COUNTRY STUDIES

Norway – Marketisation of Government Services – State – Owned Enterprises

2003

Introduction

The Review is one of a series of country reports carried out under the OECD's Regulatory Reform Programme, in response to the 1997 mandate by OECD Ministers. This report analyses the marketisation of government services and state-owned enterprises in Norway. This report was principally prepared by Ms. Elizabeth Roderburg for the OECD.

Overview

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FOREWORD

Regulatory reform has emerged as an important policy area in OECD and non-OECD countries. For regulatory reforms to be beneficial, the regulatory regimes need to be transparent, coherent, and comprehensive, spanning from establishing the appropriate institutional framework to liberalising network industries, advocating and enforcing competition policy and law and opening external and internal markets to trade and investment.

This report on *Marketisation of Government Services – State-owned Enterprises* analyses the institutional set-up and use of policy instruments in Norway. It also includes the country-specific policy recommendations developed by the OECD during the review process.

The report was prepared for *The OECD Review of Regulatory Reform in Norway* published in 2003. The Review is one of a series of country reports carried out under the OECD's Regulatory Reform Programme, in response to the 1997 mandate by OECD Ministers.

Since then, the OECD has assessed regulatory policies in 18 member countries as part of its Regulatory Reform programme. The Programme aims at assisting governments to improve regulatory quality — that is, to reform regulations to foster competition, innovation, economic growth and important social objectives. It assesses country's progresses relative to the principles endorsed by member countries in the 1997 *OECD Report on Regulatory Reform.*

The country reviews follow a multi-disciplinary approach and focus on the government's capacity to manage regulatory reform, on competition policy and enforcement, on market openness, specific sectors such as electricity and telecommunications, and on the domestic macroeconomic context.

This report was principally prepared by Elizabeth Roderburg, Competition Division of the OECD. It benefited from extensive comments provided by colleagues throughout the OECD Secretariat, as well as close consultations with a wide range of government officials, parliamentarians, business and trade union representatives, consumer groups, and academic experts in Poland. The report was peer-reviewed by the 30 member countries of the OECD. It is published under the authority of the OECD Secretary General.

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Executive Summary

State ownership in commercial entities in Norway is extensive, and has a variety of organizational forms. It has evolved not only as the result of direct involvement in industrial development of the country but also in connection with the significant commercialization of the provision of public services at national government level over the past two decades through the formation of state owned enterprises. Many of these entities have now been transformed into incorporated companies and some have been privatized. Overall this reform has been very successful: efficiency, effectiveness and quality of service have improved, competition has increased, profitability has improved and real prices have gone down. These reforms were sensitive because of concerns about service provision and loss of national control of strategic sectors. There have been no significant problems with the implementation of reforms, as reforms have been implemented after extensive consultations and consensus-building efforts at the political level.

It is essential for successful reform in these areas to observe a number of key policy underpinnings, including the need for separation of regulatory and business functions, that competitive neutrality apply between private and public business entities and that governance systems are "fit for purpose". These requirements were broadly observed in the Norwegian reforms, but inevitably there is scope for improvement. An increasing number of enterprises are being transformed into incorporated companies, thereby increasing the distance to the regulator. Regulatory and ownership functions have been separated with the aim of collecting ownership responsibility in one Ministry - but this has not yet been done across the board. Sectoral ministries retain ownership of the companies that are considered important policy instruments in themselves. Some violations of competitive neutrality remain and should be addressed, particularly the issues of cross-subsidization. A recurring debate relates to the best means of ensuring appropriate governance structures while allowing sufficient flexibility to operate in commercial markets. Assessing alternative organizational forms i.e., the establishment of holding companies, has caused delays in further reform.

The goal is a reduction in state ownership, yet broad scale privatization is not necessarily seen as an end point for these reforms. Norway's primary focus is on achieving a highly developed ownership policy. Privatization, where it has occurred, has been careful, staged, and carried out on a case by case basis according to the pragmatic circumstances of the company concerned and the external environment. The impetus for change often has come from the company concerned. The extent of privatization is limited by a lack of broad agreement in Parliament on the benefits of reducing state ownership, and a fear that the comparatively small private Norwegian capital base could not absorb a large scale sale of shares. Privatization has proceeded furthest – i.e. full scale disposal of ownership - in sectors which are purely commercial and do not have significant public policy elements. This is implicitly consistent with a well principled privatization policy but ultimately the policy position about what the government should and should not own, and thus what it should or should not privatize, is fragmented. While the strong financial position of the state does not require privatization, it would nevertheless be desirable to take forward privatization more broadly, according to a principled policy if that would assist, as ultimately this will improve efficiency and innovation in business and industry.

This study looks at reforms in civil aviation and non-market driven areas (hospitals, and labor market institutions) as examples of the commercialization process.

1. STATE-OWNED ENTERPRISES AND MARKETIZATION OF GOVERNMENT SERVICES

Overview of the Study and Main Issues

The public sector has a very significant direct involvement in the Norwegian economy through its ownership of commercial entities and through direct production at the municipal level of government. Partly, this reflects the fact that Norway is a "Nordic welfare state", where the government directly provides most social and welfare services, such as heath and education. It also reflects the historical fact that the State was significantly involved in the industrial and commercial development of the economy. Although Norway made a relatively late start in relying more on market forces and less on the state in the

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provision of goods and services, over the past two decades broad commercialization of formerly public services has occurred at the national level and there has been substantial privatization of state owned enterprises, particularly in manufacturing industries. In the municipalities commercialization has taken place in day care, elderly care, technical services and transport, but across the board it is still at a relatively early stage.

The overall economic context of these developments and the surrounding circumstances was discussed in Chapter 1. We can summarize by noting that policies that have driven commercialization in government economic activity are motivated and constrained by the following critical factors:

- Income from the offshore sector has benefited the Norwegian economy and made it possible to maintain and strengthen an extensive welfare system, but has also masked the need for structural reforms and has made their implementation more difficult. Double-digit budget surpluses since 2000 (15 per cent of GDP in 2002) and substantial government assets associated with oil production are exacerbating pressures to raise spending. Improved control of public spending is necessary in order to cope with the fiscal consequences of ageing and of the depletion of oil reserves.1

- The strong financial position of the State provides a temptation to increase funding rather than promote structural change. But as has been seen in a number of public service sectors increased funding has not led to improved efficiency or user orientation. Public spending accounts for more than half of mainland GDP (around 40 per cent of total GDP). Increased funding of the public sector together with continued public employment growth threatens to crowd-out private sector labor demand in a tight labor market.

- International agreements and obligations, particularly the European Economic Area Agreement, technological progress and the desire for greater freedom of action on the part of public enterprises operating in commercial markets are far more likely to prompt continued detachment from the state than budget constraints.

- Efficiency is not and should not be the only objective of the state but, there is scope to significantly improve productivity, including in the government sector. This has the potential to improve service delivery without the adverse effects of increased fiscal sending.

- Improving the efficiency of the state is also possible through a privatization of assets that can be used more productively in the private sector and for which there is not an over-riding public policy purpose in keeping a function directly within state control. Given the political choice in favor of the welfare state, the policy challenge is thus to manage the reform process carefully and without disruption of services so that efficiency is enhanced through private participation and a more commercialized orientation is applied to ongoing state production, while the role of government shifts progressively in favor of steering and procuring services rather than producing them.

- The overall level of state involvement in economic activity through ownership is relatively high in Norway and is expected to remain high for the foreseeable future. The Government goal to reduce the level of state ownership has not been endorsed by Parliament, yet partial or full privatization is continuing on a case by case basis.

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- A constraint on further commercialization is the fairly pervasive conviction that the Norwegian private capital market is not strong enough to absorb a broad privatization of State holdings at real share value. Underlying this concern is a desire to maintain Norwegian ownership of significant assets.

This chapter focuses on the reform process where commercialization of state agencies has been undertaken to marketise services formerly produced directly by government agencies free of charge. It does not cover local government, county or municipal ownership of commercial enterprises. The chapter is laid out as follows. Firstly, the extent of state ownership is set out followed by a brief description of the various organizational forms used. Secondly, a conceptual framework to consider the issues of competition, regulation, privatization and corporate governance is set out and examined in the context of the existing framework for regulation of state ownership.[2] Some possible policy options are then developed. The final part of the chapter looks in more detail at reform in civil aviation and two non-market driven areas (hospitals, and labor-market institutions).

1.1. State owned enterprises

The Extent of State Ownership

About three quarters of all Norwegian savings are controlled by the State, and state ownership in commercial entities is extensive both at the central and municipal level. As an illustration, the State's holdings amount to about 40 per cent of the total value of the companies listed on the Oslo Stock Exchange.[3] Prior to the partial privatization of Statoil and Telenor the share of state holding on the OSE amounted to around 15 per cent. The high level of State ownership of commercial entities in Norway is not the result of one concerted strategy, and the motivations for specific ownership involvement have varied over time and have to some extent been random. Historically, however, the desire for national control of the utilization of natural resources has been a driving force behind state ownership. Another has been the need to develop infrastructure and infrastructure-based provision of services. State ownership has accompanied the development of the welfare state, and has played a role in developing industry and commerce. State ownership in Norway is extensive, not only in traditional public service related sectors, but also in industry, particularly the energy, transport and telecom sectors. Norway's financial situation is comfortable and there has been little pressure to commercialize or privatize for fiscal reasons.

The State's direct involvement in the industrial and commercial development of the economy started prior to the turn of the century with the establishment of infrastructure based service provision (telegraph, postal services, public roads) and continued with the introduction of concession laws in 1906-1917 which were intended to safeguard public interests in the exploitation of waterfalls for production of electricity. State participation in the establishment of power stations started in the 1920s. State involvement was expanded after World War II particularly in the establishment of the iron and steel industry and partly through state acquisition of German assets in several industrial companies (for example Norsk Hydro AS).[4] Prior to that foreign capital was dominant in the Norwegian economy. The Norwegian State was financially weak and private capital was relatively scarce. The inter-war and post-war period also saw the establishment of institutions and enterprises such the Norwegian National Grain Administration (1927), the state wines and spirits monopoly (1932), the state-run housing bank (1946), the Postal Savings Bank (1948) and the pharmaceutical wholesaler (1957). The establishment of Statoil AS, the state oil company in 1972, is perhaps the most significant national resource motivated state ownership. Public involvement in the commercial banking sector came in response to the banking crisis in the late 1980s and early 1990s. The government has subsequently sold its shares in most of the banks, but has retained a 47.28 per cent share in the largest commercial bank, Den norske Bank (DnB) through the Government Bank Investment Fund (Statens Bankinvesteringsfond).[5]

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State ownership takes a number of forms ranging from portfolio investments or capital investments to direct ownership or full or partial ownership of limited companies. A number of state owned companies have been reorganized the last decade as the regulation of markets has taken other forms than through ownership. In addition enhanced separation of activities exposed to competition from natural monopolies or the government administration has also occurred. Privatization has not been a dominant issue in the Norwegian reorganization debate, although in the 1980s and early 1990s major state owned manufacturing companies were restructures and privatized fully or partially: ÅSV (aluminum), Kongsberg Vaapenfabrikk (defense, aerospace, and maritime products and automotive components), Norsk Jernverk (iron). Around 20 companies have been partially or fully privatized since 1999. Consequently, reform is described as a pragmatic incrementalism: a step-by step consensual process rather than driven by fundamental principles.

Table 1: Main state-owned companies[1]

Company	Sector	Persons employed in 2001 (incl. Abroad)	% State Ownership	Established	Ministry
Norsk Hydro ASA***	Aluminium, fertilizer, oil and gas	35,567	43.82	1905	Trade and Industry
Cermaq ASA***	Fish feed and farming	2,686	79.38	1994	Trade and Industry
Telenor ASA***	Telecommunications	22,000	77.68	1994/2000	Trade and Industry
DnB Holding ASA***[2]	Banking, insurance, financial services	7,236	47.30	1999	Trade and Industry
Store Norske Spitsbergen Kullkompani AS***	Use of company property on Svalbard	249	99.94	1916	Trade and Industry
Statoil ASA***	Oil and gas	16,408	81.80	1972	Oil and energy
SAS AB***	Airline	31,035	14.30	2001	Trade and industry
VESO As	Veterinary research and services	48	1000	1991	Ministry of Agriculture
Bjørnøen AS**	Land-use administration Svalbard	0	100.00	1918	Trade and Industry
Grødegaard AS**	Catering, hotels	700	100.00	2001	Trade and Industry
Norsk Eiendomsinformasjon as**	Runs property registration	18	100.00	1987	Local Government
Kings Bay AS**	Realty, promote R&D Svalbard	20	100.00	1916	Trade and Industry
NRK AS**	Public broadcasting	3,486	100.00	1996	Church and Culture
SND Invest AS**	Promote industrial development	27	100.00	1998	Trade and Industry
BaneTele AS**	Infrastructure development for tele-Communications	160	100.00	2001	Trade and Industry
Norsk Tipping AS****	Lottery	273	100.00	1946	Church and Culture
Gassco AS**	Natural gas transportation	100	100.00	2001	Oil and Energy
NSB BA**	Railroad passenger transportation	10,029	100.00	1996/2003	Communication and Transport
Posten Norge BA**	Mail service	32,365	100.00	1996/2003	Transport and Communication
AS**** Vinmonopolet	Retail alcohol distribution	1,461	100.00	1932	Social affairs

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Enova SF*	Promotion of energy conservation and alternative energy use promotion	19	100.00	2001	Oil and Energy
SIVA SF*	Investments, loans for regional development	39	100.00	1968	Trade and Industry
Statkraft SF*	Electricity sales, distribution, production	1,187	100.00	1992	Trade and Industry
Statnett SF*	Electricity transmission and system operator	785	100.00	1992	Oil and Energy
Statskog SF*	Forestry management	248	100.00	1993	Agriculture
Cernova AS***	Holding company for investments in grain and feed sector		100.00	2001	Trade and Industry
Kommunal-banken AS	Banking, loans to municipal sector	29	80.00	1999	Local Government and Regional Development
Kongsberg*** Gruppen AS	Defense, aerospace and maritime products	4,012	50.001	1987	Trade and Industry
Moxy Trucks AS***	Production and sale of construction machinery	220	48.99	1991	Trade and Industry
NOAH AS***	Special waste management	102	70.89	1991	Trade and Industry
A/S Olivin***	Quarrying	194	50.99	1948	Trade and Industry
Raufoss ASA***	Automotive components etc.	1,090	50.27	1896	Trade and Industry
Arcus ASA***	Import, export of alcoholic beverages	466	34.00	1995	Trade and Industry
Eksportfinans ASA***	Financial services related to exports	88	15.00	1962	Trade and Industry
Nammo AS***	Munitions manufacture	1,521	45.00	1998	Trade and Industry
Stor-Oslo Lokaltrafikk AS***	Public transport in Oslo	84	33.33	1974	Transport and Communication
Government Bank Iinvestment Fund	Capital supply for banks	3	100.00	1991	Trade and Industry
Statens investerings-selskap AS	Investment company		100.00	2001	Trade and Industry
The National Insurance Scheme Fund	Financial investor	22	100.00	1968	Finance
Petoro AS	Management of the State's Direct Financial Interest (SDFI) in oil and gas	60	100.00	2001	Petroleum and Energy
Avinor AS**	Civil aviation – airports, air safety	2900	100.00	2003	Transport and Communication

* Statutory enterprise
** Government owned limited companies
*** Limited company with government ownership
**** Hybrid companies

1. The above table does not include enterprises owned by the municipalities not does it include a number of smaller companies – among them companies owned by the above mentioned companies.
2. Ownership of DnB is managed by the Government Bank Investment Fund.

Source: Ministry of Trade and Industry.

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1.1.1. Objectives and Mechanisms of Reform

There is no single model by which different countries have chosen to marketize public services – either as to the way it is has been done nor its extent, but there are a range of common threads, in terms of the objectives and outcomes and consequential policy issues – see Box 1. The following addresses the Norwegian experience in terms of these policy issues and deals with the efforts to reform state ownership in trade and industry.

Commercialization[6] of public services in Norway has taken a number of forms and progressed through different stages depending on the sector. While commercialization has been a broad goal since the early 1990s, the policies, principles and solutions have varied between enterprises and sectors. There has in other words not been a concerted or overarching policy determining commercialization in all areas. Norway has a fairly long history of discussions and decisions concerning the organizational form of state ownership; up until the 1960s the focus was on parliament's constitutional control of particularly government manufacturing enterprises. In the mid 1980s the debate focused on modernizing the public sector. A reassessment of State affiliation and ownership for a number of public enterprises was initiated as part of this process based on recommendations laid out in a 1989 study *A Better Organized State.* This study led to a formalized policy position in Guidelines from the Ministry of Government Administration in 1994 that the state would commercialize using one of two vehicles, a limited company and a state owned statutory enterprise.[7] A limited company would be used where corporate governance arrangements were seen as sufficient to exert a relatively low degree of government control, while a statutory enterprise would be used when the needed government control was significant. In the event, however, this "neat" outcome was not achieved, with major companies operating in monopoly infrastructure sectors in a form of a hybrid closely controlled government company. The following section gives a brief overview of the various forms, particularly their legal and management characteristics.

Net budgeted agencies, including administrative enterprises, statutory enterprises and incorporated companies have all been used to organize the provision of services. The choice of organizational form has been determined by a number of factors, some sector specific, others such as labor concerns, public interest concerns, or international obligations, particularly those deriving form the European Economic Area Agreement (the EEA), have determined the organizational form chosen

The creation of ***administrative enterprises*** (Forvaltningsbedrifter) involves the creation by statute of an entity that is *functionally* separate from the state, with its own management structure (subject to governance mechanisms) and operating according to "business principles", i.e. along commercial lines; yet it is part of the state as a legal person and is included in the government budget. The Parliament fixes the administrative enterprises' net budgets, total investment levels and powers and thereby exercises general control. In addition, income is often bound through parliamentary decisions on prices, quality and coverage of the services to be provided. Employees are civil servants, but administrative enterprises have extended powers in the salary and personnel sphere and when it comes to buildings and property management. Consequently, such enterprises have more operational or day-to-day independence from government to deliver their objectives than would a state agency, yet the Government retains the option of direct intervention in enterprises' activities.

Administrative enterprise was the organizational form that was first introduced and implemented for public development and operation of infrastructure and commercial service production. By the mid 1980s the railways, the postal and telecom services and state power boards were all organized as administrative enterprises. A number of organizational changes have taken place since then, particularly the separating out of commercial activities. Reorganization of state-owned network services, particularly electricity and railways, has moved in the following direction:

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- The part which is exposed to competition is organized as a limited liability company or as a statutory company.

- The monopolist part of the business is organized as an administrative enterprise (or statutory company or a company subject to a separate law).

- The regulatory authority is organized as an administrative agency.

The administrative enterprise form is no longer in common use and is considered anachronistic.[8] No new administrative enterprises have been formed in recent years. Most recent processes of commercialization of public services have occurred through the establishment of state-owned enterprises (either statutory, incorporated or hybrid companies).

The ***statutory enterprises*** (Statsforetak)[9] are separate legal entities and their capital and income are not part of the Treasury. They are allowed to operate on almost the same terms as private companies, but with some limitations. They must be wholly owned by the State. There are limitations on the companies' activities, often established in the letters of association, that are related to sectoral policy obligations the companies are expected to carry out.

The Government exercises proprietary authority through the annual meeting (equivalent to a limited company's general meeting). The annual meeting (foretaksmøtet) is comprised of the ministry representatives, the managing director, head of board of directors and the company auditor. Only the Ministry has voting rights at the annual meeting. The annual meeting appoints the Board of directors. The Office of the Auditor General[10] assesses the financial management and accounts of these companies. The Act governing these companies specifies that the companies must provide board-records to their ownership-ministries and all actions which could significantly alter the companies' activities must be presented in writing to the responsible ministry prior to decision or enactment. In addition, articles of association for the company can specify which types of decisions must be cleared with the ownership ministry. This has particularly been used to ensure that significant sectoral policy decisions are cleared with the ministry.

The State has, until 1 January 2003, been a guarantor for loans for statutory companies. The Act governing such companies was amended in December 2002 after the EFTA Surveillance Authority (ESA) had termed the conditions governing the provision of government guarantees to these enterprises as being in contravention of the EEA Agreement.[11] New loans are not guaranteed by the State as from 1 January 2003. State guarantees apply only for older loans until expiry, and a commission is required. Accordingly, statutory companies may go into bankruptcy. Statkraft SF, the State electricity production company, Statnett SF, the State electricity network company, and Statskog SF, the State forestry management company, are all examples of statutory companies.

The Government has recently announced[12] that it intends to transform Statkraft SF into a state owned limited company. The Minister of Trade and Industry has pointed out that privatization (selling of shares) and listing on the stock exchange is not currently on the agenda for the company, but that a reduction in the state ownership share, for example through Statkraft entering into alliances with other companies is envisaged.

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The ***state owned incorporated companies*** (Statsaksjeselskaper) [13] include companies that were to some extent previously organized within the central government. This is the preferred form of business organization in commercial and industrial activity in which *no particular sectoral policy considerations apply,* or where the enterprises operate in a competitively exposed market and are given this organizational form in the interests of business efficiency and freedom of action. Increasingly companies that are considered to be important policy instruments are nevertheless organized in this form in order to provide them with the greatest possible freedom to run the companies according to normal business practice.

One must distinguish between incorporated companies that are 100 per cent state owned on the one hand, and companies where the state holds a majority or minority share, on the other. The Companies Act applies to both types of companies, yet some specific provisions relate to 100 per cent state owned companies:

- The Government can overrule decisions in the corporate assembly concerning investments and change of activity if societal concerns warrant it. A special general meeting can be called by the ministry on short notice.

- The board is appointed by the general meeting and not the corporate assembly. The general meeting is not bound by the corporate assembly or board's proposed financial return.

- The Office of the Auditor General supervises these companies, and is entitled to request information it deems necessary for control purposes from the board of directors, managing director and company auditor.

- The minister with the ownership role for the company is the company's general meeting.

Control by the state with these companies is on a general level, and usually linked to the enterprise's sphere of activity, financial return and dividend, and the constitution and composition of the enterprise's governing bodies. Profitable operations are usually the main operating criteria for these companies, however, the Government may draw up special responsibilities that need to be met, for example country-wide broadcasting, or basic telecommunications services across the country. The state's financial liability is limited to the subscribed share capital and such companies may be put into compulsory liquidation. Special provisions allow for specific instructions from the government to the managing director if the government so wishes. This is particularly the case for companies where Parliament exercises control over incomes. The Norwegian public broadcasting corporation, NRK AS, is an example of such a company.

Incorporated companies with state ownership. For majority or minority share companies The Companies Act – that regulates all incorporated companies - applies without the special provisions that apply to 100 per cent State owned incorporated companies. The Government may thus only use its ownership influence by participating and voting in the general meeting. Examples of such companies are the to be found among the largest Norwegian companies, Norsk Hydro ASA (minority share) and Statoil ASA (majority share) and Telenor ASA (majority share) and DnB Holding ASA (minority share).

Hybrid companies (Særlovselskaper) are a composite group whose common factor is that they are established under special legislation for each enterprise. This form of organization emerged initially with the establishment of the state wines and spirits monopoly, AS Vinmonopolet, in 1932. The company is governed by a specific law which regulates its operations and specifies the social policy objectives it is to promote. Hybrid companies are legal entities in their own right. Most hybrid companies are established in areas where they are essentially in a monopoly situation. Hybrid companies can take the form of either incorporated companies or statutory companies. Both the state railways (NSB AS) and the postal service

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(Posten Norge AS) remained administrative enterprises until 1996 when they were converted into hybrid companies. These companies have subsequently been converted into wholly state owned incorporated companies effective 1 July 2002. The regional health authorities established 1 January 2002 (see chapter 1.3.) took the form of hybrid companies with special legislation governing their activities.

The governance mechanism is considered in section 1.1.2.

Box 1. **International Experience with Reforming Public Enterprises**

The OECD undertook a study on "Reforming Public Enterprises"[14] in 1998 by examining the reform experience in Australia, Netherlands, Spain, Switzerland and the UK. The following draws out some issues that are reflected in the Norwegian experience.

In the Netherlands, privatization has been launched through extensive consultation processes that must address mandated questions about the rationale for initial government involvement in an activity and whether that rationale still exists. While this has aided coherence of the program actual implementation has been hampered by a slow legislative process and other technical requirements. Employees are protected by a right of transfer to a continuing civil service function.

In Spain, non-strategic government companies were privatized in the later 1980s. This was followed by a period of commercialization of state entities aimed at efficiency until 1996 when a new government was politically committed to privatization leading to a very significant reduction in state ownership of commercial activities

In Australia, commercialization and privatization progressed on a case by case basis but were in some respects hampered by the federal structure where the distribution of tax powers was different to the ownership of government enterprises. One unique element of the reform program was the adoption in 1995 by all Australian governments of the National Competition Policy Reform. NCP had the effect of coordinating further reform by laying out a blueprint of principles for competition related reforms (including reform of public enterprises), an implementation timetable and a system of "competition payments" designed to share the benefits of reform among the different governments. These "competition payments" were made contingent upon actual implementation of the required reforms.

In the UK, all state enterprises have been corporatized and most privatized. Reform started earlier in the UK than most countries. One of the early lessons was the need to give considerable weight to competition conditions in privatization so as not to create industry structures with significant market power.

The formation of state owned companies in public service sectors has taken place as these sectors have become deregulated and been opened for private participation. The incorporated company as an organizational form has been chosen in order to allow these companies to compete with private providers, and develop competitive markets in these services. This competition objective has been more obvious in respect of some areas (such as telecommunications) than others (such as the railways) but it is fair to say that the overall emphasis upon competition has increased over time. The commercialization and competition objectives are mutually related and reinforcing. Clearly, private competition reinforces the pressure for efficiency gains within state owned enterprises and commercialization increases the potential for management action that can release efficiencies. And, reform of state economic activity into a form where there is broad competitive neutrality with potential private entrants is important for fostering private entry and competition – clearly, if state owned enterprises retain significant competitive advantages over private companies then private entry is not likely.

A key advantage in company arrangements is greater flexibility to respond to changes in the business environment. This is because activities which are undertaken "on budget" inevitably are constrained by the lack of flexibility inherent in Government budgeting. In addition companies in competitive markets will often need to make quick decisions, but drawing in the government as owner in detailed decision making is time-consuming and not efficient (and Government often lacks company

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specific expertise to make sound judgments). Flexibility and timely decision making was also an element focused on in the debate on reform of the hospital sector. (See section 1.3.) There has thus been general agreement that the Norwegian State should govern state owned companies through general framework conditions rather than detailed intervention. Direction from the government in the corporate form (in a 100% owned government company) generally takes place through ownership/governance channels, i.e. shareholder meetings and board decisions. Norway moved in the direction of governance through the general framework with independent boards (without government participation) much earlier than most countries, and most major companies now are managed in this way. This has its background in the so-called Kings Bay affair and the ensuing vote of censure of the incumbent government in 1963. The affair concerned a coal mining accident at Kings Bay in Svalbard. "It was asserted that the placing of government officials and officers on the boards to strengthen the opportunities for control may actually have been counter-productive since conflicts of loyalty arose between the owner-role and controller role."[15]

Marketization inherently separates the roles of governance or procurement and production and reduces political influence on the latter so that production of services becomes more orientated to the demands of consumers. Similarly, focussing of the state on its public objectives should become more explicit because if public objectives are to remain they can no longer be left as implicit objectives that are pursued through direct control or ownership channels. In the case of privatization any public objectives need to be pursued through regulation or contract. This range of mechanisms is summarized in the following table.

Organisation Form	Administrative enterprise / Government Agency	Statutory Company	State Owned Incorporated Company	Private Company (majority or minority share)
Public Objective Mechanism	Direct Control Legislative Steering	General Regulation Proprietary Governance	General Regulation Governance	General Regulation Governance

The administrative enterprise form in Norway has thus served as a first transitional stage to a company form for a number of entities. The Norwegian telecommunications infrastructure and service entity is a case example. Norwegian Telecom (Televerket), now Telenor was first turned into an administrative enterprise in the mid 1980s as deregulation of the telecommunications sector started. The administrative tasks of regulation and control were separated into the Norwegian Telecommunications Authority (Statens Teleforvaltning). Telenor was subsequently turned into a state owned incorporated company in 1994, and was partly privatized and listen on the Oslo and New York Stock Exchanges in December 2000.

Today Norwegian policy is that as a general rule the **incorporated company** should be chosen as the organization form for state owned businesses.[16] Transformation of the railways and postal services are examples of this policy, as is the recent (January 2003) transformation of NATAM (air traffic and airport management) into Avinor, an incorporated company, and the separating out of the construction services from the roads administration. The organizational form of Statkraft and Siva are also being assessed. The incorporated form provides the greatest distance between the regulator role and the ownership, especially when the companies are "owned" by a separate ministry the MTI. The incorporated company form also makes the transition to further marketization or privatization more feasible.

Personnel Issues

Some flexibility to increase and decrease labor inputs in line with demand is essential for any entity that is run along business lines; otherwise, it cannot adjust to market developments and its financial sustainability is at risk. This risk is clearly amplified if there is actual competition in the sector with private

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firms staffed by employees. Therefore, in order not to have a competitive disadvantage vis a vis private firms, it is appropriate that the personnel of state owned enterprises also be employees with broadly similar terms of employment as comparable private sector firms.

Personnel issues have not figured strongly in the debates on commercialization and have not been a strong constraint on reform in Norway. The main constraint to commercialization has been the focus on maintaining national control of resources or assets. Yet personnel issues have emerged in connection with the transformation of individual entities from the administrative enterprise form to a company form. As mentioned, administrative enterprises are part of the state sector and all personnel are "civil servants" and thus enjoy strong formal protection against dismissal. Civil servants' rights are regulated through the Civil Service Act, while private sector and municipal employees' rights are regulated through the Working Environment Act. There is little difference in the short term in the severance pay a civil servant receives and the unemployment benefits a private sector worker receives. However, civil servants may retain their benefits unreduced for a longer period of time. Civil servants also have a preferential right to a new position in state service if their position is withdrawn or eliminated. Consideration of employees' interests has been an important premise for the choice of the hybrid form of business organization for major enterprises such as Posten Norge (Norway Post)[17] and NSB (BA). While the original goal was to give these entities a company form, continuation of the rules on priority, notice and severance pay for civil servants on a permanent basis could only be achieved through special legislation.[18] With their transformation to incorporated companies in 2002, the government decided to maintain the employees' special access to priority and severance pay until 1 January 2005.[19] The same procedure has been followed for the newly established Avinor (air traffic and airport management) (See Section 1.2). The employees are provided a three-year transitional period, where they maintain their rights concerning priority and severance pay as civil servants.

Membership in the State Pension Scheme has not presented a problem in the transformation of these entities. The Government has basically allowed the Boards of the new companies to decide if membership in the State Pension Scheme should be maintained or a private scheme introduced.

Reorganization measures have so far been of little significance for the staff situation. Some state owned companies have shed staff – particularly Telenor ASA and more recently Norway Post (BA) - but this has generally occurred without significant dispute. Both organizations established special units to help employees facing redundancy. While unions have accepted the need to achieve efficiencies, they nevertheless remain wary of labor shedding from further commercialization and privatization.[20] Consequently, the unions prefer the government to retain a significant minority interest in privatized companies, even where these have no other social objectives, as "insurance" should influence need to be brought to bear on a re-location decision. Apparently this insurance has never been actually called but it is regarded as real by the unions and could be seen to operate if ever the state were to bail out one of its firms rather than let it fail.

1.1.2. Current reform efforts

The current Government launched a new reform initiative in January 2002, *Modernizing the Public Sector in Norway – making it more efficient and user oriented*.[21] The initiative concentrates on four objectives: a less complex and more efficient public sector; public services adapted to individual needs; a public sector that promotes productivity and efficiency; and an inclusive and motivating human resources policy. The main principles underlying the efforts to promote efficiency are ***delegation*** and ***decentralization***. The aim is to provide state public service providers with increased autonomy, and to decentralize tasks to the municipalities.[22] Consumers of public services should be given greater choice. Increased competition between public and private service providers by establishing a level playing field is

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a means of enhancing efficiency and providing consumers with greater choice and improved services. Private service providers should increasingly be allowed to provide services. A clearer separation between administration and service provision should allow for more flexible and user-oriented models of organizing public services.[23]

The Government aim is "to introduce private service providers in sectors when interaction and competition between public and private actors may be beneficial." The following sectors have been identified in this regard: healthcare and educational sectors, within transport and communications and measures for unemployed and the occupationally disabled, and in state property administration.[24] The Government has appointed a committee to prepare a new law on higher educational institutions, with a mandate to consider alternative organizational forms of universities and colleges, including hybrid enterprises. Some state owned research institutions have already been transformed into limited liability companies, while the Minister of Education and Research has excluded this alternative concerning universities and colleges.

Consolidating and reducing ownership interests is seen as an important means to ensure that the public sector maintains a sound division between its various roles – as a regulator, owner, service provider, source of financing and supervisory authority. The Government White Paper to Parliament in April 2002 entitled *A Reduced and Improved State Ownership* summarizes policy goals as follows:

- State ownership is not a goal in itself. But the State is likely to remain a considerable owner and shareholder also in the future.

- Enhancing the clarity and increasing the distance between the State's role as owner on one hand and the State's role as regulatory authority on the other is important. The State will follow "Good Governance" principles and guidelines in the exercise of its ownership.

- Private owners will generally be in a better position to meet the requirement for good ownership than the State will be. The State should only own business activities where such ownership can act as an instrument to achieve particular and stated targets, or where such ownership is a sensible investment of the State's savings, taking into consideration return and risk.

- Action should be taken to strengthen private ownership and the State's extensive ownership in Norwegian business should be reduced.

In the following developments in policy and practice are discussed under the four main headings: Separation of commercial and regulatory or public functions; Improved Governance; Increased Competition; and Reduced State Ownership/Privatization.

Separation of commercial and regulatory or public functions

A standard feature of the reform in Norway, as elsewhere, has been the separation of commercial and regulatory functions that were previously combined within state agencies. This is particularly important in cases where actual competition exists, as otherwise a commercial enterprise would be able to selectively use regulatory powers to disadvantage its competitors. The EEA Agreement has spurred such developments, particularly in the transport and communications sector, where the Agreement specifically requires separate regulatory oversight entities in the areas of telecommunication, postal service and railways.

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There remain a few administrative enterprises, for example the Norwegian Mapping Authority and the Public Roads Administration where service provisions have been organized along with regulatory tasks in a multifunctional entity. The Government has recognized that such combinations of task may cause inefficient use of resources and distort competition. The Government has recently (1.1.2003) separated the production activities from the Public Roads Administration. The production activities have been converted into a state owned limited liability company, Mesta AS. The company will compete with other road construction companies.

Since the fall of 2001 there has also been a move to further separate regulatory considerations from ownership considerations pertaining to state owned companies. The Government's political platform stated:

> "The State ownership interests in the Norwegian business sector are extensive, and organized in a number of different ways and with different objectives. In many cases, conflicts arise between the State's role as an owner and as a regulatory authority. At present both ownership of and regulatory authority over public companies may fall within the same ministry. In order to avoid role conflicts, all State ownership should be brought within a single ministry."[25]

The Ministry of Trade and Industry (MTI) has been designated the "ownership" ministry of choice, and a number of companies have been transferred to the MTI since this Government came into power, notably DnB, SAS AB, SIVA SF, Statkraft SF, SND Invest AS, Entra Eiendom AS, Grødegaard AS, and most recently Banetele AS. Telenor ASA was transferred to MTI already on 8 September 2000, allegedly in response to pressure from the EFTA Surveillance Authority.

A number of the companies that are considered important for sectoral policies, however, are still owned by their respective sectoral ministry. For example, Statnett SF, and Statoil ASA, the state owned oil company remain under the Ministry of Petroleum and Energy; NRK AS under Church and Culture, and the hybrid companies have mainly remained under the responsibility of their respective sectoral ministries. The Government has indicated that it will continue its efforts to reduce the role-conflict inherent to its position as regulator and owner.

The transfer of ownership of BaneTeles AS to Ministry of Trade and Industry effective 1 January 2003 is an example of these ongoing efforts. BaneTele was originally established in 2001 under the state's railroad agency (Jernbaneverket) which sorts under the Minister of Transport and Communications with the aim of establishing and running the commercial side of the telecommunications network for the railroads. The transfer of ownership was founded on a need to separate the state's ownership role and regulatory role. BaneTele developed into a different and more commercial company than what was foreseen. The company moved aggressively into the broad-band (GSM-R) market beyond the needs of the railways after purchasing a bankrupt Enitel. The Ministry of Trade and Industry announced after taking over ownership that it intends to bring private owners into the company and it has already recruited external consultants for that purpose. The establishment and maintenance of GSM-R will now be opened for tender.[26]

The Government has indicated that an important rationale for separating regulatory and public service roles on the one hand and ownership roles on the other is to increase the legitimacy of the State, and enhance confidence in the neutrality of Government in its regulatory role. It has also drawn attention to the importance of the EEA Agreement as a mechanism to ensure such legitimacy.[27] Through use of the EFTA Surveillance Authority (ESA), competitors can initiate a substantive investigation if there are allegations of favoritism.[28] However, as long as State ownership is extensive, the Government questions whether a total separation of roles is possible. Regardless of organization, the State's role as regulator and owner will come together either in the Cabinet or Parliament. Collecting ownership responsibility in a single place also has the advantage that it would be easier to deal with ownership issues in a more consistent way than is possible under the present arrangement.

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Transparency in the state ownership role is essential to ensure legitimacy. A lack of transparency and predictability will not only affect the company concerned, but may also undermine confidence in all state owned enterprises, including those listed on the stock exchange. Good regulatory practices - good governance - may alleviate some of these risks and will be discussed below.

Parliament made a number of decisions[29] (a total of 8) in connection with the White Paper on *Reduced and Improved State Ownership*, which require the Government to return to Parliament with proposals to increase the availability of capital for industrial development both regionally and country-wide.[30] The decisions also included a specific mandate to reduce state ownership shares in Telenor ASA to 51 per cent and a mandate to allow Telenor ASA to use its shares in exchange in connection with purchases or mergers, provided the state ownership share is maintained at a minimum of 34 per cent.

Parliament also specifically requested that Government return with a various models for a more professional administration of state ownership, and asked Government to establish a committee to address issues of improving the organization and management of State ownership. Thus, while recognizing the need for good governance there is at the same time calls for a more "active ownership" policy, i.e. that the state should involve itself in the building of alternative industrial bases for the future.[31]

In response to the decisions, the Government has recently appointed such a preparatory committee (Statseierskapsutvalget), which will also address the transfer of administrative responsibility for individual companies out of the ministry to specialized administrative companies.[32] The Committee's task is three-fold:

- Propose organizational, judicial and business oriented solutions to alternative administrative models.
- Assess how to ensure democratic control both for the Government and Parliament and The Office of the Auditor General for various organizational models.
- Assess the need for changes in specific mandates by Parliament for approval of mergers and/or the sale of state shares.

The Committee is to present its report by the 1st of March 2004. This is not a new debate, administrative mechanisms for the organization of state ownership have been considered by parliament on a number of occasions, 1964, the mid 1970s, the late 1980s and the late 1990s.[33] A number of committees have also in the past looked at the separating out of ownership responsibility to specialized administrative companies or holding companies. While potentially increasing the distance between the State as and owner and the State as a regulator, and potentially improving state oversight of companies, such a transfer is no "easy way out". Problems related to such transfers that have been pointed to in the past include the risk of amassing too much "wealth" if concentrated in one ownership company; the difficulty involved in outsourcing ownership of companies with multiple purposes and hence the need to clearly define ownership goals; and difficulties related to government oversight and increased bureaucracy.

Another important element of the separation of the state's role as owner and regulator relates to the independence of supervisory bodies from the central government administration. The Norwegian Government recently (24 January, 2003) put forward a White Paper (St. meld. Nr. 17 (2002-2003) on these supervisory bodies. The Government's goal is to increase their autonomy and to increase the separation of roles in Government. The physical relocation of agencies and establishing separate appeals bodies outside the ministries are among the proposals. The issues relating to the supervisory authorities will be dealt with extensively in *Chapter 6: Regulatory Institutions in Norway*.

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Improved Corporate Governance

In the narrowest sense "corporate governance" is about control of the managers by the shareholders, so as to set the objectives of a company, the means to attain them and performance monitoring. Some broader concepts of corporate governance incorporate the interest of other stakeholders – financiers, suppliers, employees and customers. Different countries place varying emphasis on the interests of different groups. As such, corporate governance systems are designed to improve on market mechanisms to provide an institutional framework to formulate and monitor contracts that provide the management agents with incentives that are aligned to shareholder and stakeholder interests and which punish unsatisfactory behavior. Box 2 provides a brief summary of the main elements of private sector corporate governance systems.

Box 2. **General Principles of Corporate Governance**

The OECD Principles on Corporate Governance were approved by Ministers in 1999 as a common basis that Member Countries consider essential for the development of good governance practice. While they were primarily developed for publicly traded companies they are also to the extent deemed applicable a useful tool for non-traded companies and state owned enterprises. The Principles include guidelines under five headings:

- The Rights of Shareholders: The corporate governance framework should protect shareholder rights to transfer shares, obtain information, vote, elect the board and share in profits.
- The Equitable Treatment of Shareholder: The corporate governance framework should ensure the equitable treatment of all shareholders and the right of redress for violation of shareholder rights.
- The Role of Stakeholders Corporate Governance: The corporate governance framework should recognise the rights of stakeholders as established by law and encourage active co-operation between corporations and stakeholders in creating wealth, jobs and the sustainability of financially sound enterprises.
- Disclosure and Transparency: The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership, and governance of the company.
- Responsibilities of the Board: The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of the management by the board and the board's accountability to the company and the shareholders.

Several factors make the governance task more complicated in the state sector. Firstly, for fully state owned firms[34] there is no market for the ownership of the firm, so the market based mechanisms that allow the monitoring of performance and which partially align managerial incentives with performance do not operate. Secondly, even where there is a market value in the case of partly privatized entities, governments are constrained in their exit options as owner. Thirdly, lenders to a firm and possibly private shareholders have smaller incentives to monitor performance if it is perceived as government guaranteed. Fourthly, public sector managers are generally less likely to be dismissed for poor performance and their remuneration is less often directly or indirectly related to performance. As a result, public sector managers may have less financial incentive to pursue performance and may have more discretion vis a vis performance than their private sector counterparts. A priori, one might expect the performance of government owned firms to be lower than comparable private firms and this appears to be borne out by empirical evidence[35]. So, in the absence of the market surveillance mechanisms, administrative governance structures become effectively the sole means to address the principal-agent problem in publicly owned companies and enterprises.

However, the larger task for corporate governance in the public sector is not easily achieved even if it is a 100% owned firm. This is because the owner (state) also is likely to have a richer set of objectives than simply profit maximization. It is conceptually possible to deal with other objectives through arms

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length regulation but governments may choose to use their ownership leverage to achieve these aims. For example, in some industries a government may have objectives relating to universal service delivery and quality standards, employment or regional issues. Alternatively, ownership could be used instead of regulated private ownership to control monopoly problems. These objectives may also change over time, may not be clearly defined and may partly conflict – such as efficiency and USO (universal service obligation) delivery. Consequently, it may be difficult to measure the extent to which objectives are achieved. It is harder to write a performance related contracts with managers in these circumstances and the informational advantage enjoyed by managers will be higher. This adds to the complexity of the governance problem.

Moreover, even where a government 100% owns a firm, the governance and monitoring mechanisms may not be as direct as for the private sector. This is because there is range of participants within the structure of the government (voters, parliament, executive, civil servants) which adds to the chain of principles and agents in the governance structure. The consequences of this will depend upon the constitutional makeup and political norms that apply in particular countries and influence the relationship between these different levels in the government and the way the government functions. Therefore, it is not feasible to say that there is a best single governance structure that will apply in all countries and all situations.

Although governance arrangements between governments and state owned entities are necessarily varied and complex, there are several general principles that can be adopted that are likely to assist the attainment of the government's objectives, whatever they might be. Broadly, these are

- better definition of the objectives,
- better measurement of performance
- better alignment of managerial incentives to efficient achievement of these objectives.

Moreover, as governments have allowed competition in formerly government controlled sectors, they have been more explicit about their regulatory objectives. As a result, governance arrangements of firms which remain government-owned have been focussed more on efficiency based performance criteria. Consequently, it is possible to pose a number of "solutions" to the governance problems in the state commercial sector as follows:

- If it is possible to define the objectives of the government clearly and these do not vary over time then governance forms like that of a company will be feasible and are likely to reap at least some efficiency benefits from more commercially orientated management. Essential to achieving this is adherence to the state objectives and to buffer commercial decisions from day-to-day political interference.
- Where governments are competing with private companies, efficiency and equity demand that there be competitive neutrality between them and, so far as governance in concerned, this requires a separation of ownership and governance functions within the government.
- Formulate regulatory objectives through transparent and explicit regulation, including where necessary an independent regulator to enforce it.
- Better emulating private sector incentives can be done through corporatizing into a private law company and creating a transparent relationship between the state, Board of Directors and the company. This should include clear rules for the appointment of independent directors, clear

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corporate goals, a defined governance role for the Board and regular disclosure of relevant information. Where the company remains state owned some private surveillance mechanisms can operate if its debt is held privately. Nevertheless, to ensure appropriate incentives, the state should not be seen as guarantor for these companies.

- Performance contracts between SOEs and the state can be especially useful when there is relatively little competition which would otherwise guide the evolution of services provided by the enterprise. Over time, these performance contracts have tended to rely less on production targets, and give additional commercial flexibility and more clarity in the financial relationships.

- Privatize commercial companies where there is not an overriding policy reason to retain a commercial function in state ownership.[36] This is all the more appropriate for companies that are operating in a competitive environment.

Norway recognizes the importance of good corporate governance, and is continuing efforts to develop a comprehensive State ownership policy generally along the lines of the "solutions" indicated above. Governance policy issues have been debated in Parliament on a regular basis in connection with the reports every two years on the status of state ownership. There is broad agreement that the State as a general rule should execute its control of companies at the general level, and not through direct intervention in the daily running of the enterprise. The companies should be allowed to operate flexibly within set and predictable parameters, particularly concerning dividend policy. Most State owned companies operate with the same business goals as private companies, where maximizing earnings is a main criterion. The State as an owner should as a rule apply the same principle of return as do private investors, i.e. that the required rate of return should be adapted to the risk incurred by the owner as a result of the activity in question. The significant transfer of ownership to the Ministry of Trade and Industry as discussed above, has contributed to implementation of these goals.

Thus, a number of the general observations above do not hold for Norwegian state owned companies: managers of state owned companies are not considered "public sector managers" and some have had to step down because of poor performance, notably the manager of NSB, the railroads; and the first and second managers of Statoil. Managers of state owned firms in Norway have also been given remuneration basically on par with the private sector. It is the Board of directors that appoint managers, and the Boards also signal dismissal.

The results of performance studies of Norwegian state owned businesses are at best indicative and are not consistent. A study performed for the Ministry of Trade and Industry of eight partially owned companies, where five of them were listed on the Oslo Stock exchange, showed their cash flow return on investment was basically in line with that of other private companies, both Norwegian and foreign. There were, however, large variations between the companies. [37]

In connection with the White Paper *On A Reduced and Improved State Ownership* the Government has identified 10 good corporate governance principles on which the State's ownership in individual companies should be based. The principles are to govern state ownership in statutory companies, incorporated companies and hybrid companies and are considered a supplement to the legal framework established in the Acts governing the various organization forms of ownership. In the case of certain hybrid companies there may be regulations that are not fully in conformity with the principles.

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Box 3. **Norway's 10 Good Governance Principles for SOE's**

- All shareholders shall be treated equally.
- There shall be transparency in the State's ownership of companies.
- Ownership decisions and resolutions shall be made at the general meeting.
- The State may set performance targets for each company, together with other owners. The Board will be responsible for meeting these targets.
- The capital structure of the company shall be consistent with the objective of the ownership and the company's situation.
- The composition of the board shall be characterized by competence, capacity and diversity and shall reflect the distinctive characteristics of each company.
- Compensations and incentive systems shall promote the creation of value in the companies and shall be generally regarded as reasonable.
- The board shall exercise an independent control of the company's management on behalf of the owners.
- The board shall adopt a plan for its own work and shall work actively with the development of its own competence. The board's activities shall be assessed.
- The company shall recognize its responsibility to all shareholders and stakeholders in the company.

Source: White Paper No. 22 (2001-2002) On Reduced and Improved State Ownership

As is evident these principles mirror the general principles of corporate governance that were identified in Box 3. The principles are meant to guide the conduct of State ownership, but have no formal status, and are only advisory vis a vis the boards and management in State owned companies.

While Parliament can exert direct influence on administrative enterprises, and can influence the operations of 100 per cent owned state enterprises inter alia through appropriations and the budget process, the Constitution provides for the Government to administer or manage state ownership/holdings. However, major changes in state ownership including the sale of state shares in state owned companies must be based on a special mandate from Parliament. Formally state owned companies may sell shares in their own subsidiaries, yet in practice Parliament requires that also such transactions be mandated in certain situations, particularly when it involves share sales in subsidiaries which are fully state owned, since they represent a change in overall state holdings.[38]

The Government continues to exercise proprietary authority in varying degrees vis a vis particularly the statutory and hybrid companies and the fully owned limited companies. The companies that are considered to have sectoral policy importance are generally owned by the sectoral ministry. Most often it is the same section in the ministry that formulates sectoral policy that manages the ownership. For example in the Ministry of Agriculture it is the Department of Fores and Natural Resources Policy that manages ownership of Statskog SF. It is the Oil and Gas Division in the Ministry of Petroleum and Energy that manages ownership of Statoil. This same division is responsible for licensing policies.[39]

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A recent example of proprietary intervention took place in the media sector. A decision to merge a number of regional offices to save costs by the board of the public broadcaster, NRK, was overturned by the Minister of Church and Culture in February 2002. The intervention was made with reference to § 10 in the Companies Act which stipulates that "all questions that may be assumed to be important, principled, political and of social importance shall be put to the general assembly". The cut-backs were deemed to be of political importance as they would affect NRK's activity as a public broadcaster. [40]

A study by Statskonsult in 1998[41] revealed that the ministries/ministers to a very limited extent used the general assembly or the statutory companies' annual meetings for political directives. This may be an indication that the ministers govern according to business principles and not political policy, but not necessarily. The possibility of political intervention in many instances may be a sufficient signal to the company of what is expected policy.

The boards in Norwegian companies are independent, Members of Parliament are prohibited from appointment, as are civil servants in the Ministries or central government. The CE/managing director of a state owned company is also prohibited from being appointed to the board. The boards of directors are appointed by the shareholders, either directly, at the annual general meeting or indirectly by the Corporate Assembly. Employees are entitled to nominate up to one third of the board. In incorporated companies safeguards against political interference in the running of the company are secured through the Companies Act. Companies listed on the Stock Exchange are also to some extent protected against political interference by the Stock Exchange regulations. This was evident on two occasions reported in the media in 2002 when the public pronouncements by the Minister of Petroleum and Energy concerning Statoil resulted in a letter from the Director of the Oslo Stock Exchange (OSE) to the minister requesting clarification as to whether his remarks were an indication of a disparate level of information among the different stockholders, and underlining that no special preferences shall be afforded the Ministry regarding information. The OSE director also commented publicly on comments from the Minister concerning a tentative Statoil proposal to cut costs. The comments led him to question whether the major shareholder had other goals for the company than maximizing earnings.[42]

Most of the state owned companies with book values of equity exceeding NOK 1 billion are listed on the Oslo Stock Exchange, with the exceptions being, Statkraft SF (power generation), Statnett SF (power grid), NRK AS (public broadcasting), NSB AS (railways), Posten Norge AS (postal service), and Norsk Tipping AS (lottery).

In terms of dividend policy, the EEA Agreement has also led to the State operating according to the same principles as private investors. The Agreements article 61 on state support requires that the State operate in the same fashion as a private investor when transferring capital to or investing in public companies.

In cases where ownership is used to attain non commercial goals, these are to be clearly stated and be possible to monitor and assess. Reporting obligations are attached to such obligations. Moreover, non-commercial obligations should be covered by specific economic transfers tied to the provision of the service. [43] This model has been chosen for regional flights where the Public Service Obligation is covered by state subsidies. With the advent of the Norwegian Air Traffic and Airport Management as a limited liability corporation, Avinor, the Government has indicated that it intends to introduce a system of purchasing services from Avinor in 2004, rather than budget transfers. (See section 1.4.)

The setting of dividend policy is important in providing the companies with a predictable economic framework. As mentioned the Government goal is that the same principles that steer dividend policy in private companies should be used for the state owned companies. However, in practice Parliament has on a number of occasions raised the dividend that would be taken out – contrary to the

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recommendations of the company boards or the government. In the course of 2002 the dividend was increased for two enterprises, Statkraft (power generation) and Statnett (electricity transmission) in the fiscal budget proposal from the Government. Instead of "approximately 50 per cent" the Government based its budget on a dividend of 90 per cent for each of the two, resulting in public complaints by the companies concerned that the decision would adversely affect their ability to raise investment capital.[44]

Emergence of Competition and Competitive Neutrality Issues

Competition has emerged in a number of sectors that have been reformed or liberalized, particularly the energy market, broadcasting, and telecommunications. However, in some cases, the emergence of competition has been less strong than expected or initially hoped. In sectors such as health and education there is relatively little competition and price signals have not been used to improve efficiency of services. Chapter II of the OECD Economic Survey of Norway, *Enhancing the effectiveness of public spending*, (OECD: 2002) focuses on the need for increased competition between public and private providers in order to improve efficiency and increase user choice.

Liberalization and improved competition in a number of markets in Norway have come as a consequence of the EEA Agreement and the concomitant regulatory framework required by that Agreement including competition rules supervised by the EFTA Surveillance Authority. (See *Chapter 4: Enhancing Market Openness through Regulatory Reform*) The EEA Agreement, however, does not prohibit state owned enterprises. Such companies are subject to the general competition rules and government involvement in such companies falls under regulations governing state aid. The concept of state aid is a broad one, embracing not only subsidies in the strict sense of the word, but also public support measures in various forms. This can be *inter alia*, tax exemptions, loans on preferential terms, state guarantees and investments in share capital by public authorities on terms not acceptable to a private investors.

When state owned enterprises are involved in commercial activities in competition with private companies it is essential that the State as owner observes the principle of competitive neutrality. [45] This is recognized by the Norwegian Government which has stated:

> "….several of the large enterprises which are currently subject to State ownership for reasons of sector policy, are in a process which increasingly brings them into competition with private enterprises. This applies for example to the Post Office (Posten BA), the Norwegian State Railways (NSB BA), and the Broadcasting Corporation (NRK). The Government's approach to such cases will be to ensure that the State's management of companies does not distort competition between publicly and privately owned companies competing in the same industry. This requires continues reassessment of such companies, as industries and markets develop over time."[46]

Competitive neutrality problems can also arise from the way state owned entities are run, particularly the possibility of setting low profit targets. Some other countries have more developed and explicit competitive neutrality frameworks which are designed specifically to deal with neutrality problems that arise within the threshold of potential application of the competition law. A brief description of some of these is set out in Box 4. It is notable that an important motivation for these frameworks is one of equity rather than efficiency and that they deal with cases where lax steering imparts an advantage to a pubic enterprise because it does not earn a reasonable rate of return on the capital employed. It is also notable that these frameworks provide the possibility for private parties to seek to resolve neutrality problems that are adversely affecting them.

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Norway does not have a competitive neutrality framework (see Box 4: Competitive Neutrality Mechanisms: A Survey of OECD Practices). Instead there is reliance on the Norwegian Competition Authority (NCA) and the EEA Agreement as important means to secure the legitimacy of the state as a neutral regulator for commercial entities. While the EEA Agreement provides competitors with an avenue (through the EFTA Surveillance Authority, ESA, which may also self-initiate investigations) of complaint and ensures diligent reviews of allegations of distortion of competition, it is a mechanism that comes into play "after the fact".[47] There is no framework proactively fostering competitive neutrality in the management of state owned enterprises apart from general goals to avoid distortion of competition.

Public enterprises and actions by government entities might be subject to the Norwegian Competition Act, depending on the nature of the activity and the status of the entity. (See *Chapter 3: The Role of Competition Policy in Regulatory Reform* for an extensive discussion.)

In the non-commercial public service sector there is no mechanism to ensure that private providers are treated equitably with public providers. For example there is no clear provision for ensuring that private hospitals that enter into an agreement with a regional health body to obtain public funding receive the same amount of public money for the same treatment as do public hospitals or that they get equal treatment with regard to investment costs. The same is the case in the education sector where funds per student in private schools cover only 85 per cent of working expenses per pupil received by public schools and do not cover investment costs.[48]

Differences in treatment based on differences in ownership have been criticized as deterrents to competitive entry. The Norwegian Competition Authority has identified two issues of competitive advantage for state owned companies. Both concern electricity generation. The first is of a financial character: Through the provision of 16 billion NOK in equity loans, and guarantees, Parliament enabled Statkraft SF, a wholly state owned statutory company, to follow an aggressive growth strategy through acquisitions in Norway. The company had a market share of 35-40 per cent and was aiming at a market share of more than 50 per cent.[49]

The second issue relates to ownership of hydropower resources where current Norwegian legislation differentiates between public and privately owned generators. Under the current legislation a private company is obliged by law to return any rights and assets for electricity generation to the state after 60 years. Publicly owned companies are not bound by such constraints. The ESA has determined that the legislation is discriminatory to private entrants and in conflict with EEA Agreements provision on free right of establishment and free movement of capital. The Government prepared draft legislation that would harmonize the licensing conditions applied to public and private parties in an owner neutral form (subjecting all concessions to the same fixed term), but later decided to seek advice from a committee in these matters. The committee was appointed on 4 April 2003, and is to submit its report in the autumn of 2004.

Financing regimes aimed at public functions such as the universal service obligations, for example in the postal sector[50], may result in cross-subsidization[51] of other activities. There is no general prohibition against cross-subsidization in Norway, but complaints can be launched with the EFTA Surveillance Authority if such action distorts competition within the EEA Area. Such arrangements may, however, undermine competition and may in some cases be in contravention of regulations prohibiting state aid. The Norwegian Competition Authority has pointed to two possible solutions to such problems: either prohibiting an entity to offer products in question where they compete with private enterprises, or separating out the commercial activity in an independent enterprise with separate accounts. In the White Paper the Government advocates the use of public tendering for services that the Government pays for when produced in competition with private actors to avoid suspicions of cross-subsidization.

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Norwegian competition law applies without exception to publicly owned or managed enterprises where these are carrying out a business undertaking. The concept of business undertaking extends to commercial activities carried out directly within state agencies as well as to separate entities such as a statutory or hybrid enterprise or incorporated company. The Competition Act, nevertheless, does not give the NCA the authority to intervene against public entities by prohibiting their commercial activities or by deciding that they should outsource these activities or keep different accounts for their commercial and non-commercial activity. The NCA may, though, call attention to the restraining effects on competition of public measures.[52]

The creation of state owned enterprises, which involves the "transfer" of assets from the State to the enterprise and the creation of a liability structure (debt and residual "equity") establishes the balance sheet of the enterprise[53]. This has a significant influence on the basic cost structure of the enterprise, which flows through to prices, and thus determines a starting point for the potential for competition to emerge through private entry. If assets are taken onto the books at a substantial undervalue, and if debt and equity positions are not broadly in accord with private sector norms for the sector then the state owned enterprise may have "built in" competitive advantages over its potential private sector rivals. This has been pointed to as a potential concern with establishment of the public Roads Construction as a state owned limited liability company.

The Government has indicated that their aim has been to assign asset values at the going market price and leave enterprises with a balance sheet that corresponds with private entities of the same size and in the same sector, i.e. of a comparable private sector competitor. It is difficult to independently evaluate the implementation of this aim ex post, since there exists a different system of accounting in public vs private enterprises and the fact that administrative enterprises have generally not had comparable private sector competitors from the start.

When selling state shares the Government has also stated that in principle the sale should take place in a manner that allows the Competition Act to come into play. The Norwegian Competition Act[54] applies to both private and public businesses. However, in instances where a parliamentary decisions determines the specific sale or partial privatization of a government owned enterprise the Competition Authority (NCA) may not intervene. With increased use of mandates from Parliament to negotiate sales, the Government intends to allow the NCA greater possibilities to review competition issues.

Taxation is another significant aspect of competitive neutrality. In Norway there is a general obligation to pay Value Added Tax (VAT) on both goods and services. But neither public entities nor private entities have to pay VAT on their own production for their own use. Municipalities have to some extent produced some of the products and services they consume in order to save money. Thus the VAT system can result in more efficient providers becoming relatively less competitive. The VAT treatment of municipal services has been studied by a preparatory committee (Rattsø-utvalget), which handed over its report to the Ministry of Finance on 18 December 2002. The committee proposes VAT compensation for all municipal purchases (which implies an extension of the present system with VAT compensation of only certain specified services.) The Government will follow up on the committee recommendations with proposals to the Parliament in the 2004 budget.

Most competition laws can apply to adverse competitive neutrality problems if it gives rise to a situation that comes under the applicable abuse of dominance (or equivalent) provisions. Generally, these set relatively high thresholds either in terms of the requisite market power required to attract jurisdiction or the severity of the conduct. Norway's Competition Act does not prohibit abuse of dominance. Rather anti-competitive conduct that could maintain or strengthen a dominant position is subject to control through intervention if it impairs economic efficiency. The EEA Agreement does, however, prohibit abuse of dominance.

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Box 4. Competitive Neutrality Mechanisms: A Survey of OECD Practices

Competitive neutrality policies are intended to remove resource allocation distortions arising out of public ownership of business activities and to improve competitive processes. A key feature is that prices charged government businesses need to fully reflect resource costs, otherwise there will be distortions of decisions on production, consumption and investment. A number of countries have implemented explicit competitive neutrality frameworks that operate at a lower threshold of distortion than would general competition law prohibitions on abuse of dominance. In part this reflects a policy view that it is simply unfair for a government to use the coercive powers of the state to selectively advantage its own business operations over those of private citizens. Even if, by hypothesis, the allocation of resources and level of prices and output are unaffected.

Netherlands

A set of "*Instructions for the performance of commercial activities by central government organisations*" came into effect in 1998. But these were found to be inadequate to address the full range of competition issues since private companies complained of unfair competition from the commercial activities of government organisations. Competitive advantages of government entities can include lower risk, public subsidies or tax advantages or access and privileged relationships with policy makers. Following experience with these *Instructions* and further policy development, the Government decided in 2001 to legislate a framework of formal rules for government commercial activities involving the supply of goods or services to third parties in actual competition with private providers so as to create more equal competitive conditions. Consequently, the Market and Government Bill was [insert status at end point]. The Bill will impose obligations on government organisations (State, provincial and municipal) and organisations with exclusive and special market rights[55] (OEMs), as follows:

- Rules for ***market access*** by government organisations – commercial activities undertaken by government entities must have a specific statutory basis and result from a decision that has been underpinned by a thorough and transparent, prior assessment of the desirability of the commercial activities by a government organisation. This access rule also applies to the participation of the government in an incorporated company involved in commercial activities where the company is controlled by the government[56]. The benefits of serving the pubic interest (not merely to generate income) through the activity must outweigh any negative consequences for private providers. Interested private businesses can provide input to this assessment, before the government organisation decides to engage in commercial activities, and have recourse to administrative law remedies if they believe the decision was not properly considered. The decision must be reassessed every 5 years[57]. A Government and Market Commission will be an expert, non-binding advisory body for government organisations undertaking this analysis and making the decision. This Commission can also advise any private entity and its advice can enter into any administrative law complaint proceedings and act as an expert witness.

- Rules for ***conduct*** by government organisations and OEMs that aim to prevent unfair competition. Policy functions must be segregated from production functions and policy areas must not grant preferences to production areas. Specific conduct rules include a requirement that all costs attributable to the commercial activity are included in the price for the good or service (intended to prevent cross subsidies) and rules concerning accounting for such costs. OEMs may not use government funds provided to them to perform their function for any other purposes (also intended to prevent cross subsidies to non-exclusive activities). Confidential government data cannot be used in government commercial activities and non-commercial data cannot be used unless it generally available to all commercial entities. Administrative law remedies are available in the case of misapplication of these rules as they related to internal administrative functions of the government entity while the Netherlands Competition Authority (NMa) applies the rules of conduct. The NMa may issue a decision of violation in respect of government organisations and may also penalise OEMs.

An administrative law finding against a government entity could form the basis of an action for a civil penalty for damages by a private entity that had been adversely affected by competition from the government.

Preexisting commercial activities and liberalisation programs are treated under transitional provisions that provide for continuation of existing contractual activities. Existing specific competitive neutrality frameworks – such as in respect of post and energy activities - will continue and after liberalisation be reviewed for compatibility with the Government and Markets Bill.

Australia

Part of the National Competition Policy Reform implemented in the mid-1990s involved the formulation of competitive neutrality principles and the establishment of special complaints mechanisms to ensure that the principles were applied effectively and the private entities could seek a solution if they had been damaged by unfair competition from a public entity with an inappropriate competitive advantage. The competitive neutrality principles required that significant government business activities should not enjoy net competitive advantages over their private sector competitors simply by virtue of public sector ownership. Consequently, governments committed not to use their legislative or fiscal powers to advantage their own businesses over the private sector. The motivations behind this policy were efficiency and equity concerns. Thus:

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"In the public sector, increased attention has been given to the core role of government and how government services can be best delivered in an environment of resource constraint. This imperative has driven reforms ranging from privatisation, deregulation of public monopolies, competitive tendering and contracting to various management reforms, including devolution and accountability frameworks. Competitive neutrality requires that where governments choose to provide services through market based mechanisms that allow actual or potential competition from a private sector provider, that competition should be fair. In this sense, competitive neutrality will operate to ensure the integrity of other reforms to improve the operation of government businesses."

Competitive neutrality requirements are applied essentially to commercial activities, i.e. significant government business activities that charge for their services in an actual or potentially competitive environment where the business managers have some discretion in price setting. The requirements do no apply to non-profit, non-business activities.

The principles were elaborated in the following areas:

- Corporatisation: The legal and governance structures of businesses were reviewed.
- Taxation: All tax exemptions were removed or tax equivalent regimes were developed for entities not legally separate from government.
- Finance: Advantages from implicit guarantees could be addressed by a neutrality charge.
- Rate of return requirements: Businesses were required to fully recover costs and earn appropriate rates of return on capital.
- Regulatory neutrality: Special exemptions from regulatory arrangements (eg safety or reporting requirements) were removed.

The complaints mechanism is an administrative procedure undertaken by specially established complaints bodies in each jurisdiction that can assess whether the competitive neutrality requirements are being complied with. If the complaint is found to be verified, including by means of a public enquiry, and the matter is not then remedied the complaints body makes a public report with recommendations to the Treasurer who must determine the matter. Investigations have been implemented at the national level in a range of areas including airport services, meteorological services, post, television, security services, railways and job placement services.

Other Countries

In other countries competitive neutrality issues can be partly addressed to the extent that competition law is applicable to state enterprises and that the neutrality problem is caused through conduct. The applicability of competition law in these circumstances will be limited to cases where relevant thresholds (dominance, substantial market power) are met and, broadly speaking where the conduct can be shown to be predatory. The limits on state aids in the EU are also potentially relevant. Less serious conduct and structural competitive non-neutralities (e.g. tax and regulatory exemptions) are often subject to advocacy efforts by competition authorities.

Reducing State Ownership (Privatization)

Norway does not as such have a broad privatization goal, but has privatized (partially or fully) approximately 19 companies, mainly manufacturing industries, in the period 1999-2002, and Parliament has endorsed the (further) selling of shares in a handful of other companies. Parliament has not, however, endorsed the more general goal to reduce the State's extensive ownership in Norwegian business and to consolidate ownership to sectors "where ownership can act as an instrument to achieve particular and stated targets, or where such ownership is a sensible investment of the State's savings, taking into consideration return and risk."[58] Instead Parliament has directed the Government to focus its efforts on how to improve management of state owned companies and how to stimulate profitable and sustainable industrial growth and development in Norway. Specifically Parliament has asked for an assessment of the potential drawbacks and benefits of transferring ownership to holding companies or administrative companies. This last point has re-raised an old debate about democratic control and constitutional responsibility. As mentioned the Minister of Trade and Industry established a special committee to look at these issues and report on 1 March 2004.

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Privatization in many countries has often been motivated by a view that private firms would be more efficient than continuing public ownership[59]; and that the government could reap some of this efficiency gap in the form of a capitalized value in privatization proceeds. Given the strong financial position of the Norwegian State fiscal improvement considerations have not been drawn on as a motivation for privatization. Privatization in Norway has, as a general rule, been carried out after individual assessment of companies. The main arguments put forward for selling of shares have been related to improved efficiency, greater flexibility and speed in decision-making, improved access to private capital markets, greater opportunities for alliance building, and improved benchmarking of company value. These are often arguments for privatization that have been presented by the individual companies themselves. Notably the initiatives to privatize Telenor and Statoil originated with the companies' managing directors.

The Norwegian rationale for maintaining state ownership in companies varies, but can be grouped under four main categories:

- ***Sector policy concerns.*** Ownership is in some instances seen as an important means of attaining specific sectoral goals, for example, the monopoly on wines and spirits is used to restrict and control availability of alcohol. Regulation of the provision of public services through ownership has also been an important argument for state ownership of the infrastructure based companies such as Statnett.

- ***Norwegian ownership.*** Maintaining Norwegian ownership in strategic sectors such as in the petroleum sector, the hydropower sector and the financial sector are deemed important for the whole of business activity in the country. Maintaining the Norwegian presence in the polar region is an example.

- ***Natural resources.*** There is broad consensus on the need to maintain political control with the utilization and extraction of natural resources. Political control is however increasingly upheld through regulation and taxation, and the need for direct ownership has been reduced.

- ***Head office location.*** State ownership ensures that companies establish their head office in Norway, ensuring employment of key-personnel and taxable earnings in the country.

The weight of such arguments has changed over time, for example in relation to the status of Telenor and Statoil. This is a reflection of the fact that key determinants will change in an economy over time and this may change the scope of activities that are better placed in the private sector. For example, development of capital markets, or growing sophistication of tax and regulatory systems, or improved technology that enhances the potential to measure and monitor outcomes are all likely to promote the scope for privatization.

There is now a large empirical and analytic literature on the actual effects of privatization. These effects are difficult to isolate empirically from the effects of broader regulatory reform because, in most instances, privatization has been accompanied by significant regulatory or structural change. And, there is a complex sequencing of cause and effects where the implementation of a policy is staged over a period of time and is also anticipated by participants. A survey of 61 empirical studies by Megginson and Netter (2001) concluded that privately owned firms are more efficient and profitable than otherwise comparable state-owned firms; that privatization works in that divested firms almost always become more efficient, more profitable, financially healthier and increase their capital investment spending; most studies show a fall in employment as a result of privatization, except where sales increase substantially; and privatization helps to develop and deepen capital markets and thus improve the general business environment. A substantial collection of work on these issues can be found in OECD (2000)[60] which includes the following points:

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- Labor productivity and, in some cases, total factor productivity increases with privatization.

- Consumers reap part of these gains in the form of lower real prices[61], and this effect is strongest where there is competition. Regulation of post privatization monopolies is less successful than competition – regulation is hard.

- Service quality and range improves, often beyond minimum regulated levels set by the state – the important exception to this outcome is where the reform fails due to partial, incomplete or inconsistent reform design.

- Privatization makes a significant positive contribution to public finances – the pre-privatization earnings yield from the entities is usually less than the yield the government pays on its debt. The private sector investors recognize the efficiency gains and consequently higher earnings that are possible from more commercial management and this efficiency gain is partly capitalized into the privatization price. The state also captures part of any efficiency gain in the form of taxes on increased corporate profits of the privatized firm

The issue of whether privatization or competition is more important for performance improvement is vexed and no attempt to resolve this issue is made here. It is reasonable to expect that the effect is cumulative, i.e. liberalization and privatization are more effective than either privatization of a firm with continuing market power or continued government ownership in a liberalized sector. The latter result is what would be expected given the additional challenges of governance of commercial activities with continued state ownership.

Norwegian authorities are continuing their assessment of individual state owned companies with a view to determining whether the political motivations for ownership are still valid and if so if they can be better handled through other mechanisms, such as regulations, financial incentives or inter alia through contractual arrangements. The Government has indicated that it intends to return to Parliament with specific proposals for privatization. The Government has, however, indicated that even after reductions state ownership is expected to remain extensive, thus the importance of continuing to improve corporate governance mechanisms.

Given the strong financial position of the State and the relatively weak private capital market in Norway it is to be expected that reductions in ownership, if approved by Parliament, will take time. The Government has recognized this and indicated:

> "….The Government is of the opinion that changes in the State's shareholdings must take place in a way which retains share values, and at the same time contributes to a positive development for the companies involved. This means, among other issues, that the timing, method and execution of an intended reduction in an ownership stake will have to be planned carefully…"[62]

There is no broad endorsement in Parliament for the reduction of state ownership. Yet, specific proposals for privatization have been met with approval. Parliament provided a mandate to reduce the ownership share in Telenor AS, and to sell SND Invest AS in December, and most recently Parliament approved a mandate to sell remaining shares in Raufoss ASA; and in NOAH Holding AS.

Summary and Policy Options for Consideration

The pressure for regulatory reform in Norway has been less marked due to the strong financial position of the State and the high levels of employment. Deregulation and liberalization of markets and concomitant restructuring of state owned commercial entities have all, nevertheless, taken place in order to

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improve efficiency and business flexibility, separate regulatory entities from service providers, increase user choice and responsiveness to the needs of the citizens.

Marketization has led to public service providing companies competing with private providers in a number of market sectors and issues of competitive neutrality, good governance and the separation of the state's role as regulator/public service provider and owner have become increasingly important to resolve in order to maintain the legitimacy of the state in exercising its various roles. **The Government clearly recognizes the challenges posed by these issues and has taken a number of steps to resolve potential conflicts.** A number of further policy options could be considered:

- The wide variety of state ownership forms and regulator frameworks does not contribute to transparency in how the state operates as owner/regulator. **Consideration could be given to streamlining the number of ownership forms by reducing the number of variations.**

- One approach could be to transform all state owned companies operating in competition with private operators into incorporated companies. The incorporated company format compels the State to clearly define its ownership goals for the entity.

- The most blatant competitive neutrality issues have arisen in connection with the statutory company format, given the special loans- and guarantees provided to these companies in the past. The law governing these companies has been amended to remove this distortion. **Consideration could be given to doing away with this organizational form.**

- **Consideration could also be given to developing an explicit competitive neutrality policy framework to address neutrality problems that arise from the way an enterprise is run, also entities operating in non-market driven sectors.** A lack of such a framework may lead to complacency with regard to the regulation of state-owned companies operating in markets without current competition, as there is no focus on anti-competitive effects from the market itself. With a competitive neutrality framework the potential for new entrants into markets will be enhanced.

- Separation of regulatory and ownership functions is essential for successful reform otherwise new entrants are likely to at least perceive non-neutral regulation as protecting the government owned incumbent. In Norway there has been a marked move to separate ownership and regulatory responsibilities by transferring ownership responsibility to the Ministry of Trade and Industry and by current efforts to increase the autonomy of supervisory agencies. Nevertheless ownership responsibility has been retained by the sectoral ministerial for major companies that are defined to have important sectoral policy purposes. It is particularly for these companies that it is important to separate the ownership and regulator role. **Considerations should be given to also transferring ownership responsibility of companies that are considered important in a sectoral policy context. This could also contribute to a greater uniformity in good governance practice.**

As in many other countries, there is an interesting paradox in the Norwegian approach to reform in this area. Commercialization has progressed basically without difficulties and major efforts have been undertaken to ensure good governance – this is a quite highly developed policy. However, the next and final step in the commercialization process, which is privatization, has not been conducted according to a solid and agreed conceptual framework. Privatization has been careful, often motivated by the companies themselves, staged and carried out on a case by case basis according to the pragmatic circumstances of the moment. Privatization has proceeded furthest in sectors which are purely commercial and do not have significant public policy elements.

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The Government is advocating a reduction in state ownership based on efficiency considerations, and has attempted to raise a debate on the boundaries of state ownership. Given the strong position of State finances Parliament has seen no need to establish an overall policy for reducing state ownership. Instead focus has been on how to improve state ownership. This focus is not necessarily concerning itself with improved ownership in terms of good governance, but with how to promote a more direct and active state ownership that is conducive to industrial development in strategic sectors. **A move in the direction of an interventionist industrial policy would seem to undermine the reforms taken the past two decades and exacerbate tensions related to good governance and competitive neutrality.**

- **It would be desirable to take forward privatization more broadly, as the extensive state ownership of business and industry, even with optimal good governance and competitive neutrality, nevertheless creates an inference of potential state intervention, and thus potentially thwarts new entrants.**

1.2. Civil aviation

1.2.1. Introduction

Across the OECD, traditional state-owned and regulated public utility industries have been transformed by reforms that have fundamentally changed the way these industries are regulated. In Norway the ***civil aviation*** sector has undergone extensive changes over the last decade, in terms of market access, ownership structures and organization of the regulatory bodies.

In addition to being the overall regulator of civil aviation, the Norwegian State also owns the majority of airports in the country, and is part owner of the country's major dominant airline. Furthermore, the State has taken on a number of public service obligations in order to ensure availability of air transport services across the country. At the same time there have been moves to improve efficiency through commercialization and competition with respect to regional airports and regional air services.

Domestic air routes in Norway are among the most traffic dense in Europe and the average Norwegian takes by far the largest number of flights per year of all Europeans. This is a reflection of the dispersed population patterns, geography and topography, but also of the cold climate and difficult surface travel. For example, the flight time between Stavanger and Oslo is 45 minutes, while travel by train or car takes more than 8 ½ hours. In 2000 48.6 per cent of all air passengers traveled on domestic routes, totaling approximately 10.5 million passengers. [63] The extreme degree of concentration in the domestic commercial airline sector has emerged as an issue of concern, and the government and the Competition Authority have introduced measures to improve the competitive climate.

Reform of the regulatory framework

The regulatory framework governing civil aviation is found in *The Aviation Act* of 11 June 1993 and with secondary regulations deriving from it, particularly Regulation No. 691 of 15 July 1994. The Civil Aviation Authority (CAA, Luftfartstilsynet) is organized as an independent regulatory body under the Ministry of Transport and Communications, and is responsible for ensuring safety in the aviation market, controlling the quality of material and issuing licenses to airports, airlines, pilots and crew.

During the 1990s the domestic aviation market changed from a market based on exclusive rights to a market with regulated competition. The European aviation market was regulated by bilateral aviation agreements up until 1992. The gradual deregulation of the internal community market and the EC

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regulations that were adopted to foster deregulation were introduced to the Norwegian aviation market already to some extent in 1993 and further in 1994 with the entry into force of the EEA Agreement. Until October 1998 when the Oslo Airport was opened, slot constraints had limited the number of competing services.

Slot allocation is governed by EU Council Regulation (EEC) No. 95/93. There is no slot capacity problem in the domestic airline market restricting new entrants, though at Sola Airport in Stavanger and Oslo Airport regulation of capacity is considered necessary. Oslo Airport is, in addition considered a coordinated airport. The system of allocating slots, however, favors incumbents through so-called grandfathering of slots.

Prior to the year 2000, regulatory functions, airport administration and air traffic management all rested in one administrative enterprise, Luftfartsverket. On January 1 2000, the regulatory function was separated out into a state agency, the Civil Aviation Administration (CAA). Luftfartsverket[64] continued to handle the functions of airport management and air traffic control services as an administrative enterprise until 1 January 2003, when it was transformed into a wholly state owned limited liability company, Avinor AS. The transformation is seen as a vehicle for further commercialization of the airport services and management, while maintaining state ownership.

State ownership of airports is administered Avinor AS, a wholly state owned limited liability company established 1 January 2003. The Ministry of Transport and Communications in turn owns Avinor AS. Avinor owns and operates 45 of the 53 Norwegian airports across the country, 14 in association with the armed services. 17 of these airports are so-called main airports, while 28 are regional airports. [65] Avinor is also responsible for air traffic control services in Norway. Avinor is largely self-financing, but it receives an annual transfer from the government to offset operating deficits from the regional airports. The government transfer for 2003 is 250 million NOK for the 27 airports. [66] Roughly three-quarters of Avinor'ss revenues comes from aeronautical charges which are fixed (maximum charges) annually by the Ministry of Transport and Communication. The other major sources of income are based on market and property, airline related user fees and other commercial income from airport related services and sale of services to non State owned airports. Following the transformation to a limited company, the government transfer is meant to compensate fully for operating deficits attributable to the regional airports, which were only partially covered prior to transformation.

Avinor operates as a network system where the economic results are believed to be more optimal given centralized management structures and economies of scale. Only 6 of the 45 airports are profitable.[67] Charges are geographically uniform based on weight and passengers. Since cost structure varies across the network the uniform price structure implies cross-subsidization between regions and airlines. Avinor has two fully owned subsidiaries which are also organized as incorporated companies: the Oslo Lufthavn AS (Oslo Airport Gardermoen), and Luftfartsverkets Parkeringsanlegg AS which finances and builds parking facilities at Norwegian airports.

Oslo Airport, as a separate company, was not as such part of the NATAM network. That is, its earnings were not used to cross-subsidize other airports in the NATAM network. With the advent of Avinor as a limited liability company, the relationship with Oslo Airport is changed. Oslo Airport can now be considered part of the Avinor corporation, and transfers from Oslo Airport to Avinor are for example not subject to taxation. The potential for increased economic coordination between Oslo Airport and the Avinor network was one of the motives for the transformation of NATAM to an incorporated company. On presenting the decision the Minister of Transport and Communication stated:

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"Transforming NATAM from an administrative enterprise to an incorporated company fully owned by the State, will provide the company with a clearer economic responsibility and greater flexibility. At the same time it will make it easier for NATAM to take up loans and to coordinated its activities with the subsidiary Oslo Lufthavn AS…."[68] (Author's translation.)

The governments of Norway, Sweden and Denmark together hold a 50 per cent ownership in the airline SAS (Scandinavian Airline System AB), with the Norwegian State holding 14.3 per cent, 2/14 share. In 2001 ownership was transferred from the Ministry of Transport and Communications to the Ministry of Trade and Industry in order to avoid potential conflicts of interest between the roles of owner and regulator. Due to the joint government ownership, Norway pursues a common aviation policy with Sweden and Denmark.

Regional airports

The Norwegian regional airport system consists of 27 airports owned by Avinor. In the remoter parts of the country air transport plays a vital role in enabling people to access education and medical facilities, and is an important means of freight and mail delivery. These are mainly served by operators under public service obligation (PSO). The regional airport network is relatively dense, especially along the western and northern coastline, 23 of Norway's airports are located north of the Arctic Circle. The regional airports were mainly built between 1968 and 1986 to serve community centers with poor surface transport accessibility. Most of them are STOL-ports (short take off and landing) constructed in "difficult" terrain. The runway lengths are approximately 800 meters, with only a few exceptions.

The regional airports were originally owned and operated by the local municipalities. From 1998, the State, represented by NATAM, now Avinor, took over ownership. The policy change was promulgated by safety concerns. With the change in ownership capital could be earmarked for lengthening of runway and provision of more sophisticated navigational aid at the peripheral airports. [69]

Privatization of airport ownership – such as has occurred in many OECD countries - has not been raised in Norway. Nevertheless, the transformation of NATAM to an incorporated company is an implicit recognition that private sector style management or commercialization could lead to greater operating efficiency and innovation. It should be noted than one of the private, independent airports operating at a profit in Norway is Torp (Sandefjord Lufthavn) – around a 1 ½ hours drive from Oslo – in the vicinity of Skien and Porsgrunn. Torp is jointly owned by two local municipalities, one county, and a group of private investors, and has remained outside the Avinor network, but under license from the Ministry of Transport and Communication. The airport purchases air traffic services from Avinor. The airport is now the second largest in terms of direct international flights to London, Glasgow, Amsterdam, Copenhagen, Frankfurt and Stockholm. More than 1 million passengers use Torp annually, around half of them on international flights, a large number of which are low-fare.

A number of the larger city-airports (Stavanger, Bergen, Kristiansand) that are operating with a profit, have expressed a desire to be separated out from the Avinor network and to take on a similar ownership structure to Torp. That has, however, not been considered acceptable by the Government and Parliament. In connection with the decision to transform NATAM, it was specifically indicated by the Minister of Transport and Communication that partial or full privatization of NATAM core activities would not be possible without prior approval from the Minister.[70] In the Parliamentary debate leading up to the decision, there was broad agreement that individual airports should not be separated out now. Nevertheless, greater flexibility should be introduced to allow the profitable airports to use part of their earnings to invest in improvements and expansions.[71]

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In connection with the 2002 PSO (see section on Regional airline services) tender process a broad scale cost benefit analysis study of ten regional airports, including operational conditions and possibilities for further expansion of the individual airports was carried out.[72] The location (terrain) of many of the airports limits large scale expansion. Given that STOL aircraft are no longer manufactured and the limitations on airport facility expansion there is uncertainty about the future of a number of the regional airports, particular in the event of new safety requirements from the aviation authorities.

The analysis which studied net benefit to society concluded that five of the regional airports were clearly unprofitable, and the remaining five were most likely unprofitable. The Government subsequently proposed discontinuing PSO services at three of the regional airports. Parliament opposed closure of all three airports, and instructed the Government that no further no closures would be considered without extensive consultations with all affected parties.

Regional Airline Services

Originally Widerøe (a SAS-owned subsidiary) was the monopoly licensee for regional air services and received a subsidy from the State to supply a service at a regulated quality and price. Given the STOL status of the regional airports Widerøe procured special aircraft – a Dehaviland Dash (turbo-prop with non-standard high power engine) to operate at these airports to the specified quality level that required 30 seat capacity flights.

According to EU regulations[73], which Norway under the EEA Agreement is obliged to implement, PSO routes are subject to competitive tendering for periods of three years. The PSO sets the service standards for each individual route area.[74] These standards were amended somewhat after the first tender to provide for increased competition. If competition proves to be too weak, subsequent negotiations with potential providers may be held. At the time of the introduction of auctioning of PSO services with Regulation no. 256 of 15 April 1994, Widerøe was in a monopoly position.

In the first public tender held in 1996 for the period 1997-2000, the Widerøe carrier won all concessions. In the tender from 2000-2003 Widerøe was able to renew most of their concessions, apart from some routes along the west coast which were awarded to Coast Air. The first auction significantly reduced the subsidies paid from the State under the previous single licensee system, the second resulted in substantially higher prices. There have allegations in the media that Widerøe engaged in selected bidding, with low prices on potentially competitive routes and higher prices on routes where they have a monopoly given the quality specifications. This is not perceived as a problem, provided it does not represent predatory foreclosure through cross subsidization.

A new invitation to tender was made in May 2002, and a total of seven air carriers have submitted tenders for the 15 route areas – covering 29 airports, 5 of them Norwegian, one Danish and one Swedish carrier. None offered to operate all routes. In 4 of the route areas the airline Widerøe was the only tenderer to offer scheduled services. In the other routes the competition varied between 2 and 5 airlines. The two major domestic carriers SAS and Braathens did not participate in the competition. Widerøe won the tender for 9 out of 15 routes and will hence receive more than 80 per cent of the public funding, 1.1. billion NOK for the period.

The PSO system is unaffected by the transformation of NATAM to an incorporated company.

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Domestic Commercial Services

The domestic aviation market has changed drastically since 1990.[75] Until 1993 the Norwegian air traffic market was regulated through government granted traffic rights, and price regulation. In this setting, the two carriers SAS and Braathens, operated two almost non-overlapping route networks, unsubsidized on the main airports, whereas the carrier Widerøe operated on a network of regional airports, funded partly through a state subsidy. In 1993-1994, the marked was deregulated through the introduction of the so-called third package for liberalization of air transport in the EU. Although not a member of the EU, Norway has adopted the EU regulations regarding civil aviation through the EEA Agreement. As a consequence of this, between 1994 and 1997, the system of government granted traffic rights was gradually replaced with a free access for all EEA air carriers to exercise traffic rights on all routes within the EEA area. In accordance with EU Council Regulation no. 2408/92.

With the opening up of the market in 1994 both airlines pursued increased capacity by entering each others' routes. This continued until 1998 when the new Oslo Airport Gardermoen opened capacity to the previously capacity restricted Oslo region. Color Air, a low-far airline entered the marked in 1998 and both the incumbents responded by increasing their capacity and lowering prices. Less than a year later Color Air went out of business. Prices on domestic flights increased by nearly 50 per cent after the fourth quarter of 1999.[76] SAS and Braathens were both slow to reduce capacity. While Braathens in 2000 was the largest carrier in the domestic Norwegian aviation market in terms of passengers carried, it encountered financial difficulties in 2000, and the airline was subsequently taken over by SAS. Since that consolidation SAS has reduced its capacity by 15 per cent measured in seat/km, by 20 per cent in number of flights already the first year.[77] Prices, have, however, fallen by nearly the same percentage in the same period, partly due to the removal of the flight passenger surcharge from 1 April 2002.[78]

The Norwegian domestic market is highly concentrated, particularly so after SAS's takeover of Braathens AS in the fall of 2002.[79] While four airlines, SAS, Braathens, Widerøe and Norwegian Air Shuttle, seemingly provide the majority of domestic services, SAS controls both Braathens (100 per cent) and Widerøe (96.4 per cent), and in practice holds approximately a 91 percent share of the total market. There is only competition in a select number of routes, NAS' total share is estimated at around 5 per cent.

With the entry of Norwegian Air Shuttle, NAS, into the domestic commercial market on 1 September 2002 an element of competition was reintroduced, albeit small. NAS started with six daily flights between Oslo Airport Gardermoen, Bergen and Trondheim and 2 daily flight between Oslo and Tromsø. The following week six daily flights between Oslo and Stavanger (both ways) were introduced. Norwegian Air Shuttle carried 446.000 passengers in the half year from October 2002 to March 2003. The total number of passengers on domestic routes (no charter, no transfer) reported from AVINOR the same period amounted to around 8.6 million.[80]

NAS' entry was contingent upon the banning of frequent flyer programs (FFP) for domestic routes after 1 August 2002. (See Box 5) This ban applies to the earning of points only, but applies to all domestic routes, not just the ones that are competitive.[81] Points earned on international flights can be redeemed domestically, as can points earned prior to the ban on FFP domestically.

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Box 5. **Frequent Flyer Programs**

The Nordic Competition Authorities have drawn a number of conclusions concerning the characteristics and effects of frequent flyer programs (FFPs) which almost all major airlines offer their travelers. Most have the following characteristic in common:

- "Discounts" are granted not in the form of money, but in the form of free services, not necessarily of the same type as purchased. The frequent flyer points are no ordinary rebate.
- To obtain free flight to more or less distant destinations, the customer needs to surpass certain thresholds in terms of travel purchases. The customer thus has an incentive to concentrate her purchases to one or a few providers. The closer the customer gets to a threshold, the stronger is her incentive to buy another flight from that particular airline or alliance.
- The "discount" is given to the traveler, who – in the case of business travel – tends to differ from the purchaser. This gives rise a pronounced principal agent problem, by which the decision maker (agent) is faced with a quite different set of incentives from those of her superior (principal). This may lead to a distorted (inefficient) resource allocation.
- Although in principle taxable in many countries, the private use of frequent flyer points earned by an employee is in practice rarely taxed, for lack of information on the part of the government. This tax loophole is likely to aggravate the inefficiency du to the principal agent problem.
- Alliance airlines join their FFPs to offer attractive, and extended networks to bonus point travelers. Smaller airlines or alliances have a distinct competitive disadvantage. The FFPs are thus liable to strengthen any dominant position and to reinforce the anti-competitive effects of hub-and spoke networks.

The Nordic Competition Authorities have concluded that frequent flyer programs are thus loyalty inducing, giving rise to artificial economies of scope and switching costs. They have welfare decreasing and anti-competitive effects, and are clearly at variance with the spirit of competition law in most countries. The anti-competitive effects are particularly evident in a setting with one or a few established firms and a potential entrant.

Source: Report from the Nordic competition authorities No.1/2002. Competitive Airlines. Towards a more vigorous competition policy in relation to the air travel market.

In view of the report from the Nordic Competition Authorities, the European Competition Authorities have initiated a European-wide cooperative effort in order to combat competitive problems in Airline Traffic.

Providing for competition

While in the past (1998) The Norwegian Competition Authority has urged the Ministry of Transport and Communication to change the system of cross-subsidies between airports,[82] the NCA has recently expressed the view in a consultation process (October 2002) that since all but one conventional airport are owned and run by the same entity, Avinor AS, and this entity is required to completely cover its own costs, then Ramsey pricing can be seen as an economically efficient solution. This is, however, based on a number of conditions, such as: lower charges at airports with a low rate of capacity utilization and hence low marginal costs per passenger, peak load pricing, reduced charges for carriers with reduced requirements on and use of airport infrastructure and charges that are in part proportional to the fare payable by the passenger. The NCA concludes that it is economically efficient to let the busier and more profitable airports cross- subsidize the less profitable ones. [83]

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A network system of airports may have benefits in the form of economies of scale and coordination of services. It is, however, a challenge to provide sufficient incentives to generate potential efficiency gains, when external subsidies are introduced into the system. Avinor may potentially increase incomes and reduce costs on the main airports as they receive no subsidies for these airports. The subsidy granted to Avinor's regional airports is now in the form of a purchase of airport services. The latter will increase transparency concerning the costs of maintaining these airport services.

The degree of competition for each regional route enables a lowering of subsidies on each route. In areas where there is no competition subsidies stay high. Competition over time is difficult to maintain, as runner ups in tendering processes tend to go out of business. Improvements in the auction design – for example through smaller packages – have proven successful in attracting new entrants.[84]

The three year length of the concession period for the PSO routes is determined by the EU Council Regulation 2408/92. Given the large scale investments needed to run the regional routes, a three year contract period is too short to establish a sound footing in the market. It is expected that an extension of the concession period may lead to an increase in competition, as well as lowering the demands for compensation.

The developments in the Norwegian domestic air travel market have resulted in a near monopoly situation for SAS. The Government has taken a number of commendable initiatives to improve access for new entrants, particularly

- the ban on FFPs for domestic flights, (effective 1 August 2002)
- the elimination of the air passenger surcharge, (1 April 2002)
- the corporate agreement entered into by the Government with NAS from 1 September 2002
- the 90 per cent reduction in surcharges at six airports for international flights[85]

Further measures will, nevertheless, very likely be called for if a competitive market is to be reinstated for domestic air travel in Norway. The Nordic Competition Authorities have identified a number of other areas which may affect the contestability of the domestic air travel market:

- ***Corporate discount schemes***. Corporate discount schemes are agreements by which large airline customers have been able to negotiate lower (net) fares on all or certain parts on an airline's network. Discounts of up to 30 to 50 percent on business class tickets are not uncommon. Such schemes may engender important lock-in effects. Large carriers will obtain an inherent advantage compared to smaller ones. The largest Norwegian corporations such as Telenor, Norsk Hydro and Statoil have entered into such discount schemes. Statoil has reportedly entered into a 3 year Agreement (with the option of a three year extension) effective 1 February, 2003 with SAS that is valued at around 500.000 NOK p.a. and a total of 3 billion NOK.[86] The Norwegian Government's contract with NAS by comparison has an estimated value of 250-300 million NOK p.a.[87]

- ***Travel agent agreements***. Such agreements sometimes provide incentives for an agent to concentrate his sales to one or a few larger airlines. Such contracts may be anti-competitive and in contravention with the principles laid down by the EU Commission.

The Minister of Labor and Government Administration requested the Competition Authority address the above issues in November 2001.[88]

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- ***Ground handling***. Currently a minimum access to ground handling is ensured through Council Directive 96/97EC at all airports with at least two million passengers annually. The Directive sets a minimum standard that at such airports the number of third party providers not be fewer than two, where one may be controlled by an incumbent airline. Access to ground handling may thus be a barrier to entry.

- ***Value Added Tax***. In addition taxation of ground handling and catering services, for example through output value added tax (VAT) without being able to deduct input VAT may also serve as a barrier to entry. Larger carriers undertaking self-handling thus typically obtain a competitive advantage to smaller competitors for whom it would be uneconomical to set up their own self-handling operation at every airport. The latter are therefore confined to buy these services in the market, at a 24 per cent higher price, in many cases from their largest competitor. Independent ground handling firms are unable to compete with the services offered by the larger airline carriers and may thus be forced out of business. The NCA had advocated a change in the VAT regime to ensure a level playing field. The matter is currently under review in the Ministry of Finance.[89]

There is some question as to whether national competition authorities have sufficient authority to intervene against abuse of dominant position for example through predatory pricing. Council regulation (EEC) No 2408/92 which guarantees free access for EEA air carriers might be interpreted to preclude intervention against excess capacity. Similarly there is a question of whether Council Regulation (EEC) No. 2409/92 which deals with fares and rates for air services allows for intervention against predatory pricing.[90]

SAS has appealed the ban on FFP in the domestic market to the Minister of Labor and Government Administration. The appeal was turned down. SAS has argued that banning the FFP domestically will affect their competitiveness internationally, as bonus points earned on domestic flights would lead to bookings on SAS international flights. This may to some extent be the case, yet the argument can also be made that Norwegian passengers will still choose SAS for international flights, as the bonus points earned on these flights can be used for free flights domestically.

After six months of service it is still too early to say if the new entrant, Norwegian Air Shuttle AS, will be able to establish a profitable service share in the domestic air flight market. Norwegian appears to have an average capacity utilization rate of 56 per cent (according to its own web site).[91] This is presented as a 2 per cent increase from November. On 15 January 2003, however, the company cancelled two PSO routes in the north of Norway which it had been awarded in the PSO tender for the next three years. The routes together carried an annual average subsidy of 24 million NOK. The rationale given is that the company prefers to focus on low-cost fares on its other routes, rather than having to invest in new airplanes for the routes. It will however have to service the routes until 31 December 2003.

1.2.2. Conclusions and Recommendations

In its Economic survey of Norway 2002, the OECD concluded that greater competition is urgently needed in domestic air travel. While a number of significant measures have been taken to improve the competitive environment, a continued tough stance by the Norwegian Competition Authority, including close scrutiny of a number of loyalty inducing measures, is justified in a market where there is a near monopoly.

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The commercialization of NATAM should allow for greater flexibility in airport management, particularly with the introduction of the purchasing of service from Avinor for unprofitable airports to be introduced in 2004. This system of government purchasing of a service will contribute to greater transparency concerning the costs of the various regional airports, and may result in a revisiting of the potential benefits of closing certain airports.

Restrictions on Avinor's flexibility remain, however, as the Minister of Transport and Communications (who is the general meeting of Avinor) has stated that there should not be any significant partial or full privatization of Avinor's core activities without prior approval from the Ministry.[92]

The technical specifications for the regional air services open for tender should be revisited with a view to removing requirements that may restrict competition or new entrants, in extension of the measures already taken to reduce the packages and reducing the capacity requirements on a number of the flights.

1.3. Hospitals

1.3.1. Introduction

A key feature of the Norwegian health care system, as in the other Nordic countries and the United Kingdom, is the predominance of tax-financed public provision of services. The Norwegian health care system has succeeded in securing universal coverage and high quality service, not only in the urban areas but throughout the country.[93]

The Norwegian hospital sector was reformed by a parliamentary decision with effect from the 1st of January 2002. At that time ownership responsibility for the hospital sector (the reform also covers most county specialist health services, within both somatic and psychiatric health care and the ambulance service), was transferred to the central government from the counties. In all approximately 350 specialist health institutions, including 85 hospitals, were transferred.

This transfer represents break with a more than 30 year tradition of hospitals being owned and run by the 19 counties. The move also appears to represent a break with the stated goals of greater subsidiarity (decentralization and delegation) of the modernization program for the public sector. The Government has underlined, though, that the reform represents a decentralization of the management process, while at the same time centralizing control, or "centralization of policy and decentralization of delivery responsibility". The reform was promulgated by the following:

- Increasing use of resources, but greater financial problems.
- Increased growth in the number of patients treated, but stable or growing waiting lists.
- A strong rise in the number of health care professionals, but an apparent lack of health care professionals. In the 1990's the number of physicians rose by 50 per cent in terms of man years.
- An inability to shift patients from over-utilized to under-utilized capacity.
- Variation in the services offered, depending on the place of residence.

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- A great disparity between hospitals as regards use of resources.

The Norwegian health sector is now divided into five health regions run by separate legal entities (so called regional health authorities) organized as hybrid companies subject to special legislation (see section 1.1). The hospitals are organized as individual enterprises (health enterprises) owned by the various regional health authorities, but with status as separate legal subjects. The regional health authorities have organized the hospitals into a total of about 33 health enterprises.

The reform of the hospital sector represents a quasi-commercialization of services. Enterprises are established in the sector as hybrid statutory companies that are separate legal entities, and where consumer choice is provided. The reform as such does not, however, represent a marketization of services, as a fundamental principle underlying the reform is that private purchasing power should not affect access to public health services. Nor does the reform represent a privatization of the hospital sector, as the law establishing the health authorities explicitly prevents selling of hospital services to private actors without prior consent of Parliament.

Under the reform, the overall responsibility for provision of health services remains with the State. The policy goals will be established centrally by Government and with the approval of Parliament. The State ownership of the regional health authorities rests with the Ministry of Health. The goal behind the reform is to enhance coordination and efficient utilization of resources, nationwide, but also within and among the various regions. State ownership is perceived to ensure equity of access to health services irrespective of place of residence in the country.

The private hospital sector in Norway is marginal, with ten small private hospitals with outpatient clinics in Oslo - providing only 90 beds, less than 1 per cent of total capacity. Norwegian law imposes tight restrictions on establishing such private hospitals and the current reform has not changed this or the status of the private hospitals. Nor does the reform initiate a change to the actual system of funding.

The reform does, however, open for the hospitals to increasingly use or cooperate with private providers of goods and services in its non-medical operations. This follows from an important aim of the reform, which is to provide the hospitals with possibilities, responsibilities and freedom to organize and form the services in the manner they find most patient-oriented and cost-effective. Norway spends more than NOK 50 billion annually on hospitals, making it one of the European countries with the highest level of public spending on health service per capita. Reform of the hospital sector had been discussed on many occasions prior to the decision in June 2001, both in 1987, 1994 and 1996.

1.3.2. Elements of the reform

While it is beyond the scope of this paper to provide a detailed presentation of all the elements of the hospital reform, some salient elements have been focused on below. While the hospital reform has taken the form of hybrid enterprise, in organizational form the statutory company model discussed in section 1.1. of this chapter has been used.

- ***Central government control and responsibility.*** The new organization will give the Minister of Health greater opportunity to intervene directly in the setting of principal health policy goals and frameworks for the sector. Such direction is to be provided through the articles of association, budget priorities or by means of decisions reached at the enterprise meetings ("general meetings"). The day to day running of the enterprises will be the responsibility of management.

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- ***Clearly defined responsibilities for the enterprises.*** The regional health authorities have both a provider role and a purchaser role. They have a purchaser role: the overall responsibility for ensuring that specialist health service is available for the population in the region; either through its own hospital, other hospitals (in other regions or private, or foreign). And a provider role: the responsibility as owners of the health enterprises in the region. It is, however, the health enterprises that are the actual providers.

- ***Increased flexibility in operations.*** The individual enterprises will be responsible for their employees and will be responsible for their finances, with the restriction that they may not go into voluntary liquidation.

- ***Financing.*** The reform includes a new accounting system, but does not involve any change to the system of funding in existence prior to the reform, where approximately half is provided through block financing and the other half by matching grants based on the number of patients treated, their diagnosis related groups, and a national standardized cost per treatment. Future financing of specialist health service has been reviewed by a special committee that presented its report 17 December 2002. The report from the committee is currently subject to a consultative round that expires 15 March 2003. The Government is expected to present a proposal for a new financing system to be implemented January 2004. There have emerged probable budget deficits in all regional health authorities, that have been partly offset by additional funding through the national budget in 2002. Around half of the increase was tied to higher activity than projected.

- ***Employment.*** The reform entails a transfer of the hospital employees from the county level to the health authorities. Approximately 100,000 employees are affected by the reform. For most of them the transfer does not alter their status, the law on the Working Environment will continue to regulate their employment. Approximately 6000 were civil servants having previously been employed by state hospitals. The legislation provides for a three year transition period, in which these employees retain their right of priority, and severance pay as civil servants.

- ***Hospital choice.*** The reform maintains the patient's right to freely choose which hospital she wishes. Transport costs are covered for the patient with a private share of 220 NOK in 2003.

- ***Reduction in queues.*** The latest statistics on health queues show a reduction in the waiting time of approximately 2 months for the whole country. At the end of August 2002 255.383 "cases" were on waiting lists, a reduction in 17.000 cases.

The Government has indicated that it intends to introduce performance criteria to assess the five regional health authorities. As part of this process the Government is currently studying strategies to respond to health authorities that fail to meet these criteria. Some of the regional health authorities have already established criteria to link the performance of the regional health board with re-appointment (4 year terms).

Both the regional health authorities and the hospitals have their own executive boards and managing directors. The regional health board (executive boards) are appointed by the minister of Health in the annual enterprise meeting (general assembly). The directors of the regional health authorities are appointed by the regional health boards, their remuneration is decided on in the annual enterprise meeting. The Office of the Auditor General has access to general meetings both at the regional health authority level and in the subsidiary health enterprises.

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A number of the Regional Health Enterprises have experienced turnover in management already during the course of the first year (3 out 5 Chairmen of the Boards have resigned, and a number of directors have resigned). The most recent CEO to quit was the head of the Northern Regional Health Authority, citing management difficulties vis a vis the heads of the hospitals owned by the enterprise. She called for a reassessment and clarification of the division of responsibilities at the regional level, and pointed to the need for clarification of the future financing system of the sector.[94]

The inherent challenge in the reform lies in finding a balance between local autonomy in the individual enterprise while maintaining the desired overall central government control.

Conclusions and recommendations

The reform of the hospital sector was implemented very quickly – proposed by the Government in April 2001 and passed in June 2001 and enacted 1 January 2002. The speediness in the decision making process is related to the broad consensus that changes needed to be made and the extensive consultative process that took place prior to the proposal being tabled. The consultation revealed that there was broad support in the hospitals and among the regional doctors for a change of ownership structure. Not surprisingly, the arguments against a change in ownership structure mainly came from the county authorities. It is still early to draw conclusions about the effects of the reform.

To some extent the reform moves along a path chosen in other countries, particularly **the focus on improved patient choice and patient rights**. It does not, however, fit the pattern of increased decentralization to local government or private actors, nor does it introduce a stronger role for market mechanism as has been the trend in many countries. The reform provides for decentralized management and delegation of financial responsibility, yet the Minister of health can in theory instruct the regional health authorities and overturn Board decisions in all cases. The reform does, however, introduce a business structure which should lead to improved efficiency and flexibility if the subsequent changes to the financing arrangements are well designed.

One criticism of the reform is that it does not sufficiently separate the State's roles as purchaser and provider. The regional health authorities are specifically tasked to maintain both roles. This combination of roles can lead to the pursuit of one to the detriment of the other, for example tensions may arise in relation to whether the regional health authority should focus its efforts first and foremost on providing the service or on purchasing it.

The Norwegian health care system has provided for hospital choice (an "implicit voucher") and also for treatment abroad in cases where the guaranteed treatment period (6 months) has been surpassed. Despite the extensive queues, however, utilization of patient choice has not been significant, nor have hospitals used the opportunity to send patients for treatment abroad to its full capacity. (Significant portions of allocated funding for such treatment remained unused.) This is a reflection of the health sector being a difficult market that is prone to significant market failure, given, *inter alia* the large information asymmetries between doctor and patient. Patients will invariably not have sufficient information to decide which hospital is the best until several have been tried. Nor do patients readily seek out information on availability of services until they are in need of them and at that time they may be under time constraints to make a decision.

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The reorganization of the hospital sector aims to improve coordination at the regional level. Moreover, increased information efforts have also been undertaken to improve awareness of where hospital care is available – a special free telephone number – provides information on which hospitals operate with which waiting lists. Yet there appears to be a need to make the provision of information on alternatives a mandatory obligation for doctors/hospitals, as these are often the first/or second point of contact for a patient. [95]

A potential efficiency problem with the reform is tied to the fact that hospitals and primary health care are still financed by two different government layers. The supply of preventive and outpatient care may remain lower than it should be, and thus could continue to strain hospital resources. In particular, municipalities, have an incentive to postpone the reintegration of patients who are no longer in need of hospital-based medical treatment into the health care services they finance (in particular outpatient and elderly care), leading to longer hospital stays than necessary. Municipalities are allowed by law to wait for 14 days before assuming responsibility for patients who no longer need acute care. This may lengthen waiting periods for hospital treatment and raise health care costs.[96]

1.4. Labor market institutions

Introduction

Norway has, in contrast with most other European nations, not suffered extensive unemployment the past decade. The unemployment rate remains relatively low at around 4 per cent, although there has been a marked increase in recent months. Registered unemployment currently stands at approximately 93,000 – the highest level since 1997 – and is projected to increase to around 110,000 in 2004. This section reviews the commercialization or quasi-commercialization of labor market institutions, i.e. job placement agencies, job creation schemes and vocational training.

Labor market policy is a state responsibility in Norway. Funding is provided through the national budget. The Public Employment Services (PES, Aetat) receives yearly allocations from the Ministry of Labor and Government Administration to cover unemployment benefits, benefits for the vocationally disabled, means for active labor market programs (ALMP)[97] and administrative resources to PES. In 2001 the PES was staffed by approximately 3500 employees (measured in man years), and administered approximately 18.6 billion NOK, with the following distribution:

- Administration: 1.7 billion NOK
- Unemployment benefits: 6.6 billion NOK
- ALMP for ordinary unemployed: 3.8 billion NOK
- Measures for vocational rehabilitation: 6.4 billion NOK

The funding for PES was increased to allow for 220 new employees in the Fiscal budget for 2003; and an extraordinary increase has recently been approved by the Norwegian Parliament (Stortinget) to allow for an additional 200 new employees to deal with the increased work-load resulting from the increasing number of unemployed. The Parliament also adopted an extraordinary increase in ALMP of 276 billion NOK.

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The PES' main task is to place and qualify unemployed. The agency is both a provider and a purchaser of services in addition to administering unemployment benefit payments. The Government has indicated that it aims to introduce private sector providers to some extent into this market, and the future organization of the PES is currently under review. In recent years the PES has been subjected to a number of reorganization measures – the level of employees has been reduced by more than 800 since 1995, and new IT tools have been introduced to improve efficiency. The level of morale in the institution is reportedly low, as indicated by an almost record level of sick leave among the employees – 9.6 per cent in 2002. This is allegedly related to the reorganizations, introduction of new benefit rules regarding vocationally disabled, increased numbers of claimants and the introduction of elaborate IT systems. The negative publicity for the entity - particularly in 2000 in connection with the discovery of exaggerated data (24-30 per cent) on the number of job placements reported by the organization – has very likely also contributed.

The Minister of Labor and Government Administration sets the targets for PES activity annually in the "letters of allocation" accompanying budget transfers. The volume of ALMP is one such target.

ALMP. ALMP for ordinary unemployed consists of three parts:

- Wage subsidies (paid to the employer)
- Work practice (allowance for life maintenance)
- Labor market training (purchased by the PES after a tender process at the county level).

Commercialization of services

The Norwegian market for labor market institutions was deregulated in July 2000. The monopoly on placement services was abolished, the ban on hiring out of labor in areas other than the office sector, which had been open, was also abolished. More than 400 firms were offering placement service or were hiring out labor in 2002. Entry into the market is regulated by the following: Charging unemployed for placement services is prohibited. Private providers must also hold a bank guarantee on an amount equal to the minimum share capital required (100.000 NOK). Municipalities and labor unions are not under this obligation.

In parallel with the deregulation of the market efforts have been made to make the PES more efficient through *inter alia* commercialization:

- The PES no longer runs labor market training centers itself, while a decade ago it ran such centers in nearly all counties. Instead the PES purchases courses from others by tender invitations, usually twice a year. Both secondary schools and private training providers are able to participate. Around 45 per cent of the courses are run by secondary schools.[98] The PES defines the type of labor market training, sets the syllabus, and chooses the participants. The course modules are short (not longer than 10 months, normally allowing for flexibility and maintenance of motivation.
- Job seeking courses which have traditionally been run by the PES are increasingly being run by private actors selected through tender processes. The PES is not allowed to participate in such tenders.

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- The PES has reduced its share of activity in the ALMP area (16 per cent of the unemployed participated on average in 2001), and has shifted a larger share of its activities to the vocationally disabled[99]. This is to some extent a reflection of the composition of the registered unemployed. In 2001 the average monthly numbers of vocationally disabled was larger (63 900) that the number of normally unemployed (62 600).

- The PES has started an experimental program in a few counties where unemployed are allowed to choose between different private providers in searching for employment. The private actors are pre-selected by the PES after tender, yet the private providers are given broad leeway in designing the search for employment. The target group for this program is the vocationally disabled and the long term unemployed (i.e. more than six months unemployed).

- Funding related to results/outcomes has been introduced on an experimental basis in some areas to improve PES efficiency. Allocation of funding is, for example based on the extra number of disabled being considered for employment (more than the planned number within available resources), and on the number of placements by private agencies of unemployed from the public sector.

- Performance measurements have been introduced, but are not directly linked to the budget allocations. For 2002, the PES had fourteen input and output targets which may blur the setting of priorities. In addition, pursuing too many targets makes it difficult to establish a link between its actual performance and budget appropriations. There is also a danger that performance measurements – if not carefully defined and monitored - may create incentives to retain, for example people on disability pensions enrolled in labor market programs rather than facilitating their return to the labor market.(OECD:2002)

- The possible future use of vouchers is currently being assessed by the Ministry of Labour and Government Administration. It is still unclear which if any areas of activity are suitable for such vouchers and what modalities should govern their possible use.

With the liberalization of the sector the PES entered the commercial market for short-term work placement hiring out of labor on an interim basis with the creation of a subsidiary (Aetat Bedrift). Parliament supported this move provided the commercial activities were separated out from the state funded activity, and provided that the activity did not contravene EEA- competition law. The unit was closed down in December 2001 as it proved difficult to establish a framework for operations where the activities were not cross-subsidized by PES' government funded activities. The PES has, however, continued its short-term work placement activity but without charging for the service. The activity has not been seen to be directly substitutable to the activities of private short-term work placement agencies, as the PES does not assume any employer responsibility for the placed employees – that is ultimately carried by the employer. A question can, nevertheless, be raised as to whether or not this practice is distorting competition in the short-term placement market. The Norwegian Competition Authority has found that this activity, while not directly substitutable, nevertheless, reduces the total market for private short term placement.

The Norwegian Competition Authority has evaluated the market for hiring out of labor and found that the market is characterized by high market concentration (two companies, Manpower and Adecco, have a market share of 50 and 25 per cent, respectively) yet the competitive situation is seen as satisfactory given the profitability, the large number of agencies, and the availability of substitutes.

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Challenges faced by the sector

The public employment services are facing a number of challenges that are currently subject to a government review, and which are dealt with in a White Paper to Parliament presented in December 2002[100] (SATS). The Parliamentary debate on the issues raised was due to take place in June 2003. Parliament has, however, postponed the discussion. A parliamentary committee has asked for renewed consideration of the question of establishing one joint agency for social assistance, social insurance and labor market services. The government has indicated that it intends to present a white paper on the whole of labor market policies later this year.

The OECD has pointed to the lack of coordination across government layers as one such challenge.[101] "Some municipalities have complained about their lack of control over the public employment service (PES) strategy to reduce the number of unemployed and to respond to new demands for active labour market programmes. Their main concern is that, because the PES fails to internalise the cost of social benefits paid by municipalities, it could under-invest in active labour market policies." In 2000 one-third of social assistance recipients were also registered as unemployed or vocationally disabled at the PES. Several municipalities have started their own placement schemes in order to assist difficult social assistance clients that are not being served by the PES.

A second challenge – connected to the above - relates to the composition of the unemployed. Norway has the last decade witnessed growth in people on disability pensions. Norway's disability pension scheme is large, about one quarter of those aged 55 to 59 and about one third of 60 to 66 year olds are recipients. And total spending is equivalent to about 2 1/2 per cent of GDP, among the highest in the OECD. Only about one per cent of those with disability pensions in Norway leave the rolls each year due to recovery or work resumption, a figure relatively low by international standards. (OECD:2002) The political focus related to labor market programs has consequently turned to how to keep people with weak productivity at work through, inter alia, individual programs, and increased cooperation with the social insurance authorities and social assistance programs at the municipal level.

The three entities have not been well coordinated in their support schemes to date, with resulting goal conflicts and strategies pursued that are at cross purposes with each other.

A unanimous Parliament requested in 2001 that the government assess the question of establishing one joint agency for social assistance, social insurance and labor market services. This request was motivated by the increasing number of people having to deal with two or all three entities. The recent White Paper discusses such a reorganization in addition to the following alternatives:

- Merging the agencies at the state level, but leaving the municipalities the same responsibilities as today.

- Changing or redistributing the responsibilities of the agencies at the state level without altering the responsibilities of the counties.

- A model where the State takes responsibility for securing income while the municipalities have responsibility for production of services.

The White Paper, concludes with a recommendation along the lines of the second model above. The Government proposes to establish a new "work agency" and a new "pension agency" to replace PES and the Social Insurance Authority. The responsibilities of the municipalities will remain unchanged. It also proposes to establish a joint first contact service point in cooperation with the municipalities' social services. The goal of the proposed reorganization is to increase the number of people employed and reduce

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the number of recipients of social insurance or social assistance. Efforts to coordinate services between the PES and social assistance at the State and municipal level have, nevertheless, already started. The goal is to improve satisfaction at the user level, and avoid that users/clients, particularly those with complex needs (for example disabilities or social problems in addition to unemployment), fall between the cracks between the various agencies and do not receive optimal support.

If approved and implemented, the above reorganization will entail one of the most extensive reforms of the Norwegian public sector in recent history.

The current government has an overriding goal of modernizing the public sector. The program concentrates on four objectives: a less complex public sector; public services adapted to individual needs; an efficient public sector, a public sector that promotes productivity and efficiency and an inclusive and motivating human resource policy. In a statement to Parliament 24 January 02, the Minister of Labour and Government Administration laid out the principles governing the reform program, including the importance of distinguishing more clearly between administration and service provision, and between the responsibility for the financing of public services and the actual production of these services. These distinctions are seen as important because they allow for the possibility of exposing service production to competition and also enable the agency financing a service to impose requirements on the provider. The PES is one are which is under review with a view to modernizing it.[102]

Conclusions and recommendations

The liberalization of the market for labor market services has led to increased user choice. The separation of the provider and purchaser role for labor market training for regularly unemployed within PES has led to improved flexibility in the services offered, and the use of tender has increased cost-effectiveness in this activity area. These developments are in line with the trend in other OECD countries. The availability of training provided by widely accredited institutions – such as secondary schools as opposed to internal PES courses - is also likely to have improved job prospects for the unemployed.

The PES as such, and the greater portion of PES activities, have not been commercialized, and it is difficult, within the framework of this report, to assess fully which services are contestable and suitable for outcome-based financing. There does, however, appear *primae facie* to be room for a greater separation of the purchaser and provider roles also in other labor qualifying areas than labor market training. Efforts already underway to identify such services, for example in assisting long-term unemployed, could usefully be pursued.[103] Consideration could also be given to applying the "money follows the user" principle as recommended in the OECD Economic Survey (OECD, 2002) Increased use of performance measurements and outcome-based financing is likely to lead to improved efficiency. Detailed analysis of existing experience in other countries with commercialization, however, suggest that key issues are: adequate systems for measuring placement outcomes, the right system for assessing the relative performance of different providers and paying (or selecting) providers according to performance; and indirectly allowing commercial providers influence on whether job seekers meet conditions for benefit entitlements. The efficiency gains from commercialization depend on finding the right solutions to these and other detailed issues of implementation.

Active labor market policies have contributed to maintaining Norway's low levels of unemployment, and Norway's PES has been deemed to do well in international performance comparisons. While Norway has one of the lowest rates of unemployment and highest rates of labor participation there is, however, an increasing strain on the social insurance schemes and social assistance service by people in their "labor productive years". The increased cooperative efforts underway with the Social Insurance Authorities and the social assistance schemes administered by the municipalities intended to improve user friendliness (improved user choice and orientation), could also have added benefits in the form of improved incentives to work and increased cost effectiveness.

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NOTES

1. OECD, Economic Survey of Norway, 2002, (ECO/EDR(2002)13.

2. The conceptual framework used has been drawn from the OECD Regulatory Review of Finland, OECD (2002) DAFFE/COMP/WP2(2002)7

3. Approximately 25 per cent of the value was foreign held as of April 2003. Source: Oslo Stock Exchange, Monthly Statistics for Equities, http://www.oslobors.no/ob/mndstatistikk-aksjer.

4. OECD: 1998. *Reforming Public Enterprises*, PUMA/SBO(98)6.

5. Ibid. St. meld. Nr. 22 (2001-2002).

6. Commercialization/marketising of public services is defined as the process by which a government entity which directly provides goods or services to the public for free is transformed into an independent entity with separate accounts that charges for its goods and services while remaining in government ownership. Privatization is taken to mean the sale of a commercialized independent entity to private investors.

7. The Government owned statutory enterprise form was established as a consequence of the study.

8. The following entities are organized ad administrative enterprises:

   - Statsbygg – The Directorate of Public Construction and Property
   - The Guarantee Institute for Export Credit
   - Forsvarsbygg – Defense Construction
   - The Norwegian Mapping Authority
   - The Norwegian Public Service Pension Fund
   - The Norwegian National Coastal Administration.

9. The Act of 30 August 1991 No. 71 relating to State-owned Enterprises, with amendments of 20 December 2002 in Act No 88, regulates these entities.

10. The Office of the Auditor General (Riksrevisjonen) is an independent agency responsible to Parliament that monitors that public assets are used and administered according to sound financial principles and in keeping with the decisions and intentions of Parliament. It employs around 450 people.

11. The EEA Agreement entered into force 1 January 1994 between the EFTA states Norway, Iceland and Liechtenstein and the European Union. The Agreement provides for the free exchange of goods, the free movement of persons, capital and services. Under the Agreement Norway is obliged to implement into Norwegian law all EU directives and regulations governing these areas. The Agreement provides for common competition rules and rules for state aid and government procurement, as well as harmonization of rules and standards for goods and services for health-, safety-, environmental and consumer protection reasons. The Agreement led to the establishment of the EFTA Surveillance Authority (ESA)which has as central task to ensure that the EFTA States fulfil their obligations under the Agreement. In addition to general surveillance ESA has extended competence in three fields: public procurement, competition and State aid.

12. *Aftenposten, (Daily newspaper)* 16 January 2003.

13. The Companies Act of 13 June 1997 No. 44 and Act No 45 of June 13 1997 regulate such companies.

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14. See OECD (1998) Reforming Public Enterprises PUMA/SBO(98)6 and PUMA/SBO(98)6/ANN

15. OECD: 1998, *Reforming Public Enterprises*, PUMA/SBO(98)6.

16. *The National Budget, 2003* op.cit.

17. BA stands for limited responsibility.

18. *State Involvement in Production of Goods and Services – Development and Company Formation, Report from Norway – October 1997. The Norwegian Ministry of Labour and Administration.*

19. St.prp. nr. 62 (2001-2002) *On the transofrmation of NSB BA and Posten Norge BA to incorporated companies.*

20. This appears to be more an issue in connection with commercialization and privatization in the municipalities than in the central Oslo region where most of the government owned enterprises are located.

21. The major goals and principles for the reform were laid out in a statement to Parliament by the Minister of Labor and Government Administration on 24 January 2002.

22. The principles underlying the disposition and treatment of the fiscal budget sets important parameters for reform efforts at the local level. 27 January 2003 a committee (Andreassen-utvalget) presented a report with recommendations on changes that should be made in central government's budget and accounting principles. Firstly, the committee recommends a change in central government's budget and accounting principles from cash-based to and accruals based system. Secondly, the committee recommends introducing disaggregated multi-year budget forecasts in order to trace the future consequences of current and past decisions and to take better account of projects that span several years.

23. *The National Budget 2003, Government White Paper*, St. meld. No. 1 (2002-2003)

24. *Modernizing the public sector.* Op.cit.

25. *Sem Declaration, October 2001*.

26. Press release No. 135/2002, 25 October 2002 from the Ministry of Transport and Communications, Press release No. 02/03 of 9 January 2003 from the Ministry of Trade and Industry.

27. St. Meld. Nr. 22 (2001-2002), Chapter 4 State ownership - goals and relations to other government roles.

28. ESA has brought focus on a number of issues pertaining to state ownership, for example the government guarantee for loans for statutory companies, which has led to a more general review of the law governing such companies. The law was amended 20 December 2002 with effect from 1 January 2003. Act No. 88.

29. Norway has a parliamentary democracy where all decisions must have support of a majority in Parliament. The current government is a minority one, and it is obliged to take into account the "will of parliament". Majority decisions by Parliament are increasingly used to direct the Government.

30. Innst. S.nr. 106 (2002-2003) 23 January 2003. Innstilling fra næringskomiteen….

31. This is in part motivated by "rent seeking activities" by private investors who are advocating using proceeds from sales of state shares for investments in specific clusters to promote industrial development.

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32. Press release from The Ministry of Trade and Industry No. 37/02, 15 November 2002. The committee's ten members are drawn from business and industry, academia, the Confederation of Trade Unions (LO) and the Confederation of Norwegian Industries (NHO)as well as the Solicitor General's Office.

33. Government White Paper, *St. meld. Nr. 40 (1997-1998) Ownership in Business.*

34. The following discussion draws on OECD (1998), *Corporate Governance, State owned Enterprises and Privatisation,* and the studies therein, particularly that by Saul Estrin (1998) *State Ownership Corporate Governance and Privatisation.*

35. See subsequent discussion on privatisation.

36. As an alternative, some countries have adopted a strategy of having public holding companies that are interposed between the state and the state's commercial firms, with the objective of applying private secto governance practices to the subsidiaries. However, experience with this approach has not been particularly successful. See for example Baumann, H (1998) "The Cost and Benefits of Public Sector Holding Companies*", in OECD (1998) Corporate Governance State-Owned Enterprises and Privatization.*

37. Op.cit. St. meld. Nr. 22

38. Specified in a parliamentary decision, Dok. Nr. 7 (1972-73) Innst. S.nr 277 (1976-77).

39. *Staten som eier. (The State as Owner)* Report by Government appointed interministerial working group. Presented 23 February 2002.

40. Press report from the Ministry of Church and Culture No. 16/02, 28 February 2002.

41. The study was published in 3 parts: Staskonsult (1998a), Report 199:16, Statskonsult (1998b), Report 1998:28, Statskonsult (1998c), Reports 1998:21.

42. *Aftenposten,* (Daily newspaper) 17 September 2002.

43. The same principle has also been introduced for public service providers that are still government agencies. A system of "letters of allocation" was introduced in 1996 where the ministry defines the performance targets, budget appropriations at their disposal, and reporting requirements on actual performance.

44. *Aftenposten* (Daily newspaper) 14 November 2002.

45. Historically this has not always been the approach, rather, the point of state ownership has been to be able to steer and manage the company and the sector it operates in in a manner that allows it to expand and prosper. A classic example is the advent of Statoil, the State oil company (now partially privatized and listed on the Stock exchange), which was afforded preferential treatment in most, if not all, all aspects of the development of the Norwegian Petroleum shelf until 1994. Kindingstad, Torbjørn: *Norwegian Oil History, (*Wigestrand, 2002).

46. The Ministry of Trade and Industry (2002): *The Norwegian Government Policy for Educed and Imrpoved State Ownership,* Publication Based on White Paper No. 22 2001-02.

47. In the area of state aid, ESA has, however, prior approval before a measure is enacted.

48. OECD:2002. Economic Survey of Norway. Enhancing the effectiveness of public spending.

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49. The Act No. 71on Statutory Companies of 30 August 1991 was amended 20 December 2002 by Act No. 88 in response to an ESA requirement. Government guarantees at "no-risk premium were deemed to constitute state aid.

50. A complaint was raised with ESA that Norway Post had cross-subsidized its activities in the fully competitive parcels market with revenue from its monopoly activities. After a thorough investigation ESA concluded that there was not sufficient evidence that such practices had taken place. Source: EFTA Surveillance Authority, Annual Report 2001.

51. The Norwegian Competition Authority defines cross subsidization as a situation where a product is sold in the market at a price that does not cover its production costs and where the financial source of the subsidy may be budget grants that finance and entity's core activity or income from the entity's monopoly activity granted by law or as a result of a public service obligation.

52. The Competition Act is currently under review and proposed changes are expected that will make the NCAs work with public measures more efficient.

53. The actual legal position is that a state enterprise is not a "limited liability" structure, with the Government guaranteeing and ultimately being responsible for its debt. Similarly, a state enterprise administers state assets but these remain formally owned by the state. In this sense a state enterprise is not a separate asset entity but for ther purposes of the following paragraph and in so far as the competition implications are concerned the state enterprise can be treated "as if" it were a separate entity.

54. Act No. 65 of 11 June 1993 with amendments 12 April 2000.

55. An example is an entity licensed with the exclusive right to provide an electricity network in a defined area.

56. Activities which result directly from tasks assigned to a government organisation pursuant to a statute or decision of an administrative body are not subject to this access rule nor, consequently, the conduct rule. For example, the provision of education services by state run schools is not subject to the market and government framework. Similar exceptions apply in respect of: activities pursuant to international treaties and agreements, the use of residual capacity of fixed assets that are used to perform the duties of a governmental organisation; and *de minimus* activities (<€75,000).

57. 15 years in the case of a government owned company with partial private ownership.

58. Publication from the Ministry of Trade and Industry, *The Norwegian Government Policy for Reduced and Improved State ownership.* Op.cit.

59. Note that this statement is equivalent to a view that governance structures for SOE are inherently less able to motivate efficiency than private governance due to the blurring of political and business objectives and that these "deficiencies" cannot be addressed fully by reforms to governance structures.

60. OECD (2000) Privatisation, Competition and Regulation

61. Except where pre-reform prices were unsustainably low and substantial new investment was required to maintain services.

62. *The Norwegian Government Policy for Reduced and Improved State Ownership,* op.cit.

63. Report from the Nordic competition authorities No. 1/2002. *Competitive Airlines: Towards a more vigorous competition policy in relation to the air travel market.*

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64. Luftsfartsverket was given a new name in English, The Norwegian Air Traffic and Airport Management (NATAM), after the separation of the CAA.

65. NATAM operates the 45 state owned airports. In addition there are 8 additional airports which are open to public flights.

66. Press release No. 117/2002 from the Ministry of Transport and Communication.

67. Williams, George. *Comparative Study of European Airport Provision,* Air Transport Group, College of Aeronautics, Cranfield University

68. *Press release* No. 136/2002, from the Ministry of Transport and Communication, 25 October 2002.

69. Williams, *op.cit.*

70. Press release, op.cit.

71. B.innst. S.nr. 13 Tl.01(2002-2003) Parliamentary records.

72. The remaining 17 were a priori assessed as fixed, in the sense that they are indisputably necessary for a number of reasons, such as: no other alternative transport mode, a key role in the oil and gas offshore industry, proximity to hospitals or regional administration centers.

73. Council Regulation (EEC) No 2408/92 Article 4, on access for Community Air Carriers to intra-Community air services.

74. The standards may include minimum offered seat capacities, minimum number of frequencies, minimum standard of aircraft, maximum fares, required number of non-stop flights etc. These standards have been formed individually for each different route areas, based on the expected number of passengers, length of flight, different kind of traffic, and on historical standards set over time for the particular route.

75. *Norwegian Domestic Aviation – Competition and Monopoly,* Report by Norway's Institute of Transport Economics (TØI), no. 586/2002.

76. NATAM press release, 2 September 2002 on the occasion of start up of NAS services.

77. TØI ibid.

78. *The National Budget 2003,* St. meld. Nr. 1 (2002-2003).

79. The NCA may intervene against mergers or acquisitions by prohibiting acquisitions if the NCA finds that it will create or strengthen a significant lessening of competition. The NCA reviewed SAS's take-over of Braathens, however, did not intervene as a failing firm argument was invoked. If one enterprise is a failing firm, and if bankruptcy does not lead to a preferable situation in terms of competition, the conditions for intervention by the NCA are not fulfilled. (Report from the Nordic Competition Authorities *op.cit*.)

80. Source: Norwegian Air Shuttle (http://www.norwegian.no, and Avinor (http:77www.avinor.no.

81. The Swedish ban on FFP is only routes where there is competition.

82. In 1998 the NCA had pointed out that airport charges should be stipulated to reflect the costs of airport facilities and services, including externalities such as air and noise pollution. The level of charges should be stipulated to reflect the differences in demand for the services in various periods during the day. Use of peak-load pricing may contribute to more efficient use of the airport and airport facilities. The deficit

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created at airports with scarce traffic should be covered by financial transfers directly from the state not from the airports making a surplus. With the introduction of a system of purchasing services directly from airports which cannot provide the service level wanted by government on commercial terms. This would reduce the need for cross subsidization. OECD:1998, DAFFE/CLP(98)3.

83. NCA, Note to the ECA Air traffic Working Group, January 2003.

84. Parliament has no formal role in the setting of specifications, yet any changes that may result in what is perceived as a reduction in a public service will be criticised, and the Government invariably will avoid inducing parliamentary displeasure.

85. Introduced by the Minister of Transport and Communication 20 December 2002 as a trial measure in order to improve the economy of some of the regional airports, and to improve competition in the air flight market. The measures is introduced for the following airports: Haugesund, Molde, Kristiansund, Røros, Evenes and Lakselv.

86. Stavanger Aftenblad, (Daily Newspaper) 23 January 2003.

87. Source: The Norwegian Competition Authority, 2003.

88. *The National Budget 2003*, St.meld. Nr. 1 (2002-2003).

89. The Norwegian Competition Authority: *Note to the ECA Air Traffic Working Group, January 2003.*

90. The German Competition Authority has intervened against predatory pricing of the German flag carrier where there was competition from a small low-price carrier. Source: The Norwegian Competition Authority

91. While low by international standards, according to the company's own assessment their break-even cabin load factor hovers slightly above 50 per cent. Source: The Norwegian Competition Authority.

92. Press release from the Ministry of Transport and Communication, *op.cit.*

93. OECD, *The Norwegian Health Care System. Economics Department Working Paers No. 198.* ECO/WKP(98)11.

94. *Dagens Næringsliv*, (Daily newspaper) 7 January 2003.

95. A recent newspaper report concerned a woman waiting for an orthopedic operation. She was told the waiting period was close to one year. After several attempts to reduce the waiting period she was told she could be operated on in the adjacent municipality. While recovering from her operation she was informed by her local hospital that she could elect to have her operation abroad.

96. OECD: 2002. *Enhancing the effectiveness of public spending.*

97 Although total ALMP spending is relatively high, most of the participants are disabled. In 2001 non-disabled participants in ALMP were a low 0.4 per cent of the labor force, 16 per cent of the registered unemployed participated in ALMP in 2001 (monthly average). Job creation schemes are currently not in use.

98. This is likely connected to the fact that a large number of the unemployed lack an upper secondary diploma.

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99. "Vocationally disabled" is a broad term that covers people that are not able to work for a variety of reasons stemming for example from health concerns or social concerns.

100. St. meld. Nr. 14 (2002-2003) from the Ministry of Social Affairs, *Coordination of the PES, Social Insurance Authority and Social Services.*

101. OECD:2002, OECD Economic Survery of Norway, Chapter II: Enhancing the effectiveness of public spending.

102. Publication by the Ministry of Labour and Government Administration, P-0907 E, Statement to Parliament 24.01.02. *Modernizing the public sector in Norway – making it more efficient and user-oriented.*

103. Splitting the role of purchaser of reintegration services and providing such services was proposed by the OECD in connection with a Review of Social Assistance Policies. (OECD: DEELSA/ELSA(97)18).

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