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ADMINISTRATIVE INEFFICIENCY AND POLICY INEFFECTIVENESS AS ROOT CAUSES LEADING TO HIGH TRANSACTION COST: EXAMPLE: SLOVENIA 1993-1996

OBJECTIVES OF THIS ARTICLE

Countries suffering from high transactions costs are often victims of administrative inefficiencies and policy ineffectiveness at central governmental level. The objective of this article is to describe such inefficiencies and ineffectiveness as they presented themselves after Slovenia reached independence from the former Yugoslavia in 1991. In particular, the author describes the multiple causes of inefficient administrative and ineffective policies as they presented themselves in the subsequent period of gradual administrative modernization during the years of 1993-1996. Most of the material presented and discussed is based on the experience made during a bilateral capacity building and institution development project co-organised by Swiss and Slovene experts over the period of three years. Slovenia has since become a member of the EU however the analyses made, even though country and time specific, are nevertheless instructive for other countries transiting through similar development steps and challenges.

ECONOMIC SITUATION IN SLOVENIA IN 1991-1992

Slovenia is a small country with hardly any natural resources. At the time of independence, it was, however, highly industrialized and export-oriented. In the past it served as the export base between the former Yugoslavia and the West. It's location between Eastern and

Western Europe also makes it important to transit transport and tourism. The manufacturing sector consisted in 1993 of electrical and non-electrical machinery, metal processing, chemicals, textiles, wood processing and furniture which contributed about 33% to the GDP. Services contributed more than 50% of GDP and included transport and communications, trade, finance, and tourism among others.

Slovenia's industrial sector was made up of many small companies. This resulted in a high degree of flexibility due to the fact that production was not concentrated in a few very large companies. For example, the top 130 largest companies employed only 40% of the workforce and the 20 top exporters accounted for less than 35% of total exports.

In 1991 Slovenia had a per capita GDP of over ECU 5,000 and was the wealthiest and most developed of the republics of the former Yugoslavia. Slovenian companies which were traditionally self-managed at near market conditions, served as an export channel for the other republics in the federation. However the outbreak of war in former Yugoslavia in 1991 and the breakdown of the CMEA trade block caused industrial production to fall by 12% and unemployment to increase over 8%.

Since then real output continued to decline, however at a somewhat slower rate, In 1992 the most serious declines occurred in industry, especially the production of capital goods, raw materials, consumer goods and retail trade. There were several reasons for this, namely the transition to a market economy, collapse of trade within the CMEA countries, and the toll taken by the war. Investment also dropped dramatically resulting in an increase in unemployment. The rate of unemployment reached 12.7% as of November 1992. Even though private sector grew slightly, its share of total employment was still far less than the public sector which employed 84.9% of employees in the first half of 1992.

Inflation continued to be a constraint to economic recovery. Although the hyper-inflation which occurred at the end of the 80s (2,770%) was controlled, it was still running at around 38% as of the last quarter of 1992 and average real interest rates are running close to 24%.

Situation of the Public Sector at Same Period

The public sector in Slovenia consisted of three categories of actors, namely, the state administration, the parastatal administration, and the socially-owned independent agencies. The task of transformation from a centrally controlled economy to a market-oriented economy was not as speedy as hoped for. All three branches of actors were confronted with issues of maintaining their day-to-day operations while transforming themselves into new entities befitting their new operational context. The results were confusion, inefficiency and disorder.

Although the public administration in Slovenia seemed much decentralized, even under a socialist regime, this was only an outward appearance. In fact, the administration was highly centralized through the ties of membership and loyalty to the Communist Party. Although the Party was made up of five different "socio-political" organizations, decision-making was left to a small circle of leaders in the government. The old structure was geared towards directing almost every activity in society through strong central planning. The public administration, like the State, was all pervasive. Thus the huge gap between employment in the public sector and private and social sectors

The personnel working at that time in public administration were, to a large extent, the same as under the previous regime. They were people who were chosen primarily for their loyalty to the Party. Although many of them were experts in their respective fields, they lacked, however, the necessary knowledge and skills to implement a modern, democratic public administration.

This situation was further exasperated by the sharp increase of administrative tasks. When Slovenia became an independent state in 1991 they had to establish a complete public administration of a sovereign state. New state functions had to be assumed by the administration which was both inadequately prepared and under equipped. As the result, the administration was not able to perform at an optimal level. Therefore, the institutional reform in Slovenia needed to focus urgently on adapting Slovenia's public administration to the new administrative demands and on enhancing its institutional capabilities. Compounding the deficiency of the existing public administration, the presence of "parastatal administration" which was prevalent in the former Yugoslavia also impeded on the functioning of the new state. Under the principle of "Self-Management", public services were performed by socially-owned independent agencies. These socially-owned independent agencies were not given the legal status of public enterprises; instead they were regulated and controlled by the parastatal regulatory bodies. Parastatal regulatory bodies, therefore, were responsible for planning, organizing, and financing, regulating and supervising the provision of public services. Therefore the transformation of Slovenia demanded reorientation and reorganization of both the parastatal administration and the socially-owned independent agencies. The process of transformation proceeded on a slow pace and produced various legal, administrative and managerial issues. The third specific feature of Slovenian public administration was the "communal system", which was a mixture of local government and local administration. They performed tasks of local administration and functions of the local government, making them unaccountable. In the same vein, these local governments at times assumed functions of the state creating confusion of policies and irregularities. The reform of the "communal system" was an important issue which needed to be addressed urgently.

NEED FOR INSTITUTIONAL REFORM AT 1993

In the past the Communist Party was the highest authority in the country. Its eventual fall resulted in a crisis for Slovenia's institutions, its legal system and decision-making systems. The appearance of numerous political parties accompanied by fierce power struggles led to a further increase of uncertainty and a further prolongation of Slovenia's transition period.

The need for institutional change was generally well-accepted in Slovenia. But frequent political deadlocks, lack of defined competencies, and an inadequate legal system made it a very slow process. Up until then, the haphazard and slow tackling of these problems caused legal loop-holes, conflicting laws and overlapping jurisdictions, all resulting in legal and institutional instability. More pressing problems such as establishing institutions of an independent state, agreeing on a border with Croatia, determining citizenship of former Yugoslav citizens and achieving international recognition, took precedence.

All this was coupled with the economic crisis. A planned economy can only work in highly predictable circumstances and is not equipped for the rapid rate of change that Slovenia experienced after independence. An example of this was the proposed restructuring of the steel industry in Slovenia in 1990.

"Where no progress has been achieved despite government intervention and the nationalization of the steel-producing companies. The reasons for failure range from a lack of execution and the dominance of local interests at plan level, through a lack of competence and the inability to take decisions at corporate level, right up to a lack of understanding and a reluctance to make hard choices at government level."

The domestic events combined with such unfavourable external developments as recession in the world steel industry and the collapse of the Yugoslav market, led to grave consequences: more than 12,000 jobs were endangered, about DM 1 billion of assets were unproductively employed, and close to DM 100 million subsidies were spent annually, leading to nationalization, a new DM 500 million bail-out by the new government, and prospects that continued to look precarious."¹³

Reform of the administrative system in Slovenia required changing the legal system and changing the way things were done. As the process of legal reform was extremely long, it was generally agreed that it was quicker and easier to reorganize the administrative system. This implied changing the human element of the system. This did not require a complete replacement of the existing employees, but required changes concerning their work habits, attitudes and thinking. More emphasis needed to be given to professional

¹³ The McKinsey Quarterly, "A new iron curtain?" Number 1, 1993, p. 27).

knowledge, merit, apolitical performance, promotion of new ideas and initiatives and a clear distinction between professional officials and political functionaries. No ready-made models could be adopted for the reform process. Solutions had to be invented which were tailored to the cultural background, traditions, expectations and experience of the people of Slovenia.

The reform of public administration was not a one-step action in which a modern and democratic public administration could be created; it was rather a long process of searching and applying transitional solutions in organization and in function of public administration; this was not only because of the specific transitional needs of Slovenia, but also because only limited human and material resources were available for the administrative reform and because the public administration at that time could take only a limited amount of organizational stress.¹⁴

Inefficiency & Ineffectiveness of Slovenia's public Administration & civil service System at 1993

Drawing on extensive discussions with many representatives of the Slovenian Government and relevant publications from Professor Rajko Pirnat¹⁵ (Annex 8) and Danica Purg¹⁶ (Annex 9) the following observations were made by the author of this article in collaboration with his team of experts from Switzerland and Slovenia.

PUBLIC ADMINISTRATION

Lack of Efficiency within the public sector resulted in a general tendency of duplication of work. While certain work was not done at all, some work was started but not completed and other work done was unnecessary. Consequently, the public administration tended to be overburdened with unjustified workload and under performing concerning critical tasks. The output of individual administrative units tended to be unstable, varying in quality and unpredictable in meeting deadlines.

Information Gaps caused by the rapid changes in Slovenia rendered civil servants at different levels of the administration outdated regarding current policies and procedures. Civil servants and the public at large were confused about which laws and procedures

14 Pirnat, Rajko: "Public Administration Reform in Slovenia", paper delivered during the Seminar on Comparative Administrative Systems, Ljubljana, 18-20 May 1993.

15 Pirnat, Rajko; idem.

16 Purg, Danica: "Developing Managers for Eastern and Central Europe: The Missing Ingredients: Professional Management and Leadership. The Case of Slovenia", Development and International Cooperation, Vol. VIII, No. 14-15, June -December 1992, pp 215-224.

were valid. Illegal activities remained unchecked resulting in a general erosion of public order and the government's credibility.

Structure and Functions not Synchronized: Many new laws were being drafted, some were approved by Parliament, and others were in the process of being amended. What was often missing, however, were the corresponding organizational structures and management functions which were needed to implement the new laws. Also, adequate channels of communication and cooperation within and between ministries essential for the functioning of an administration were not yet established. Increased institutional uncertainty discouraged civil servants from showing initiative and taking decisive action.

Excessive Litigation: Amid the public, complaints increased. More and more the lack of clearly defined structure and functions forced the administration to deal with crisis situations which made it less and less possible to attend to mid-term and long-term policy and strategic issues. As a consequence, morale of civil servants was affected resulting in loss of qualified and competent staff.

Frequently mentioned remedies of these problems consisted of, e.g., simplification of work procedures, rationalization of structures of Ministries, clarification of roles and responsibilities of civil servants, improvement of work methods, better utilization of staff and improvement of policy-making instruments. However, at that moment, Slovenia was faced with both skill shortage and objective institutional bodies to undertake these pressing reform measures.

PUBLIC SERVICES

Inefficiency and Ineffectiveness: Slovenia's public services manifested itself in many sectors. Some of these performance problems related to the use of outdated technology and equipment. A large number of performance problems however, were related to organization and management shortcomings. The latter was illustrated by the situations prevailing in the water supply and liquid waste disposal sectors. An analysis of the problems in these two sectors indicated similar issues to that of the public administration and required management interventions.

Perceived Lack of Price Equity: The price for services in both sectors varied greatly from place to place depending on quality, availability of services, and other administrative criteria. Depending on the localities the high costs for installing new facilities were often passed on to individual customers on an extremely unequal basis. The cost accounting systems were virtually non-existent and the country's financial management system was

ineffective, prices were established by the communities, but the factors taken into account in setting the prices were sometimes arbitrary and may be political as well as economic.

Water Pollution: The public was often unaware of the pollution caused by farm and industrial waste. This caused health problems due to the continuous use of contaminated water. Polluters were often left unchecked due to insufficient judiciary and law enforcement infrastructure.

Poor Maintenance: Aging infrastructure lead to water loss, and thus insufficient supply, as well as further contamination due to leakage into the faulty pipelines. Poor maintenance of the past had also led to frequent breakdown of services. There was a need to replace the few facilities and to better maintain the existing ones.

Ineffective Planning was a major cause of inefficiency in the public service in general, and in the water supply and liquid waste disposal sectors in particular. Planning procedures was lengthy, sometimes taking 3 to 4 years, and often the plans were obsolete before they have been implemented.

Insufficient Customer Communication: Not only were there no information dissemination systems available to the consumer, there was no mechanism neither for receiving feedback from the consumer on the adequacy and quality of services being provided.

Ineffective Organizational System: The organizational structure then was dysfunctional. There was practically no coordination or communication between the various administrations involved in each public service sector, both at local and central government level. Up to then, public services were delivered by each municipality in their own way. As a consequence, the services provided differed widely in regard to quality, price, speed, etc and coverage.

Inoperative Regulatory Function: As is the case with public administration in general, regulations were often not being followed or reinforced. Monitoring methods were ineffective and lacking mechanism. Both had rendered the cost of monitoring prohibitive. Furthermore, penalties were negligible and sanctions were difficult to enforce when violations were detected.

Some of the solutions to Slovenia's public services problems were similar to those of the public administration: e.g. simplification of work procedures, rationalization of organizational structure etc. In addition, institutional capacities needed to be developed to enable the public services to better define their functions, establish equitable and cost-efficient pricing mechanisms, and strengthen their respective regulatory mechanisms.

CIVIL SERVANTS

Uncoordinated Recruitment: Since 1989, recruitment and selection of civil servants was decentralized to the individual Ministries. Certain Ministries established a small unit in charge of personnel functions. Personnel quota was set by the Ministry of Finance. This decentralized practice resulted in a variation of skills profiles of the new recruits and a confusion of personnel standards.

Lack of Performance Review: There was never a performance review of Slovenia's civil servants. In the past, civil servants were supervised and controlled by the communist party. Since independence, the communist party no longer operated as a 'shadow cabinet' which resulted in more freedom for individual civil servants, but did also create a vacuum in regard to the effective and efficient performance of Slovenia's civil servants.

Inadequate Work Methods: Difficulties existed in regard to prioritizing of tasks, communicating on horizontal and vertical lines, planning necessary steps for project implementation, time management, and economical mindedness. Up to now; relevant training seminars were practically non-existent.

Outdated Leadership Style: The dominant leadership style was traditionally paternalistic which did not encourage initiative and participation by staff members. As a corollary, civil servants in subordinate positions were not encouraged to take responsibility or to show initiative.

Lack of Service Orientation: Public administration of the pre-independence period was more bureaucratic and less managerial. Civil servants executed orders which in general related to administrative measures. They were not used to considering the citizens at large as customers who are entitled to good quality work and equal access to their services.

Ignorance of Externalities: Policy making and implementation relating to macroeconomics and foreign affairs were centralized in Belgrade during the pre-independence period and had to be established and created after 1991. In addition, many civil servants were not aware of the interdependencies between public administration, business, economics and international relations.

The qualifications of Slovenia's civil servants needed to be reassessed and if seen appropriate they needed to be adjusted to fit the performance requirements of tomorrow. A prequalification system had to be envisaged once the new public administrative law was going to be passed by Parliament. In order to support the current civil servants in improving their work efficiency, massive training programmes needed to be undertaken coupled with complementary organizational consulting in the areas of team work, interdepart-

mental cooperation and management studies. Other measures which fell into the area of civil service codes needed to be examined and redefined as well.

Creating an Administrative Academy and Efficiency Section in Slovenia's Government as Initial Solution to Improve Inefficiencies and Ineffectiveness

Initial contacts between the author of this article and his organization CSEND in Geneva together with colleagues from the Institute of Public Law at the University of Ljubljana led to a full blown joint capacity building project in the field of public administrative reform and institution development. The Project was named Managing Administrative Systems through Training, Education and Research (M.A.S.T.E.R.). The project, financed by the Swiss government, was successfully completed in December, 1996.

As part of the 2.7 million Swiss Franc project, Swiss and Slovene experts helped the Slovenian government modernize its central administrative system by creating two new administrative units and retraining civil servants. The first new unit was given the mandate to assess the effectiveness of Slovenia's public utilities and administration and the second unit's mandate was to retrain and upgrade Slovenia's senior civil servants.

The M.A.S.T.E.R.TM project emphasised teaching the trainees to ask insightful questions through analysing and reflecting on their experiences in solving current issues within the Slovene public sector. Supported by Swiss and Slovene academic advisors, trainees working in teams carried out a total of 18 consulting projects in 1996.

The underpinning change method of the M.A.S.T.E.R.TM project was based on Action Learning and Action Research which emphasised learning through practical work in the real work environment. Consideration was also given to the established adult learning theories so as to ensure the efficiency and effectiveness of the learning process.

As a result of the three year joint project, two new governmental units were established at the end of the M.A.S.T.E.R.TM project. Specifically these were the Department of Organisation and Management Techniques, which focused on management and organisation studies within the public sector of Slovenia, and the Department of Training, later called Administrative Academy, which carries out action-oriented management training and development activities for senior civil servants. Both administrative organisations are fully functioning at the time of writing this article, in other words proved sustainable beyond the conclusion of the administrative reform project.

Main Features of Joint Capacity Building Project

The change method used consisted of a mix of traditional training and consulting and action-learning projects (see Annex 1).

a. Establishing two new administrative units within the central government.

In order to establish these two new administrative units (23 new posts), different steps needed to be undertaken ranging from preparing draft laws and procedures, facilitating budget negotiations within the government and between ministries, to redrafting final decrees and administrative procedures. This institution development process lasted two years and was completed only a few days before the official end of the project.

b. Training Slovene civil servants to become trainers and organizational consultants

Forty civil servants of 35-40 years of age were nominated to the project by their respective ministries. They underwent intense teaching and training on topics ranging from New Public Management to Organizational Consulting. The teaching inputs were conducted by 30 foreign experts from Western Europe, North America and Asia who provided a multitude of functional teaching and consulting inputs in Slovenia and assisted the Slovenian trainees during their complementary study visits to Switzerland.

The selection criteria for this one year intensive and full time learning programme were as follows:

	Track 1 (Organisation & Management)		Track 2 (Management Training & Development)	
	Senior	Junior	Senior	Junior
Level:	University degree (Master or Ph.D.)			
Language:	English proficiency			
Professional representation:	60% social science, economics, business administration, law; 40% engineering, system engineering or other sciences		A balanced mix of expertise on financial management, economics, general management, law, social science, human resources, organizational science, system operations & management	
Regional representative:	70% Ljubljana 30% provinces		>20% from provinces	
Work experience:	5-10 years	2-5 years exp. (in gov't or enterprise)	10 yrs. managerial exp. (gov't or enterprise)	5 yrs. managerial experience
Age:	35-40	25-30	35-40	30+
No of trainees:	10	10	10	10

The selection of the trainees was done jointly by the National Project Director, the two Academic Heads, the Swiss Project Manager and the two Swiss Chief Advisors.

c. Action learning projects to ensure transfer of know-how and to prepare for new jobs.

Upon completion of the basic training phase, the trainees were given the opportunity to apply their newly acquired consulting skills. Under close supervision, they conducted organizational diagnoses of six public utilities and ministries, assessed the need for training of the total Slovene government and established a first three year plan of action of the future Administrative Academy. In order to oversee and facilitate the implementation of the change projects, a National project council was established under the Chairmanship of the Minister of Interior. Another four ministers were also represented on the council as well as the Secretary General of the Slovenian Chancellery.¹⁷

17 For a more detail description of the project see :Yiu, L.; Saner, R. (Editors), "Compendium of Pilot Projects for Improving Working Procedures in the Slovene Public Administration and Training Modules", Institute of Public Administration, Ljubljana, 1997.

CONCLUSION

The goal of this article was to describe how transaction costs can be caused by administrative inefficiencies and policy ineffectiveness and to illustrate the reported symptoms of inefficiencies and ineffectiveness through the use of a case example namely that of Slovenia as it emerged from the former Yugoslavia around the period of 1991-1993.

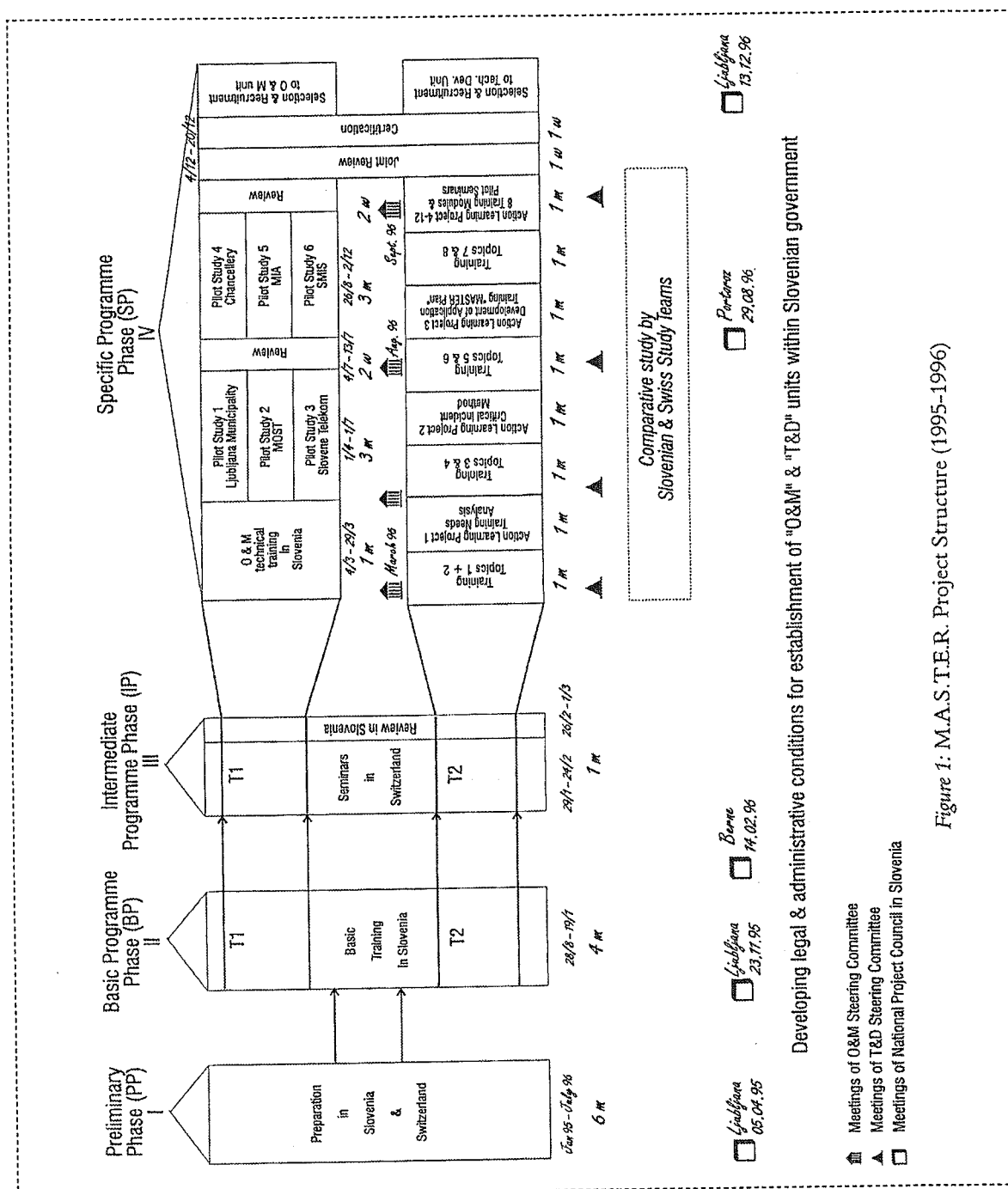


Figure 1: M.A.S.T.E.R. Project Structure (1995-1996)

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TRANSACTION COSTS IN THE MACEDONIAN ECONOMY



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- 111 EU Regulatory Framework for Utilities: Energy and Electronic Communication**
Prof. Nevenka Hrovatin, Ph.D.
- 121 Administrative Inefficiency and Policy Ineffectiveness as Root Causes Leading to High Transaction Cost: Example: Slovenia 1993-1996**
Raymond Saner, Ph.D.
- 135 Introducing the Concept of Trade Facilitation**
Zlatko Veterovski
- 149 The Impact of Bankruptcy Procedures on Economic Agregates for Improving the Economic Climate**
Kiro Spandzev

157 FINAL CONFERENCE

- 159 Discovering and Measuring Transaction Costs in the Macedonian Economy**

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