and performance evaluation) can be applied to the commercial activities of the enterprise. For non-commercial activities the use of broader concepts of cost-benefit appraisal and effectiveness measurement can be developed.

(v) There is more scope for the operation of market mechanisms in the production of goods and services by government, since a more explicitly commercial orientation can be adopted in the business operations of the enterprise.[52]

The contract subsidy system already has attracted attention in New Zealand as a possible means for resolving the social cost aspects of public enterprises, i.e. compensating from public funds for the commercial sacrifices made when services are provided on policy rather than financial grounds. It is being applied currently in the Railways Corporation; and has been raised in connection with Air New Zealand's provincial services. It could equally be applied to the Tourist Hotel Corporation which could be directly compensated for operating hotels in uneconomic locations.

The greatest limitation on this approach to public enterprise management is the difficulty in practice of distinguishing clearly between commercial and non-commercial objectives. It is true that major developments in management information systems have transformed the possibilities for identifying and quantifying costs and returns in government activities, but there is still the matter of negotiating between the enterprise and the government what should be regarded as 'commercial' and what 'policy' in the agency's operations. A particular risk is that any activity which makes a financial loss could be defined as a social service, entitled to compensation from public funds, which would remove the incentive to improve performance in that area. Government financing then becomes simply a means by which the enterprises can cover general operating losses.

Two other questions are raised:

(i) should the enterprise pay tax on the profits made on its commercial activities, and

(ii) on what basis are profitability criteria, (which provide the targets against which financial performance is assessed), selected?

The use of the system in the Railways Corporation could well be regarded as a pilot exercise, to assess its potential and especially to show where modifications might be needed for its effective and wider application.

The concept of the contract subsidy has implications both for the role of public enterprise, and for its performance.

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52 The Chairman of the Board of the Railways Corporation regards the restructuring as an opportunity to blend private enterprise with the national interest. He is quoted as saying that he saw no difference between the Railways and any major company in the approach to its commercial functions, except for its responsibility to the public, (National Business Review, 8 March 1982). The Minister of Transport, Hon. G.F. Gair, has stated that the new Corporation could inject a "greater element of commercialism" to rail services, (Evening Post, 1 April 1982).

As an approach to management and financing, the concept is indifferent between public and private ownership of enterprise, but the segregation of the costs of providing commercial and non-commercial services extends the options available for the public financing of privately-produced goods. To the extent that specific subsidies for social services enable public enterprises to operate on a basis comparable with private enterprise, then private sector organisations could equally well be contracted to provide the necessary service.[53]

In terms of performance, the principle which underlies the social service contracting approach is that public enterprise has the same essential management requirements as private enterprise, and the same need to use appropriate techniques for achieving commercial success. In both sectors, the main elements of decision making and management are: definition of objectives and setting of measurable targets; formulation, appraisal and selection of programmes and projects; adoption of strategies for implementing activities; provision of operational and administrative procedures; and assessment of performance. In the private enterprise sector the market provides the guide for effecting these processes, by signalling the profit implications of decision options, and showing performance outcomes in financial terms. A range of sophisticated financial (profitability-oriented) techniques is available for the formal, systematic analysis of decision options and of actual results. The most commonly preferred financial analysis techniques are now those based on discounted cash flows (involving the calculation of present values or internal rates of return). Increasingly, these are being applied in the context of strategic and corporate planning.[54]

The counterparts to the techniques of commercial enterprise based on profit are those developed for public sector decision making and management, to deal with non-financial costs and benefits, where the criteria for appraising decision options and evaluating performance need to be expressed in terms of the economic and social benefit of a given amount of public financing. The techniques of cost benefit analysis, cost effectiveness analysis and programme evaluation are well known, and can be used where external costs (such as environmental damage) and benefits (such as improved health) are involved, and where goods and services are provided free or at subsidised cost to the public. A third situation in which public enterprises are often placed is where market prices do not reflect real resource costs, and therefore the

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53 C.f. the comment on this trend in public enterprise in Europe ('The State in the Market', The Economist, 30 December, 1978): 'but the industries themselves are in some confusion. The more they argue for separation (separate accounting for social objectives), commercial criteria and strictly-specific subsidies, the less reason for keeping them permanently in the public sector', 39.

54 See David S Wright, OR/MS Applications in Corporate Planning in New Zealand, Proceedings of the 17th Annual Conference of the Operational Research Society of New Zealand (1981), 81-90.

apparent commercial outcome of a particular activity is different from the true economic effect. In such cases the standard 'private sector' techniques can be applied with appropriate modifications, for example by calculating a shadow price to reflect real prices.[55]

The availability of decision and management techniques is not reflected in the extent of their use in the public sector generally in New Zealand, which has lagged behind developments in the theory and behind the practice of these techniques in some other countries. It is the case that:

(i) some very good individual studies have been carried out using systematic methods for formal analysis for example in project appraisal (the Development Finance Corporation's project analysis being highly regarded);

(ii) some isolated developments are taking place, for example in corporate planning in the Post Office and Railways, and in the application of techniques such as cost benefit and cost effectiveness analysis, zero base budgeting and rates of return;

(iii) pilot exercises are being conducted in some departments in the use of financial management techniques which substitute for profit techniques and are designed to give more flexibility and incentive to selected activities, namely bulk allocations and revolving funds;

(iv) developments in accounting systems are taking place which among other advantages allow the proper measurement of costs and performance (these having advanced to the point where they represent considerable unutilised potential for application in the routine use of the techniques of formal analysis).

The examples, however, do not constitute a systematic use among public enterprises of available decision and management techniques. It is evident that there is no consistent, across-the-board perspective on how, or when, they should be applied, even though there is increasing realisation of the potential of formal analysis to improve performance in the achievement of commercial and non-commercial objectives.[56]

Probably the main problem for public enterprises in developing and applying these methods for systematic analysis is that, as illustrated earlier in Part II of this paper, it is not always clear how the mixed objectives of the enterprise are to be translated into performance expectations. Indeed, objectives and their priorities are often not well defined in the first place. There are genuine difficulties in establishing clear, precisely measurable objectives for agencies which carry out social and economic policy

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55 A detailed study of public sector financial management techniques covering these aspects has been produced by David Preston of the Treasury, entitled Financial Management. The study was printed in limited numbers, and unfortunately is not widely available.

56 This was borne out by the fact that the relevant government sources were unable to provide the authors of the present paper with adequate information on the extent to which formal analysis is used by public enterprise agencies, or on what techniques are in use. The information which was obtained suggested a very uneven pattern.

and administrative and regulatory functions on behalf of government, and these should not be underestimated. A major constraint on quantifying the relevant variables for analysis is the inadequacy of existing information systems which may not be capable of generating the necessary data, although new management information systems are currently being developed at the central government level which will greatly improve the availability and form of information available for effective decision making and evaluation of performance. Other constraints are less easily handled, but nonetheless critical for developing the analytical capacity in public enterprise agencies: inappropriate or out-of-date administrative procedures; and the absence in some cases of managerial expertise and business acumen within the enterprise.

Reviewing Public Enterprise

Review is a critical link in the chain of accountability, between the management of the enterprise on the one hand and the need to be able to demonstrate how well the enterprise is performing in relation to its objectives on the other; and is a necessary part of the government's responsibility to monitor the performance of agencies in public ownership, on behalf of the public.

The great majority of new public enterprise agencies are introduced, and existing activities continued and modified, without any form of systematic analysis being undertaken to justify the action, and monitor effectiveness.

Existing public enterprises are subject to review from three sources:

(i) the State Services Commission, which is concerned with the promotion of efficient and effective administration of the agencies within the public service; and with 'machinery of government' aspects such as the need for new agencies, and the distribution of functions between agencies;

(ii) the Audit Office, which has the roles of:

(a) an independent review agency, able to conduct studies of individual enterprises (or sections of larger enterprises) aimed at suggesting improvements to management, and

(b) as a watchdog for Parliament and the taxpayer, highlighting situations requiring remedial action by other agencies;

(iii) the Public Expenditure Committee of Parliament, which can undertake investigations on a wide range of financial matters in respect of any agency in receipt of money appropriated by Parliament.

The Treasury also exercises a review function, in association with its role in supervising the allocation of public funds.

The activities of these bodies in reviewing public enterprise have been directed, naturally, to their respective purposes. In the past, defined responsibilities and a particular orientation in each case have limited the scope, regularity and effect of the existing review procedures. The jursidiction of the State Services Commission normally extends only to Public

Service departments, and the Commission traditionally has focused on organisational and management issues. The Audit Office, while having much wider jurisdiction, has had an orientation primarily towards financial aspects, and may not question government policy. The Public Expenditure Committee has found itself excluded from investigating certain areas of public enterprise by restricted intepretations of its terms of reference.

Recently, there have been a number of significant indications that these limitations on the extent of the review of public enterprise are being removed. The following are some examples.

(i) In some recent reviews involving the State Services Commission, consideration has been given to the role, objectives and justification for particular agencies or functions, as was the case in the review of the New Zealand Forest Service in 1981, which included the examination of whether the government should continue active participation in plantation forestry and sawmilling, and, if so, in what manner.

(ii) The principle has been established that the Controller and Auditor-General should be responsible for the auditing of any new companies or investments in which the Crown has in excess of 50 per cent ownership. The Controller and Auditor-General this year reviewed and commented upon the adequacy of controls exercised by the Ministry of Energy over the rapidly expanding oil and gas exploration programme in which the government is involved. Further, the Controller and Auditor-General has announced the establishment of a consultative committee of accountancy experts from the public and private sectors, which will be drawing on private sector experience to assess the applicability to government activities of current and financial management practices.[57]

(iii) The Public Expenditure Committee has sought to strengthen the accountability of public corporations and other companies with substantial public equity, by interpreting its terms of reference more widely, to allow the investigation of the financial affairs of agencies in years subsequent to the year in which an appropriation of public funds actually was made. On this basis, the Committee has been able to carry out an examination into Air New Zealand Limited.[58] The Committee is taking a continuing interest in the government's trading activities, specifically in the question of developing financial management information systems suited to commercial objectives.

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57 These three developments are referred to in the Report of the Controller and Auditor-General on Financial Audits, Special Studies and Review, and Other Matters, B.1 (Pt.III) (1982), on pages 47, 17 and 6 respectively.

58 Report of Public Expenditure Committee, I.12 (1981), 5.

The preceding analysis in Part II highlights not only the wide range of activity and organisation of public enterprises in New Zealand, but also the implications of their commercial orientation, in role and performance. The prerequisite for effective review is an explicit conceptual framework, which would provide a coherent, practicable approach to the establishment and operation of public enterprises. It is not clear that the developments described above, though important, are taking place within any such framework. Review aso needs to be continuous and comprehensive (to avoid the accumulation of financial and management problems in individual enterprises), and be capable of ascertaining the justification for government involvement in the light of changes in the economy, the market and in government policy.

Using techniques for financial and economic analysis not only enhances the quality of decision making and the prospect of achieving intended results, but also produces information which can be used to evaluate actual performance outcome. Performance evaluation is most useful when carried out as part of a formally recognised system for review which allows for the interpretation and feedback of results, and consequent modification of the agency's objectives and operations. Performance measurement, necessary for effective accountability, is not well advanced in the public sector generally in New Zealand. The major shortcoming is that success factors are not isolated or defined, and hence not measured. For public enterprises, as for private enterprises, a primary performance factor now is the cost of, and return on, capital. Increasing critical attention, (for example, by the Public Expenditure Committee and the Controller and Auditor-General), also is being directed towards the absence of systems in public sector agencies for producing financial information relevant to the activity, and sufficient for good management. In public enterprises, the information is needed both to show the full costs of the agency's commercial activities to allow sound financial decisions in relation to market and other signals; and to measure the cost of non-commercial, or social, services as the basis for determining the contribution to the running of these services required from public funds.

In the absence of settled, clearly defined objectives, a recurring problem in public enterprise, it is not possible to develop procedures that will provide adequately for efficient and accountable public enterprise agencies, especially where there is a conflict between commercial and non-commercial objectives. This is recognised in future directions proposed in Part III.

PART III

FUTURE DIRECTIONS FOR PUBLIC ENTERPRISE

It is not surprising that the public debate about the role and performance of government in the field of commercial enterprise should have failed to find answers as conclusive as the questions are apparent. The analysis of public enterprise issues in this paper confirms that behind what seem to be straightforward questions are complex matters of appropriate public-private sector balance, relative efficiency and effectiveness, representation in the market, and management approach and decision techniques. The extensive experience of government intervention in the economy by means of public enterprise has not produced any consistent, systematic approach to these issues. This accounts for widely varying principles of and practices in such critical aspects as degree of commercial independence, form of supervision, and provision for accountability, owing more to historical accident than to the rationale of government intervention in the market.

The two sides of the public debate about public enterprise - on the one hand the advocacy of 'privatisation', as representing the alternative to continuing and expanding government ownership and control of public enterprise, and on the other the demand for a demonstration of greater effectiveness and efficiency by the agencies of public enterprise - reveal an inherent disparity of view about the respective roles and responsibilities of government and the private sector. In turn this reflects the absence of a logical framework within which these would be resolved. Further confusion is caused by the argument that public enterprises should be run on private enterprise lines, in terms of organisation, financing and management.

The point to emerge most clearly from this study is that it is not acceptable that the public enterprise sector should carry on as in the past. The most compelling argument is that, given the significance of public enterprise in the economic and social life of New Zealand, anything less than maximum efficiency and effectiveness in the achievement of commercial and non-commercial objectives means that potential gains in the use of the country's resources remain unrealised. This applies equally to resource use in the private enterprise sector. For public enterprise, the broad significance of any differences between the two sectors is that these should not be permitted to become justifications for lower expectations of effectiveness and efficiency. This means seeking forms of organisation and approaches to management that will improve performance, rather than necessarily "selling out" to the private sector, or making allowances for lesser performance. A systematic, rational approach is more likely to produce changes which accord with the economic and social interests of the country than the continuation of the piecemeal, pragmatic approach which has characterised the history of public enterprise in New Zealand, and which has failed to provide a context for addressing directly the following questions:

(a) where a commercial activity can be profitable, and given that it involves some aspect of government policy, should it be carried out by public enterprise or by the private sector with possible public funding and/or appropriate regulation;

(b) where provision is by means of public enterprise, what sort of framework for its organisation and management will best meet the requirements of effectiveness and efficiency.

The following findings, drawn from the analysis in the preceding sections of this paper, represent one perspective on these questions.

1. The potential for private provision is not often enough considered explicitly as an alternative to a proposed or existing government intervention.

2. On few, if any, occasions have the reasons for establishing and maintaining public enterprises been sufficiently clearly and publicly stated to provide a convincing case for this method of provision of goods and services in preference to others.

3. The argument for privatisation, however, assumes a distinction between public and private enterprise which is not always clear, and in various ways is being lessened. The choice between public and private enterprise is not necessarily one of a larger, or smaller, public sector or of more, or less, public expenditure.

4. The opportunities for transferring government enterprise activities to the private sector are limited by a number of important considerations.

(a) Role of Government - that the government has a substantial role directly intervening in a number of commercial and productive areas of the economy is widely recognised. The public has become accustomed to an extensive public enterprise sector and rapid or radical change is unlikely to find wide acceptance.

(b) Justifiable Government Intervention - if thorough assessments were to be made of the justification for government's public enterprise activities, strong and sufficient reasons could be established for retaining a moderate to large proportion of existing agencies, e.g. for the maintenance of economic/social infrastructure and growth of strategic industries which the private sector may not have the desire or the resources to undertake, or where the existence of a significant public interest factor makes public accountability desirable.

(c) Practical Constraints - decisions to privatise inevitably would involve complexities which it might not be possible to resolve within the bounds of public acceptance, e.g. establishing the conditions required to attract private sector investors.

5. The question which remains is whether more value for money could be obtained from public provision rather than from private provision publicly financed. The answer to this question depends on whether the private sector is a more efficient producer than the public sector. The greater responsiveness of private enterprise to market forces is the ground for assuming its superiority in the commercial sector, but when the public policy functions of public enterprise are taken into account there is no information available at present to show conclusively where, or whether, private enterprise is relatively more effective. All that can be said is that when public enterprise is used as an instrument of public policy (e.g. the delivery of goods and services at subsidised rates) efficiency requires that production

should be at minimum economic and social cost. This will not be achieved if the public enterprises concerned are less efficient than a private sector counterpart.

6. The effective management of public enterprise remains a matter of highest importance. This opens up a wide area of possible action, and carries several requirements. These include defining the broad purposes and specifying the objectives of individual enterprises, determining the desired balance between commercial and non-commercial objectives (which requires that these be separately identified), ensuring an appropriate organisational form and management structure, having appropriate personnel policies, and using systematic, formal techniques for decision making and management operations. Although these requirements seem basic, there is no consistency in the extent to which, or the success with which, they are met among the wide range of public enterprises in New Zealand.

7. Possibly the most intractable problem for public enterprise, and one which underlies all its key aspects, is the contrasting requirement for independence and control. Too much control may stifle commercial success, too much independence for publicly-owned enterprises may put them beyond responsibility to central government, while at the same time 'normal' private sector controls do not apply.

8. However independently public enterprise agencies may operate, a condition of public ownership is that they remain accountable, and thus responsive, to government and Parliament. Yet the provisions for, and observance of, public accountability in public enterprise in New Zealand vary widely, without always good reason. The external scrutiny which occurs under public accountability is well established as an alternative to the disciplines of the open market in providing an incentive for good performance.

The consideration of future options in the field of public enterprise, as much as in any other area of potential change, needs to be based on New Zealand's own experience. It is not to be assumed that approaches developed in other countries are readily transferred: first, although the issues which public enterprises present to governments in New Zealand and elsewhere are similar, public enterprise systems in different countries are not fully comparable; and second, it is hard to find overseas examples where these common issues have been successfully resolved. Neither can rapid change be expected. What is important is that the right long term decisions are made.

Future Directions

1. Alternatives to Government Provision

Although there are limitations on transferring the ownership of existing enterprises to the private sector, this approach should be recognised as a realistic possible response to at least some of the present questions associated with state ownership. Alternative ways of achieving the intended purpose, such as by controls and subsidies rather than by direct provision and financing are not always properly considered. The choice of active government involvement should not be made before the question is asked whether there are other means of meeting the objectives so that the alternatives can be investigated. Public provision has costs and disadvantages as well as advantages, in particular cases. The choice between public and private provision, other things being equal, depends on the criteria:

(a) that the achievement of policy objectives is not prejudiced, and

(b) that the net economic result is maximum efficiency and effectiveness in the overall use of resources.

Both criteria require that using the most efficient producer should override any tendency to relate financing to ownership. Government subsidisation and regulation can be extended to private enterprises in a variety of ways to ensure that public policy purposes are met. Government should be able to buy at the lowest cost, or with the lowest subsidy requirement. This applies as much to 'natural' monopolies, which per se need not be publicly owned, as to the areas in which government competes in the market. On the basis of these criteria, serious consideration needs to be given to the possibilities for reducing or eliminating government ownership and control, with the purpose not of privatisation on a large scale, but rather of seeking a more carefully balanced allocation of enterprise between public and private sectors, consistent with public preferences and government policy.

There are two market situations in which there will be a clear the case for government withdrawal from the market. These are:

(a) when, in the case of a public enterprise set up to regulate the market by competition, increased competitive strength in the market removes the need for direct government intervention; and

(b) when, in the case of public enterprises set up to meet inadequacies and distortions in the market, independent changes occur in the market environment such as developments in market information, amendments to restrictive legal provisions and removal of barriers to private operators, which overtake the role originally performed by the government agency.

Before privatisation can be considered in any particular case (either in existing or proposed public enterprises) the objectives must be clearly defined to establish whether in fact they could be achieved by means other than direct participation by ownership and control, e.g. by private provision with an appropriate mixture of subsidy, licensing, regulation and taxation (all of which are presently used to 'control' private sector activities, but not for any consistent purpose). It is also necessary to look critically at the obstacles which may be raised against possibilities for transferring public enterprise activities to the private sector: for example, where undue emphasis is put on the potential effects on public sector employment, or where the valuation of assets, needed before a sale of assets could be effected, is not properly provided for.

2. Management of Public Enterprise

For the effective management of enterprises which continue to be owned by government, there are two options: moving either towards more independence, subject to appropriate conditions; or towards a more uniform system of central government control. The preference in this paper is for the former approach, but subject to the following conditions.

(a) Objectives

(i) The government should ensure that the objectives of individual public enterprises are defined clearly, distinguishing commercial from non-commercial objectives; and should establish and state the priorities which the enterprise is expected to observe in meeting these two sets of objectives.

(ii) Where public enterprises are required by government policy to deliver non-commercial goods and services, these 'social' objectives as far as possible should be separately identified, and the cost to the enterprise of providing them fully reimbursed by the government. This method of public sector provision and financing should be formalised in contracts negotiated between each public enterprise agency and central government.

(b) Market Conditions

(i) Competitive public enterprises should operate under the same market conditions as private enterprises in the same commercial field. This would require the scrutiny, and removal, if there was not a compelling reason for their continuation, of special advantages (such as exemption from regulatory provisions, protected markets and explicit and implicit guarantees) and of disadvantages (such as restrictions on areas in which an enterprise may operate) which presently apply to public enterprises. It also means that public enterprises should pay the full economic cost of resources used, whether they are self-financing or are funded by government. This would include paying the market rate for borrowings, and recognising the opportunity cost of equity capital (which for publicly listed companies is reflected in share prices).

(ii) Public sector enterprises should be subject to any general monopoly legislation and regulation (such as price justification procedures) which applies to private sector monopolies, so that in terms of direct disciplines they are treated the same. There is a case for strengthening the general control of monopoly situations, the provisions for which in New Zealand are less developed than in other comparable countries.

(iii) The possibilities for allowing the entry of private investors and operators into areas of government monopoly should be identified, and pursued where obvious benefits to market efficiency are revealed. Such possibilities may be either in the substitution of private for public provision (in which case some degree of government control may still be needed) or in the introduction of private sector competition (which would expose the government monopoly to market disciplines).

(c) Public Accountability

The principle of public accountability should be met fully. The preservation of public accountability, especially if public enterprises move towards more independence in their commercial operations, requires that information about performance, in relation to objectives, be made publicly available as far as practicable. Guidelines on the question of limiting publication of information for reasons of commercial competitiveness should emerge after the impending legislation on official information has come into effect. Information for public accountability falls into two categories:

(i) to allow informed assessment of the agency's performance;

(ii) to indicate forward investment and financial plans, in relation to objectives.

The extent of accountability required and the procedure for effecting accountability should be established clearly for each enterprise and with more consistency in principle. To be held directly responsible for their performance, individual public enterprises need to be free of ad hoc government interventions which confuse what the agency is acountable for, and affect the achievement of stated objectives. The exercise of government influence should be in accordance with the ongoing purposes of the enterprise.

Other directions suggested for the management of public enterprise would have the effect of enhancing public accountability, namely: the definition of objectives (paragraph 2(a)); the use of means for measuring performance (paragraph 2(f)); and adequate review procedures (paragraph 3).

(d) Ministerial Direction

If ministerial directives (to effect government policy) are to be applied under (a)(ii) above, the agency would be directly compensated by the government so that the impact on the performance of the enterprise was isolated from, its business operations, leaving these to be assessed solely on commercial performance. Ministerial directives, and the costs involved, should be made public, giving the public the choice of supporting, or not supporting, the policy behind the order.

(e) Organisational Form

(i) The choice of organisational form should be made by explicit reference to the nature of, and intentions for, the enterprise: both when new ventures are being set up, and when the restructuring of existing enterprises is proposed. There are good reasons for favouring the corporate form of organisation to cope with mixed commercial and non-commercial objectives (assuming that these are separately identified). On the one hand, the corporation allows the opportunity for adopting appropriate business decision and management techniques for the agency's commercial operations; on the other, it provides a structure which can respond, by negotiation when appropriate, to the policy requirements of government. Even more autonomy and flexibility is achieved under a limited liability company structure, but less public accountability.

(ii) In the use of the corporate form of organisation for government-owned enterprises, practice has shown a need for defining the relationship between the government (as the shareholder) and the board of directors (which will include public servants in its composition). Inevitably, special considerations beyond the normal shareholder/board relationship arise. These should be codified in the legal articles of the corporation (or in the participation agreement in the case of joint ventures), stating the respective responsibilities of the board and of individual directors, and the government. An unsatisfactory gap exists between the present body of law on the functions of directors, and the present practice in publicly-owned corporations and joint ventures.

(iii) Spreading the ownership of shares in public enterprises more widely should be considered, for example by increasing public equity participation and increasing holdings in the enterprise by its employees.

(f) Management

(i) In the context of the enterprise's own management (as distinct from matters which involve central government decision and oversight), directions taken in areas such as set out above should be accompanied by the routine use of formal management techniques, including those for:

- corporate/strategic planning (involving the setting of objectives and financial targets)
- the development of performance targets and performance measures
- efficient accounting systems
- internal monitoring systems
- investment review and project appraisal procedures.

These involve techniques common to commercial operations in both the public and private sectors. Treating public enterprises as businesses in respect of their commercial activities would facilitate the application of appropriate management techniques and the development of financial performance measures. Separate attention needs to be given to developing methods for the effective management of 'social service contracts'. There appears to be a need for more focused research to find solutions to problems of cost and benefit measurement in areas where financial data is not relevant.

(ii) The availability and reliability of data about the agency's operations should be improved, to provide the basis for developing and applying formal management techniques. Special attention should be paid to developing information systems which allow the costs and performance outcomes in commercial and non-commercial activities to be separately identified.

(iii) While the main prerequisites of good management are indicated in preceding points, much depends on the level of management skill and flair available to the enterprise. This is a matter of recruitment, training and experience not covered in the present paper, but warranting careful consideration. In the appointment of management and staff of public enterprises more emphasis could be placed on commercial competence and expertise.

3. The Review of Role and Performance

(a) Central Procedures

The sorts of changes proposed above will not occur unless a more systematic approach is taken to decisions on future government interventions in commercial ventures, and to the management of existing and new public enterprises. Additional institutional arrangements, as established in some other countries, are not needed, provided full use is made of existing control and advisory agencies, to deal with public enterprise. Three functions, in particular, have not been carried out systematically, or with adequate effects, in the past.

(i) <u>Review of role</u> - periodic assessment of the continuing justification for particular public enterprise activities, to establish that there remains sufficient reason for government involvement.

(ii) <u>Monitoring</u> - monitoring the performance of individual public enterprises.

(iii) <u>Advisory</u> - formulation of guidelines, for example on accountability requirements and financial arrangements; examination of proposed new government ventures, in the context of these guidelines, and to assess the alternatives to the proposed intervention; assessment of the need for new procedures, for example relevant information systems; and financial and economic analysis relevant to the commercial activities of the government in order:

- to examine the financial and economic environment in which the various public enterprises operate;

- to develop sound guidelines on investment criteria and performance expectations;

- to provide consistent information for use by public enterprises in the development of corporate/strategic plans.

Recent developments in the approaches of existing central agencies to the commercial activities of government should go some way to meet these past shortcomings. Insofar as there is a case for new provisions, it would be the need to co-ordinate the results of present review, monitoring and advisory procedures, to ensure their effective implementation. Such co-ordination would need to involve both the State Services Commission and the Treasury. Any future developments should have regard to the independence of managers in running the enterprise, and should avoid restrictions on the necessary responsiveness of management decision making.

(b) Parliamentary Review

The essential counterpart to the supervisory and review functions of central government is the parliamentary process of scrutiny and monitoring of the public expenditure implications of public enterprise. This process would be strengthened by the appointment of a select committee, or of a permanent subcommittee of the Public Expenditure Committee, specifically for this purpose. This is a matter for Parliament itself, which would need to consider, as pre-requisites:

(i) the defining of clear criteria for parliamentary access to relevant information, including defining the responsibility of non-public service agencies to respond to parliamentary investigations;

(ii) the need for any new procedures to make good use of the information resulting from the review and monitoring of public enterprise carried out by the central agencies;

(iii) the provision of adequate research and advisory staff.

The present paper, as a general survey of the issues in public enterprise, leaves aside numerous points of detail which are of sufficient importance to warrant further study. A programme for continuing study of public enterpise in New Zealand should be undertaken to produce a series of background studies on:

(a) general principles in public enterprise management, where guidelines should be developed and applied, e.g. on financing policies (including capital structure, requirements to be self-financing), pricing policies and practices, profitability criteria, the taxing of public enterprise profits, and application of financial and economic appraisal techniques;

(b) individual enterprises, which present significant opportunities for future directions in such areas as privatisation, competition, pricing and investment and management approaches.

It is suggested that the Planning Council would be an appropriate body to initiate such a programme of study, in conjunction with government departments and other agencies with special interests in these areas.

If the future of public enterprise is indeed to be 'directed', success, in terms of achieving an effective public enterprise sector, will depend on sufficient account being taken of the circumstances of individual enterprises. It would be not only inherently difficult, but also misguided, to attempt to devise a uniform framework of institutional arrangements, financial targets and performance criteria for all public enterprise agencies. Ultimately, these broad aspects and their detailed implications are matters for the government, which will need to take account of the economic impact and the social and political realities of particular enterprises as much as of their effectiveness and efficiency. The best future outcomes, however, will be based on judgements taken in the context of firmly established guidelines, and informed by the fullest possible knowledge of the market and about its public sector participants; and will be those which ensure responsiveness, but a better balance between the pragmatic and the systematic, in public enterprise in New Zealand.

SELECTED CHARACTERISTICS OF SOME PUBLIC ENTERPRISES

(Based on a table compiled by Joan Ferner and John Roseveare of the State Services Commission)

TITLE	HOUSING CORPORATION OF NEW ZEALAND	NEW ZEALAND POST OFFICE
STATUS	Government Department and Statutory Corporation.	Government Department (trading, except for compilation of electoral rolls).
BOARD	Chairman is Director-General of Housing Corporation. Secretary to Treasury, 4 members from private sector appointed by Minister of Housing.	N/A
CHIEF EXECUTIVE OFFICER	Director-General. Salary determined by Higher Salaries Commission.	Director-General. Salary determined by Higher Salaries Commission.
STAFF	Public servants (including Director-General) employed under State Services Act 1962. State Services Commission is the employing authority. Subject to sinking lid and staff ceiling control.	Staff apointed under Post Office Act 1959. The Director-General is employing authority for purposes of the State Services Conditions of Employment Act 1977. Staff are state servants, and provisions of State Services Conditions of Employment Act apply.
REQUIREMENT TO IMPLEMENT GOVERNMENT POLICY	Establishing Act requires implementation of written directions by Minister of Housing. Copies to be included in annual report.	Yes, as advised by the Postmaster-General.
FUNDING/ FINANCIAL CONTROLS	Annual appropriation voted by Parliament from Consolidated and Loans Accounts. The amount voted for lending activities is reduced by anticipated revenue from capital repayments which is credited directly to this programme. An amount equal to 1% of outstanding loans is paid to the Corporation for operating expenses. Corporation empowered to issue securities deemed as Government securities. Corporation empowered to make loans to industry and hold interests in companies concerned with approval of Minister of Finance.	Funds are voted by Parliament from the Post Office Account and all revenue is paid into this Account. There is provision for redistribution of voted funds between expenditure items in consultation with Treasury provided that total vote is not exceed. Additional amounts may be voted from the main Consolidated or Loans Account if required.

	Corporation may give indemnities or guarantees in respect of money owed by one party to another, subject to conditions advised by Minister of finance. Corporation required to maintain a General Revenue Fund and to invest in government securities approved by Minister of Housing an amount not less than the amount credited to the General Revenue Fund. Annual surplus is paid into Public Account unless Minister authorises it to be credited to General Revenue Fund.	
INCOME TAX LIABILITY	Yes	No
AUDIT ARRANGEMENTS	Subject to audit by Audit Office.	Subject to audit by the Audit Office.
ANNUAL REPORT	To Minister; to Parliament.	To Postmaster-General and then referred to Parliament.
SUBJECT TO OMBUDSMAN	Yes	Yes

TITLE	THE GOVERNMENT LIFE INSURANCE OFFICE	NEW ZEALAND RAILWAYS CORPORATION
STATUS	Government Department, and Statutory Corporation sole.	Statutory Corporation.
BOARD	Advisory Board (non-statutory): one member fom SSC or nominated by SSC; 4 members fom the private sector appointed by the Minister in Charge of Government Life. Investment Board (statutory): Minister, Commissioner, Secretary to Treasury, Public Trustee, Valuer-General, an appointee of the Governor-General in Council.	Not more than 7 Directors appointed by the Governor-General on the recommendation of the Minister.
CHIEF EXECUTIVE OFFICER	Government Life Insurance Commission. Salary determined by Higher Salaries Commission.	General Manager, appointed by the Corporation. Salary determined by Higher Salaries Commission.
STAFF	Public servants (including the Commission) employed under the State Services Act 1962. However sales agents and agency managers are not public servants. SSC is the employing authority. GLIO is exempt from the sinking lid but subject to staff ceiling control.	Appoints own staff. The Corporation is the employing authority, and provisions of the State Services Conditions of Employment Act apply to remuneration and conditions of employment for Corporation employees.
REQUIREMENT TO IMPLEMENT GOVERNMENT POLICY	No formal requirement but the office is under the control of the Minister, and the Minister and Secretary to Treasury are members of the Investment Board on which the Minister has a deliberative and casting vote.	Corporation to comply with written directions from Minister in respect of provision of cutailment of passenger services. Ministerial approval required to close lines, undertake any substantial activity or to cease or reduce any substantial service or activity. Copies of directions given and details of approval given or declined by the Minister are to be included in the Corporation's annual report.
FUNDING/ FINANCIAL CONTROLS	GLIO is funded entirely by policy-holders. Revenue is paid into the Government Life Insurance Account and Parliament appropriates funds annually from this account to cover GLIO's operating expenses. If this account is insufficient to meet operating expenses, the Minister of Finance can meet the deficiency from the Public Account under the warrant of the Governor-General. This provision has never been used.	Capital determined, and may be increased, by Govenor-General by Order in Council on advice of the Minister of Finance. Outstanding loan finance advanced by the Crown converted into capital by NZ Railways Corporation Act. Consent of Minister of Finance required for borrowing, issuing debenture, mortgaging or charging property. Loans advanced by Minister of Finance are

	The GLI Account may be in overdraft at the end of the financial year. The Commissioner is empowered to arrange temporary advances with the approval of the Minister from the Public Account, the Reserve Bank or some other bank. Government exercises control over investment through Ministerial and Treasury representation on the Investment Board. The GLIO Actuary recommends the net surplus of profits for division amongst policy-holders after allowing a recommended sum to the Reserve Fund.	paid out of Consolidated or Loans Accounts from money appropriated by Parliament for the purpose. The Corporation may invest in New Zealand Government securities. Approval from Minister of Finance necessary for acquisition of shares, stocks etc, for investing funds on deposit with banks and for any other form of investment. Capital works expenditure programme must be provided annually to the Minister. Minister of Finance fixes the dividend on Corporation's Capital, which is paid to the Consolidated Account. The Corporation is entitled to contribution towards the cost of certain services. Sum determined by Ministers of Finance and Transport in consultation with Minister of Railways and the Corporation. $5000 limit on unauthorised expenditure.
INCOME TAX LIABILITY	Yes	No
AUDIT ARRANGEMENTS	Audited by Audit Office.	Subject to audit by the Audit Office.
ANNUAL REPORT	To Minister; to Parliament.	To Minister; to Parliament.
SUBJECT TO OMBUDSMAN	Yes	Yes

TITLE	BROADCASTING CORPORATION OF NEW ZEALAND	TOURIST HOTEL CORPORATION
STATUS	Statutory Corporation.	Statutory Corporation.
BOARD	7-9 members appointed by Governor-General on recommendation of Minister of Broadcasting.	5 members appointed by Governor-General on the recommendation of Minister of Tourism, General Manager of the Tourist and Publicity Department; General Manager of THC.
CHIEF EXECUTIVE OFFICER	Director-General, appointed by Board. Salary determined by Higher Salaries Commission.	General Manager, appointed by the Board. Salary determined by Higher Salaries Commission.
STAFF:	Staff employed by BCNZ which is an employing authority for purposes of State Services Conditions of Employment Act 1977.	Employs own staff, who are not State employees.
REQUIREMENT TO IMPLEMENT GOVERNMENT POLICY:	BCNZ required to have regard to general policy of Government in relation to broadcasting and to comply with written directions from Minister of Broadcasting. Minister's power does not extend to particular programmes or complaints. Written directions to be published in the Gazette and laid before Parliament. (Legislative amendment at present before the House.)	Required to give effect to Government policy as communicated in writing by the Minister and to any specific written direction received from the Minister. Copies of such directions to be included in annual report.
FUNDING/ FINANCIAL CONTROL:	Current share capital is $38.9 million. Activities are funded from Corporation income e.g. TV licence fees. BCNZ required to bank with BNZ and may go into overdraft, but other borrowing is subject to approval of Minister of Finance. BCNZ may advance money to people involved in broadcasting and, with approval of Minister of Finance, deal in shares or stock of companies involved in Broadcasting. Investment must be in government securities, PSOB, other banks or securites approved by Minister of Finance. Annual programme of capital works expenditure submitted to Minister of Broadcasting, and BCNZ is required to have regard to written directions in respect of capital works.	THC is funded by share and loan capital. Authorised share capital is $11.9 million. Capital may be increased by the Governor-General in Council. All shares are taken up by the Crown. Amounts may be advanced to THC by the Minister of Finance and amounts advanced by others guaranteed. Debentures may be issued with the consent of the Minister of Finance. The following activities are subject to approval of Minister of Finance or Minister of Tourism: - borrowing, and mortgaging of property; - setting aside reserves and investing money so set aside; - acquisition and disposal of land and stock; - advancement of monies to specified companies.

		Money must be invested in government securities, POSB, other banks authorised by the Minister of Finance or other securities approved by the Minister of Finance. Minister of Finance determines annual dividend which is paid into Consolidated Account. Treasury approves capital works expenditure.
INCOME TAX LIABILITY:	No	Yes
AUDIT ARRANGEMENTS:	Subject to audit by Audit Office	Subject to audit by Audit Office
ANNUAL REPORT:	To Minister, then referred to Parliament	To Minister, then referred to Parliament
SUBJECT TO OMBUDSMAN:	No	No

TITLE	DEVELOPMENT FINANCE CORPORATION	APPLE AND PEAR MARKETING BOARD
STATUS:	Statutory Corporation	Statutory Board and body corporate
BOARD:	Six directors (including Chairman) appointed by Governor-General on recommendation of the Minister of Trade and Industry; Secretary of Trade and Industry and Secretary to Treasury.	Six members appointed by Governor-General on recommendation of Minister of Agriculture. Four appointed on nomination of Fruit Growers' Federation; two members to represent the interests of consumers.
CHIEF EXECUTIVE OFFICER	General Manager appointed by Board and salary determined by Higher Salaries Commission. DFC's establishing legislation provides for a Managing Director to be appointed by the Board from among the Directors.	General Manager, appointed by board and salary determined by Higher Salaries Commission.
STAFF:	Employs own staff, who are not State employees. However pay and conditions are determined in consultation with SSC.	Employs own staff, who are not State employees.
REQUIREMENT TO IMPLEMENT GOVERNMENT POLICY:	DFC required to abide by written directions from Minister of Trade and Industry. Copy of such directions must be included in annual report.	Required to comply with general trade policy of Government and with any general or specific directions from the Minister.
FUNDING/	DFC is funded by government loan and equity capital. Issued equity capital is $25 million (authorised capital of $35 million). Share capital may be increased by the Governor-General in Council. All shares must be allocated to the Crown. Monies may be advanced to DFC by the Minister of Finance, and advances made by others guaranteed. DFC may issue bonds, debentures and other negotiable or transferrable instruments and accept deposits of money. DFC may only borrow and mortgage its property with the consent of the Minister of Finance. Funds not immediately required can be deposited with any bank or authorised dealer in the short-term money market, invested in government securities or with the National Provident Fund. DFC is exempt from reserve asset ratio regulations.	Board has authority to fund costs from the Apple and Pear Industry Account held at the Reserve Bank. With Minister's approval, Board can pay for any purpose outside its functions and powers deemed to be of benefit to the apple and pear industry. Approval of Minister is required for forms of borrowing other than overdraft with the Reserve Bank, and for investments other than BNZ deposits or government securities. Minister of Finance may advance funds appropriated from the Public Account to meet guaranteed prices. Ministerial approval is required for the imposition of a levy on growers. Proceeds from levy go to Capital Reserve Fund for acquisition of capital assets and other purposes approved by the Fruit Growers' Federation. $500 limit on unauthorised expenditure.

	Board fixes ratio of liabilities to authorised capital, subject to approval of Minister of Finance, and may declare an annual dividend of not more than 6%. Annual surplus is paid into a Reserve Fund and may be invested.	
INCOME TAX LIABILITY:	Yes, but DFC's Industrial Research and Development Account, which receives an annual appropriation of funds from Parliament, is exempt from income tax.	No.
AUDIT ARRANGEMENTS:	Subject to audit by the Audit Office.	Subject to audit by Audit Office.
ANNUAL REPORT:	To Minister and referred to Parliament.	To Minister, to Parliament.
SUBJECT TO OMBUDSMAN:	No.	No.

TITLE	BANK OF NEW ZEALAND	AIR NEW ZEALAND
STATUS	Statutory Corporation.	Limited liability company registered under Companies Act.
BOARD:	5-7 members appointed by Minister of Finance.	Directors nominated by Minister of Finance.
CHIEF EXECUTIVE OFFICER:	General Manager appointed by Board. Salary determined by Higher Salaries Commission.	Chief Executive appointed by Board. Salary determined by Higher Salaries Commission.
STAFF	Employs own staff, who are not State employees.	Employs own staff. Registered agreements contain State linkage clauses which provide for application of State general adjustments. Informal consultation with SSC on pay-fixing issues.
REQUIREMENT TO IMPLEMENT GOVERNMENT POLICY:	BNZ required to have regard to any representation from Minister of Finance in respect of BNZ's activities and to give effect to written directions from the Minister of Finance. The Minister is prohibited from making any representation or direction that relates to the accounts or banking affairs of any existing or prospective customers.	Company abides by written Government directive issued originally in 1964 which sets out various requirements relating to policies, financial management, and services to be provided.
FUNDING/ FINANCIAL CONTROLS:	Authorised capital is currently $41.5 million. Governor-General in Council, on advice from Minister, may increase capital. Acquisition of more than 20% voting interest in any company and the disposal by the Bank of any interest or a substantial part thereof in any company is subject to approval of Minister of Finance. Crown is not liable for debts of bank other than payments to the Bank in respect of shares not fully paid up or contributions by virtue of any guarantee, indemnity or security given by the Minister under the Public Finance Act 1977.	Authorised capital is $100 million. Current paid up capital $70 million: 7 shares held by Treasury; remainder held by Minister of Finance. Capital may be increased or reduced by shareholders. On 29 March 1982 Cabinet decided to lend Air New Zealand $50 million. The loan is constructed so that some, or all, may be converted to share capital at a later stage. Money can be advanced to the company by Government or advances made by others guaranteed. But the Government directive includes a statement that, in general, the company should aim to meet all operating expenses from revenue. Type and number of aircraft subject to approval by Minister of Civil Aviation. The purchase of aircraft and expenditure of more than $400,000 require approval of Minister of Civil Aviation. No specific restrictions on borrowing or investment. Annual programme of operations and estimate of revenue and expenditure submitted to Minister of Transport. Profits dealt with as directed by Minister of Finance having regard to company's recommendations.

	Board may resolve that a specified amount of BNZ's profit may be paid into the Public Account, subject to the Minister's approval of the amount.	
INCOME TAX LIABILITY:	Yes.	Yes.
AUDIT ARRANGEMENTS:	Auditor appointed by the Minister.	Auditor appointed by company.
ANNUAL REPORT:	To Minister of Finance, then referred to Parliament.	Report required under Companies Act is tabled in Parliament.
SUBJECT TO OMBUDSMAN:	No.	No.

TITLE	SHIPPING CORPORATION OF NEW ZEALAND	PETROLEUM CORPORATION OF NEW ZEALAND LTD
STATUS:	Limited liability company registered under the Companies Act.	Limited liability company registered under the Companies Act, which is holding company for five subsidiary companies.
BOARD	Directors, appointed by the Minister of Transport. No restriction on number.	Nine directors: 7 appointed by Minister of Energy; Secretary to the Treasury; Secretary of Energy. Each subsidiary company has a board of directors, drawn primarily from the private sector.
CHIEF EXECUTIVE OFFICER:	General Manager appointed by Board. Salary determined by Higher Salaries Commission.	Group General Manager, appointed by Board. Salary determined by Higher Salaries Commission.
STAFF:	Employs own staff, who are not State employees.	Employs own staff, who are not State employees.
REQUIREMENT TO IMPLEMENT GOVERNMENT POLICY:	Required to have regard to representations from Minister of Transport and give effect to Government decisions given in writing by the Minister.	No statutory requirement, though Ministers of Energy and Finance are only shareholders and Minister of Energy appoints Board.
FUNDING/ FINANCIAL CONTROL:	Authorised capital is $50 million, not all of which is paid up. All but one of the shares is held by Minister of Transport. Share capital may be increased by ordinary resolution, but unless a General Meeting otherwise directs, new shares must first be offered to Minister of Transport, who may decline, in which case they may be offered elsewhere. Money may be advanced to the Corporation by Minister of Finance and money advanced by others guaranteed. The Corporation may only borrow and mortgage its property with the consent of Minister of Finance. Directors may recommend declaration of a dividend after amounts set aside as reserves or carried forward. The company in General Meeting may declare a dividend which is no more (but may be less) than that recommended by Directors.	Paid up capital is $99.76 million and authorised capital is now $101.8 million. All shares are owned by the Crown (the Minister of Energy holds a majority shareholding and the Minister of Finance owns the rest), except in the case of Petralgas Chemicals NZ Ltd in which Petrocorp has a 51% holding and the rest of the shares are owned by Alberta Gas Chemicals Ltd. Government also provides grants and loan funds for activities such as exploration. The parent company is empowered to raise funds in the money market and to guarantee loans raised for its subsidiary companies.
INCOME TAX LIABILITY:	Yes.	Yes.

AUDIT ARRANGEMENTS:	Subject to audit by Audit Office.	Holding company and four wholly-owned subsidiaries audited by Audit Office. Auditing of Petro-chem has been delegated to private Chartered Accountants, but responsibility remains with Audit Office. Petralgas is privately audited.
ANNUAL REPORT:	To Minister, then referred to Parliament.	Annual report and audited accounts to shareholders. Not required to table report before Parliament; though does so in practice.
SUBJECT TO OMBUDSMAN:	No.	No.

INDICATORS OF FINANCIAL PERFORMANCE

(a) CORPORATE FINANCIAL STATISTICS 1981

Industry Group	$ Million Net Profit/ Loss	$ Million Capital and Reserves (Share-holders' Funds)	% Return on Capital and Reserves
Forestry and Wood	158.2	1,102.8	14.3
Printing and Publishing	17.9	155.3	11.0
Total Manufact-uring (other than food)	469.5	3,466.2	13.5
Construction	4.7	49.3	9.5
Gas	1.6	16.4	9.7
Transport	26.2	232.6	11.3
Total Other	197.2	1,740.5	11.3
Non-Life Insurance	0.6	68.2	0.9
Other Financial	64.6	298.4	21.6
Total Financial	65.2	366.6	17.8

SOURCE: New Zealand Corporate Financial Statistics 1981, Reserve Bank of New Zealand Supplement to the Bulletin (April 1982).

(b) SELECTED PUBLIC ENTERPRISES*

	Net Profit/ (Loss) $M		Rate of Return on Average Capital and Reserves %	
Air New Zealand	(30.8)		(30.9)	
BCNZ	0.45	1	0.9	
BNZ (Trading)	20.8		17.9	
DFC	3.54		10.8	
Government Life Insurance Office	52.8	2	9.5	
Government Printing Office	1.22		3.7	
Government Tourist Bureau	(0.7)	3	NA	
Housing Corporation	5.4	4	0.3	
NZED	158.1		37.0	5
NZ Forest Service (Commercial Division)	5.55		25.9	
NZ Post Office	88.56		11.8	
Post Office Savings Bank	2.68		0.15	
Public Trust Office	12.27	6	235.5	
Petrocorp	8.7	7	8.2	
Railways	(88.1)		(29.9)	8
Rural Banking and Finance Corporation	3.3		7.1	
Shipping Corporation	6.3	9	7.1	
State Coal Mines	(9.0)		NA	
State Insurance	10.53	10	14.2	
Tourist Hotel Corporation	0.5	11	3.3	

* All figures for public enterprise in this summary are the latest published results available at June 1982.

Table compiled by the Treasury.

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1 Before extraordinary items.
2 Increase in reserves.
3 Affected by operations in areas that are not directly profitable.
4 Net surplus payable to the Public Account. In effect represents an offset to the budget allocation of $17.4 m (1% of mortgages outstanding) intended to cover management costs, which were in fact $11.1 m.
5 Not an appropriate measure as electricity capital works are loan-financed.
6 Net profit plus profit allocations to estates.
7 Before extraordinary items.
8 Not a meaningful figure given the manner in which equity capital has been recorded, i.e. as the result of conversion of outstanding loans over a long period without, in large part, capitalisation of deferred interest. In some cases loans were merely written off.
9 Excludes $11.4 m recovered depreciation relating to sale and lease-back of the 'New Zealand Pacific'.
10 Excluding prior period adjustments but including Social Welfare beneficiary concessions.
11 Before extraordinary items.