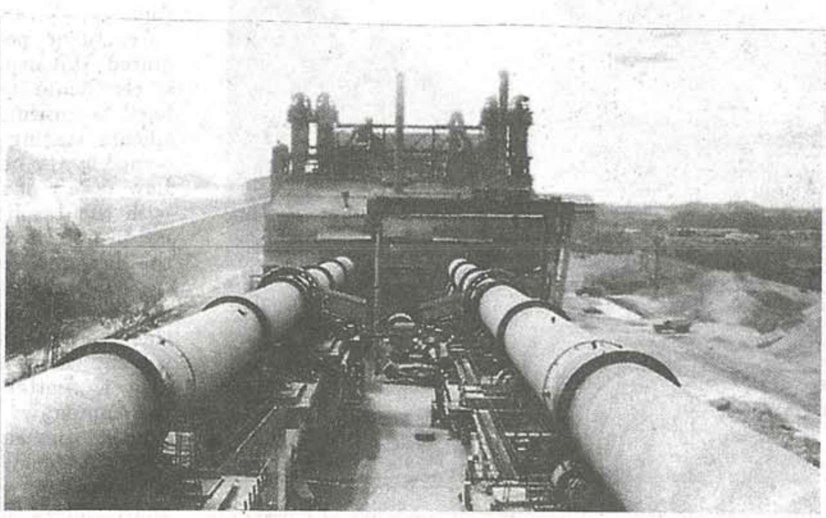
TO REFORM THE FINANCIAL MANAGEMENT SYSTEM OF STATE-OWNED ENTERPRISES

by Prof. Dr. TRẦN VĂN CHÁNH



In the process of restructuring the economy, the Party and the Government asserted: "The public sector has to implement the leading role, state-own enterprises (SOEs) are major economic forces, state corporations has to really become strong economic groups and the backbone of the national economy". Over the past ten years, the public sector has taken shape and developed more uniformly. In the meantime, SOEs have played a certain role in strengthening the state economic forces, steadily reformed, re-arranged organizational models, restructured ownership and management systems, renovated financial management system, equipment and technologies, and etc. As a result, the state sector has made the best use of its advantages in developing the multisectoral economy.

1. NECESSITY TO REFORM SOE FINANCIAL MANAGEMENT SYSTEM

SOEs are economic entities which are allocated capital, established, organized and managed by the Government. They run business for profits or public utility with the aim to carry out the Government's socio-economic programs.

SOEs have such characteristics as: legal status, civil rights and obligations, self-responsibility for all business activities within the granted amount of capital. They can either seek profits in the market or provide public services as assigned by the Government, or implement tasks of defense and security. SOEs are foundation of the socialist economy. They are regulating instruments of the Government. At the same time, they help the economy grow, and the society develop fairly and firmly.

In recent years, although SOEs have recorded some achievements but they have not yet fulfilled their leading role, they often face persistent shortcomings such as: slow growth rate, poor performance due to slow decisions on owner representatives and weak competitiveness. After they were re-arranged in line with Decree 388, their number totaled 5,700, including 2,200 making profits and contributing 85% of the State budget revenues and the rest mainly operating perfunctorily. This shows to improve their business, the system of SOE financial management should be soon renewed in accordance with the market mechanism. That is a shift from bureaucracy and subsidization to autonomy and self-responsibility before law.

The Prime Minister always requires controlling ministries and localities to stop their strong intervention in SOE business and production activities. The Government Decree 59/CP dated Oct.3, 1996 repaired the regulations on SOE financial management and accounting, specified the independence and financial liabilities of SOEs, fixed the time-limit of abolishing subsidies for these entities including indirect ones like soft loans, preferences in land rent, and so on. Such new kinds of enterprises as joint ventures, one-owner limited companies (applicable to 100% state-owned firms) are entitled for establishment.

The current system of SOE financial management indicates some following properties:

a. The Government still makes strong intervention in SOE operations, for example, ruling that all fee collections of public utility enterprises must be put in the Treasury (while

it's difficult to distinguish public utility fees and business revenues). All of the SOE's asset collateralization must be approved by authorized agencies. In the meantime, the owner's major powers such as determining the use of after-tax profits (retaining, contributing to the State budget, transferring to another firms) are not clarified.

b. The responsibilities of the SOE's director are not detailed in line with their rights. The inspection and settlement of violations reveal deficiencies, resulting in losses to the state assets due to embezzlement or low managerial skills. Moreover, these events have not been resolved properly because of ambiguous and overlapping regulations.

c. The SOE financial autonomy is though expanded, but encounters a lot of constrains in determining investment projects and levels of asset amortization (still depending on the regulated schedule). The limited costs of advertisement, marketing, translation, transaction, commissions have placed barriers to the enterprise's sensibility and flexibility, eventually affecting its performance and competitiveness.

d. Regarding organization and management, there is nominally only one owner of the SOE's assets, but the reality is not so. The rights to decide on making initial investments, mortgaging and selling assets, and entering joint ventures still belong to the government agency issuing the decision to set up the business. The responsibilities are not transparent and the solutions to troubles are divergent. The system of SOE financial management is still greatly affected by administrative instructions, loose and ineffective.

e. The financial relations between corporations and their affiliates have not yet been specified and are still pressed by administrative factors. As a result, in reality there are two trends: first, the corporation controls their subsidiaries strictly and makes strong interference in the business financial management; and second, it loosens financial management.

f. The SOEs' lack and waste of investment capital is a prevailing event. They thus cannot invest in innovation of equipment and technologies to manufacture new products, improve quality and reduce prices of products.

There are many ironical lessons of lavishing money due to careless calculation and impulse purchase. A series of sugar mills, for example, have been set up hastily, leading to an oversupply and slow sales. Certainly, the ineffective investment projects have brought huge wastes. In case where the project lends foreign capital, this debt burden has to be removed for a long period, even tens of years.

g. The Government's inspection and supervision via banking, business financial management and accounting-auditing systems have not yet been paid full attention to.

At present, our enterprises' competitive forces have not yet met the level and standard of the regional and global markets. The authorities cannot control illegally imported commodities, making the local businesses' shares contract steadily, and foreign commodities flood the local market.

The obvious and most important causes of the above-mentioned deficiencies derive from major shortcomings of the current legal frame. The bad debts have been generated because of lacking strictness of regulations on business establishment, rights of government agencies, business financial independence; capital mobilization; lending and contract payment, mortgage and guarantee, compensation, dispute settlement, and so on.

II. TREND OF REFORMING BUSINESS FINANCIAL MANAGEMENT SYSTEM

The renovation of business financial management system aims at the improvement of the autonomy and self-responsibility for business results. Basically, the self-responsibility is a requirement for the investor and based on his ownership of assets. As a result, the SOE takes its own charge of business activities only when the investor's ownership is separated from the enterprise's right to use assets. The relations between the two rights must be stipulated distinctly. It is a legal entity obtaining civil rights and obligations.

The SOE operates independently with its whole legal assets and assumes full responsibility for its performance, pays taxes, maintains and increases the investor's asset value. The investors enjoy benefits according to their shares, that is, dividends and voting rights for electing important plans and executives. When the business goes bankrupt, the investor takes limited responsibility for the debts within his share.

To assess impartially the firms' situation of business and production and avoid evaluation based on reports from administrative agencies, we have to depend on evaluation criteria in business and production, and investment.

1. In business and production activities, there are some noteworthy criteria as follows:

- The profit ratio to working capital;
- The ratio of net revenue to total equity;
- Debt solvency: This criterion is calculated by the sum of total cash and revenues divided by short-term liabilities (including due debts, short-term payment and other costs).

In the market economy, the third criterion is most important. It shows whether the firm's disposable assets (fast liquidated into money) in the short run are enough to repay debts when due. The Government has not paid attention to the SOE's solvency previously, so it can hardly knew if its assets remained or lost, leading the phenomenon "false profit, actual loss".

2. Investment activities: The SOE is granted capital by the Government and operates like limited companies (joint stock or one-owner limited companies). We use following criteria to assess the SOE's investment activities:

- Internal rate of return;
- Time and rate of capital recovery;
- Analysis of break-even point;
- Net present value method;

The fourth criterion is most important, it is used to assess the efficiency of an investment project. The method to figure out this criterion is based on annual dual interest rate to see if the total amounts of income during the investment period (20 years for example) is equal to the present value of the invested capital sum. This method is not common in our country.

III. SOME SOLUTIONS TO THE REFORM OF SOE FINANCIAL MANAGEMENT SYSTEM

To reform the SOE financial management system and see it as an effective managerial instrument, actual economic lever as well as one of important measures to intensify the business performance and competitiveness, the relevant authorities should focus their efforts to solve the following issues:

1. Specifying the financial management system for SOEs operating for profits and public utility. The for-profit SOEs should be given full financial autonomy but initially granted investment capital only one time. Then they shall preserve their capital stock and themselves mobilize more money to expand production and business on their own.

The public utility SOEs' capital is secured to implement the public tasks assigned by the government. At the same time, they operate under the government's strict supervision and inspection in financial management, use of capital, revenues, costs, losses and profits.

2. Clarifying the state ownership to the business, including the right to enjoy benefits from good business performance. Asserting that the after-tax profits belong to the Government (having rights to retain profits for the enterprise, pay to the Treasury, transfer to other enterprises).

Regarding state-owned properties, the enterprise is fully entitled to purchase, sell, mortgage and etc. If controlling, the Government should depend on the total value of asset as compared with the total capital it grants to the enterprise, not on each kind of assets.

3. Expanding the enterprise's autonomy. The business is authorized to make decisions on fixed asset amortization (the Government regulates the floor level only), enlarging production, using costs and so on. However, it shall have mechanisms for supervision and inspection, for example, equipment purchase bidding, asset auctions, and disclosure of payments (the Government's Decree 07/1999/NĐ-CP dated February 13, 1999).

Clearly stipulating responsibilities of business executives and financial punishment for violations and cases where the investment and business doing cause losses.

4. Changing the business financial management from "administration and subsidization" to "financial investment" system. Applying the system of assigning and preserving capital, and collecting "fee of capital use" (not tax on capital use). The Government assigns capital to the SOE - a legal entity, not to its director or the chairperson of the Management Board). The workers' wages, including directors', is relative to the profit ratio to capital assigned.

The relations between corporations 90-91 and their affiliates should shift to the form of investors or relations between parent and subsidiary companies.

5. Improving the internal audit and state audit through the system of business financial statements. Disclosing the situation and efficiency of capital use, due and overdue debts; revenues and expenditures from business activities and others.

6. Intensifying investments in innovating equipment and technologies of SOEs. The technological renewing is one of crucial factors of the business. The Government should help businesses to attract money for technological innovation. In the meantime, the Government should supervise and inspect the renovation of equipment and technologies in SOEs and strictly prohibit them from importing out-of-date equipment and machinery.

7. Restricting and then separating social costs incurred by the enterprise. These costs affect greatly business and production activities of the enterprise. For example, the Vietnam Coal Corporation, Vietnam Coffee Corporation had to make investments in building roads, electricity grids, kindergartens and health stations in the area where they are located.

8. Making strict execution of legislation and policies whenever they have been promulgated. Avoiding the fact that the legislation and policies exist only "on paper" or if arbitrarily applied as "the King ruling has to yield to the village custom", or misapplied to gain individual benefits.

Although the SOEs have faced many challenges in the process of business and production but most of them have made great efforts to find markets for their products; every capital source to innovate their equipment, machinery and technologies; and use their capital stock thriftily and effectively. They also seek every way to mobilize capital from different sources with a view to expanding production, improving product quality and reducing product prices.

It is important that the Government should reform the business financial management system; remove hurdles and troubles; create a strict legal frame in order that SOEs meet conditions of healthy competition with other domestic and foreign enterprises; and heighten their business performance and leading role■