CUBA’S PERFECCIONAMIENTO EMPRESARIAL LAW: A STEP TOWARDS PRIVATIZATION?

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1 INTRODUCTION

On August 18, 1998, Cuba enacted Law-Decree No 187 (“Law 187”) 1 This law provides the framework for Cuba’s Enterprise Optimization (Perfeccionamiento Empresarial) Program (“EOP”) 2 The program seeks to establish a foundation and to set specific guidelines for a process whose goal is to improve efficiency and productivity in Cuba’s state-owned enterprises (“SOEs”)

Cuban sources describe Law 187’s intent as improving the national economy through the enhanced efficiency of the SOEs, always in the context of continued state ownership and state control over the enterprises 3 Notwithstanding Cuba’s intent to retain state ownership of the SOEs, it is of interest to the future development of the Cuban economy to determine whether, as a practical matter, the law constitutes a meaningful first step towards what some believe is the inevitable privatization of Cuban SOEs 4

This Article seeks to address this question. To assist in the analysis, the Article compares Cuba’s EOP with steps taken in the early stages of the privatization programs of some other countries

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2 The literal translation of “perfeccionamiento empresarial” is “enterprise perfecting”


4 See, e.g., MATIAS TRAVIESO-DIAZ, THE LAWS AND LEGAL SYSTEM OF A FREE-MARKET CUBA ch 6 (1996)
that have undertaken, to some degree or another, the privatization of SOEs. Thus, Section 2 of the Article provides a summary of the actions that are generally required to prepare an SOE for its privatization. Section 3 describes the genesis, framework and current status of the EOP. Section 4 presents a summary of the actions taken by the governments of China and former East Germany in the early stages of their respective privatization programs. Those countries were selected because they represent opposite poles in the range of potential approaches to SOE privatization. Section 5 compares Cuba’s EOP with the methods adopted by the comparison countries to determine whether Cuba’s EOP is consistent with the processes utilized elsewhere in moving towards privatization. Finally, Section 6 offers the Author’s conclusions as to whether the EOP is a meaningful step towards the implementation of a privatization program in Cuba.

2. STEPS IN PREPARING AN ENTERPRISE FOR PRIVATIZATION

This Section provides, as necessary background to the discussion that follows, a brief summary of the actions that are generally required to prepare an SOE for privatization. The discussion does not include addressing external conditions, such as outstanding judgments, liens or claims against the enterprise. Clearly, such “clouds on the title” of the state to the enterprise need to be removed before the SOE can be sold. In the case of Cuba, a factor that may complicate the prospects for privatization is the existence of a large number of claims by U.S. nationals, Cuban Americans, and Cubans living in the island for the expropriation of their assets after the Cuban Revolution. Cuba has failed to compensate any of these groups, and thus they all have outstanding claims against the state, and may seek restitution of the confiscated assets in lieu of compensation or other remedies. The outstanding expropriation

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6 Cuba may need, for political reasons, to provide comparable remedies to claimants living on the island with those given to Americans and Cubans living abroad. See, e.g., Rolando H. Castañeda & George P. Montalván, Economic Factors in Selecting an Approach to Confiscation Claims in Cuba, 5 CUBA IN TRANSITION 227, 236-37 (1995), available at http://lanic.utexas.edu/la/cb/cuba/asce/cuba5
claims must be addressed early in Cuba's transition to a free-market society in order, not only to make possible the privatization of SOEs, but also to restore full relations with the United States, to foster political stability, and to encourage foreign investment. To the extent that any expropriation claims are resolved through restitution of the assets to their former owners, privatization of those properties will automatically occur.

A frequently used privatization technique is to sell the SOE as an ongoing concern. Frequently, however, SOEs cannot be sold on an "as is" basis, and privatizing them may require a wide array of preparatory restructuring measures. These measures seek the transformation and reorganization of poorly performing SOEs into profitable, self-sufficient business concerns that may be attractive investments for the private sector.7 In most cases a necessary preparatory action is that "a feasibility study should be conducted to determine whether the enterprise can be sold as an ongoing concern or should be liquidated."8

Assuming the enterprise can be sold as an operating entity, it should be prepared for the sale.9 This requires: (1) converting the state-owned enterprise's accounts and financial records into a form that meets international accounting standards and allows the preparation of reliable financial statements; (2) writing a report identifying any potential problems with the sale; (3) engaging advisors to help address legal issues related to the sale and to prepare the necessary legal documents; and (4) appointing an economic/financial advisor to valuate the company's assets and liabilities and perform other financial analyses.10

The enterprise may also have to be restructured to make it more attractive to potential purchasers. First, if this has not been done, the enterprise should be transformed into a corporation, to

10 Id. at 43.
provide flexibility in the format of the subsequent sale, which may proceed through the sale of the enterprise’s assets or of its corporate stock.

Other necessary structural changes may include refinancing or writing off debt, eliminating unprofitable lines of business, reducing the number of employees, hiring new managers, and disposing of assets and liabilities that make the enterprise more difficult to sell.\footnote{ACCOUNTING, supra note 8, at 14-15.}

The discussion that follows examines the extent to which these steps have been taken by Cuba’s program and, if not, whether the measures taken as part of the EOP are likely to facilitate taking those steps at the onset of an SOE privatization program.

3. Cuba’s Enterprise Optimization Program

3.1. Background

The management of SOEs in state-dominated economies, such as Cuba’s,\footnote{12 Private ownership of income-producing property in Cuba is limited to small plots of land in the hands of farmers, and the assets of joint ventures between state enterprises and foreign investors. CONSTITUCION DE LA REPUBLICA DE CUBA, reprinted in Gaceta Oficial art. 19-23 (Aug. 1, 1992).} suffers from a number of shortcomings that prevent the effective operation of the enterprises.\footnote{13 See, e.g., JOZEF M. VAN BRABANT, PRIVATIZING EASTERN EUROPE: THE ROLE OF MARKETS AND OWNERSHIP IN THE TRANSITION 23, 26 (1992) (explaining that some of the problems caused by centralized authority such as political patronage and a constrictive bureaucracy have dire economic consequences, including misallocation of capital, natural resources, and even land).} Basically, the government uses SOEs to further its social and political goals. The state’s lack of concern for their efficient operation renders the SOEs uneconomical and, in most cases, incapable of functioning without financial aid.\footnote{14 Horst Brezinski, The Autonomous Sector in a Society of Shortage, in PRIVATIZATION AND ENTREPRENEURSHIP IN POST-SOCIALIST COUNTRIES: ECONOMY, LAW AND SOCIETY 33 (Bruno Dallago et al. eds., 1992).} As a result, SOEs become a burden on the state’s finances and may cause imbalances in the country’s economy.

In Cuba, the inefficiencies in the operation of SOEs were first addressed by the country’s armed forces (“FAR” or “Fuerzas Armadas Revolucionarias”) through a program initiated in 1987 to improve the operation of the numerous enterprises managed by the
FAR. The FAR program progressed gradually from four firms in September 1987 to essentially all FAR-operated enterprises ten years later. However, the FAR enterprise upgrading remains incomplete after fourteen years.

Cuba's EOP, as instituted by Law 187, is an expansion to the entire SOE apparatus of the FAR EOP, which the country's leadership judged a success. The Fifth Congress of the Cuban Communist Party adopted in October 1997 an Economic Resolution that praised the FAR experiment as "particularly relevant" to improving the performance of the Cuban economy and called for the "extension to other areas of the economy of the principles followed by the Armed Forces towards the perfecting of their enterprise system, to be carried out to the fullest extent, in an orderly and programmed manner, taking into account the characteristics of each activity." Issuance of Law 187 followed after "a broad process of consultation."

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15 The FAR operate many enterprises in several segments of the economy, including tourism. For example, Gaviota S.A., organized in 1990, owns resort hotel properties that at the end of 1998 accounted for seven percent of Cuba's hotel rooms and accommodated ten percent of the visitors to the island. See Grupo de Turismo-Cuba, Gaviota, S.A., http://www.gaviota.cubaweb.cu/espanol/index.html.


17 In the annual review meeting on the status of the EOP program for the FAR, General Raul Castro, head of the FAR, stated that five enterprises still had not approved optimization plans and noted the existence of widespread resistance to linking employee salaries to enterprise performance, leading to the formulation of unrealistic budgets and business plans. Remarks of General Raul Castro, El Perfeccionamiento Empresarial Tiene que ser un Camino sin Retroceso, GRANMA (May 18, 2001), available at http://www.granma.cubaweb.cu/2001/05/18/nacional/articulo1.html.

18 Enterprises wholly owned by the state currently provide employment to over seventy percent of the Cuban workforce. Vascos, supra note 3.


20 Law 187, supra note 1.
3.2. Framework Created by Law 187

3.2.1. Fundamental Principles

The objectives of Law 187 are set forth in the "General Bases for Enterprise Optimization" (Bases Generales del Perfeccionamiento Empresarial) ("General Bases"), which are part of the law.21 The "central objective" of the EOP is "to increase to the maximum the efficiency and competitiveness of SOEs by giving them such powers, and establish such policies, principles and procedures, as will tend to foster the initiative, creativity and accountability of all managers and workers."22 By linking the maximization of efficiency and productivity with the grant of additional "powers" to the SOEs, the General Bases establish the fundamental premise of the legislation, i.e., that by decentralizing the management of the SOEs within established "policies, principles and procedures," will make the enterprises more efficient. Implicit in that premise is the assumption that decoupling the management of the enterprise from its ownership will be beneficial to the SOE's economic health. For that reason, under the EOP the state would retain ownership of the SOEs but would allow the enterprise to manage its own affairs in a market environment.23

Another fundamental principle of Law 187, proclaimed in the General Bases, is that the SOEs should become economically self-sufficient.24 Since labor costs are a crucial component of enterprise

21 Law 187 is a very short (less than half a page) document, consisting of an introduction, two articles, one special provision, and two final provisions. Article 1 approves the General Bases which are "an annex" to the law, but which are not included in the copy published in the Gaceta Oficial. Bases Generales del Perfeccionamiento Empresarial (Aug. 18, 1998) [hereinafter General Bases], available at http://www.nuevaempresa.cu/Ol_5.htm. Article 2 of the law authorizes the establishment, by the Executive Committee of the Council of Ministers, of a temporary Government Group headed by the Secretary of the Executive Committee of the Council of Ministers and comprised of five ministers and the head of the Central Bank. The Government Group, assisted by an Executive Secretary, is charged with the review of optimization proposals submitted by SOEs in accordance with the General Bases. The proposals are not to be submitted by the SOEs directly, but through the Organizaciones Superiores de Direccion Empresarial, described below. Id.

22 General Bases, supra note 21.

23 See Empresa Estatal, supra note 16.

24 "Enterprise optimization is based on enterprise self-financing, which requires that the enterprise pay its costs out of revenues and generate a profit." General Bases, supra note 21.
operating expenses, a related principle is that the labor costs should be commensurate with the enterprises' economic performance. To accomplish this, salaries are not to be fixed, but pegged to productivity.\textsuperscript{25} After-tax earnings may, if authorized, be retained by the enterprise as capital reserves.

A corollary to the granting of administrative autonomy to the SOEs is the principle that each enterprise could propose and implement its own "tailor-made" approach for implementing its version of the EOP—subject to approval by several layers of bureaucracy.\textsuperscript{26}

Other fundamental principles are also set out in the General Bases.\textsuperscript{27}

3.2.2. Organizational Framework\textsuperscript{28}

As provided by Law 187, the main instruments in the implementation of the EOP are the Government Group and its Executive Secretary, both part of the Executive Committee of the Council of Ministers. Below the Government Group are overseeing organizations known as "Higher Organizations of Enterprise Direction" (Organizaciones Superiores de Direccion Empresarial) ("OSDEs"). The OSDEs are set up by the Ministry of Finance for the purposes, among others, of coordinating the EOP efforts of the various enterprises in the same area of business, overseeing the preparation of each enterprise's EOP, business plan and budget, and submitting and defending those documents before the enterprise's governing board and before the Ministry responsible for the enterprise's economic activity.\textsuperscript{29} Within each OSDE, there is a "governing board" consisting of five members chosen by the Executive Committee of the Council of Ministers.\textsuperscript{30} The board over-

\textsuperscript{25} Id. The General Bases declares bluntly: "Rewards will be given to results, not efforts." Id.

\textsuperscript{26} Id.

\textsuperscript{27} For example, the management of each enterprise is to have the authority to develop annual plans and budgets and to manage the enterprise's physical and financial assets, as well as its labor force. Id.

\textsuperscript{28} The discussion in this Section is based on sections 1.2 and 2 of the General Bases.

\textsuperscript{29} General Bases, supra note 21, § 2.1.

\textsuperscript{30} Id. § 3.1. The members of each board include one representative from the Ministry of Economy, one from the Ministry of Finance, one from Cuba's Central Bank, and another from the local government. The last member is an expert in the SOE's specific industry. Id.
sees each enterprise’s business plan and budget and the execution of the plan, and approves new lines of business.\textsuperscript{31} This structure is similar to those of the board of directors of a corporation in a capitalist country, except that under the Cuban program, the board’s sole shareholder—whose interests are represented by the board—is the state.

At the enterprise level, there are one or more parallel bodies to the governing board of the OSDE. These bodies, whose establishment is compulsory, have the generic name Collective Direction Organs (“CDOs”), but in a given enterprise, they might be denominated “governing council, management council, or board of directors, among others.”\textsuperscript{32} Their functions, modes of operation, and composition are established by the enterprise’s General Manager. The CDOs provide advice on business strategy and on how to develop and implement the enterprise’s business plan. Thus, the CDOs help manage the day-to-day affairs of the enterprise. CDO recommendations become mandatory within the enterprise if the General Manager approves them.

3.2.3. \textit{Stages in the EOP}\textsuperscript{33}

The EOP is to be implemented in seven stages. First, the workforce and the labor unions must be trained to accept and support the process, and become active participants in it.\textsuperscript{34} This stage focuses on explaining to the workforce the general principles of the EOP and how they are accomplished, and securing through persuasion the workers’ active cooperation.

The second stage is to conduct an initial diagnostic analysis of the enterprise. This analysis is performed either by the SOE or “an external group,” depending on the condition of the enterprise. The analysis evaluates the enterprise’s history, its current status, its future prospects, the state of its resources, its internal culture, and its technical and managerial functions. The main purpose of the

\textsuperscript{31} Id. § 3.1.2.

\textsuperscript{32} Id. § 3.2.

\textsuperscript{33} These stages are described in section 1.2 of the General Bases, supra note 21.

\textsuperscript{34} The possibility that increased enterprise efficiency will result in employee layoffs is addressed quite obliquely, as follows: “As workers become available, the most appropriate measures will be taken (in coordination with the organizations in the sector and the local labor oversight authorities) so that no worker is left unprotected.” General Bases, supra note 21, § 1.2.4.1.
analysis is to identify internal and external problems and determine the manner in which the enterprise is being inefficient.\textsuperscript{35}

The third step is an evaluation of the results of the diagnostic analysis of the enterprise. This evaluation is conducted by the Government Group of the Executive Committee of the Council of Ministers. The purpose of the evaluation is to determine whether the enterprise should be allowed to continue to implement the program.\textsuperscript{36}

The fourth step is to have each enterprise selected for participation in the EOP develop an optimization proposal (designated as "\textit{expediente de perfeccionamiento empresarial}" or "EPE"). The EPE is in reality a detailed business plan that summarizes how the enterprise proposes to optimize its operations. The EPE is required to address, among other subjects, the enterprise’s business objectives, its functions, its organizational structure, the proposed changes in the manner in which the production of goods and services is accomplished, and the methods to implement internal controls, planning, contracting, human resource management, marketing, and information systems.\textsuperscript{37} Each proposed change to the SOE is to be evaluated in terms of cost and anticipated economic results. The EPE is to set forth proposed economic performance objectives and compare them to the enterprise’s performance prior to implementation of the EOP. The EPE must also include an implementation schedule.

In the fifth stage,\textsuperscript{38} the EPE is submitted by the enterprise to the OSDE that oversees the business sector. The OSDE, in turn, (presumably, after review and discussion with the enterprise) presents the EPE to the Government Group of the Executive Committee of the Council of Ministers, which determines whether the proposed business plan satisfies the optimization principles set forth in the General Bases and rules on whether the projected economic performance is acceptable. If the EPE is approved, this approval is communicated in writing to the enterprise, the OSDE, the corre-

\textsuperscript{35} Id. § 1.2.4.2.

\textsuperscript{36} Id. § 1.2.4.3. The General Bases do not specify the consequences of a finding that an enterprise does not qualify for the EOP. Presumably, however, since the Cuban Government has placed great emphasis on the implementation of the EOP, those enterprises that are deemed unqualified to participate in the program may be candidates for eventual dissolution.

\textsuperscript{37} See id. § 1.2.4.4. (describing the functions and operations of an EPE).

\textsuperscript{38} See id. § 1.2.4.5. (explaining the OSDE’s review and analysis of the EPE).
sponding Ministry and other state instrumentalities, and the enter-
prise is released to implement the EPE.

The sixth stage is the implementation of the EPE by the enter-
prise.39 The seventh stage is described as a continuous process of
increased optimization, to be undertaken once the initial EPE ob-
jectives are accomplished.40

3.3. Functional Areas to be Addressed in the EOP

In implementing the EOP, each enterprise must address a
number of areas of enterprise activity or “subsystems,” which are
defined in Section 1.3 of the General Bases to include:

- General Organization
- Management Methods and Styles
- Organization of the Production of Goods and Services
- Organization and Oversight of the Work Processes
- Quality Assurance
- Labor and Salary Policies
- Planning
- Contracting
- Accounting
- Cost Accounting
- Internal Controls
- Taxes and Internal Finances
- Outside Contracting
- Internal Communications
- Prices
- Human Relations
- Marketing

Each of these subsystems is addressed in a separate section of
the General Bases. The level of discussion is, in most instances,
non-specific: the General Bases only provide broad concepts with-
out the accompanying performance standards. For example, sec-
tion 8.3 describes the “Valuation and Data Presentation Principles”
applicable to enterprise accounting systems as follows:

39 General Bases, supra note 21, § 1.2.4.6. (describing the process of imple-
mentation for the EPE).
40 See id. § 1.2.4.7.
The financial statements issued by an enterprise must be prepared using adequate and uniform techniques.

To do this, and based on generally accepted principles in effect in the country, it is necessary to establish general accounting norms, giving priority to those qualities that accounting information must possess.

The accounting norms must be uniform, appropriate, and explicit, with the objective of presenting information that is adequate, correct, and timely. They must also be easy to interpret and useful to all their users.\footnote{General Bases, \textit{supra} note 21, \S\ 8.3.}

The rest of the accounting section (section 8) of the General Bases sets forth equally non-specific standards. Not all sections of the General Bases, however, are devoid of specific content. Some sections provide detailed insights into how the enterprise is expected to conduct its business. Of particular interest is the discussion of internal finances, which establishes provisions for the uses that can be made of enterprise profits. These uses include payment of taxes, establishment of reserves against contingencies, making capital contributions to the state, and establishing other types of authorized reserves (e.g., reserves for research and development). After these obligations have been funded, the remainder of the enterprise profits (if certified as such by outside accountants) can be treated as retained earnings and, if so decided by the management of the enterprise, distributed to the employees as “material incentives.”\footnote{See \textit{id.} \S\ 11.2.2.2.}

Other sections that provide specific guidance to the enterprise in carrying out the EOP are as follows.

3.3.1. \textit{Labor and Salary Policies}\footnote{See \textit{id.} \S\ 10.}

Under the EOP, a Cuban SOE is free to develop its own workforce management and make its own hiring and work assignment decisions, based on the applicants’ qualifications. The enterprise can also set work schedules, work hours, breaks and other employment terms and conditions (including occupational
health and safety provisions), disciplinary measures, training, and other aspects of workforce management.

The law repeals previously existing requirements which specified that candidates for particular positions demonstrate having a specified number of years of experience; prior experience becomes one of the factors in judging applicant qualifications. Three types of employment contract are recognized: employment for an indefinite period; employment for a specific period or for a defined task; and employment to render services at home. All employment must be pursuant to a written contract, the general terms of which are specified in the General Bases.

In terms of salaries, the General Bases establish four fundamental principles: (1) salaries must be pegged to economic results obtained both by the employee and by the enterprise; (2) there must be sufficient differentiation among salaries to account for the degree of responsibility and technical demands of the different positions; (3) salary decisions must be decentralized to the extent possible; and (4) any salary readjustments must be preceded by a showing that they can be financed from the economic resources available to the enterprise. The General Bases also establish a sliding scale of salaries based on four categories of employees: production personnel, support personnel, administrative personnel, and technical personnel. The bottom salary, for unskilled laborers, is 130 pesos per month, while the top salary for an enterprise manager is set as 600 pesos per month. The members of the governing boards of the OSDEs are allowed a salary of 700 pesos per month.

As noted above, incentive payments may be provided to workers (based on retained earnings) up to thirty percent of their base salary; on the other hand, when the projected after tax profits are not met, salary reductions of up to twenty percent of the base salary may be assessed.

3.3.2. Internal Controls

Each enterprise must set up an internal controls program to protect the enterprise’s resources from “waste, fraud and inefficient use.” The internal controls are to include procedures for the

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44 U.S. $6.50, at the prevailing rate of exchange of approximately U.S. $1 = 20 pesos.
45 General Bases, supra note 21, § 10.
control of each enterprise activity, which must be “authorized, approved, carried out, and recorded.” Another required control mechanism is the functional separation between the accounting and operation functions and between assets and their accounting records. Also required are internal and external audits, with the external audits being conducted only by independent accounting firms approved by the state. Other internal control measures identified in the General Bases include, among others: (1) keeping cash in safes to which only the cashier has access; (2) performing unscheduled audits of the cash at hand; (3) requiring petty cash vouchers to be countersigned by the requiring petty cash cashier and the cash recipient; (4) requiring daily deposit of sale proceeds; (5) requiring that different people authorize and issue checks, on the one hand, and reconcile bank statements; (6) keeping control of warehouse inventories and transfers of warehoused materials; (7) requiring that the person receiving goods at the warehouse be different from the one receiving the invoices for the goods; (8) requiring periodic inventories of ten percent of the stored goods (9) maintaining controls over the issuance of tools and materials; (10) separating the functions of sale or delivery of goods from the invoicing and collection for such sales; and (11) keeping control over the supply of blank invoices and requiring that such invoices be pre-numbered.

3.4. Status of Enterprise Perfecting Program

Currently, there are 1,004 SOEs (thirty-one percent of all Cuban firms) undergoing the EOP. In 1998, over 1,400 SOEs were selected for transformation under the EOP; however, 400 had to abandon the process due to serious deficiencies in internal accounting. The majority of the firms chosen for upgrading are in key industries that Cuba hopes to develop. Nearly all nickel exploration companies, petroleum refineries, power companies, and many agriculture companies are candidates for reform. Although the government hopes to eventually reform all of Cuba’s 3,000

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SOEs, the firms in these fields are the most significant for Cuba's economy.48

The number of SOEs that have reached the sixth stage of implementing the optimization process has grown steadily, if not rapidly. In 1999, only five firms received authorization from the Government Group to proceed with their proposed reforms. In 2000, thirty-five firms had advanced to the implementation stage.49 As of May 2001, one hundred firms have been approved by the Government Group to implement the process.50 An additional two hundred are expected to reach the EOP implementation phase by the end of the year.

The government has taken other steps to hasten implementation of the reforms. On December 28, 2000, the University of Camaguey released an interactive CD-ROM that will help businesses meet the goals of the EOP. The CD-ROM offers virtual consulting, information on the EOP process, and advice from Cuban business and managerial experts.51 The CD-ROM comes in response to the lack of business intelligence on the island. There is insufficient training in Cuba in the use of business intelligence because the budgets of many SOEs do not allow for expenditures towards the collection of information.52 Consulting groups, such as Gestion Tecnologica in Santiago de Cuba, are being set up as the demand for business advice becomes more evident.53 Consulting firms help SOEs develop their EPEs, which then must be approved by the Government Group.

In March 2001, Carlos Lage, Secretary of the Executive Committee of the Council of Ministers and Vice President of the Council of State, announced the creation of the first twenty-six OSDEs, an important step in the advancement of the EOP. As discussed earlier, the OSDEs, which are comprised of ministers, vice-

49 See Tortuga, supra note 47.
50 See Cambio, supra note 48.
ministers, and other high functionaries of the Cuban government, serve as direct intermediaries between the SOEs and the Council of Ministers. They are also responsible for monitoring and assessing the progress of the various firms as they implement the EOP.54

Despite claims that the EOP is moving too slowly, government officials claim to be satisfied with its progress. Armando Perez Bentacourt, executive secretary of the Government Group, claims that the process may seem to be moving slowly because the Cuban population is so anxious to see results. However, positive results cannot be expected to instantly materialize.55 Still, several signs indicate that the EOP is working:

- Government subsidies to failing SOEs have decreased. These subsidies placed a great strain on the Cuban budget. In 1994, for example, the government paid 5.75 billion pesos in subsidies to SOEs. In 2001, the government plans to reduce this amount to 300 million pesos.56

- Enterprises that have already implemented the EPEs are growing more quickly than the overall economy. Last year, SOEs that implemented structural reforms reported a 9.5% increase in sales over 1999 levels.57

- The petroleum industry, which was almost non-existent before the collapse of the USSR, has also made substantial economic improvements. In 2000, Cuban refineries produced a record high three million tons of petroleum, a fifty percent increase over the 1999 output.58

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55 Tortuga, supra note 47.


57 See Tortuga, supra note 47.

Despite these signs of success, many people remain skeptical of the EOP, and in some SOEs the optimization process has been delayed by workers’ concerns over salaries and monetary incentives. Currently, a sixth of Cuba’s work force receives monetary rewards for increased production, which are awarded if the enterprise exceeds some production goal. As noted earlier, the EOP links individual salaries to individual output, not the output of the entire enterprise. This system is criticized as inequitable.

Workers also worry that they may be fired from their jobs, an inevitable step due to the restructuring of inefficient SOEs. The first sixty-four SOEs to implement reforms laid off 2.5% of their workers. Cuban law guarantees these workers sixty percent of their income while they look for new jobs. However, it is feared that implementation of the EOP will ultimately lead to massive unemployment.

Another obstacle to the success of the EOP is the lack of accountability in Cuban enterprises. Except for the few enterprises that have entered the final stage of the EOP, Cuban businesses operate under “soft-budget constraints.” Since bankruptcy is not a threat, SOEs are not confined to their budgets as capitalist businesses are. The lack of business accountability and the poor accounting practices have made it extremely easy to embezzle money or commodities from one’s place of employment. In March of 2001, the Ministry of Prices and Finance declared that only 675 of over 3,000 SOEs employed adequate accounting measures.

In many cases, there are no incentives for managers and workers to reform the SOEs, since they can make more money by under-

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60 See id. at 6.

61 Cambio, supra note 48.


63 Interview by Buro de Informacion de Derechos Humanos with Oscar Espinosa Chepe (Oct. 24, 2000) [hereinafter Chepe Interview] (discussing the critical situation in the Cuban economy).


65 See Cambio, supra note 48.
reporting earnings or stealing unaccounted-for products than they could earn from productivity bonuses. An independent Cuban economist states: "The lack of control in the management of public goods and the corruption constitute the gravest problems that society has faced over the past years. These phenomena not only produce immeasurable losses, but degrade society as a whole."66

As a result, the EOP faces as its most serious challenge changing the way that enterprises and their managers do business.

4. ENTERPRISE REFORM CASE STUDIES

4.1. Introduction

A privatization program may be designed to be implemented slowly, or to take place as rapidly as the circumstances permit. Gradual privatization is used in countries that seek to retain a centrally-planned economic system. China and Vietnam, for example, are implementing gradual privatization programs designed to be carried out over long periods of time.67 These programs have proved to be cumbersome and their effectiveness has been impeded by political constraints. Nonetheless, even these limited efforts have been beneficial in driving the management and workers of SOEs toward profit-seeking activities, resulting in increased productivity.68

A rapid privatization program is one whose goal is to turn SOEs over to the private sector as quickly as practicable. Rapid privatization methods attract private investors and foster the re-emergence of a domestic enterprise sector. They are, therefore, the most appropriate methods for handling the transition from a state-controlled economy to a free-market economy. As discussed be-

66 See Chepe Interview, supra note 63.
68 China has coupled the limited opening of SOEs to private ownership through the sale of enterprise stock to the public with a grant of increased operational autonomy to its SOEs. BARBARA LEE & JOHN NELLS, ENTERPRISE REFORM AND PRIVATIZATION IN SOCIALIST ECONOMIES 7, 9 (1990). As discussed earlier, the second half of that equation is analogous to a stated objective of the EOP in Cuba.
low, rapid privatization was the method used in East Germany after Germany was reunified in 1989.

This Section examines both privatization styles by summarizing the enterprise reforms instituted in China (as the prime exponent of gradual privatization) and East Germany (as an example of rapid privatization). The Article makes no assumption regarding the method of SOE privatization that Cuba may seek to implement; rather, the focus will be on what activities prior to (or in the early stages of) privatization tend to facilitate the successful completion of the process.

4.2. The Chinese Experience

4.2.1. Initial SOE Reforms in China

China is a self-proclaimed socialist country that continues to retain its allegiance to a command economy. Yet, it has gradually become marketized through a process that involved, among other things, a reform of the state enterprise system. The main objective of SOE reform involved providing incentives for enterprises and individuals to be more effective through profit retention, a dual-price system, and the contract responsibility system described below. All these measures were designed to reduce price distortion, increase SOE competitiveness, and reap the profit generated by free markets.

To bring SOEs within the market's orbit without relinquishing state ownership, China created a framework aimed at separating the government's ownership of an enterprise from its management and administration. Reforms began in the rural areas, where people's communes were disbanded and replaced by a "household

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69 Lan Cao, Public Perspectives on Privatization: Chinese Privatization: Between Plan and Market, 63 LAW & CONTEMP. PROBS. 13 (2000) [hereinafter Perspectives]. Since the beginning of market reforms, however, Chinese officials have drawn a distinction between marketization (which they favor) and SOE privatization (which they oppose). As will be further discussed below, parallel with the institution of SOE reforms, the Chinese government has also allowed the development of a non-state sector side by side with the state sector. See Lan Cao, The Cat That Catches Mice: China's Challenge to the Dominant Privatization Model, 21 BROOK. J. INT'L L. 97, 100 (1995) [hereinafter The Cat That].

70 See Perspectives, supra note 69.

71 See id.

The land remained communally owned, but households were allowed to contract to cultivate the plots and were given incentives to increase productivity. The communes' assets needed for production were sold to the households at low prices, and a type of contractual arrangement was instituted under which farmers organized by "household unit," contracted with the state to sell a set quantity of products at a government-set price, but any surplus above the established quota could be sold in the open market at open-market prices. This initial, limited reshaping of the SOE system led to improvements in the performance in the agricultural sector, especially in the production of grain.

The Chinese government expanded in 1984 the agricultural sector reforms to other SOEs. The concept of "responsibility contracts" was made applicable to all SOEs and all levels of the production and distribution chain. Under the reformed system, SOEs enter into contracts with the state that set production targets for the enterprise to meet within a specified period of time. After the targeted performance goals are met, the enterprise is allowed to retain any excess profit for use as its management deems necessary, thus giving management limited rights over production, marketing, labor, procurement, investment, and asset disposition.

Subsequently, in 1992, regulations were issued that expressly conferred upon a SOE a number of powers, including the power to:

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74 Perspectives, supra note 69 at 29-30. Cuba copied the Chinese model when it instituted the Unidades Basicas de Produccion Cooperativa ("UBPCs") in 1993 and subsequently established the "mercados agropecuarios," that is, agricultural markets in which agricultural products are sold by farmers to the public at free-market prices. See, e.g., Hans-Jürgen Burchadt, La Descentralización de las Granjas Estatales en Cuba: ¿Género para una Reforma Empresarial Pendiente?, 10 CUBA IN TRANSITION 64 (2000), available at http://lanic.utexas.edu/la/cb/cuba/asce/cuba10/bruchardt.pdf.

75 Sun, supra note 73, at 20-21.


(1) make decisions with respect to production and operation; (2) fix prices for their products and services; (3) purchase materials; (4) import and export; (5) make investment decisions; (6) dispose of reserved funds; (7) dispose of assets; (8) form a joint venture, or merge, with another enterprise; (9) hire employees; (10) sell its products; (11) manage its personnel; (12) decide wages, salaries and bonuses; (13) set up internal offices; and (14) resist or reject resources offered by the state, including human, material resources and financial apportionment.\(^7\)

Under the regulations, SOEs are expected “to become, under the law, units for commodity production and management with autonomy, sole responsibility for their own profits and losses, self-development and self-command, and to become legal persons competent to enjoy civil rights and to assume civil responsibilities independently.”\(^8\)

The potential evolution of the SOEs into more independent entities, however, was hampered because the Chinese government authorized the establishment of enterprises that included limited or no state participation.\(^9\) These enterprises included joint ventures between the state and a foreign investor, collectives known as township and village enterprises (“TVEs”) and even wholly owned foreign enterprises.\(^10\) Completion from these private enterprises had a detrimental effect on SOEs, which never had faced true competition in the market.\(^11\) High costs and low efficiency continued to plague the SOEs, which remained unable to compete with the private sector.

4.2.2. The “Modern Enterprise System”

Another solution was needed, and China instituted the “modern enterprise system” program in 1995 with the goal of “corpora-

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\(^{78}\) Regulations on Converting the Operational Forces in the Industrial Enterprises Under the Ownership of the Whole People (1992), quoted in Sun, supra note 73, at 23-24.

\(^{79}\) See Rules on Transforming Managements of State Enterprises, supra note 77, art. 2.

\(^{80}\) See The Cat That, supra note 69, at 102.

\(^{81}\) Id. at 103.

\(^{82}\) See Sun, supra note 73, at 21.
tization” of the SOEs. Selected SOEs were reorganized into corporate entities having ownership rights, property rights, and clearly defined managerial responsibilities. The government established two stock exchanges to promote the development and expansion of the enterprise transformation program. Only a small portion of the SOEs have participated in this program, and most of the enterprises participating are small or medium size SOEs. This is “due to the government’s reluctance to introduce [private] ownership into large and super-large state-owned enterprises.” Many small enterprises were left to fend for themselves, and either succeeded, sold out, or merged.

The major features of the Chinese enterprise reform program included:

- Transforming the SOEs into corporations by a re-definition of their ownership.
- Allowing individuals to buy shares in the SOEs in the stock markets and become minority owners of the enterprises.
- Requiring the corporatized SOEs to set up boards of directors that represent all owners’ interests.
- Establishing separate entities (supervisory boards) that supervise the management of each enterprise.
- Requiring that the supervisory boards include outside specialists in business management.

84 See Sun, supra note 73, at 28.
85 See id.
86 Of the 380,000 SOEs in China, only 1.5% have become joint stock companies. They represent, however, six percent of the production and account for thirteen percent of the profits of the Chinese SOE system. Id. at 21, 28-29.
87 MA, supra note 83, at ch. 5.
88 See Sun, supra note 73, at 35.
89 See id. (describing the major aspects of the Chinese enterprise reform program).
The expectation which underlays the initiation of the modern enterprise system was that it would help separate the government's regulatory duties from the commercial functions of the SOEs.90 Experts have concluded, however, that the "modern enterprise system" has had only limited impact on improving the SOEs' efficiency, and that there are still serious organizational problems in the SOEs from the standpoint of corporate governance.91

Corporatized SOEs still have inconsistencies in the relationships between the "shareholders' congress" (the shareholders' meeting) and the government, the board of directors and the enterprise managers, and the government organizations and the governance of the enterprise.92 First, the shareholders congress is required to obtain authorization from the government before its decisions become effective, thus the shareholders—particularly the private ones—have no independent powers but continue to be subordinated to the government.93 Second, enterprise managers are not appointed by the board of directors but by the government authorities, and the post of general manager is held by the chairman of the board.94 Third, the chairman of the board (and enterprise general manager) is appointed by the government instead of being selected by the board or the shareholders.95 In short, the creation of the "modern enterprise system" has failed to achieve the separation of functions between enterprise ownership and management, both of which remain with the state.

There are also structural problems with the modern enterprise system in that there are functional overlaps between the general managers and the director of the board, and in the administrative appointment of SOE managers.96 Furthermore, three pre-reform committees, party committee, trade union, and the congress of workers representatives, co-exist with the three new ones, the

90 See id. (explaining the expectations underlying a modern enterprise system).
91 See id. (describing the limitations of a modern enterprise system).
93 See id.
94 See id.
95 See id.
96 MA, supra note 83.
shareholders congress, the board of directors, and the supervisory board. There seems to be a lack of clear definition of the responsibilities of these entities and the relationships among them causes internal conflicts and inefficiency in decision-making. 97

The implementation of the modern enterprise system has also not resulted in a change of the internal structure of the SOEs. 98 According to the results of a study that examined the composition of the board of directors and the supervisory committee in the corporatized SOEs, members of the board and the supervisory committee are dominated by the government officials, and the state shareholders are over-represented in proportion to individual shareholders in both the board and the supervisory committee. 99 This is true even though the law prohibits government officials from remaining entrenched in company management. 100

Despite these deficiencies, the results of China’s enterprise reform initiatives have been generally positive. Reported data reveals that the gross output value of state enterprises increased from 342.1 billion yuan in 1978 to 1.35 trillion yuan in 1988. 101 The total factor of productivity in state-owned industries also increased during the 1980s at an annual average of 2.4%. After enterprise reform, joint-stock companies have demonstrated greater vitality and performed better in the market than traditional SOEs, even though they make up only 1.5% of all SOEs in China. 102

4.2.3. Flaws in the Chinese SOE Reform Model

As just described, those SOEs that the Chinese government has allowed to institute the “modern enterprise system” in order to become more competitive have exhibited operational improvements. However, the progress of SOEs towards optimization has been im-

97 See id.
99 See id.
100 See Sun, supra note 73, at 32.
102 See Sun, supra note 73, at 28.
peded by a number of constraints and problems, which are strongly reminiscent of those reported in Cuba under the EOP:

- Lack of separation between enterprise ownership and management.103 This is ironic (because, like in Cuba, the fundamental tenet of SOE reform in China is to allow enterprises a greater degree of enterprise self-government) and at the same time predictable. As in Cuba, multiple layers of Chinese bureaucracy exist at the national, provincial, and local level, all with entrenched powers over the SOE, which they are unwilling to give up.104 The SOE management is powerless to raise objections to the government's meddling in the internal affairs of the enterprise, since the state is both owner and regulator, and SOE managers who oppose government directives risk transfer or removal.105 The most effective way to accomplish this separation, and the one that is now being instituted to a limited extent in China (but not in Cuba) is the privatization of at least the small- and medium-sized SOEs.106

- Corruption, particularly among managers. As their power increases, managers have more opportunities (which they often seize) to appropriate an increasing share of the corporate resources.107

103 Id. at 38-39.
104 Id. at 40-43. The problem has been characterized as follows: "Various administrative agencies at both the national and local levels invested in an enterprise vie to exercise control over it, thereby subjecting the enterprise to overlapping and often conflicting vertical—usually one of the industrial administrative bodies attached to a central ministry—as well as horizontal—usually the local people's governments or their agencies—lines of authority." Perspectives, supra note 69, at 57.
105 Sun, supra note 73, at 39-40.
106 Privatization is not always feasible, however, because many Chinese SOEs cannot be sold, either because of their poor financial condition or because there are few Chinese nationals who can afford to buy them. With respect to SOEs engaged in important industries, such as transportation, telecommunications, and national defense, it would be politically unacceptable to sell to foreign nationals. Id. at 43.
107 Id. at 44-45. Potential ways to address the corruption problem include external auditing, formal control systems, budget restrictions, the establishment of suitable incentive compensation systems, and reforming the state employment system so that managers have a real risk of unemployment if the enterprise is not successful. Id. at 45-46.
• Enterprise asset stripping by managers acting in collusion with workers.\textsuperscript{103}

• Misuse of public resources through the purchase of commodities at lower, official prices and subsequent resale at a higher price on the non-state market.\textsuperscript{109}

• Informational uncertainties, unreliable accounting, and inconsistent financial data.\textsuperscript{110}

• Arbitrary and excessive taxation.\textsuperscript{111}

• Overproduction and reckless investment in plant capacity.\textsuperscript{112}

• Asset inflation due to measures by managers to show profits, whether true or not. Such measures include unwillingness to recognize bad debts, inflation of receivables and credits, and underestimation of depreciation and costs.\textsuperscript{113}

• Siphoning of public resources towards weaker SOEs through improvident loans by state banks and state infusions of cash to stem potential layoffs by failing enterprises.\textsuperscript{114}

These difficulties have led an analyst to the following pessimistic assessment of the SOE reform process in China:

Within the [SOE] itself, governmental decentralization, the downward transfer of rights, and the separation of the firm from the state have resulted in more autonomy for managers as intended, but they also set in to motion a web of

\textsuperscript{103} Perspectives, supra note 69, at 42.
\textsuperscript{109} Id.
\textsuperscript{110} Id. at 37.
\textsuperscript{111} Id. at 38.
\textsuperscript{112} Id. at 41.
\textsuperscript{113} Perspectives, supra note 69, at 41.
\textsuperscript{114} Id. at 42.
causally linked and distorted incentives that are difficult to rectify because of the absence of internal and external controls.\textsuperscript{115}

The Chinese government has continued to experiment with methods to privatize medium and large-size SOEs.\textsuperscript{116} An ongoing experiment has designated enterprises throughout China to experiment with optimizing the capital structure and establishing modern business operating systems.\textsuperscript{117} It remains to be seen whether the experiment will constitute another step towards the eventual privatization of these and other SOEs.

4.3. The East German Model

Some economists have called the East German ("GDR") economy a transfer economy rather than a transitional economy.\textsuperscript{118} East Germany adopted the German Deutschmark, instituted German laws and legal norms, and sold the majority of its firms to German investors.\textsuperscript{119} Unlike China or the U.S.S.R., which slowly restructured and privatized SOEs, East Germany turned all former SOEs into companies under German corporate law. These companies remained under the control of a trust agency, the Treuhandanstalt ("Treuhand"), until they were sold as private companies or liquidated.

The transformation to a private property system was initiated by the GDR's enactment of the Treuhandgesetz ("Trust Law").\textsuperscript{120} The law created the Treuhand, which instantly became the largest holding company in the world with control over 12,370 busi-

\textsuperscript{115} Id. at 42-43.

\textsuperscript{116} Privatization of small SOEs is no longer a problem. Government regulations issued jointly in 1998 by the State Commission of Economy and Trade, the Treasury Department, and the People's Bank (China's central bank) establish guidelines for the sale and purchase of small SOEs. Such sales are well under way in China, although the process is not officially acknowledged as privatization. Sun, supra note 73, at 35.

\textsuperscript{117} Id. at 36.

\textsuperscript{118} Bernhard Seliger, Two Sides to This Coin, 3 CENT. EUR. REV. 3, Jan. 22, 2001, [hereinafter Coin], available at http://www.ce-review.org/01/3/seliger3.html.

\textsuperscript{119} Bernhard Seliger, Ten Years After German Unification, 3 CENT. EUR. REV. 2, Jan. 15, 2001, [hereinafter Unification], available at http://www.ce-review.org/01/2/seliger2.html.

\textsuperscript{120} Gesetz zur Privatisierung und Reorganisation des volkseigenen Vermögens (Treuhandgesetz), v. 22.6.1990 (GBI. I S.300) (G.D.R.) [hereinafter Trust Law].
Cuba's Perfeccionamiento

The first words of the Trust Law declared emphatically that privatization was to occur "as quickly and as comprehensively as possible." The Treuhand, in turn, became the owner of all of the shares of these companies and was responsible for preparing them for sale to the private sector. The Treuhand was required by law to evaluate the economic positions of these companies; it determined which enterprises were competitive enough to be privatized, which should be dismantled, and which should be liquidated. In all companies with over 500 employees the Treuhand established advisory boards. These boards, consisting mainly of representatives from West Germany's government, businesses, and banks, were responsible for drawing up plans to restructure the corporation, contract short term managers, and make other necessary changes.

The sale of the companies was the most important part of the privatization process. Before the Treuhand could sell interests in the formerly state-owned enterprises, it first needed reliable valuations of them. The Financial Statement Law required enterprises considered for privatization to prepare financial statements using Deutschemark valuations. If the prospects for survival were questionable, the Treuhand decided against privatization and liquidated the company. If, however, the company's prospects for survival were promising, the Treuhand would fund the company

121 The Treuhand was created by the GDR prior to reunification and was integrated into the government of the Federal Republic in the Treaty on Unification, where it became a federal agency overseen by the Minister of Finance. See Vertrag zwischen der Bundesrepublik Deutschland und der Deutschen Demokratischen Republik über die Herstellung der Einheit Deutschlands (Einigungsvertrag), art. 25, v. 28.9.1990 (BGBl. II S.897), translated in 30 I.L.M. at 481 [hereinafter Unification Treaty].

122 Trust Law, supra note 120.

123 See id.

124 See id.


126 See Unification, supra note 119.


128 Id.
up to the amount of its debt. The company would then be prepared for direct sale into the private sector.

The strategy of rapid privatization was grounded on the assumption that the costs of rehabilitation faced by private investors would be considerably lower than those of the Treuhand. Aside from the transfer of economic and technical knowledge and the mobilization of private capital, what the Treuhand ultimately expected from a rapid privatization was the chance for East German enterprises to overcome barriers to market entry. The survival of East German firms could be ensured only by making them competitive, which could be accomplished only by investing substantial sums into their rehabilitation. The Treuhand for the most part decided against financing rehabilitation itself, opting instead for a "privatization of rehabilitation."

Many East German companies, however, were unattractive to private investors. Although the Deutschmark was valued 1:4 to the Ostmark, the two currencies were officially united at a 1:1 ratio. Subsequently, East Germany's labor force became grossly overpaid, and capital stock devalued by fifty percent. These factors, combined with the poor state of East German companies and resources, discouraged many investors.

The Treuhand was faced with two options: retain and restructure these companies until they could be sold at market prices, or sell them to private investors at subsidized prices. The Treuhand opted for the latter. Thus, the Treuhand invited investors by assuming outstanding company debt, subsidizing costs of development, and assuming environmental liabilities. In many cases, the Treuhand sold companies for a loss, after taking into account payments on accrued debt. In return, investors agreed to invest set amounts of money, maintain a certain number of jobs, continue and increase production levels, and consent to labor wage contracts that would slowly increase wages.

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130 See, e.g., HERBERT BRUCKER, PRIVATIZATION IN EASTERN GERMANY (1997).
131 See id.
132 See id.
133 See id.
134 See Coin, supra note 118.
136 See id. at 83.
Other than initial evaluations and limited restructuring in larger companies, the Treuhand did little to prepare former SOEs for privatization. Many critics claim that the Treuhand should have restructured these companies and sold them at competitive prices and at a time when the economy was stronger. Instead, after four years the Treuhand incurred a 270 billion Deutschmark debt which must be financed by the German state. The desire to quickly dump these companies on the world market led the Treuhand to sell them at only ten percent of what they had formerly expected to raise.

The Treuhand did, however, maintain control of key industries for East Germany until they could find appropriate buyers. The Treuhand, for example, maintained and invested in EKO Stahl, a large steel mill by the Polish border, for four years before eventually selling it. Even though the Treuhand could have liquidated these companies and avoided losses, the subsequent loss of jobs would have created social unrest.

The effect of East Germany’s rapid privatization has had mixed effects on the economy. Unemployment initially skyrocketed as managers downsized the overpaid workforce that was draining capital reserves. About half of the workers in the former GDR lost their job, and 600,000 migrated to western Germany. Nevertheless, East Germany’s economy grew about nine percent in 1994. GDP, per capita income, and productivity have all increased relative to West Germany. Still, unemployment remains a problem in East Germany. This is due to the Treuhand’s efforts to provide “equal pay for equal work” in the former GDR and West Germany. Companies agreed to boost wages eleven-fold by 1996, rendering many companies inefficient and struggling to compete.

Although Germany’s method of privatization has had mostly desirable effects, it may not be a suitable model for other countries to follow. The GDR had the advantage of unification with an economic superpower that could finance the debt incurred by the privatization of inefficient companies. Furthermore, unification with Germany provided the economic and political stability needed to...
attract foreign investment. Finally, the well-educated East German work force, and a strong service sector offered insurance that the privatization process would eventually be profitable, even if it would suffer in the short run. Thus, East Germany's transition cannot be evaluated or applied to other scenarios without carefully considering the surrounding factors.

5. IS CUBA'S PERFECCIONAMIENTO EMPRESARIAL LAW A STEP TOWARDS PRIVATIZATION?

5.1. Actions Contemplated in the EOP that Would Aid in the Preparation of Cuban SOEs for Eventual Sale

As noted in Section 2, a first step in privatization is a thorough examination of the SOE's finances and operations. Cuba's EOP program ostensibly accomplishes this step through the performance of the initial diagnostic analysis of the enterprise. To the extent that the evaluation is thoroughly performed, it will be a valuable first step towards a possible privatization. If the assessment is based on proper accounting methods and provides an adequate disclosure of the company's finances, the program will give potential investors a good sense of how much an enterprise is worth. In addition, if the valuation is performed competently, it will serve (as was the case in East Germany) as a triage tool to allow the state to determine which enterprises can be sold and which need to be liquidated.

The second necessary step towards the privatization of SOEs involves taking a number of measures to prepare it for the sale. Of these, only the first (bringing the enterprise's accounting records and methods to modern standards) can be accomplished before the decision to sell is implemented. Cuba's EOP gives at least lip

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143 Depending on how far into the future the actual privatization takes place, this evaluation may need to be updated or repeated, but the initial exercise should provide a good starting point in any instance.

144 Although Cuba has yet to take steps to liquidate unprofitable enterprises, the initial selection of SOEs to be included in the EOP, and the subsequent culling of some enterprises based on the results of the valuation, suggest that Cuba has already indirectly made the cut as to what SOEs will be supported towards possible solvency and which will be eliminated by some method or another.
service to accounting reform, which is one of the subsystems intended to be covered by the program. Because transparent, competent accounting is inconsistent with enterprise raiding by management and employees, actual implementation of accounting reforms may be as difficult in Cuba as it has been in China.

The third step is to transform the SOE into a corporation, so that there is flexibility in the format of the subsequent sale. East Germany took this step at the outset, and China did so to a limited extent in the second phase of its SOE reform program. Cuba has not yet done so.

The fourth step includes taking a series of enterprise “get well” measures including refinancing or writing off debt, eliminating unprofitable lines of business, reducing the number of employees, hiring new managers, and disposing of assets and liabilities that make the enterprise more difficult to sell. In order for the EOP to result in profitable SOEs in Cuba, some of these measures will inevitably have to be undertaken, and should be part of the business plan in the enterprise’s EPE. Thus, at least in theory, the EOP should accomplish this step wholly or in part. In addition, to the extent that enterprises are made more efficient, this would lead to a higher valuation and a better sale price.

5.2. Comparative Outlook Based on Reference Countries’ Experience

Cuba’s EOP is closest in structure and objectives to the Chinese enterprise reform program. In China, early reforms focused on making Chinese enterprises more competitive, efficient, and productive, as does Cuba’s current program. Specific productivity goals were set for each company, and incentives were given to meet or exceed them. Cuba has already instituted such a program in the agricultural sector, and is moving towards doing so in the EOP. Cuba, however, has yet to allow the development of a non-state sector to complement the SOE transformation.

With the adoption of the modern enterprise system, China went a step further as it sought to achieve structural reforms within its SOEs. The specific strategies of the program are very similar to those in Cuba’s EOP. Both countries have sought to establish independent management structures through the establishment of boards of directors, and have tried to make their SOEs closer in operational freedom to Western business organizations. However, while Chinese corporate law nominally seeks to extricate the state from the day-to-day business of the SOEs, the actual com-
position of boards and key offices is still directed and peopled by government actors. Cuba’s EOP does not even make such an attempt, since the program specifically requires that the majority of the members of outside governing boards be state officials. It also subjects enterprise management to the authority of both the OSDEs and the Cabinet-level Government Group. In this sense, Cuba has made even less progress in removing the state’s control over the enterprise than the Chinese approach. Perhaps China’s more liberalized system reflects its acknowledgment of past failures with enterprise reform, an experience likely to be repeated in Cuba.

East Germany’s pace of privatization was very swift, as compared to China’s. Its focus on SOE efficiency was not an effort to improve enterprise operations, but a test administered to determine whether a company should be selected for privatization or liquidation. Reforming and improving efficiency of SOEs was left to the purchaser. Overall, this approach stands in stark contrast to that prescribed by the Cuban program even though both involve evaluating and hand-picking the enterprises that will participate in the program.

The East German model of rapid action is unlikely to be imposed on Cuba absent a major near term transformation in the state apparatus. Nor is there a familiarity with a market-based economy and the presence of institutions that embody market principles in Cuba, as there was in Germany during reunification. The Chinese government addressed this gap by building a non-state sector before privatizing the state sector. This was both consistent with prevailing “Chinese socialism” conceptions and with China’s gradualist approach to economic reforms. Perhaps over time Cuba, as it has done with other aspects of enterprise reform, will come to imitate this aspect of the Chinese program.

6. CONCLUSION

The efforts in Cuba under the EOP reflect a political structure that parallels that of China. The reforms instituted are the product of a strong socialist government that is unwilling to relinquish either ideological or operational control over the country’s economic activity, even while recognizing the imperiled state of the economy.

See The Cat That, supra note 69, at 104.
To what extent Cuba’s EOP will exhibit the same deficiencies as China’s program remains to be seen. The characteristics that led to China’s problems are also found in Cuba, primarily the pervasive government control over the SOE’s operations. In any case, Cuba’s program seems to be a viable, albeit limited, first step towards reforming its state enterprises and making them more efficient. Improved enterprise operation would, in turn, better position those enterprises to be successfully sold or otherwise privatized when a privatization program is set in place in the island.