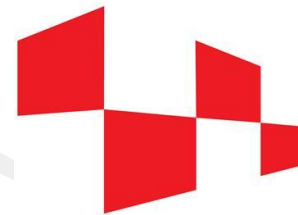




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EVALUATION OF STATE FINANCIAL ASSETS IN THE FORM OF SHARES AND STAKES IN ENTERPRISES OWNED BY THE REPUBLIC OF CROATIA

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12th International conference "Challenges of Europe"
Bol, Island Brač, 17-19 May, 2017

Content:

1. Introduction
2. Framework of coverage, classification, measurement and evaluation of state assets
3. Legal and institutional framework of management of financial assets owned by the Republic of Croatia
4. Coverage of Registry of state assets and classification of financial assets
5. Characteristics of data disclosed in the Registry of state assets and their applicability
6. Conclusion

1. Introduction

- State assets in the Republic of Croatia isn't classified, recorded and evaluated in enough adequate way
- It is necessary to ensure institutional preconditions, i.e. to determine strategy and management plan in order to achieve rational and quality financial assets management
- After more than 20 years of state establishment the question of recording of state financial assets as well as plan for state assets usage isn't solved
- 2013 – Strategy for management and disposal of state assets for the period from 2013 till 2017 was brought

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- The main precondition of that Strategy is that all assets which are used from public sector should be evaluated and recorded in state books
 - Assets of State and local and regional governments is financial and non-financial assests owned by the State and local and regional governments – Art. 61 State Budget Act
 - Focus on shares and stakes
 - The biggest part of financial assets of general government is in enterprises in which state has majority or minority stakes
 - Financial asset is not diversified and is not transformed into marketable instruments

2. Framework of coverage, classification, measurement and evaluation of state assets

- The most appropriate classification of assets for state units is:
 - ❖ Cash
 - ❖ Financial assets
 - ❖ Physical assets
 - ❖ Intangible assets
- Assets classification in budget accounting in the Republic of Croatia accents financial and non-financial assets
- State balance sheet - obligatory financial statement which contains data about the condition of state assets classified by economic classification according to prescribed accounts from unique budget chart of accounts

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- According to The Act on Management and Disposal of Assets owned by the Republic of Croatia state assets consist of:
 - a) Shares and stakes in enterprises owned by the Republic of Croatia
 - b) Real estate owned by the Republic of Croatia
 - c) Shares and stakes in enterprises owned by State agency for deposit insurance and bank resolution
 - d) Shares and stakes in enterprises, real estate owned by intitutes and other legal entities of the Republic of Croatia
 - e) Previous assets of abolished Governement asset management agency
 - f) Other assets

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- Recognition and measurement is connected to applied basis of accounting as a base characteristic of accounting and reporting system
 - Asset valuation is carried out on accrual basis with the historical cost method which means that assets are shown at their book value and revalued amount
 - For determination of assets value according to accrual basis and according to International public sector accounting standards following measurement basis can be used: purchase price, current price, market price, replacement costs, net sales price, value in use.

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- Above mentioned measurement basis in the case of state assets are amended with the measurement according to symbolic value
 - Symbolic value is certain estimated value which purpose is not to present assets by its real, fair and recoverable value but to represent certain asset positions in financial statements without pretension to determine its real value
 - There is few reasons for that: assets is not intended for sale so precise real values are not necessary, asset is permanently owned by the state and only exact evidence about it is needed

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- For accounting treatment of financial assets an International public sector accounting standard 29 Financial instruments: Recognition and measurement is relevant
 - In the Republic of Croatia in budget accounting IPSAS are not in direct application
 - In Instruction it says that according to the article 104 of State Budget Act the value estimation of assets is basically conducted by accrual basis with the application of historical cost method.
 - The Instruction is not precise about accounting treatment of financial assets.

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- According to IPSAS 29 when financial assets is initially recognized subject will measure it at its fair value increased for transaction costs which can be directly assigned to achieving or issuance of financial assets in case that financial assets is not measured by fair value through surplus/deficit
 - With the purpose of financial assets measurement after initial recognition IPSAS 29 classifies financial assets into four categories: financial assets at fair value through profit or loss which include assets which is held for trading; held to maturity investments such as obligatory securities and preferential shares; loans and receivables and financial assets available for sale

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- After initial recognition the subject has to measure financial assets including derivatives which are assets at their fair value without deduction of transaction costs which can arise when selling or other reclassification except for following financial assets:
 - ❖ Loans and receivables to be measured at amortized cost using the effective interest method
 - ❖ Held to maturity investments which should be measured at amortized cost using effective interest method
 - ❖ Investments in proprietary instruments which don't have market price on active market

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- Fair value is the price that two parties are willing to pay for an asset or liability in an orderly transaction.
 - The hierarchy of fair value indicators according to IPSAS 29:
 - ❖ The best evidence of fair value is the price that quotes on an active market
 - ❖ In opposite, subject applies the method of estimated value which rely on market data and contain market transactions on newest date, according to current value of other instrument that is quintessential congenerous as concerned instrument and then through analysis of discounted cash flow or methods for option price determination

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- It arises that according to IPSAS 29 financial assets should be measured at fair value initially and subsequently.
 - In order to apply fair value it is necessary to ensure numerous previous conditions and assumptions

3. Legal and institutional framework of management of financial assets owned by the Republic of Croatia

- In state assets management emphasis is given on formation of Registry of state assets
- Establishment of the Registry opened a question who is obliged to send data into the Registry, i.e. a question of the owner or owner's rights opened in comparison to users or right to use as well as the criteria of coverage and classification of assets and its recognition and measurement
- In attempt to make a distinction between the framework and economic nature of the assets in legal framework in the Republic of Croatia the emphasis is put on the distinction of ownership from management rights and from rights to use

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- Terms of management and assets disposal are defined by The Act on Management and Disposal of Assets and by the Strategy for management and disposal of state assets from 2013 till 2017
 - According to The Act on Management and Disposal of Assets (Narodne novine 2013) management is entrusted to Central state property management administration which acts as the Ministry of state assets from 13th November 2016 after the Act on amendments on the Act of organization and scope of Ministries and other central government bodies

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- With the Ministry of state assets there is also Restructuring and sale center.
 - The activity of the CERP includes management of shares and stakes in enterprises owned by the Republic of Croatia and which are not defined as enterprises from strategic and special interest for the Republic of Croatia, as well as shares and stakes in enterprises owned by Croatian pension insurance institute and State agency for deposit insurance and bank resolution for shares and stakes in enterprises
 - According to data on the 31st December 2016 portfolio managed by the CERP was 2.150.740.520 kn for the portfolio which is managed by CERP to 50% in the subscribed capital of enterprise hence 4.233.163.160 kn for the portfolio which is managed by CERP more than 50% in subscribed capital of the enterprise.

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- In the Resolution on establishing a list of enterprises and other legal entities of strategic and special interest for the Republic of Croatia (Narodne novine 2013b, 2015, 2016) there are enterprises from strategic interest in which the Republic of Croatia realizes strategic besides economic goals
 - In the context of the establishment of the system for efficient state assets management and reporting on financial position of the state and in accordance with relevant provisions of The Act on Management and Disposal of Assets owned by the Republic of Croatia, Resolution on registry of state assets and State Budget Act the Instruction to the recognition, measurement and recording of assets owned by the Republic of Croatia was issued

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- Obligated users of that Instruction are budgetary and non-budgetary users of state budget, budgetary and non-budgetary users of local and regional government and other users of state assets
 - According to the Instruction analytical evidence and secondary books about financial assets – shares and stakes must contain at least data and information prescribed by the Resolution about registry of state assets
 - Regarding presenting of asset value all types of asset, individually and in total must be presented in value

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- According to the Instruction and article 104 of State Budget Act evaluation of asset value is basically carried out at accrual accounting basis with application of historical cost method
 - Concrete methods for recognition, measurement and evidence of financial assets owned by the Republic of Croatia are not given in the Instruction

4. Coverage of the Registry of state assets and classification of financial assets

- Began in 2014
- The base and internet application of the registry are established according to Resolution about state assets
- New data about state assets are disclosed on a monthly basis
- Registry functions on the basis of delivered data
- Types of assets in Central registry are real estate, shares and stakes in enterprises while the registry doesn't include other types of state assets

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- Documentation about state assets is dispersed in different evidences of state institutions
 - Also, certain types of state assets are completely omitted from accounting and other evidences or data are uncompleted due to its specificities and applied accounting concept
 - The above mentioned brings to conclusion that data about state assets presented in consolidated balance sheet aren't real
 - In order to consolidate evidence about assets in the main book of state treasury the list of state assets should be made

5. Characteristics of data disclosed in the Registry of state assets and their applicability

- In the Registry of state asset (Ministarstvo državne imovine, 2016) on date 29th November 2016 there are shares in 383 enterprises and stakes in 209 enterprises that are registered as limited companies.
- Those data include: name of the joint-stock company or legal entity / limited companies; place and headquarter, code of securities, personal identification number, value of subscribed capital and currency, number of issued shares and nominal value of one share, ownership, percentage of ownership of the Republic of Croatia, ownership of other state holders as well as percentage of ownership of other state holders.

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- Value of shares or stakes is given as nominal value of subscribed capital and nominal value of one share.
 - Ownership of the Republic of Croatia and other state holders is given at nominal value of ownership (which is compatible with the number of shares and stakes) and as a percentage of stakes in total capital of an enterprise.
 - The main characteristic of shares and stakes evidence in enterprises in the Registry is static of the data (on a certain date) and nominal value of the subscribed capital.

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- The Registry doesn't include data about changes on the capital that are arising from business (earned capital).
 - Instructions for data management don't imply the fair value concept for exposure of portfolio value of state assets for shares of enterprises that are included in the stock-market.
 - Subsequent valuation of shares and stakes is prescribed for the case if shares and stakes are sold.

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- It was already emphasized that shares and stakes evidence in enterprises in the Registry is static and subscribed capital is expressed in nominal value without representing any changes on the capital.
 - Such evidence opens a question in which measuring those data about stakes reflect the value of state assets which is used by an enterprise hence state as a majority owner of enterprises from public interest.

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- Settled research question where and how public asset is presented in financial statements of enterprises from strategic interest is solved different.
 - Infrastructure can be presented:
 - In the balance sheet of an enterprise (as its assets)
 - In the under balance sheet of an enterprise in which is separately presented public assets and public capital or
 - In off balance sheet records (borrowed assets with the right to use).

6. Conclusion

- By analysis of available sources and data base about legal, institutional and accounting framework for state asset management it can be concluded that in the Republic of Croatia state assets isn't classified, recorded and valuated in efficient way.
- There are legal and institutional shifts which make preconditions for efficient state asset management but also there is a lot of space for improvement.

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- According to legal framework state asset management is entrusted to Central state property management administration which is established as the Ministry of state assets from November 2016 and also to Restructuring and sale center (CERP). The emphasis is put on formation of the Registry of state assets when managing state assets in the Republic of Croatia.

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- By analysis of available data it can be observed that financial assets – value of shares or stakes is expressed by nominal value of subscribed capital and nominal value of one share and the ownership of the Republic of Croatia and other state holder expressed at nominal value of ownership (which matches the number of shares or stakes) and as the percentage of stakes in total capital of enterprise.

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- The main characteristic of such an evidence of shares and stakes in enterprises in the Registry of state assets is static of data and nominal value of subscribed capital without any changes in capital and doesn't consider fair value concept for portfolio valuation of state asset for shares of enterprises that are on stock-market.

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- Such evidence opens a question in which level those data about stake in capital represent the value of state assets which is used by enterprise i.e. state as a majority owner of enterprises from strategic interest.
 - It can be concluded that data from the Registry cannot answer the question regarding the value of financial assets owned by the state and that those are just input data into more precise value determination of certain positions of financial assets.

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- The above mentioned is emphasized by different approach in the evidence of public assets in financial statements of public enterprises which can have as a consequence that public assets isn't presented neither through state stakes in the capital of public enterprises (balance sheet of state assets) neither through assets of public enterprises (balance sheet of public enterprises).

AKNOWLEDGMENT

This paper is a result of Croatian Science Foundation's funding of the project 8509 Accounting and financial reporting reform as a means for strengthening the development of efficient public sector financial management in Croatia. Any opinions, findings, and conclusions or recommendations expressed in this material are those of the authors and do not necessarily reflect the views of Croatian Science Foundation.

Thank you for your attention!

Questions?

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