Center for Social and Economic Research

CASE Reports

Understanding Reform: The Case of Poland

Jacek Kochanowicz
Piotr Kozarzewski
Richard Woodward

No. 59/2005

Warsaw, 2005

The views and opinions expressed here reflect the authors' point of view and not necessarily those of CASE.

This report was prepared as part of the Global Development Network project "Understanding Reform". The publication of the report was financed by the GDN.

Keywords: **Poland, reform, transition.**

Graphic Design: Agnieszka Natalia Bury

DTP: CeDeWu Sp. z o.o.

ISBN: 83-7178-376-0

Publisher:
CASE – Center for Social and Economic Research
12 Sienkiewicza, 00-010 Warsaw, Poland
tel.: (48 22) 622 66 27, 828 61 33, fax: (48 22) 828 60 69
e-mail: case@case.com.pl
http://www.case.com.pl/

Contents

The Authors

Jacek Kochanowicz is Professor of Economic History at the Warsaw University and Recurrent Visiting Professor of History at the Central European University in Budapest. He has published books and articles on the history of peasant economy, on comparative modernization, and on post-communist transformation. His most recent publications are: "Trust and social capital in Poland: a historical perspective," in: Ivana Markova (ed.), *Trust and Democratic Transition in Post-Communist Europe*, Oxford University Press/The British Academy, Oxford 2004 – "Die polnische Wirtschaftskultur – Persistenz und Wandel", *Berliner Debatte Initial* 15 (2004); 5/6 (with Mira Marody), and "Towards understanding Polish economic culture," *Polish Sociological Review* 2003, no. 4 (with Mira Marody).

Piotr Kozarzewski is a senior research fellow at the Institute of Political Studies of the Polish Academy of Sciences and a senior expert at CASE – the Center for Social and Economic Research in Warsaw. He is the author of numerous publications on systemic transformation in post-Communist countries, especially on privatization and corporate governance. Some of his recent publications include: „Nadzór właścicielski, kontrola i zarządzanie" [Corporate governance, control, and management], in: M. Jarosz (ed.), Pułapki prywatyzacji [Privatization traps], ISP PAN, Warsaw 2003; "Poland I: Ownership and Performance of Firms Privatised by Management-Employee Buyouts," in: B. Błaszczyk, I. Hoshi, R. Woodward (eds.), *Secondary Privatisation in Transition Economies: The Evolution of Enterprise Ownership in the Czech Republic, Poland and Slovenia*, Palgrave Macmillan, Hampshire and New York, 2003 (with Richard Woodward); "Corporate Governance and Secondary Privatisation in Poland: Legal Framework and Changes in Ownership Structure," *Studies and Analyses*, no. 263, CASE, Warsaw 2003; *Sukcesy i klęski prywatyzacji w krajach postkomunistycznych* [Successes and failures of privatization in post-communist countries], ISP PAN, Warsaw 2002 (with Maria Jarosz).

Richard Woodward is an economist at CASE - the Center for Social and Economic Research – in Warsaw and a lecturer at the Management School and Economics of the University of Edinburgh. He is the author of numerous publications on privatization in post-Communist countries (especially management-employee buyouts) as well as local development and SME support in Poland, and is currently researching the innovation networks of European enterprises. Some of his recent publications include: "Integration of Poland into EU Global Industrial Networks: The Evidence and the Main Challenges" (with Michał Górzyński and Stefan Dunin-Wąsowicz), in F. McGowan, S. Radosevic, N. von Tunzelmann (eds.), *The Emerging Industrial Structure of the Wider Europe*, London: Routledge, 2004; "Absorptionsprobleme der EU-Struktur- und Regionalpolitik in den MOE-Ländern" (with Wolfgang Quaisser), in *Konjunkturpolitik: Zeitschrift für angewandte Wirtschaftsforschung / Applied Economics Quarterly*, no. 53, 2002, and "SME Support in Post-Communist Countries: Moving from Individual to Cooperative Approaches (Reflections on the Polish Case)", in *MOCT-MOST: Economic Policy in Transitional Economies vol. 11*, issue 3, 2001.

Preface

This report was prepared as part of a global research project financed by the Global Development Network (GDN) entitled "Understanding Reform." Since it was launched in 1999, the Global Development Network has brought together research and policy institutes from around the world, supporting the production and dissemination of knowledge about development which can be of use to policy makers and the public. The goal of this multidisciplinary project was to deepen the understanding of the successes and failures of various reforms through a cross-country comparison of reform policies and experiences in different regions. This report is one of thirty country studies prepared in the "Understanding Reform" project.

The last twenty years have seen a perhaps unprecedented level of economic and political reform on a global scale. It is our hope that with this report we have made some contribution to the understanding of the factors underlying the success of reforms as well as the dangers that face reformers and reforms. We should note that in discussing the success of reforms, and the factors underlying that success, we have defined success not only in terms of the degree to which the reformers' goals were accomplished by the reforms, but also in terms of the ability of reformers to gain the acceptance among legislators and the general populace necessary for the implementation of reforms. We have been interested not only in what makes a reform "good" in a technical sense, but also in what makes it implementable and sustainable. Thus, we hope that we have not only deepened the understanding of the Polish experience in the years since 1989, but also provided some insights which may be of use for other reform efforts in other countries, perhaps in very different parts of the globe.

We wish to express thanks to all the persons and institutions who made the preparation of this report possible, first of all to our interviewees. We would also like to acknowledge our appreciation to Bogna Urbańska-Jobda, who served as a research assistant and who arranged, taped and transcribed all the interviews.

1. An overview of the Polish reform process, 1989-2001

This report reviews the reform process in Poland in the period 1989-2001, from the formation of the first non-Communist government to the defeat of right-wing forces in the 2001 parliamentary elections and the formation of a governing left-wing coalition of social democrats and the peasants' party (both of them with roots in the Communist era). It reconstructs the sequence of reforms, assesses their relative successes, and focuses on the problem of the stagnation of the reform process at the end of the 1990s. The report is organized in six sections. The first one is an overview of the whole process of reforms and provides an outline of its social and political context. The second one states the hypotheses guiding the research undertaken for this report, at the same time grounding them in the relevant literature. The next four sections focus on selected areas – selected key components of the state machinery, stabilization and liberalization, privatization and enterprise restructuring, and pension system. The report synthesizes much earlier research on the topic. It also relies on several specially conducted interviews with individuals who played a key role in or made extensive studies of the reform process. As some of our interviewees declared a will to remain anonymous, we disclose only the names of those who gave their explicit consent.

1.1. The Political Context

Poland – together with other post-communist countries – represents a case of dual transition to market and democracy that started with the collapse of state socialism in 1989 and the Round Table talks between the government and opposition which led to partially free elections in June of that year and the formation of the first non-Communist government in the Soviet bloc. The character of economic reforms has, to a large degree, been determined by the political dynamics of the country and – in particular – by the nature and behavior of the collective political actors. These collective actors, particularly the parties, seemed to have little stability. In the early years of transformation, actors who had been involved in the anti-communist opposition movement around the Solidarity trade union dominated the political process, initiating economic and political reforms. By the time of the elections of 1993, the Solidarity camp had disintegrated into several factions, while the former communists, now redefined as social democrats, regrouped as the Alliance of the Democratic Left (SLD) and – building upon the rise of social dissatisfaction with reforms effects – succeeded in forming a government. The self-styled right reconsolidated under the banner of Electoral Movement Solidarity (AWS), to win the elections of 1997 and to form a government in coalition with the liberal Freedom Union (UW). The UW, however, gradually became marginalized. In a short time, the AWS itself lost its credibility as a result of mismanagement of the speeded-up reform process at the end of the 1990s, combined with corruption scandals. The 2001 election swept the AWS off the political stage. The SLD returned to government triumphantly, but scored few successes, of which a positive result of a referendum on the European Union accession was an important one[1]. The disintegration or marginalization of the "old" parties and coalitions – UW, AWS, SLD, the Peasants' Party (PSL) and the Catholic nationalist party (ZChN) – was followed by the emergence, at the end of the 1990s and the beginnings of the next decade, of new political movements and parties. The most important among them have been the liberal-conservative Citizen's Platform (PO), the conservative Law and Justice (PiS), radically nationalist and Catholic League of Polish Families and radical populist Self-Defense (Samoobrona). All of them scored considerable successes in the 2001 parliamentary elections.

The emergence of new parties, however, has had limited relevance to life outside the small world of the "political class," as in most cases they have been slightly different groupings of the same individuals, organized under new banners. The kaleidoscopic changes on the political scene reflect, however, the deeper problems of the emerging Polish democracy, which is still far from consolidation (cf. Linz, Stepan, 1996). Poland has one of the lowest election turnout rates in Europe, while research and opinion polls show a combination of a lack of interest in politics and a deep mistrust in politicians. The parties have elusive identities and do not represent social interests well (cf. Grabowska, Szawiel, 2001).

[1] Afterwards, due to policy mismanagement and corruption scandals, it was a downward slide, which ended in the loss of parliamentary support in the spring of 2004 and the resignation of the SLD cabinet. After a group of dissenters from SLD founded the Social Democratic Party of the Republic of Poland (SDRP), the number of social democratic parties in the parliament rose to three, including the Labor Union (UP).

Trade unions played an important role up to a point. At the beginnings of the transformation, the scene was dominated by the Solidarity and by the post-communist Polish Confederation of Trade Unions (OPZZ). With the progress of privatization and the rise of unemployment, the role of trade unions diminished, as they are absent in small firms and hardly visible in foreign-owned firms. Their strongholds are the state-owned enterprises and public services, where they represent the corporatist interests of professions in a way similar to other organizations such as Chambers of Medical Doctors, organizations of lawyers, etc.

While political actors style themselves as "left" and "right", their stance on particular issues does not necessarily reflect what is usually understood by those terms. The AWS, for instance, which defined itself as "the right," was more statist and pro-redistributive than the SLD, which in many respects (e.g., the advocacy by some of its leaders of a flat income tax rate) was actually closer to the neo-liberals.

At the risk of over-generalization, it is possible to distinguish four political styles. The first is that of commitment to a particular reform agenda. This is mostly characteristic for such parties as the UW, which has stressed the needs of market reforms, but also for the AWS, LPR and PiS, with their zeal to fight former communists and to defend the "national identity". To a degree, this is also the case with the UP, a watered-down Polish version of the New Left, stressing the rights of women and minorities. The second is that of political marketing, with a focus on political arithmetic and opinion polls. This was characteristic for the SLD during both periods they were in power. This style blurs into the third, which is that of clientelism and corruption, characteristic more for individuals than parties, but to which many of the parties as organizations – particularly the SLD, PSL, AWS, and Samoobrona – easily fell. The fourth is populism, gaining political support through aggressive demagoguery and cynical electoral promises which are obviously impossible to fulfill. The clearest example is Samoobrona.

The quickly changing character of the political scene is reflected in legislation. Winning coalitions have often stopped reforms started by their predecessors. Parties and politicians fight to secure support by distributing jobs and making promises to their electorates. At the same time, consecutive governments have tried to ensure a modicum of financial stability of the state, if not out of prudence, then because of the pressure of international financial institutions (IMF, the World Bank, and the Paris Club), the European Union, and the international financial markets.

The decade of post-communist transformation brought about a fundamental institutional change in politics. The 1952 Polish constitution was substantially amended in 1989, and then a new constitution was introduced in 1997. Poland became a parliamentary democracy with a president elected in a popular vote (but with a relatively restricted role). The functions of government were substantially decentralized in 1990 and in 1997. Poland's international orientation shifted radically, with the country joining NATO in 1999 and the EU in 2004.

1.2. The Reform Process

Poland became the first country in the Communist bloc to undertake comprehensive reforms designed to dismantle the remnants of command economy and to introduce market economy instead. In October 1989 the government presented a program (the so-called Balcerowicz Plan) of fast and deep reforms based on macroeconomic stabilization and liberalization of the national economy, accompanied by measures for the building of market economy institutions (this reform package is described in detail in section 4). Over the course of the next few years, the fiscal system was reformed with the introduction of personal income tax, corporate income tax, and value-added tax. Changes in social insurance and public services (pension reform, health care reform, education reform) were started with a significant delay, a half decade later than the initial economic reform. In the second half of the 1990s, a deep rewriting of existing legislation was undertaken as a part of the process of accession to the EU.

These reforms gave rise to extensive structural change in the economy. This included, most importantly, the fast rise of private businesses (mostly small and medium-sized), the inflow of foreign investment in various forms, the restructuring of foreign trade, the bulk of which is now with Western Europe (in contrast to the predominant importance of Eastern Europe and the Soviet Union under socialism), the emergence of a modern banking system (now predominantly in foreign hands), and the restructuring and privatization of state-owned enterprises (although this process is still far from completed today). Another aspect of restructuring is the relative decline in the share of manufacturing in GDP and the increase in the importance of the service sector, sadly neglected under socialism.

The achievements of the initial period of transformation were quite remarkable (see Table 1.1 for an overview). Having experienced the smallest output decline among post-Communist countries and being the first to return to economic growth (which impressive rates by the mid-1990s), Poland became a symbol of transition success.

International financial institutions and many world-known experts often referred to the Polish experience as a positive example for other post-communist countries.

And yet at the end of the decade Poland's success proved to be a fragile one. After the very favorable years 1995-1997, when annual GDP growth ranged from 6% to almost 7%, the country saw a dramatic slowdown at the end 1990s, bringing GDP growth down to 1.1% in 2001. At the same time, there was a sharp increase in the budget deficit, which in 2001 amounted to 5.5% of GDP, as well as growing balance of payment problems. The unemployment rate, which was already rather high during the first years of transition, climbed in 2000-2001 and became the highest in Europe (17.4% as of the end of 2001). Additionally, critical voices have been raised with increasing frequency concerning the competitiveness of Poland's industry. These critics have argued that the opportunity for deep restructuring in the "fat years" of the mid- to late 1990s was wasted, leaving the country's economy still dominated by extractive industries, heavy industry (steel), and national monopolies (telecommunication, utilities), while the most developed countries (as well as several East Asian countries and – among the transition countries – Estonia, Slovenia and Hungary) moved forward toward the "knowledge-based economy."

Table 1.1. Key Polish economic statistics, 1990-2001

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Inflation (CPI; end of year)	249.3	60.4	44.3	37.6	29.5	21.6	18.5	13.2	8.6	9.8	8.5	3.6
Monetization (% GDP)	22.1	26.2	27.5	29.3	29.8	29.6	31.0	33.4	36.0	39.5	40.7	43.5
Registered unemploymen (end of year)	6.5	12.2	14.3	16.4	16.0	14.9	13.2	10.3	10.4	13.1	15.1	17.4
GDP growth	-11.6	-7.0	2.6	3.8	5.2	7.0	6.0	6.8	4.8	4.1	4.0	1.0
Public sector balance (% GDP)	3.2	-2.3	-5.3	-2.8	-2.8	-2.6	-3.1	-2.9	-2.6	-3.2	-3.0	-5.1
Public sector revenues (% GDP)	45.4	42.9	44.7	47.1	44.4	43.6	43.0	42.3	41.1	41.2	39.7	38.5
Public sector expenditures (% GDP)	42.1	45.3	50.0	49.9	47.2	46.1	46.1	45.2	43.6	44.5	42.7	43.6
Balance of payments (current account; % GDP)	n.a.	-3.4	-1.8	-3.3	0.7	4.2	-1.0	-3.0	-4.3	-7.5	-6.3	-4.1

Notes: The comparability of RCSS estimates of the shares of public sector revenues, expenditures and balance in GDP for 1991-1993 and 1994-2000 is limited due to changes in the calculation of GDP introduced in 1994. 2001 public sector finance figures are CSO estimates.

Sources: RCSS (2002) except Dąbrowski (1997) for 1990 GDP growth, Piętka, Antczak (2001) for 1990 public sector finances and CSO web site for 2001 public sector finances.

1.3. Reform stagnation

There are two areas of reform stagnation which are of particular importance in our opinion. One is the reform of the state machinery, the other that of social services. While the early success of macro- and microeconomic reforms, as well as political ones, had been spectacular, reforms of public administration, administration of justice, and various social services were often flawed, substantially delayed, and in some cases have still not been made. Some of these reforms were passed by the parliament in 1998 and implemented beginning in 1999 (pension reform, health care reform, education reform, and a reform of sub-national levels of public administration). However, the design, implementation and results of these reforms are often considered to be mixed at best, and their impact on public finances has, on the whole, been unambiguously negative, especially in the case of the education and pension reforms.

We believe that the slowdown described above is indicative of a stagnation – or even a partial reversal – of the reform process, and the documentation of this reform stagnation and the examination of its causes are among the central tasks which we will address in this country report. Examples of setbacks for the reform of the economy include increased agricultural protectionism and interventionism, state support for some loss-making enterprises and industries (e.g., the coal industry), the creation of a sugar cartel, the administrative consolidation of the banking sector. Reform stagnation, if not setback, could also be observed in the case of the consolidation of the state monopoly in telecommunication and the failure to significantly reduce the number of licensing requirements. Among the factors to which various observers ascribe these tendencies are: weakening of the political will of the governing elites; the consolidation of the power of special interest groups; the closing of a "window of opportunity" for fast and radical reforms, and the degradation of the political process as clientelism and corruption began to dominate it.

Growing interest group pressure and clientelism in economic policy making led to increased dysfunctions in decision-making at all levels of public administration – a sort of "spoils system" where assets controlled by the state were used in favor of ruling coalitions and their allies. At the same time, support for deep reforms has eroded or even vanished among the majority of the society, and discontent with the current economic situation and with government is steadily growing, leading to increases in the popularity of populist politicians (clearly observable in the local elections of autumn 2002).

Moreover, while the gains due to economic restructuring and overall modernization are hard to deny, there is still much work to be done. On the positive side we observe an accessibility of goods and services unparalleled in the past, a rise in the standard of living of the majority of the population (measured, in particular, by consumer durables in their possession), the development and accessibility of information and communication technologies (ICT), and the improvement of such demographic characteristics as infant mortality and life expectancy. On the other hand, the technological change occurring in the Polish economy is generally shallow, there is little real innovation (as evidenced by the extremely low ratio of R&D spending to GDP, one of the lowest in the OECD), many small and medium-sized enterprises (SMEs) are undercapitalized and many are able to produce non-tradable goods only. Poland also suffers from a severely underdeveloped transportation infrastructure.

Finally, while the economic transformation has undoubtedly brought benefits to sizable segments of society – especially to a small, but growing middle class – it has also produced very significant social costs. These include the very high rate of unemployment mentioned above. This is the single most important factor contributing to poverty, which – although not very deep – is quite extensive, reaching 15% in 2001. In the longer run, poverty may contribute to the rise of a permanent underclass of the excluded. Coupled with relatively high income differences, this may pose a threat to the reform process, leading to continued growth of the popularity of extremist, populist parties.

2. Research questions, methodology, and hypotheses

The lessons learned from the Polish experience provide a wealth of information concerning both good and bad practices. The Polish experience shows that even a country which for several years was regarded as the leader in the post-Communist transition can encounter substantial stumbling blocks, leading to stagnation or even reversal of the reform process. Even the successful radicalism of the reforms undertaken at the beginning of transition does not in itself guarantee the sustainability of the rapid pace of the transition toward a market economy and liberal democratic society. Our main purpose is to identify both the factors underlying the success of those reforms that were successful and the factors behind the failures in those areas where success was not achieved.

For reasons of space, we cannot cover all of the reform initiatives (or areas in which reforms were not undertaken) of the period studied. We have chosen to deal with the following areas of reform:

Reform of the state machinery. Here we are interested in the reform of public administration itself. In particular, we focus on the civil service and the justice system. This represents, as it were, the “meta-level” of reform: reform of the state itself.

Macroeconomic stabilization and economic liberalization (including internal and external trade and price reform). This package of reforms, introduced on 1 January, 1990, was the cornerstone of the transition of Poland’s economy from plan to market and the key to the country’s emergence from the economic crisis that characterized the final years of Communist central planning in the country.

Enterprise reform. This includes privatization and restructuring, corporate governance, the financial restructuring of enterprises and banks, anti-trust policy, and the like. This represents the micro-level of reforms.

The pension system. This is an important example of a reform that was delayed – i.e., did not occur in the first wave of reforms at the beginning of the 1990s – but was nevertheless carried out later with a certain degree of success.

Some very important areas of reform which we have omitted include the development of democratic governance at the subnational (municipal, country and regional) level, as well as the health service and education. As stated, we have had to restrict our focus for reasons of space, and an attempt to deal with each of these issues would involve us in a great deal of fairly technical, sector-specific issues. Moreover, we believe that the fundamental factors underlying reform failure and success which we will describe in those areas which we have chosen for our study can to a large extent be generalized to those areas which we have omitted.

We will describe the reforms, assess their relative success or failure, and analyze the causes underlying those successes and failures.

On the theoretical level, our analysis will be informed primarily by work on three interrelated major areas of concern:

- The role of the state in market-based economic development;
- The nature of the state's interaction with society in effecting reform, and
- The role of institution building in the progress and sustainability of reforms.

The following hypotheses will be tested in this study:

Hypothesis 1. One of the key factors in the political economy of reform success is the degree of match between technocratic or participatory approach compatibility and the degree to which it is in fact implemented using either a technocratic or participatory approach. Reforms are successful where there is a good match.

We propose a classification of reforms on which we base a number of our hypotheses. We classify reforms by the degree to which they lend themselves to a technocratic approach as opposed to a more participatory approach involving negotiation among various social actors – we can refer to this as *technocratic approach compatibility* and *participatory approach compatibility* (e.g., we could hypothesize that macroeconomic stabilization and liberalization are relatively technical operations, which can be conducted centrally and in a rather technocratic manner, whereas enterprise reform and public sector reform are decentralized learning processes which require much more participation from various stakeholders).

Here, we build on the framework suggested by Hausner (1995) in his discussion of what he calls "imperative" and "interactive" approaches to reform in the transition environment (using the language of our hypotheses these terms could be replaced by the terms "technocratic" and "participatory," respectively). Whereas in the past debate over the relative merits of various such reform approaches has tended to take the form of advocacy of the superiority of one approach over others, our innovation in this project would consist in suggesting that there is no universally superior approach and identifying criteria for evaluating which approach is most appropriate for a given type of reform.

> ***Hypothesis 2.*** The negotiated or participatory approach is successful when the leading role is assigned to the relevant social actors themselves. The latter are thereby forced to engage in a learning process of seeking compromises amongst themselves, with the state's role limited to that of referee. On the other hand, it is unsuccessful when the state or its representatives act as distributors of public goods or rents, leading to rent-seeking behavior by the participants and tendencies of the state to seek to satisfy all conflicting interests.

A useful approach is that of Stiglitz (1987, 1999), who analyzes the nature of learning (knowledge transfer) in the economic development process. Echoing Hayek (1945), he refers to the necessity of using local knowledge about local factors to adapt global knowledge about "best practices" to local circumstances. Referring to Michael Polanyi's well-known distinction between tacit and explicit (codified) knowledge, he then goes on to discuss how practical know-how is largely tacit knowledge whose transfer requires learning methods involving personal interaction of the various participants in the process. Finally, he discusses the process of "learning to learn," whereby social actors, through participation in the process of policy design and implementation, learn how to adapt globally accessible knowledge to their particular circumstances.

> ***Hypothesis 3.*** One of the key factors leading to the stagnation of reforms in the later stage of the Polish transformation was the failure of reformers in the early stage to appreciate the importance of public sector reform and, accordingly, initiate reform efforts in this area.

Scholars ranging from Polanyi (1957) to Olson (2000) have demonstrated the importance of the state's strength and its capacity to play a "market-augmenting role" (Olson's term). Because of the importance of the state's role in building the market economy, the reform of the state itself is a necessary condition for sustainable reform success, as Amsden et al. (1994) argue. Failure to address these questions led to the capture of the reform process and the state apparatus by clientelism and corruption.

> ***Hypothesis 4.*** In order for a reform program to be successful, policy making and institution building must take account of initial conditions and existing cultural and institutional factors, and stakeholder interests. Concretely, the involvement of local actors in both the design and implementation of reforms is an important factor in their success (that is, to use a popular expression, "ownership" of the programs should be local), and reforms should be "compatible" with the country's human capital endowments and cultural habits.

Hypothesis 5. The "point of no return" beyond which a country can no longer revert to classic central planning and a totalitarian political regime is reached very early in the transition process. However, this point is often mistaken for the point at which a "critical mass" of market reforms is achieved. But, in fact, every transition country needs to pass another critical point, after which the forces and mechanisms acting in favor of further reforms become stronger than special interest groups which establish a privileged position for themselves in the early transition, and the reforms become self-sustaining.

Major stakeholder interests consolidate around de-etatization and a certain measure of political pluralism and economic liberalization in the very early days of transition. The problem is that the re-emerging pluralism and partial liberalization of the early transition period gives rise to special interest groups ("early winners") which gain rents from limited access to public goods and economic privileges (licenses, monopoly positions, etc.), while lack of effective accountability in the public sector leads to its capture by these interest groups. Slow and inconsistent reforms enhance the influence of such groups, and at the same time, enterprise behavior is adjusted to reflect the distortions of an environment which is only partially reformed. This produces a threat of slow-reform, low-level equilibrium trap. Therefore, the success of reforms depends on the degree to which both the interests of potential allies of the reformers and the need to overcome the existing (often informal) structures of group interests formed under Socialism (which may retain their influence and hinder the reform process) are taken into account.

Olson's (1971, 1984) analysis of the mechanisms whereby special interests capture the political process is very well known and will be particularly useful here. Greskovits (1998) compares the experience of the Central European transition counties with those of many Latin American countries, noting that economic reforms involving austerity programs often break down in Latin America due to public unrest and asking why this has not been the case in Central Europe. He argues that the Central European reforms have been more successful and sustainable than in many Latin American countries because of the presence in the Central European countries of various structural, institutional, and cultural factors, often absent in Latin America, that have acted as brakes on the types of special interest group collective actions analyzed by Olson which can undermine reform. On the one hand, for example, policy makers who promise populist reversals of reforms during in election campaigns find their options effectively limited due to such institutional constraints (such as those imposed by international institutions) after taking office. On the other, the social potential for unrest is limited due to the relative lack of trade union militancy and the relatively small proportion of the population which is genuinely impoverished and marginalized.

Our analysis of the role of interest groups also relies on the work of Hellman (1998) and Mitra and Selowsky (2002).

Hellman (1998) described the low-level reform equilibrium trap and claimed that even though the reforms deliver the largest gains when they are comprehensive, if in the early phases of reform there are concentrated gains among a subset of actors that arise from partially reformed economy, and if political and legal institutions do not constrain the winners, they will seek to consolidate their advantageous positions – which allow them to extract monopoly rents – in the evolving institutional framework, and block further reforms.

In addition to these early winners, two more groups of actors, whose strength and behavior affects the course and dynamics of transformation, exist.

The first group are "reform advocates" – actors interested in consistent market reforms, because they benefit from reform progress. Apart from pro-reform politicians, these are actors connected to the largest part of the emerging private sector (that part of it which is not captured by the early winners), both privatized and green-field. After Karla Hoff, they can be called "entrepreneurs," as opposed to the "tunnelers" of the first group (Hoff, 2000).

The second one is also a large group that can be described as "transformation losers" all progress in market reforms is a threat for them as an interest group. Nevertheless, with intensification of reforms, their losses do not increase with initial dynamics (because of improvement of overall economic conditions and some adaptation processes within this group of actors).

It should be noted that while these three interest groups exist during the whole period of transformation, both their composition and their influence on the reform process changes in the course of reform implementation. There are flows from one group from another. In the course of the Polish reforms, we have observed outflow from the group of reform losers in the state sector to the group of reform advocates in the case of privatization, and to the group of "tunnelers" in the case of suspended privatizations and creation of sectoral monopolistic structures (in coal mining, sugar industry, metallurgy, etc.). The "reform advocates" group may grow not only due to the privatization of the enterprises for which they work, but also due to inflows from the group of early winners, when some of its representatives are no longer satisfied with the gains they enjoy at the early equilibrium point and become aware of the possibility of gains to be had from, e.g., an efficient public administration and justice system, transparent corporate governance, a stable currency, etc. By contrast, when reforms stagnate, some actors from the reforms advocates group may adapt to such an intermediate state of economy and its institutional framework created by the low reform equilibrium trap, coming to view any changes in the *status quo* (even reform acceleration) as too risky to the gains they have realized to date.

Based on the findings of Mitra and Selowsky (2002)[2], we can draw three curves which correspond the gains of these three interest groups (see Figure 2.1). For the reform advocates, reforms would impose some temporary sacrifices, with the promise of increasing gains as reforms intensify. Early winners prefer a partial reform scenario, supporting reforms up to level R_2. Whereas reform losers prefer the status quo (R_0) and oppose all reforms.

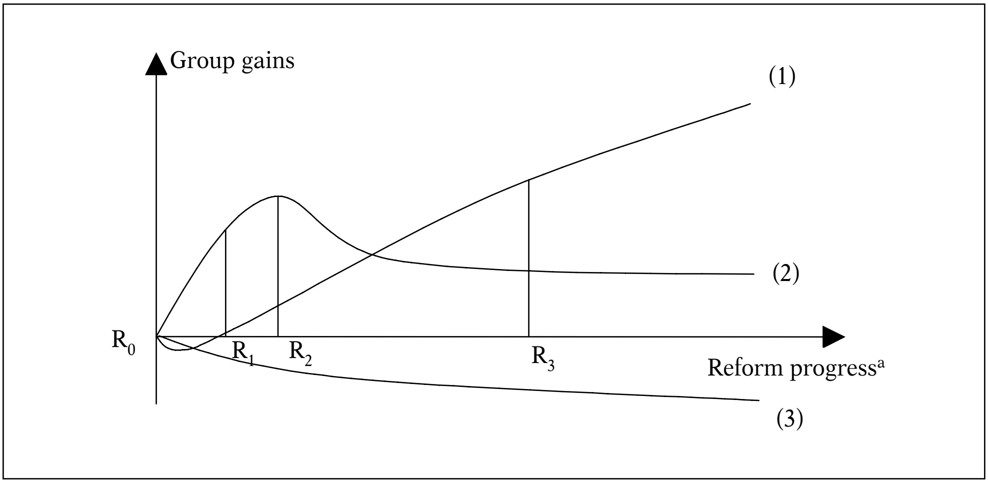
Assuming that gains of interest groups determine their impact on reform process through the voting mechanisms, lobbying, etc., Figure 2.1 shows that in the course of transition, configurations of interest groups pass through three critical points. The R_1 point is a "point of no return," after which the combined force of "reform advocates" and early winners is stronger than that of reform losers. This point is often mistakenly taken for the "critical mass" point of market reforms, but in fact it only denotes that return to centrally planned economy is no longer possible, but does not guarantee the success of market reforms. The most dangerous is the R_2 point which represents the highest gains of the "early winners" who have a still strong tactical ally in the form of reform losers – this point represents the above-mentioned equilibrium trap. As was stated above, the equilibrium is additionally enforced by adaptation of some of the "reform advocates" to the existing rules of the game and lack of credibility of the government. Some other factors also contribute to petrifaction of such an equilibrium, among others the reform fatigue syndrome (Lora et al. 2003) – loss of public confidence in the pro-market reforms and/or less pro-active stance towards them – especially if a country does not experience deep economic crisis and both leaders and society become less willing to take risks.

At R_3, pro-reform groups become stronger than "early winners" and "transformation losers" together and are able to either compensate the losses of the other groups or to generate enough political pressure to neutralize opposition to continued reform. In other words, at this point the free play of actors and interest groups no longer poses a threat to the system, there is no need in special policy to prompt development and to suppress "anti-reform" forces.

Figure 1 shows the crucial importance not only of fighting against "early winner" groups, but also of eliminating the "transformation losers" group, which can be done

[2] See also World Bank (2002a).

Figure 2.1. Interest groups gains in the course of transformation



(1) – groups interested in consistent reforms; (2) – "early winners"; (3) – "transformation losers"
R_0 – starting point of the transition;
R_1 – "point of no return";
R_2 – the most favorable point for the "early winners";
R_3 – "critical mass" point.
[a] For example, measured by the EBRD transformation indicators.

mainly by fast and consistent reforms aimed at elimination of the state sector of the economy. Figure 2.1 is a good illustration of the thesis that slow and inconsistent reforms may jeopardize the ultimate goal of the post-Communist transition: building a selfsustaining market economy and democratic society.

Hypothesis 6. External factors are important in shaping the reform process.

This hypothesis relates to three concrete aspects of the Polish reform experience:

a) The prospects of NATO and EU membership have represented both an opportunity (accession as a reward for reform) and a threat (non-accession as punishment for failure to reform). Accordingly, the strength of the incentives associated with this external factor depends on the credibility of the threat of non-accession. We hypothesize that the credibility of this threat diminished over time in the case of Poland and this was one of the factors leading to reform stagnation.

b) We will also test the hypothesis that international institutions such as the World Bank, IMF, Paris Club and London Club have played a critical role in constraining the actions of policy makers as well as in shaping their thinking about both the content of reform and the manner of their implementation.

c) Our third hypothesis concerning the external environment is that the international business cycle and external shocks such as the collapse of the CMEA in the early

1990s acted to hinder consolidation of reforms (e.g., by extending the "transformational recession" and thereby reducing the popularity of reform-oriented political parties).

To test these hypotheses, in addition to use of the existing literature on the Polish reforms, we have conducted interviews with consultants and experts personally involved in, or closely observing, the Polish reform process.

3. Reforms of the state machinery

In this section, we focus on the reforms of two segments of the state machinery: the civil service and the administration of justice. In both cases, we deal with reforms that were incomplete and/or flawed. This resulted in shortfalls in the state capacity for designing and implementing other reforms, as well as for disciplining the social actors into conforming with the rules of the game. Architects of the Polish reforms – such as Jerzy Hausner, who co-authored the Polish pension reform – perceive the ineffectiveness of state machinery as an important stumbling block. While it is capable of routine work, it is largely ineffective at designing and implementing strategic changes (Hausner, 2004).

3.1 Civil service

The creation of a competent, honest and apolitical civil service was supposed to alleviate low professional and ethical standards of Polish public administration (World Bank, 1999; Grosse, 2001). However, the laws introducing the civil service were passed relatively late and have been changed to suit successive governments. The first regulation was passed in 1996, to be quickly changed in 1998 (after the formation of the new government in the autumn of 1997). There are deep doubts as to the degree to which these regulations have really been implemented in practice (Brunetko, 2003). At the same time, there seems to be little public appreciation of the importance of these reforms, as only slightly over 20% of adult Poles have ever heard of the civil service, and only 5% have a rudimentary knowledge about its character and functions (Brunetko, 2003, 3).

Legacy and Challenges

Before 1989, there was no civil service in a legal sense. Public administration worked under the general principles of the party *nomenklatura* system, according to which all appointments in the administration were made on the recommendations of the Communist party. Thus, the period of state socialism left a particular legacy: people employed, trained and socialized in a system which the political and economic transformation was supposed to change continued to staff public administration after 1989. Moreover, there was little in the way of traditions dating from the period before state socialism. Poland has no tradition of centralized absolutism, which lay at the roots of early modern bureaucracies in France, Prussia and Sweden – quite the contrary, it developed probably the extreme case of a government system based upon clientelism (Mączak, 1994). In the crucial period for the formation of modern European nation states, Poland was partitioned between Russia, Prussia, and Austria. Although the latter two developed very sophisticated public administration systems, this did not influence the Polish tradition much, as these states were perceived as usurpers and Polish nationalist ideology considered acting against the state as patriotic. While modern public administration had developed during the inter-war years, it was a short period, and during the war, under the German and Soviet occupation, acting against the state once again became the only socially accepted behavior (Górski, 2001-2002).

Similar attitudes – although not in such dramatic force as during the World War II – were widespread among the democratic opposition during the last two decades of state socialism. While renouncing force or violence, opposition activists questioned the legitimacy of the existing state and, in their political practice, successfully relied upon spontaneous civic activity fuelled by idealistic motivations, and not upon the formal, legal-rational hierarchical structures. Thus, of the two forces that were to shape the Polish institutions after 1989 – the ex-communists and the ex-oppositionists – one had a tradition of state abuse and the other of state negation.

In contrast to very vivid debates of the early 1990s on the issues how markets should be institutionally designed, there was very little debate on redesign of the state machinery. In particular, no attention had been paid to the civil service. Moreover, when this debate started, no earlier than five years after the collapse of state socialism, it was mostly among specialists professionally involved with administrative change. During this debate, foreign experience was studied and merits of various systems were analyzed (Office of the Council of Ministers, 1995; Rydlewski, 2001; Grosse, 2001). The issue of a desirability of civil service re-emerged in the daily and weekly press only at the end of the decade, mostly in relation to a growing awareness of corruption, but rarely went beyond either complaints or demands for change.

At the beginning of the transformation, the attention of the new political elite was focused not on the desirable institutional design, but rather on the practical and political question of the suitability of the officials of the former regime in the new situation. It was evident, however, that it was impossible to introduce radical changes, as the problem concerned tens of thousands of persons for whom there were no ready replacements available (see Table 3.1).

The quality of the public sector also suffered because of noncompetitive salaries[3]. Table 3.1 shows that there was a tendency to develop public administration in size rather than in quality. There was little (if any) systematic effort to introduce pay structures that would lead to the establishment of a lean administration – not large in size, but well paid, highly competent and honest.

Table 3.1. The size of the central public administration (including regional and county authorities, in thousands)

Year	Employed
1990	75.2
1991	93.3
1992	104.7
1993	115.4
1994	133.4
1995	137.5
1996	151.0
1997	157.5
1998	166.0
1999	142.9
2000	135.0

Sources: Central Statistical Office (1992, 1994, 1995, 1996, 1998, 1999, 2000, 2002).

On top of that, there was little support from the international financial institutions playing an active part in the Polish transformation. In the early formulations of Washington Consensus type approach to transformation, the question of state capacity and strength tended to be neglected. Those arguing the need to strengthen the civil service were in the minority (cf. Nunberg, Nellis, 1990; Nunberg, Barbone, 1992). The prevailing tone of advice was to stress "government failure" and the need to reduce the state both for fiscal reasons and for all kinds of political economy reasons (rent-seeking etc.). This attitude was often amplified in the rhetoric of post-communist politics, because of the historically understandable allergy towards the state and lack of belief in the possibility of reforming the existing state machinery. There initially was little appreciation of the fact that Poland, like many less developed countries, had a weak state with a deficient bureaucracy, which required repair (Kochanowicz, 1994). Only since the mid-1990s was a revival of attention to the question of "state capacity" and the role of the state as an institution builder observed (World Bank, 1997, 2002).

[3] This prompted government to provide special treatment to those ministries which were of particular importance for the transformation – Finance and Privatization.

In fact, as Table 3.1 shows, the size of the public administration has not decreased; quite the contrary. Moreover, the figures given in this table may be doubled if local and regional administration (which does not fall under the regulation of the civil service) are added. Employment in public administration increased after the lowest level of territorial administration, the *gmina* (township or municipality) was democratized and empowered in 1990, and then once again after the reform of 1998, which introduced the *powiat* or county level.

Table 3.2 provides an indication of how high the economic costs of the low quality of Poland's public administration were approximately five years ago. The table shows results of an EBRD survey in which business managers told what percentage of their time they spent in dealing with public officials. Poland was even worse than Russia, not to mention its Central European neighbors.

Table 3.2. Time spent by managers on contacts with public officials (% of total working time)

Country	Time (%)
Poland	9.5%
Russia	9.0%
Slovakia	7.0%
Hungary	7.0%
Czech Republic	2.5%

Source: EBRD, 2002.

New Regulations

The Solidarity government made a move towards the improvement of public administration through a creation, in 1991, of the National School of Public Administration (KSAP) – a postgraduate, professional two-year school, loosely modeled on the French Ecole Nationale d'Administration, "[b]y far the most energetic, ambitious effort in public administration training" (Nunberg, Barbone, 1994, 267). However, as the number of graduates has been small, it has played a limited role in the restructuring of public service. Moreover, they also often seem not to fit the established work culture and, when entering various agencies, are treated with a lack of sympathy by the older colleagues (Brunetko, 2003). The necessity to introduce more comprehensive changes was acknowledged by subsequent administrations, but the first law was not passed until 1996, under the rule of the SLD-PSL coalition.

This legislation declared the apolitical character of the civil service and a dividing line was drawn between political and professional appointments. The PM, the ministers and their deputies, and voivods (regional governors) and their deputies were declared political appointees, resigning with the change of administration. Handpicked members of their political cabinets and their advisors were treated in a similar way. As for the civil service itself, the reform introduced the concept of the civil servant (*urzędnik służby cywilnej*), to be nominated according to a strict procedure. The 1996 regulations also introduced a distinction between heading a given sector of public administration (a function performed by a minister or equivalent official at the central level, and by the voivod at the regional level) and managing the ministry or voivodship office. The latter function was to be performed by directors general, apolitical members of the civil service.

This reform was short-lived, as the new AWS-UW administration that took office in 1997 introduced a new, differently designed law in 1998 (effective in 1999). The new regulations followed the line of the 1997 constitution, which required the creation of a professional, apolitical civil service corps, and which banned elected officials from holding posts in the public administration (except the posts of ministers and state secretaries).

The general public has not shown any particular interest in the creation of the civil service. This problem also seemed to attract much less attention of experts than other public sector reforms – such as local and regional administration reform, pension system reform, or reform of health care – that were introduced by the AWS government. Thus, the most important actors seemed to be political parties. While they paid lip service to the needs of introducing an apolitical service, their attitude in practice was negative. Poland quickly learned the spoils system and developed an informal pattern of "the winner takes all," i.e. vast changes in the administrative personnel following changes in government. The post-Solidarity forces usually justified this by the desire to bring in people untainted by a communist past, while the Social Democrats stressed the professionalism and experience of their nominees. Each side tried to influence the final outcome first by designing the actual shape of reform in a way convenient for them, and second by circumventing the rules in the appointment process if that suited the needs of the day. Clientelism and patronage have developed on both sides. For these reasons, in terms of the framework proposed in section 2 in the discussion of hypothesis 5, we identify the political parties constituted at the outset of the transition as the group of "early winners" who have blocked the implementation of reforms which would reduce the scope of the all-encompassing spoils system to create a true civil service in Poland.

The 1998 regulations defined the civil corps as all those working in the public administration and divided them into two groups: employees (*zatrudnieni*) and functionaries (*urzędnicy*). The Head of the Civil Service is appointed for a term of five years by the Prime Minister, and backed by the Bureau of the Civil Service (*Urząd Służby Cywilnej*). The Civil Service Council, appointed by the Prime Minister, makes recommendations and expresses opinions on the organization of examinations and competitions. The new law became operational in mid-1999. The new definition of the civil service resulted in the increase of its membership from 104 at the beginning of 1999 to 116,000 at the end of the year (Rydlewski, 2001, 36). As in the regulations of 1996, members of the civil corps are restricted in their political activity, business dealings and outside employment. The entrance to the corps is through a labor contract, for a probationary period of six months. Information about the available positions has to be made public. After a review procedure, the temporary contract can be changed to a regular labor contract.

The change of status to a functionary is made on the basis of examinations, organized once a year. The number of appointments is limited by budgetary considerations. KSAP graduates are exempted from the examinations. Functionaries are not employed in the sense of Labor Code, but appointed. Their position entails more privileges (pay scale, job security), but the restrictions affecting them are also more severe. The target figure for the share of functionaries in the civil corps is 15% (Rydlewski, 2001, 44). The regulations also introduced the concept of a "higher functionary" (from ministry departmental director up). Appointment to these positions requires organization of a competition, open to all functionaries. The institution of political cabinets (whose members are not recruited from among the civil service) has been retained from the 1996 regulations.

The extent of the civil service is confined to those sectors of the public administration which are answerable to the ministers and to the Prime Minister. They comprise the central institutions as well as offices of the national administration at the voivodship and *powiat* levels. The administrative staffs of elected governments at the *gmina*, *powiat* and voivodship levels are excluded, as are the offices of the President, the *Sejm* and the Senate. The customs service operates under different regulations, and the foreign service is regulated by a separate law.

The Outcomes

Without doubt, the introduction of the civil service has been a step in the right direction, insofar as it defined the role of public administrators and erected barriers between them and the worlds of business and politics. The regulations are criticized for concentrating all the issues of the civil service in one single office, for introducing a single corps and thereby failing to differentiate various specific areas of public service (with the aforementioned exceptions of the customs and foreign service), for imprecise regulations concerning the higher functionaries, etc. (Rydlewski, 2001, 56). There is also a lack of similar regulations for local administration.

Implementation, moreover, has proceeded slowly. In 1999, many individuals employed in the public administration were simply reclassified as members of the civil corps with a stroke of the pen; however, this did not change much in substance. The interest in promotion to the status of functionaries was has been low. In 2000, less than 600 people applied, and only about 200 of them got appointments (Rydlewski, 2001, 44)[4]. This obviously restricted the recruitment base for the higher functionaries and opened up the possibility that persons who went through the competition procedure would be employed on a temporary basis, which the regulations allow in specified circumstances.

The results of the first qualifying examinations for the status of functionary shed light on the overall quality of the personnel employed in the public administration (Rydlewski 2001). Only 5% of applicants had certificates of foreign language knowledge (which was required of the functionaries), and only 5% declared a willingness to acquire such a certificate. The examinations conducted in 2000 showed poor orientation in general matters and very low writing skills (Rydlewski, 2001, 44). Taking into consideration the fact that those who applied are probably the most ambitious among the civil service personnel, these results give little ground for optimism.

Reasons for the late introduction and slow and half-hearted implementation of the civil service reform can be summarized in three related points.

- Politicization. The practice of the reform implementation shows the lack of real commitment of political parties to introducing the civil service, as it deprives them of the possibility of job distribution and makes the administrative staff more independent and less servile (Grosse, 2001). The aforementioned personnel moves in 1997 may easily be interpreted as showing that both the losing and the winning coalitions were interested in having as much influence on the appointments to the civil service as possible. The same pattern seems to have been continued when the SLD regained power in 2001, as flagrant cases of violation of the civil service regulations show (Brunetko, 2003).
- Path dependency. Because of its history, Poland has little tradition and appreciation of the importance and functions of the state. As political philosopher Bronisław Łagowski (2004) puts it bluntly, "Poles are unable to build a state." Having little experience with creation of impersonal, legal-rational organizations, Poland instead has a long tradition of a political culture based on clientelism and personalized relations (Mączak, 1994; Kochanowicz, 1994, 2004; Tarkowski, 1994). Thus, clientelistic attitudes shape everyday behavior of the present-day functionaries (Hausner, 2004). Poland also shares with many less advanced

[4] The same year 260 graduates of KSAP got appointments (Rydlewski, 2001, 44).

societies a tendency of the middle classes to rely on employment by the state, often obtained through patronage. This is the case with Latin America, where – as Naím (1994) observes – "discharging formal functions that justify an agency's existence weighs much less in determining its daily operations than does the need to serve as a welfare agency for its employees and their families." This was also the case throughout the last two centuries of the history of all Central Eastern Europe (Janos, 2000).

- Passive resistance of the employees. Many of the employees, realizing their limited skills and limited possibilities of improvement, are hardly interested in introduction of the merit-based system which hinders their chances for survival and promotion.

Assessing the process of implementation of civil service reform, it is necessary to take into consideration historical experience of other countries, which shows that this process is long and protracted (Grosse, 2001). It demands an appreciation of the importance of efficient administration by political leaders, designing and building proper legal institutions and – last but not least – changes of the political culture and work culture by the functionaries and the employees of the public sector.

3.2. Administration of Justice

At the beginning of the present decade the justice system was in crisis[5]. "The Polish justice system suffers from a grave illness, and its treatment demands radical steps and the determination of decision makers" – with these words Marek Safjan, the current president of the Constitutional Tribunal, summed up the situation in 2002 (Zieliński, Zubik, 2002, 113). Symptoms of crisis included low rates of solving crimes, the backlog of cases in the courts, low rate of convictions, a high percentage of suspended sentences (which in practice often means no sentence at all), a low level of crime reporting, and overcrowding of prisons, including waiting periods for serving prison terms (Siemaszko, 1999, 2002, 2002a, 2003). In civil matters, the symptoms were long waiting periods for court hearings, high costs of legal help and protracted procedures in non-litigious cases.

There were two important outcomes of this critical situation. One was that the inefficiency of the justice system hampered economic life because of queues, delays, poor protection of property rights, and financial losses of persons and businesses

[5] The situation has not improved to any significant degree at the time of writing (early 2005).

falsely accused of tax evasions or white collar crimes, who have to wait long before their name is cleared (Instytut Wymiaru Sprawiedliwości, 1998). Another was that it has eroded the legitimacy of the state and trust in public institutions in general, or – to put it differently – that it negatively affected the process of building institutions of the democratic state and the rule of law, which were among the most important goals for the post-communist societies.

In what follows, we focus on a single, pivotal segment of the justice system, namely the courts, and one aspect of that system's operations, namely efficiency. We will not deal here with other important elements, such as the Prosecution Service, the police force and the prison service, as well as such many important aspects of the judiciary itself such as the penal tendencies or corruption.

Early Reforms

The Polish legal system is a variant of the continental European model, historically influenced by both the German and the French traditions. Although heavily affected by the period of state socialism, it nevertheless retained a certain continuity. The standards of teaching of the legal profession – at the leading universities, at least – were relatively high, as there was a continuity of professorship and legal schools through the communist period. Laws were changed and amended to suit the demands of the communist political system and command economy, but not changed wholesale. Judges were recruited and promoted according to the *nomenklatura* system principles, but – except during the times of Stalinism and cases of particular political importance – they retained a degree of independence. In the late phase of communism, even certain spheres earlier reserved for a discretionary decision of the state were put under a degree of court control through the introduction of administrative courts, labor courts and the office of the ombudsman.

The changes introduced after the fall of state socialism did not have an abrupt and wholesale character – as was the case for example with macroeconomic policies – but have had rather a piecemeal, incremental and continuous character. The basic principles of the new position of the judiciary were already negotiated during the Round Table talks of 1989. The ideas about the position of courts crystallized during the constitutional debate of the early 1990s, which stressed the idea of separation of powers, the independence of judges, and the right to appeal (Kubuj, 1999). Milestones in the reform process were amendments to the Constitution in April 1989, which stressed the separation of powers and secured the position of the judges, a law of July 1989 which introduced the Courts of Appeal, the Constitutional Act (so-called Little

Constitution) of 1992 which amended the Constitution of 1952 and the new Constitution of the Republic of Poland of 1997. Also noteworthy are the new Company Code adopted in 2001 and the new criminal code of 1997.

As a result of reforms, the system of justice is composed of tribunals and courts (Kubuj, 1999; Jankowski, Siemaszko, 1999). The Constitutional Tribunal (set up in 1985) decides in cases related to the constitutionality of national legislation and its compliance with international agreements. The State Tribunal (set up in 1982) decides in cases when holders of the highest positions in the state are charged with violating the Constitution or other legislative acts. The court system, as a result of reforms undertaken after 1990, is composed of the Supreme Court, the Chief Administrative Court (with 10 local branches), the military courts and the common courts. The common courts are divided into 10 courts of appeal, 41 regional courts and 296 district courts. Until the 1997 Constitution, misdemeanor boards also existed; the new constitution shifted their responsibilities to the district courts. The common courts have specialized divisions (often called courts as well): Family and Juvenile; Labor and Social Security; Commercial; Sanction and Enforcement, and Registration.

Together, the courts employ close to 8,000 judges. The judges enjoy very far-reaching independence and autonomy: they are appointed by the President upon the nomination of the National Judiciary Council, a self-governing body of the judicial profession. They cannot be removed from office and have judicial immunity (their disciplinary accountability is before their professional bodies). On the other hand, they are barred from political activity and outside employment. Their salaries are a multiple of the average salary in the public sector and depend solely upon position and seniority. After retirement they are granted pensions equal to 75% of last pay. Their daily work is supervised solely by the Court President (responsible for distributing cases and organizing court work). The Court President is elected by other judges.

The reforms of the early 1990s stemmed from the general ideas guiding the democratic transformation – the ideas of rule of law, of the separation of powers and of human rights. Rule of law was supposed to be the basic principle of public life, which led to the conclusion that citizens should be given easy access to courts. There was a widespread belief that the independence of courts and judges should be protected as much as possible, especially given the negative experience under the previous regime. In regard to criminal procedure, there were beliefs that protection of the rights of defendants needed to be strengthened, particularly through elaborate trial rules. These beliefs undoubtedly stemmed from the public memory of bending the legal rules in political trials under communism. Thus, in terms of the framework proposed in section 2 in the discussion of hypothesis 5, judges constitute the group of "early winners" of this reform area – a group, which, in accordance with that framework, effectively blocks further reform.

Table 3.3. Cases in the Polish Common Courts (in millions)

Year	Old	New	Closed
1989	0.3	2.0	1.9
1990	0.4	2.4	2.3
1991	0.4	2.7	2.7
1992	0.7	4.2	3.9
1993	0.9	4.6	4.3
1994	1.2	4.9	4.5
1995	1.6	4.9	4.8
1996	1.6	4.9	5.0
1997	1.5	5.0	5.1
1998	1.5	6.4	6.1
1999	1.9	6.6	6.7
2000	1.8	7.4	7.4

Source: Instytut Wymiaru Sprawiedliwości (2001, 33).

Dysfunctionalities of the System

The ideas guiding these reforms were high-minded, but they tended to produce various unintended consequences. Zieliński and Zubik (2002) state that procedures in the Polish courts are overcomplicated and protracted, access to courts restricted because of high costs of legal advice, the efficiency of execution of court decisions low, and court rulings often incomprehensible for the public. They cite opinions of experts according to which courts are inefficient, in a state close to collapse and devoid of any prestige. The most visible symptom of the court system's low efficiency is the rising backlog of cases, which in 1996 amounted to 1.6 million and by the end of 1998 reached 1.9 million (see Table 4). At that time, it took on the average 18 months to two years to have a case decided (Kubuj, 1999, 258; Zubik, 2001, 35). The protracted character of court proceedings is stressed by several analyses of the Institute of the Administration of Justice. It assesses this as the most serious problem of the Polish system of justice, although a slight improvement was observed in the year 2000 (Instytut Wymiaru Sprawiedliwości, 1998, 2000; Siemaszko, 1998; Siemaszko n.d.). As a result of *de facto* difficult access to courts, Poland lost several cases at the Strasbourg Tribunal[6]. Out of 42 rulings of the Tribunal in cases against Poland, 24 supported the claims of the plaintiffs (*Polityka*, February 22, 2003). The inefficiency of the courts has led to a dramatic decrease of the prestige of the judicial power, and generally low trust

[6] An extreme case concerned a person who waited ten years for a verdict for compensation for medical malpractice; that person died shortly after filing a complaint in Strasbourg (Zubik, 2001, 36).

in the justice system in turn has led to reduced rates of reporting crimes (Zubik, 2001, 55ff; Siemaszko, 1999, 2001). The economic effects of the low efficiency of the court system can be surmised on the basis of the EBRD statistics on remittance recovery time, as shown in Table 5. According to these data, 31 days are needed to recover remittances in Poland (as opposed to 16 days in Hungary, 12 days in the Czech Republic and Slovakia, 8 days in Russia and 7 days in Latvia).

Table 3.4. Remittance recovery time (in days)

Country	Days
Poland	31
Czech Republic	12
Hungary	16
Slovakia	12
Latvia	7
Russia	8

Source: EBRD 2002.

The main reasons for the low efficiency of the court system are as follows.

- Too wide jurisdiction of the courts. This leads to the overloading of judges and courts beyond their capacity (Siemaszko, in Zieliński, Zubik, 2002; Siemaszko, 2003; Osiatyński, 2003a). Part of the reason is constitutional, i.e. the idea of giving citizens easy access to courts. This is, however, also partly an unintended consequence of various legislation. Of particular importance for the jamming of the system are non-litigious matters (registration of businesses etc. – over 2.5 million cases in 2000 [Instytut Wymiaru Sprawiedliwości 2001, 34]), the petty cases shifted to courts after the misdemeanor boards were abolished, and the cases of disability pensions. The latter problem stems from the social insurance law. Under this law, special medical committees grant disability pensions. The changes in regulation abolished the right to appeal decisions of these committees within the social insurance administration. This prompts the dissatisfied clients to seek court appeal immediately. The number of such cases in the common courts increased six-fold between 1989 and 2000 (Instytut Wymiaru Sprawiedliwości, 2001, 40).
- Deficient legal career paths, affecting judges' work. In general, there is a tendency for the legal professions in Poland to acquire a closed, guild-like character. This is particularly the case of attorneys, the most lucrative legal profession, and one to which entry tends to be barred for people who are not from attorneys' families. Judges' careers are much less attractive, and are for young law graduates from families with no family connections to the profession (Osiatyński, 2003a; Siemaszko, 2003). Thus, becoming a judge is not the crowning of a legal career, but usually a first job, begun after a short internship process (*aplikacja*) which

often immediately follows the completion of university studies. As a result, the experience of many judges is limited both in relation to the substance of the matters they have to decide upon as well as in relation to the preparation and organization of trials (Zubik, 2001, 31; Zieliński, Zubik, 2002, 38-9). The relatively low salaries, moreover, lead the best persons to leave the profession for much better-paid jobs in the private sector (Kubuj, 1999, 261).

- The excessive independence and self-regulatory powers of judges, both as individuals and as a professional group. The idea of judicial independence had been transferred from the Anglo-Saxon tradition of common law, where becoming a judge crowns a legal career and where there is an established tradition of responsibility. Thus, the status of the judge as a functionary of the state (the continental model) had been radically altered. Moreover, this transfer has not been accompanied by the establishment of institutions safeguarding responsibility (Osiatyński, 2003a). The "early winner" group constituted by the country's judiciary organized itself and lobbies the political system to its advantage (Siemaszko, 2003; Osiatyński, 2003a). Judges cannot be removed from office, their pay does not depend upon their work efficiency but only upon seniority, and the court president (elected by his/her colleagues) has very little real power over them. They have legal immunity, and in misdemeanor cases their cases have first to be heard by a disciplinary board of their peers. While this undoubtedly protects legal impartiality, it also prevents the monitoring of efficiency and sometimes makes difficult the punishment of obvious abuses, including corruption, particularly because the National Judiciary Council tends to serve de facto as a judges' trade union, protecting their interests and safeguarding them against public criticism (Osiatyński, 2003a). They also have too many administrative powers regarding the organization of their work, which is not the same thing as independence in sentencing. This excessive independence makes them work much less efficiently than is the case with the members of the prosecution service, who have to answer to their superiors (Siemaszko, 2003).
- Overly complicated and ineffective procedures and poorly organized court work. These problems are particularly harmful in petty cases. In part, they stem from the amendments in the Code of Criminal Procedure, giving the accused and their defenders various possibilities for prolongation and extension of trials (Zubik, 2001, 39). In part, the problems also result from the lack of experience of judges and from "a tradition of transforming almost any case into a large and long trial, during which counselors for each party may argue against each other in the style known from American trial movies" (Zieliński, Zubik, 2002, 25). Polish judges often allow

for redundant evidence and testimony, which lengthens trials (Osiatyński, 2003a). Trials are rarely run in the afternoons, and rarely on consecutive days; usually they are broken up by long adjournments (Osiatyński, 2003a, 2003b). The high share of female judges, as well as the feminization of clerical work, additionally hampers willingness to work in the afternoons, as in Poland women still carry the main burden of household responsibilities (Siemaszko, 2003). Procedures disciplining defendants and hostile witnesses to appear in court are ineffective, which often causes additional delays. Court proceedings are not recorded by professional sworn court reporters; instead, oral depositions are repeated by the judges for the record. This effectively doubles the times of the proceedings (Instytut Wymiaru Sprawiedliwości, 1998; Osiatyński, 2003b, 196-8).

- Poor infrastructure and low quality of court staff. Many buildings are old and dilapidated, with trial rooms inadequate in size and number. There is a lack of offices for the judges, and office space for the clerical workers is also inadequate. (At the same time, the scarce trial space is not used in the afternoons.) Space and storage conditions for court records are insufficient. There is a lack of cells in the court buildings for the accused under arrest. Legal libraries, where they exist at all, are inadequate. Computers and access to legal databases are lacking. According to Zubik (2001, 28-9) only 2% of judges had a PC at their disposal. Judges are overburdened with administrative and clerical work (Zubik, 2001; Zieliński, Zubik, 2002, 42). The clerical staff is inadequate in numbers and skills and is extremely badly paid, which breeds corruption (Zubik, 2001, 31; Osiatyński, 2003a).

There is no lack of ideas for the improvements of the situation in the courts. Quite the contrary, experts (particularly those preparing various reports for the government Institute of the Administration of Justice and the independent Institute for Public Affairs) put together long lists of recommendations for improving the efficiency of the administration of justice. Interestingly, despite the overburdening of the system by the excessive number of cases and by backlogs, there are no proposals for increasing the number of judges. Instead, most of the proposals boil down to making their work more efficient.

Recommendations suggest reducing the workload of courts related to petty cases and non-litigious cases. The first issue is already dealt with through the introduction of special divisions of district courts (*sądy grodzkie*, borough courts) which will rely on a simplified procedures in misdemeanor and petty crime cases. For the second, there is a suggestion of either shifting the non-litigious cases to other, specialized institutions or delegating them to court officials working under judges' supervision (Zieliński, Zubik, 2002, 132). There are recommendations to make entry into the judicial profession competitive, as in Spain (Siemaszko, 2003). Suggestions have been made to make judges work more efficiently by introducing more oversight by the court presidents and through incentives in the pay system, through the introduction of court managers (Siemaszko in Zieliński, Zubik, 2002, 125), through the introduction of a two-shift work system of courts, and through the development of clerical staff. Finally, the necessity of improving the technical infrastructure (particularly, computerization) is emphasized.

Interpretation of the Reform Failure

If ills are diagnosed and experts know how to treat them, why is so little done to improve the situation? The answer is far from simple. Reconstructed in a stylized form, we see that the reform path in the sphere of the administration of justice is incomplete: steps making the system more efficient have not accompanied the strengthening of the rule of law (access to courts), the separation of powers and the independence of the judiciary. There are several possible explanations of this incompleteness.

- *Financial strain*. This is the most obvious reason, related to the tight budgetary policies of the transformation period. The administration of justice is not an exception, as all public services suffer a lack of adequate funding. They also all compete for scarce resources during each budget making cycle. What is striking is the low appreciation of the unique importance of the court system for the overall functioning of the state and the economy.
- *Collective interests*. Judges act as a group defending their interests; during the constitutional process, for example, most of their demands were accepted almost with no discussion (Osiatyński, 2003a). More generally, in this case, the logic of collective action described by Mancur Olson (1965) seems to be relevant: the small lobby of judges has a stronger incentive to retain the status quo than the large body of citizens that would benefit from changes has to actively work for reform.
- *Deficient lawmaking*. The quality of the legislative process is low (Dobrowolski et al., 2004). Part of the reason is the lobbying of interest groups, usual in any democracy, although still badly regulated in Poland. Another reason are poor procedures employed in designing and drafting the regulations by the executive branch. This is clearly related to the low quality of the public administration, analyzed in the previous sub-sections, as one of the principal tasks of the central public administration is to draft new regulations. Moreover, there are equally poor procedures in the parliament. That often leads to outright errors and contradictions, which have to be amended quickly. (Amendment of recently passed laws is a recurring nightmare of the Polish parliament.) Poor lawmaking procedures are often leading to unintended and unforeseen consequences. Not

surprisingly, as Siemaszko (in Zieliński, Zubik, 2002, 120) assesses, the lawmakers are usually not aware of the consequences of legislative changes for the courts' work-load.

- *Poor economic thinking*. The understanding of economics among the wider public, lawmakers, and the legal profession is poor. The discipline of economics of justice, in particular, is neither taught nor practiced. Neither lawyers nor lawmakers have either the methodology or the inclination to look upon their work in terms of inputs, outputs and efficiency. At best, the direct costs related to new regulations are estimated. But there is no thinking in terms of how the incentive structure of altered regulations would affect the behavior of various actors and, in consequence, how it would impinge upon economic efficiency of a given institution.
- *Low perception of the importance of the state*. Last but not least, there is a low appreciation of the importance of the state and low social capacity of state building in Poland, mentioned already at the end of the previous sub-section. This is caused both by the alienating experience of the communist period, and also by the much longer historical experience of a society which did not go through the classical Western pattern – it had no absolutism in the seventeenth and eighteenth century, no constitutionalism and nation state building in the nineteenth, and very little democracy and rule of law in the twentieth.

4. Stabilization and liberalization reforms

As mentioned above, the initial reform package (the so-called Balcerowicz Plan, named after the Minister of Finance, Leszek Balcerowicz) consisted primarily of measures aimed at the macroeconomic stabilization and liberalization of the national economy. The package, which came into effect on January 1, 1990, consisted of five major components: (1) a restrictive monetary policy, (2) elimination of the budget deficit, (3) further liberalization of prices (price liberalization had already begun under the Communists), (4) the introduction of current account convertibility of the Polish currency, and (5) a restrictive tax-based income policy designed to fight inflation.

It is important to note that this package had been preceded by a number of significant liberalizing reforms undertaken during the last two years of Communist party rule. One of these reforms was the introduction of a two-tier banking system (nine independent regional commercial banks were hived off of the National Bank of Poland in 1988). On August 1, 1989, shortly before handing over power to Solidarity (which occurred on 12 September), the ruling Communist party made steps toward price reform, eliminating the system of food rationing which had existed since the early 1980s. Coupled with the indexation which permeated the economy, increases in the autonomy of enterprises allowing for very strong wage growth, and an accommodating monetary policy (interest-free financing of the budget deficit by the central bank), this led to near-hyperinflation (Dąbrowski, 1995).

The specific measures of the Balcerowicz stabilization and liberalization reform package included the following:

- High interest rates designed to bring down inflation, supplemented by an income-based tax policy (based on the so-called *popiwek* tax, a tax on monthly increases in enterprises' wage bills exceeding a coefficient revised monthly by the Finance Ministry) which was to serve as a "nominal anchor";

- Price liberalization (with price controls remaining in effect for coal and coke[7], energy, public transportation, pharmaceuticals and rents in public housing);
- The introduction of very low tariffs in the third quarter of 1990, and
- The introduction of a fixed exchange rate to serve as a second "nominal anchor"[8] (the Polish zloty was pegged to the US dollar); the pegging of the rate was preceded by a significant devaluation.

Anti-trust policy, also an element of the Balcerowicz Plan, will be discussed briefly in Section 5.2.1.

4.1. The actors in the design and implementation of the reform package

In the summer of 1989, while the Communists continued to try to govern and Solidarity leaders began talking amongst themselves about the possibility of forming a government, Harvard economist Jeffrey Sachs, who had worked as an economic advisor to several Latin American governments and was especially well known for his contribution to the Bolivian stabilization program of the mid-1980s, began travelling to Poland at this point to advise the Solidarity group. He was successful in convincing Solidarity parliamentarians of the necessity to rapidly end hyperinflation and move quickly toward a market economy. When Tadeusz Mazowiecki became prime minister in August, he spoke of his need to find a "Polish Erhard," referring to Ludwig Erhard, the author of West Germany's "economic miracle" (Kuroń, Żakowski, 1997). After a brief search, the man found to fill this role was Leszek Balcerowicz, who became finance minister. The team Balcerowicz created when he began work in the Ministry of Finance was drawn in part from a group which had worked with him to design an

[7] Coal prices were liberated 1 July, 1990 (Dąbrowski, 1995).

[8] The use of two nominal anchors simultaneously, which might seem strange at first blush, was actually motivated (at least in the eyes of some of the government's advisors) by the fact that they were to serve two separate purposes. The tax-based incomes policy was intended to defuse the wage-price spiral generating inflation, whereas the pegging of the exchange rate was to serve the maintenance of the country's external balance. Some thought the up-front devaluation was unnecessary and could even be harmful in creating additional inflationary pressure. However, Gomułka (1995), in his role as government adviser, argued that it was necessary in order to stimulate exports and restrict imports, thereby stimulating accumulation of foreign currency reserves, which were at very low levels. He also disagreed with those who saw the fixed exchange rate as a tool for reducing inflation. In his opinion, the exchange rate's efficacy as a policy tool was limited to restoration of the country's external balance, while the appropriate tools for fighting inflation lay in the areas of monetary, fiscal, and incomes policies.

economic reform program in 1981, and partly from among a group of reform-minded economists who had participated in a series of seminars he had led at the Warsaw School of Planning and Statistics during the 1980s. These seminars had been devoted to the problems of the socialist economy, and participants had discussed a broad range of possible solutions, including fairly radical ones such as privatization and other forms of ownership transformation. As a result, these people had had almost a decade of intellectual preparation behind them as they embarked on the reform process (Gach, 1993). However, the role of Sachs remained very important, with his prestige legitimizing the Balcerowicz team's work in the eyes of many Poles while he played the role of an advocate for Poland on the international scene (e.g., in calling for a reduction of the tremendous foreign debt the country had accumulated during the 1970s). In early October 1989, less than one month after Balcerowicz became finance minister, Poland's economic reform plan was even referred to in *The New York Times* as "the Sachs Plan" (Wayne, 1989). Other foreign advisers also played important roles, especially a group of three economists of Polish origin or extraction – Stanisław Wellisz from the United States, and Stanisław Gomułka and Jacek Rostowski from the United Kingdom (the work of the latter two was financed by the British Know-How Fund).

Nevertheless, it is important to emphasize that despite the important role played by foreign advisers, the Polish reform package was definitely "locally owned," conceived and designed by Balcerowicz's team (though some particularly demagogic critics often portrayed the Balcerowicz team as being lackeys of the international financial institutions). In fact, there were often disagreements between the team and its foreign advisers, and the former did not hesitate to carry out their plans over the protests of foreign advisers and international financial institutions in such cases. For example, many experts, including those at the IMF, interpreted the high enterprise profits of 1990 falsely, seeing them as a consequence of exercise of monopoly power by enterprises rather than a simple accounting phenomenon resulting from the low nominal purchase costs of inputs relative to the sales prices of outputs in a highly inflationary environment. As a result of this misinterpretation, many experts advocated postponing price liberalization until state enterprises were broken up. It is interesting to note that in this and other cases of disagreement with the Polish reform team, foreign advisers from the World Bank and the IMF usually ended up accepting the Polish view (Gomułka, 1995). Some other cases of such changes of opinion will be discussed in Section 5.2.2 (concerning privatization policy and the restructuring of banks' bad debt portfolios).

The team which designed the Balcerowicz Plan has often been characterized as working in splendid isolation, above – and oblivious to – the political fray. According to this characterization, this was a group of technocrats which believed in the necessity of insulating itself from the political process, which the group saw exclusively as a potential source of pressures for divergence from the optimal reform path. The team thus portrayed saw themselves as experts responsible for carrying out a technical operation which they alone were competent to perform, and regarded all discussion and debate as a hindrance. However, the reality was much more complex, and the stabilization-liberalization program was implemented in an increasingly stormy political environment. The reformers were an embattled group, and the unpopularity of the reform measures and criticisms of the team itself had an effect on later actions as the implementation of the reforms unfolded. We discuss some aspects of this complex situation below.

Controversies among the general public and economists opposed, for various reasons, to the government's program began to rage within months after the introduction of the reform package, reaching a high level by the late spring of 1990. Many critics were of the opinion that the initial recession was of a Keynesian nature and could be overcome by using Keynesian stimulatory measures, and therefore advocated that the austerity measures of the reform package be reversed.

Contrary to popular opinion, the team of reformers in the Finance Ministry was not insensitive to criticism or convinced of its own infallibility. Mechanisms were set up to monitor the effects of policies as well as to identify and deal with new issues as they arose, and chief policy makers, including Balcerowicz himself, were open to suggestions about changing the course of policy. In fact, we will argue that they may have been too open to such suggestions as criticism grew heavier from increasingly broad segments of society, and that this tendency strengthened over the course of the ensuing decade.

Jerzy Koźmiński, initially director general and then undersecretary of state in the office of the cabinet (Polish acronym: URM), was responsible for communication with the media and for setting up the mechanisms for monitoring the progress of the reforms. He organized three groups at URM, one for monitoring the economy, one for public opinion research, and an intervention staff working for the cabinet's economic committee (a cabinet committee consisting of ministers with economic portfolios such as finance, industry, privatization, etc.). The first prepared reports every month on production, prices, wages, pensions, inventories, foreign reserves, execution of the budget, foreign trade, and the like (Gach, 1993).

On the basis of this feedback as well as social and political pressure decisions were made concerning modification of the reform program. The first such case was a relaxation of austerity measures in mid-1990, made in response to farmer and rail worker strikes. This consisted of a reduction of interest rates by the National Bank of Poland (the refinance rate dropped from 54% to 31% in annual terms) and an increase in the wage bill growth norms for the *popiwek* (Dąbrowski et al., 1991; Gach, 1993; Crombrugghe, 1995). The changes were proposed by the NBP, and Balcerowicz agreed (on the advice of Stanisław Gomułka, who argued that this was necessary to correct "excessive overshooting" [Gomułka, 1995]). Deputy Minister Marek Dąbrowski resigned in protest, and Balcerowicz admitted later that he had made a mistake in agreeing to this set of concessions to various groups of "transformation losers" (to use the terminology employed in our discussion of hypothesis 5 in section 2).

Unfortunately, while information about popular perceptions flowed regularly to the Balcerowicz team, there was a much smaller corresponding flow of information from the reform team. The only member of the Mazowiecki government who made intensive efforts to educate the society about the character and goals of the reforms was one who was not directly involved in the Balcerowicz team (although his efforts to communicate the rationale behind the reforms to Polish society were based on his frequent discussions with members of that team). Jacek Kuroń, who had been one of the best-known leaders of the anti-Communist opposition and became the minister of labor under the Mazowiecki government, played a very important role in explaining reforms to society through weekly television appearances. Kuroń was a highly charismatic figure who throughout the first half of the 1990s was not only the most popular politician in Poland but also the only one who consistently received high approval ratings from a large majority of the Polish population. Kuroń, who had always been connected with the democratic left and whose political tendencies were clearly of a social democratic nature, was perceived as a person of great compassion and human warmth, and at the same time was seen as being absolutely above suspicion of corruption or any ulterior motives. These perceptions made his arguments concerning the need for transition to a market economy particularly credible for the populace, including many of those whose material welfare was adversely affected in the initial stages of the transition. This was one of the all too few deliberate efforts made at the time to create a group of "reform advocates" (again using the terminology from the discussion of hypothesis 5 in section 2) in Polish society, although Koźmiński, in his interview, argued persuasively that there were too few resources – in terms of time and personnel – available to the Balcerowicz team to engage in this activity on a larger scale.

Other factors complicating the political environment in which the Balcerowicz team acted included the attitude of the rest of the government (in particular, Prime Minister Tadeusz Mazowiecki) and the lack of ability of those who opposed the team's program to formulate a coherent alternative plan which could be put forward for debate. According to one interviewee who had been a member of the Balcerowicz team, Prime Minister Mazowiecki tended to take a neutral standpoint with regard to the reform program, and the government's press speaker, Małgorzata Niezabitowska, was openly critical. (According to the interviewee, one of the main problems for the Balcerowicz team was the fact that, in the first year or two of the reforms, many persons both in the government and the parliament had a poor understanding of the nature and workings of the market economy – they knew in theory that Poland needed a market economy, but they had very little idea what that meant in practice.) As a result, the government as a whole refused to actively support the reform package, and the reform team was left to defend it by itself (with some help from Jacek Kuroń). Moreover, as Kuroń has noted, the tendency to isolate the government from the Solidarity trade union and its representatives in the parliament was due primarily to the approach of Prime Minister Tadeusz Mazowiecki. Mazowiecki and his government tended to see the union and its parliamentary representation as simply serving the role of an "umbrella" for the government, shielding it from criticism from the rank-and-file members. The latter were not to take an active role in shaping the new Poland. In fact, this often irritated Bronisław Geremek, leader of the Solidarity parliamentary faction, but in spite of this he agreed to play the umbrella role and supported the government (Kuroń, Żakowski, 1997). These constitute other important failures to create groups of "reform advocates" – even within the reform government itself.

Outside government circles, some of the most vocal critics of the reform program in the parliament did not block it when it was time to vote. In the opinion of the aforementioned interviewee, these people were unable to develop an alternative program. This was true of both the post-Communist and post-Solidarity critics of the program. The only party, he said, which was willing to actively block the program was the PSL (the peasant party), but this party was too weak to successfully block legislation in the parliament.

Nonetheless, in spite of all the foregoing qualifications, there was a strongly technocratic character to the reforms and the process by which they were designed and implemented. However, we will argue that this was due at least as much to the character of the reforms themselves as it was to the personalities of the reformers.

4.2. The technical nature of the liberalization and stabilization reform

Stabilization is by nature a highly technical operation, involving the setting of parameters such as exchange rates and interest rates, as well as the entire range of budget planning and central banking. Even in the most developed democracies these are matters which are reserved for well-trained professionals (though decisions are subject, sometimes, to debate in the legislature, and decision makers are periodically subject to approval by the legislature). Moreover, even with the best team of professional economists, stabilization programs are fraught with dangers of a technical nature. In fact, the Balcerowicz team made numerous technical errors (mostly in the area of forecasting) in the implementation of the reform. The technical dangers facing policy makers implementing a stabilization program under conditions of systemic transformation are summed up well by Gomułka (1995):

> The starting point for a macroeconomic program designer is usually the price path [...] The second major step in designing a program involves the use of the Fisher equation to determine the quarterly changes in the quantity of money that are consistent with the targeted price path [...] At this stage, assumptions have to be made about the level of real GDP and the velocity of money circulation. Again, in a period of systemic transformation, the risks are that the assumptions adopted are seriously wrong, as in Poland in 1990 and in 1991.

Specifically, he refers to forecasts of GDP growth in 1990 and 1991 of –3.5% and +3.5% respectively, as against the actually realized growth rates of –11.4% and –7.4%[9]. Other errors he lists concern the level of corrective inflation in early 1990, which was much higher than the Finance Ministry forecasts (however, low inflation forecasts helped the government meet fiscal targets and achieve a budget surplus in 1990, as higher forecasts would have necessitated higher adjustments in public sector wages, pensions and other transfer payments). These errors, which resulted in over-fulfillment of IMF budget deficit targets (a sizable surplus instead of a deficit), led some critics to complain of "overshooting." As mentioned above, these criticisms were often coupled with claims that the output decline which accompanied the beginning of the Polish

[9] These figures were later revised to –11.6 and –7.0; see Table 1.1.

transition was of a Keynesian nature and required Keynesian expansionary monetary and fiscal policies to remedy it.

However, it should be clear by now that the recession was of an entirely different nature. Hungarian economist Janos Kornai coined the expression "transformational recession" to refer to recessions caused by the need to restructure output in formerly centrally planned economies (Kornai, 1995). The underlying idea is that because both the quality and quantity of output were vastly different from those which would have been produced in a market economy in response to consumer demand, an output decline is necessitated by the fact that enterprises must cease to produce output not satisfying consumer tastes before they can adjust in order to begin to satisfy market demand. In the Polish case, this is evidenced by the figures cited by Bratkowski (1995a) for 1991, when GDP dropped in Poland by 7.6%[10], while consumption rose by 3.3%. Moreover, as short as the recession was in comparison with most other transition countries, it probably would have been even shorter if it had not been for the collapse of CMEA trade in 1991. Although the reorientation of Poland's trade had already been substantial (we will discuss this below), this eliminated export markets which remained significant for Poland. The causes of this external shock, however, were similar to those of the transformational recession, lying in the elimination of an institution (the Committee for Mutual Economic Assistance) which regulated trade on the basis of planners' preferences rather than market forces.

Not only did many critics fail to recognize these important differences between a new kind of recession specific to the conditions of the post-Communist transition, but they also were frequently in error about basic economic facts. Many critics, for example, continued to call for Keynesian stimulatory measures (larger deficits, lower interest rates and slower disinflation) long after the recession had ended. In the spring of 1991, President Lech Wałęsa organized a conference in the presidential palace on the economic policies of the government. This was used by economists opposed to the Balcerowicz program as a forum for criticism of the program. But the tone and content of the criticism was a good indicator of the extent to which the opposition was intellectually unprepared to discuss the program or develop a coherent alternative. Critical remarks concerned, for example, the lack of democratic legitimacy of the government as a result of its failure to represent any concrete interest groups such as farmers or blue-collar workers, deliberate sabotage of the economy by the government, and the accusations that decisions on economic policy were really being made in the offices of the IMF and Polish state property being sold for "pennies" to foreign capital.

[10] This figure was later adjusted to 7.0% – see Table 1.1.

It is worth remembering that these remarks were made by economists, including some of the country's better-known professors (Gach, 1993).

This brings us back to the claim of our interviewee that there were few people in Poland at the beginning of the transition who were able to go beyond sweeping slogans concerning a "Third Way," a "socialist (or social) market economy" or a labor-managed economy and formulate a consistent and detailed reform package which could have served as an alternative to the Balcerowicz team's program. This is probably one of the reasons why many of the post-Communist parliamentarians voted in favor of the Balcerowicz reform package in late 1989 – they found themselves in a situation which they were poorly equipped to understand. Because of this, it took time for even poor, pseudo-Keynesian criticisms of the program to take shape. And during that time, urgent action was needed. However, it is also true that there was an urgent need for education of the society, of parliamentarians, and of economists, both to improve the quality of the policy debate and, more importantly, to enable people to participate more effectively in the economic life of Poland's new market economy. If there is an area where one can fault the authors of the stabilization and liberalization package, it is in their failure to make adequate efforts in the area of education. However, it is also worth noting that the technical nature of this reform package which, in our opinion, made a technocratic approach necessary, also made it possible; that is, successful implementation of the package was possible in the absence of highly developed public administrative capacity. Thus, this reform also constitutes an exception to the rule (if rule it is) we formulated in Hypothesis 3 (which in turn probably contributed to the negligence in the area of public administration reform referred to in that hypothesis).

4.3. Initial results of the Balcerowicz reform package

The results of the reform package after one year included:

- The elimination of the shortages which had plagued the centrally planned economy;
- A sharp decline in inflation, which was brought under control by beginning of second quarter of 1990 (when the monthly inflation rate came down to under 10%, from over 70% in January);
- A budget surplus for 1990;
- A decline in GDP, and
- Growth of unemployment (official unemployment was probably also overestimated for reasons we will return to in a moment).

One of the negative effects, the GDP decline, proved to be the most moderate and short-lived GDP decline in the transition countries, and even so was probably overestimated, if one takes into account the rapid growth of the gray sector (i.e., unregistered economic activity) beginning in 1990 (Bratkowski, 1995a).

However, some of the positive effects were also short-lived. The favorable fiscal situation was to be reversed drastically in 1991, as a surplus was turned into a deep deficit. We will discuss this in more detail in Section 4.4.

As in the case of the fiscal balance, the reform package led to a trade surplus in 1990 which became a deficit in the following year. This was due to the fact that continued high inflation was coupled with the fixed exchange rate (as well as the depreciation of the leading European currencies against the US dollar), leading to the real appreciation of the zloty (Dąbrowski, 1995).

One of the most important goals of the reform package was to harden the budget constraints of state-owned enterprises[11]. In general, this was largely a success, although there was an important group of enterprises for which this failed. While subsidies from the state budget were discontinued, the state-owned banks continued a very liberal lending policy toward a privileged group of "regular customers" consisting of the large state-owned enterprises with which they had been cooperating for years under conditions not even remotely resembling banking in a market economy. The latter used this access to credit (in spite of high interest rates) in order to maintain liquidity, which resulted in a high rate of growth of their indebtedness, and of the bad credit portfolio of the banks (Bratkowski, 1995a). This problem, and its solution, is discussed in greater detail in Section 5.2.2.

One of the most important, dramatic, and positive changes resulting from the systemic change (and one which was effected almost immediately) was the shift in Poland's export markets from the CMEA countries to those of the European Union and European Free Trade Agreement (EFTA). Whereas in 1988 export to developed market economies represented 39.7%, and export to the CMEA 42.7%, of the country's exports, only two years later, in 1990, export to the EU and EFTA represented 60.5%, and export to Central and Eastern European countries and the former Soviet Union only 23.7%, of Polish exports (RCSS, 2002). Of course, this is an adjustment which was made by enterprises in response to changes in their environment, and the issue of enterprise adjustment and restructuring is the subject of Section 5.2.

[11] It should be noted that Leszek Balcerowicz does not share this view. He has argued against Kornai's well-known diagnosis of the ills of the socialist centrally planned economy, stating that the problem is not one of soft budget constraints, but rather simply price rigidities preventing the equilibrium of demand and supply (Balcerowicz, 2000).

In this context, we would like to make another observation concerning the technical errors of the reform team, discussed above, which led to accusations of "overshooting." This is that it was better to err on the side of caution (restrictive policies) than on the side of excessively expansionary policies. The costs of expansionary policies adopted as concessions in response to political pressures are demonstrated by the experience related to the reduction of interest rates in mid-1990. Within two months the volume of credit provided by the banks had grown to an extent which led to renewed inflationary pressures, with output growing by 15% in the second half of 1990. Even Gomułka (1995) admits that the relaxation of the second half of 1990 was excessive, and claims that this was due to the fact that wage increases were larger than anticipated, which he attributes in turn to the December presidential election. He goes on to note that the revival of inflation "forced the authorities to tighten monetary policy sharply at the end of 1990 and the beginning of 1991, which in turn may have accentuated somewhat the recessionary impact of the CMEA collapse in the first half of 1991." The central bank refinance rate went back up to 55% in December 1990 and 70% in January 1991. This restrictive policy was necessary in order to restore the credibility of the stabilization policy, which had been seriously undermined, changing the expectations of enterprise directors (Bratkowski, 1995a). Thus, it is likely that maintaining a consistently restrictive policy from the beginning would have been less costly than the attempt to accommodate political pressures with expansionary policies.

4.4. Later developments

In this section we will discuss progress and new reforms in specific areas related to liberalization and stabilization which occurred after the first year of implementation of the initial reform package. Some issues of policy in the normal sense (as opposed to the more radical types of changes which we classify as reforms) are also dealt with to the extent that they bear upon the fate of reforms enacted as part of the stabilization-liberalization program at the outset of the Polish transition. We can observe a pattern of small reversals: while reforms had been introduced on a grand scale, reversals often came in the form of small steps within the much more prosaic realm of day-to-day policy, and their cumulative effect was to weaken (and sometimes threaten to undermine) the effects of the initial reform package.

Central bank independence. In 1989 a law had been adopted according to which the governor of the NBP was nominated by the president and confirmed by the Sejm.

Additional 1991 legislation set the NBP president's term of office at six years and additionally made it impossible to replace him or her during this period except in cases of resignation or criminal prosecution. However, a requirement that the NBP's monetary program be accepted by the Sejm each year remained in place. In 1997, legislation was adopted which led to the creation of the Monetary Policy Council (Polish acronym: RPP) in 1998. This body has ten members: the president of the NBP, three nominated by the President of the Republic, three by the Senate, and three by the Sejm. The members have six-year terms, like the NBP president; thus, this represents an improvement over the previous situation, in which direct parliamentary approval of monetary policy was required. Moreover, relevant legislation (including the Constitution adopted in 1997) declares that the primary goal of monetary policy is price stability.

Exchange rate and trade policy. As a correction to the real appreciation of the zloty during the period in which a fixed exchange rate was in place, the zloty was devalued by 17% in May 1991 and crawling peg regime introduced (using a basket of five currencies). Shortly thereafter, the far-reaching trade liberalization of 1990 was reversed when tariffs were raised to a level higher on average than the average level of the beginning of 1990 (Wellisz, 1994; Dąbrowski, 1995). (Interestingly, this example of policy reversal concerns the liberals who introduced the original policy.) Since then, tariffs have in general gradually been reduced, largely as a result of the need to bring them in line with EU levels. In 1994 and 1995 the band of acceptable exchange rate fluctuations was widened. Then, in the summer of 1998, the NBP began to move in the direction of a full-blown exchange rate regime reform (given the fundamental nature of this change of course, the process was carried out remarkably quietly). It ceased direct interventions on the foreign exchange market, and 11 months later indirect interventions were also halted; in April 2000 the clean float policy which had been pursued de facto since 1998 was adopted officially. As we can see from the 1999-2000 figures on the balance of payments in Table 1, Poland experienced a dangerous external imbalance in those years, which led to widespread predictions of an imminent currency crisis. The clean float regime probably played an important role in avoiding such a crisis during this period[12].

The growth of imports which turned Poland's balance of trade negative for much of the 1990s certainly need not be interpreted negatively. Much of this was due to the

[12] Lack of a peg, and a consistent policy of non-intervention by the monetary authorities, remove a potential target for speculative attacks and thereby considerably reduce the risk of currency crisis. For these reasons, a clean float regime is often considered a safer option than a pegged exchange rate if a country is experiencing low inflation, low currency substitution and a reasonably credible monetary policy (Poland has met these criteria during the period since the clean float regime was adopted). For a brief discussion of these issues, see Dąbrowski (2003).

need to modernize the country's dilapidated capital stock, and for this purpose the decade saw a large-scale import of capital goods.

Inflation and monetary policy. The battle against inflation continued to be waged throughout the 1990s, albeit sometimes with more, sometimes with greater energy. Generally, however, progress was made continuously, and as disinflation proceeded throughout the course of the decade, one could observe the steady increase in the monetization of the economy (see Table 1.1). However, these gains were threatened when, following the drop to single-digit inflation in 1998, the monetary authorities (as in mid-1990) reacted with an excessive loosening of monetary policy, with drastic consequences (1999 inflation was higher than in the previous year for the first time since the beginning of the transformation), forcing an equally drastic re-tightening. Ironically, excessive loosening of monetary policy coincided more or less with the RPP's adoption of a policy of direct inflation targeting. In defense of the RPP we can say that the renewed burst of inflation was not only caused by interest rate cuts. The deterioration of the fiscal situation, which we will discuss in greater detail below, created greater inflationary pressure than expected (due, among other things, to the Finance Ministry's use of increases in the excise tax on gasoline to stop the gap). For most of 2000 monthly inflation exceeded annualized levels of 10%, and the RPP reacted with steep interest rate hikes. This in turn gave rise to a period in which disinflation proceeded more rapidly than had been expected; for example, the RPP's declared goal of reducing inflation to under 4% by 2003 was already attained in 2001 (RCSS, 2002). As in the cases of the 1990 expansionary policy reversal and the tariff policy reversal in 1991, in this case we observe first, a reversal of policy, and then a return to the original course (with the need, in two of these cases, to correct the reversal with a policy more restrictive than the original policy) by the same group – these changes were not associated with changes in the ruling party.

Populist forces have consistently called for a significant relaxation of monetary policy, and successive governments (despite what their members may have said while they were in opposition, or even during their terms of office) have consistently failed to meet these demands. There is a general consensus that this has been due to the fact that various Polish governments have understood the constraints imposed by the international environment, in which Poland's status as a borrower on international markets, as well as its status as a candidate for EU membership, would be seriously jeopardized by the adoption of a recklessly expansive monetary policy and a full-blown frontal assault on central bank independence. Constitutional safeguards of the independence of the RPP have also played an important role here. As we shall see, this has not been the case with respect to fiscal policy, where international pressure is weaker (it is difficult to press Poland to maintain a responsible fiscal policy when the

US budget deficit is at record levels and the leading Western European nation's deficits are also allowed to exceed Maastricht limits without adverse consequences) and policy is directly subject to the electoral cycle.

Fiscal policy. The serious revenue decline experienced in 1991-1992 was alleviated by the introduction of the personal income tax on 1 January, 1992, and VAT on 5 July, 1993. However, several analyses show that the fiscal problems of the early transition period (in particular 1991-1992) were due not to declines in revenues from the contracting enterprise sector, as was often argued by the austerity program's critics, but rather to the expansion of expenditures, primarily on retirement and disability pensions (Barbone, Marchetti, 1995; Bratkowski, 1993). The fall in revenue from enterprises was compensated by the reduction in subsidies to enterprises. The problem with social transfers, on the other hand, resulted from three policies adopted by the Labor Ministry at the outset of the transition: first, the extremely liberal eligibility criteria for unemployment benefits; second, the policy of indexing pensions to wage growth instead of price growth, and third, the policy of encouraging early retirement in state enterprises. (The eligibility criteria for unemployment benefits actually caused persons who had never worked before to enter the labor market – as registered unemployed.) While some of the effects of the policy on eligibility for unemployment benefits were probably unintended results of mistakes made by Labor Minister Jacek Kuroń and his advisers, there was certainly a conscious decision to ameliorate the consequences of the transition (in the form of employment reductions in state-owned enterprises) by allowing enterprises to reduce bloated work forces in a way which would be as painless as possible for all concerned (i.e., early retirement). The early retirement, in turn, led to a 28% growth in the number of pensioners in the period 1990-1993 (with 12% growth in 1991 alone), against annual growth rates of 2-3% in the previous three years. These mistakes gave Poland one of the highest dependency ratios in Europe, and their correction was a very long and gradual process, lasting about five years (Dąbrowski, 1995; Bratkowski, 1995a; Barbone, Marchetti, 1995).

Poland's fiscal situation was relatively stable in the high growth years of 1993-1998. However, if we consider the high rates of growth of those years, it is hard to avoid the conclusion that the public sector deficits were too high – approaching, and even in one year exceeding, the Maastricht limit of 3% of GDP (see Table 1.1) – especially given the fact that investment spending by the Polish central government is very low, consistently representing around 5% of the state budget[13]. These fat years represent a missed

[13] Calculations based on CSO (1999, 2001) show that, in the years 1995-2000, Polish central government investment spending ranged from 4 to 7% of total spending, and deficits from 5 to 10% of total spending (by contrast, in the same period Polish municipal governments spent 19 to 23% of their budgets on investments, while their balances ranged from a surplus of 1% in 1995 to a deficit of 5% in 2000).

opportunity for a much-needed structural reform of Polish public finances, which would reduce the burden of transfer payments and increase expenditure on badly needed investments in the education system and infrastructure.

Today, the country once again finds itself in a fiscal crisis, the roots of which lie in the implementation of four reforms – of the pension system, the education system, the health care system, and public administration – which began in 1999. The fiscal consequences of these reforms were apparent to alert observers well before the appropriate legislation was passed. At the end of 1998, when the parliament was preparing to pass the legislation introducing the four reforms, social policy expert and former deputy labor minister Aleksandra Wiktorow stated that the retirement insurance reform should be delayed by one year to allow time for proper preparation of the system (Cichocka, 2001).

The fiscal problems resulting from the reform package became visible very quickly. As we can see in Table 4.1, by the end of February of 1999, the first year of the "four reforms", the budget deficit had reached nearly 58% of the level planned for the entire year (as opposed to 14.2% at the end of February 1998 and 11.4% at the end of February 1997). This was largely due to increased expenditures associated with the reform of the health sector (the creation of health insurance funds – *kasy chorych*) and of the pension system. As a result of the latter reform (specifically, of the failure to prepare the computerization of the new system adequately before bringing it into operation), the social insurance fund (Polish acronym: ZUS) began experiencing problems with the collection of monthly payroll contributions (Stasik, 1999a), as well as with the transfer of a percentage of those contributions to private pension funds in the case of many insured persons.

Table 4.1. Budget deficit realization in February and at end of first quarter, 1997-2001 (% of total planned of the year)

Year	End of February	End of first quarter
1997	11.4	n.a.
1998	14.2	n.a.
1999	57.7	70.2
2000	29.3	45.1
2001	58.2	73.3

Source: Stasik (1999a, 2001).

Probably the biggest source of problems lies in the problems experienced in implementation of the pension system reform. This reform is discussed in detail in Section 6. Here we are concerned only with the effects on public finances. These have been considerable. ZUS debt to the private pension funds amounted to 9.5 billion zlotys as of end of March 2003 (Stec 2003). Five years after the initiation of the pension reform, ZUS still claimed to be unable to identify many payers for whom it has not transferred funds to the private funds, and thus this debt continued to accumulate during that period. These problems are due to the fact that the government was in a great hurry to implement this reform as well as the other reforms in its reform package as early as possible. The reasoning behind this was that the reforms should be implemented as early as possible during the four-year term of office so that the voters would have forgotten any difficulties in the early phase of their implementation by the time of the next election. Because of this concession to electoral calculus, the implementation was rushed, and the system was put in place before the necessary computerization was completed. And the difficulties turned out to be greater than anyone had expected.

These problems were compounded in the preparation of the budget for 2000 by the Finance Ministry's adoption of unrealistic assumptions for expenditure plans and revenue forecasts. This did not go unnoticed by commentators, including RPP member Boguslaw Grabowski and CASE analyst Andrzej Bratkowski, who said that the 2000 budget assumptions concerning GDP growth and inflation were too optimistic (Stasik, 1999b). Similar mistakes were made in the planning of the 2001 budget. Again, Finance Ministry macroeconomic forecasts for the 2001 budget plan came under serious criticism. Especially strong criticism was reserved for the forecasted revenues from sales of concessions for UMTS, the third-generation cellular telephone system (Stasik, 2000; Mackiewicz, 2000). Witold Skrok, director of the department of financial policy, analysis and statistics in the Ministry of Finance, resigned in protest soon after the Ministry announced its budget plan (Gadomski, 2000). The differences between Finance Ministry and assumptions concerning key macroeconomic indicators and the actually realized values are presented in Table 4.2.

Table 4.2. Finance Ministry's planned macroeconomic indicators, and actual ones, 1999-2001

Year	Level forecast by Ministry of Finance in budget projections			Actual level		
	GDP growth	Unemployment	Inflation*	GDP growth	Unemployment	Inflation*
1999	5.1%	9.4%	8.5%	4.1%	13.0%	7.3%
2000	5.2%	11.5%	5.7%	4.1%	15.0%	10.1%
2001	4.5%	15.4%	7.0%	1.1%	17.4%	5.5%

* Yearly average.
Source: Borowski (2000, 2001, 2002).

Meanwhile, as mentioned above, the Finance Ministry used increases in the excise tax on gasoline[14] as one stop-gap measure to reduce the deficit. A number of other

[14] One might ask why gasoline was targeted. The answer is simple. Excise taxes are one of the few forms of revenue which the government can legally change in the course of a tax year (the tax rates that taxpayers will pay on their incomes from a given tax year, for example, cannot be changed during the course of that year).

measures were resorted to, which amounted to accounting tricks which pushed expenditures into the next budget year. For example, the inflation adjustments to pensions made in 2000 were too low, although ministry officials realized that this would mean that expenditures would have to rise in 2001 in order to compensate pensioners (RCSS, 2002). In this manner, the official deficit numbers for 1999 and 2000 were held relatively low, although the Maastricht threshold of 3% of GDP was exceeded (see Table 1.1).

This tactic could not work forever, however. In the summer of 2000, Finance Minister Leszek Balcerowicz and his party left the government, and in November, with just over a month left in the year, Deputy Finance Minister Halina Wasilewska-Trenkner announced that expenditures would have to be cut by 3.8 billion zlotys in order to maintain the deficit at the planned level of 15.4 billion zlotys. Analysis showed that this was a result of two factors. First, in response to promises made in late 1998 by Balcerowicz to eliminate the tax deduction for new housing construction, many more people used this deduction in 1999 than foreseen in ministry forecasts (nominally, use of this deduction increased 80 percent for the tax year 1999 in comparison to the previous year), and for this reason tax offices had to return much more money to taxpayers in 2000 than had been planned. Second, planned subsidies for ZUS were too low, making it necessary to increase the subsidy to ZUS by almost 2.1 billion zlotys, from 900 million zlotys to almost 3 billion (Jędrzejewska, 2000).

Finally, in the summer of 2001, just before the general election and after months of denying the existence of a problem, Finance Minister Jarosław Bauc announced that Poland's budget was in crisis. Bauc was quickly fired by the prime minister, but this did not help matters – the ruling party was dealt a crushing defeat by the voters, and the year was closed with a public sector deficit of 5.1% of GDP.

Finally, with regard to the country's unsolved, and worsening, fiscal problems, we would like to draw attention to Stanley Fischer's (1989) comment on Milton Friedman's famous statement that inflation always and everywhere a monetary phenomenon. Fischer noted that monetary authorities usually print money in response to fiscal pressures (concretely, in response to the need to finance deficits), and that very high inflation is therefore almost always a fiscal phenomenon. Looking at the history of Polish deficit financing and inflation in the transition, we note that the NBP financed 100% of the deficit in 1989, 80% in 1991, 52% in 1992, 65% in 1993, and 30% in 1994 (Bratkowski, 1995b). Clearly there is a strong relationship between inflation and central bank deficit financing (monetary accommodation of fiscal policy), bearing out Fischer's observation. The 1997 Constitution took an important step in the direction of reducing the inflationary effects of fiscal policy by banning NBP financing of government deficits.

4.5. Assessment

Was the initial stabilization and liberalization reform package a success? How should we evaluate the follow-up over the course of the ensuing decade?

In terms of both goals and results, the initial reform package can be judged as an overall success. Almost fourteen years after the beginning of the Polish reform process, we can state with confidence that the battle with inflation has been won, but the battle for fiscal consolidation is in a critical stage. The fact that monetary policy has remained on a more or less restrictive course and the independence of the monetary authorities not seriously challenged is probably due in large measure to the constraints imposed by the international environment, in which Poland's status as a borrower and candidate for EU membership would have been threatened by serious policy reversals in this area. This seems consistent with our sixth hypothesis. We have argued, moreover, that the success of this reform package is evidence in favor of our first hypothesis – that it represents a success of the "technocratic" process in preparing a reform of a very technical nature which only a handful of the country's economists were professionally qualified to deal with at the outset of the transition.

Returning to the issue of "technocratic" versus participatory reform design and implementation approaches, we argue (oversimplifying somewhat) that the problem with the Balcerowicz Program was not what it did or the technocratic approach adopted to do it, but rather what it left undone: the creation (and recreation) of economic and social institutions which would be the actors in economic life under the new conditions. Most importantly this was a question of reform of enterprises and public administration. (It is these questions that we will examine in the next two sections in an attempt to test our second and third hypotheses.) Additionally, we have argued that while a participatory approach was not advisable in design and implementation of the stabilization and liberalization package, it would have been better for the long-term fate of the reform program if the reform team had done a better job of explaining the reforms (the nature of the market economy and the rationale for the reforms) to society and thus creating a broader group of "reform advocates" within the society. However, with respect to the other various interest groups treated in hypothesis 5, we also observe that one of the advantages of the technocratic approach adopted in the case of the Balcerowicz reform package – due to the fact that it was largely a matter of adjusting systemic parameters rather than creating institutions – was the fact that while large groups were, at least in the very early transformation period, "transformation losers", the liberalization and stabilization reform did not lead to the creation of "early winner" groups who would have had an interest in blocking further reforms. On the contrary, those groups that were made winners by the Balcerowicz liberalization-stabilization package – e.g., importers – all had an interest in staying the reform course.

With reference to our fourth hypothesis, we can state that – in spite of the important role played by foreign advisers including Jeffrey Sachs and representatives of international financial institutions – the Polish stabilization and liberalization reform package was a Polish product. This fact constitutes a great success whose importance cannot be overestimated, because part of the initial conditions and inherited baggage of the past referred to in our formulation of the hypothesis was the post-Communist countries' shortage of trained professionals competent to understand the issues involved and design and implement such a program (a shortage which was much more severe – in some cases amounting to a complete lack of such persons – in many countries of the former Soviet Union).

Again with respect to our sixth hypothesis, concerning the external environment, we have noted that the recession was deeper and longer than the reformers had expected, and drew attention to the role of unforeseen external circumstances such as the collapse of the CMEA and the Soviet Union in prolonging the recession. It should also be noted that this period was not a favorable one in the world economy, with both the United States and Japan moving into recession. Thus, external circumstances are seen to have significant effects on the popularity and political prospects of reformers, independently of the degree of success of their reform programs, which is sometimes not appreciated until several years after their implementation.

An interesting observation unrelated to the issues dealt with in our hypotheses is that a change in the ruling party is not necessary for reform reversals, which have sometimes been initiated by the same groups earlier responsible for reform policies.

5. Enterprise reform (privatization and restructuring)

In this report, we use the terms privatization and restructuring in a narrow sense. Privatization means transfer of state-owned stock into private (non-state) hands (unlike privatization in the broad sense; i.e., development of the private sector of economy – both through privatization of state-owned enterprises and spontaneous formation of *de novo* private companies[15]). We limit restructuring to changes in organizational structures, operations, interactions, and motivations within enterprises. We use the OECD definition of corporate governance as the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs.

5.1. Privatization

Intellectual and ideological context. Choosing the model

Through almost the whole period of Communist rule in Poland, serious discussions were held on improving the efficiency of Polish enterprise sector. Unlike most other countries of the Soviet bloc, those discussions went far beyond ideas of how to improve the central planning system. One of the most popular approaches was that of participation of employees in the management of state-owned firms. Apart from purely ideological justifications of such an approach (workers as co-owners of the state property), it was believed that employee participation would boost enterprise performance by overcoming labor alienation and by harmonizing interests of employees with those of the firm and the whole national economy. Even if some of the

[15] We will, however, briefly discuss the latter.

discussion participants had doubts as to whether state-owned enterprises with employee participation were the most effective form of enterprise (especially compared to privately owned companies), they believed that in the given circumstances, this was the most radical and effective solution.

In Communist times, there were two serious efforts to introduce employee participation in Poland. In 1956, workers councils were set up in state-owned enterprises, but their powers were severely limited by the unreformed centrally planned system of distribution of production tasks among enterprises. In 1981, a deeper reform of enterprise sector started, with employee self-management being part of a new set of decentralized principles of state-owned enterprise operation, known as "The Three S's" (self-management, self-financing and self-dependence). Thus, when the Communist regime collapsed in Poland, a strong self-management intellectual tradition existed, and groups supporting this approach had arisen within enterprises and academia and on the political arena.

At the beginning of transformation, the attention of the first non-Communist government was concentrated on the more obvious, and highly urgent, tasks of macroeconomic stabilization and liberalization, subjects which were perhaps somewhat less controversial than ownership transformation. Here, shock therapy measures had been applied, while privatization and institutional changes were carried out rather cautiously and gradually (in contrast to the mass privatization procedures used later in, for example, the Russian Federation and the Czech Republic). Maintaining a balanced budget, combating inflation and ensuring macroeconomic equilibrium as well as introducing a greater degree of economic freedom has always been included in a standard set of activities undertaken by many countries in the world and were applied in Poland with a considerable degree of success (as discussed above, in Section 4). Yet, with respect to radical institutional changes and large-scale privatization, recourse to existing Western practices was impossible, since there was no previous experience on this scale (the privatization of entire economies).

At the same time, there was no consensus concerning the direction of privatization processes among economic and political elites, in the government and between the government and its foreign and domestic advisers. While agreeing with the main rationale for large-scale ownership transformation (found in property rights theory, which explained the inefficiency of the socialist enterprise sector on the basis of incomplete property rights), the participants of the discussion had different views on at least three important questions:

- What type of owner (and more generally – what type of corporate control) is the most efficient?

– What other goals can be met by privatization?
– What should be done to make the privatization process itself as efficient as possible?

A general debate on the privatization concept took place in late 1989 and 1990. Three main concepts of privatization came up against each other, each providing a separate answer to the aforementioned questions:

– a commercial concept of the sale of state-owned assets using classical methods, including trade sales but most importantly public offerings (based on the British experience);
– nonequivalent privatization based on employee ownership and the US Employee Stock Ownership Program concept and backed by the Polish labor self-management tradition;
– nonequivalent privatization through free distribution of assets among all citizens, based on newly drafted privatization concepts (Błaszczyk, 1993; Gilejko, 1995).

In its first economic program of October 1989, the government gave preference to the first, "classical" concept of privatization, combined with rapid development of *de novo* private sector which would absorb workforce from the shrinking state and ex-state sector. In turn, the privatization law, passed July 13, 1990, tried to make use of all the three privatization concepts in order to ensure the widest possible impact of privatization on transformation economic, social and political transformation in Poland. Ideologically, it reflected coexistence of different views on the scope and methods of ownership transformation, and more generally – on the principles of the post-Communist transformation as a whole. The privatization law represents a certain combination of two main options: liberal conceptions patterned after solutions adopted in developed market economy countries, and a participatory approach originating from the Polish labor self-management movement and tending towards a kind of "Third Way" of development. It should be noted that despite the fact that the authors of the privatization concept were under strong pressure from the self-management movement to favor employee ownership, our interviewees involved in decision-making at the beginning of transition unanimously stressed that they (as well as the government as a whole) had virtually a free hand in designing reforms, because interest groups strong enough to influence decisions of the government and the parliament hadn't yet formed in 1989-1990.

Goals and methods of privatization

During the whole analyzed period, no detailed description of the main goals of privatization was prepared. Only a few of the goals were ever officially mentioned, and most of them had to be deduced from decisions made by the Parliament and governmental agencies.

The economic program of the first post-Communist government (the so-called Balcerowicz Plan) addressed privatization issues in the context of the creation of market institutions which had stood the test of time in Western economies. Following that simple course of thought, the main privatization goal was of a systemic character: to contribute to **the change of the economic system through creation of private entities**. Within the framework of this goal a number of sub-goals existed, of which the most important was the creation of well-functioning markets, including a securities market.

Apart from this purely systemic role, privatization was **to solve the problem of microeconomic inefficiency** of state-owned enterprises; this would, in turn, contribute to the rise in productivity of the whole enterprise sector.

Although never officially formulated, the third goal was of crucial importance: **to make the whole reform process smooth, stable and irreversible**. Privatization was expected to create not only incentives for economic development, but also to create powerful pro-reform lobby of actors, involved in privatization process and using its results. Such a lobby would exert strong pressure on decision-makers to continue pro-market reforms. The assumption was that a critical mass must be achieved, when liberal and market institutions and actors become stronger than the forces and institutions of the Communist past.

The fourth goal was **of a fiscal nature**. The value of the state-owned stock designated for privatization was large, therefore the potential privatization revenues of the budget were also significant and able to contribute to reduction of the budget deficit.

The fifth group of goals was related to the use of privatization for **solving a wide set of social problems**. On the one hand, attempts were made to attain a kind of social justice (via distribution of part of the privatized stock among the whole population and, additionally, by creating preferences for certain groups who were felt to deserve such entitlements). Additionally, attempts were made to use privatization to resolve the social problems in concrete enterprises by imposing on the buyers certain obligations concerning employment, wages, environmental protection, etc.

A set of hidden goals existed as well, when the government drew public attention to one goal while the real, most important goals were not advertised because they were less attractive to the broad public. In some cases we can describe this as an "honest" hidden agenda (for example, stressing the social profits from privatization in order to gain public support and unblock or speed up the privatization process – e.g., this included preferential treatment of insiders). Trying to build a strong coalition of pro-reform forces, the government had to bear in mind that different coalition members might have different motivations, so it seemed to be politically rational not to spell out the goals. Moreover, given the multiplicity of objectives and the constraints, a detailed description of the privatization goals would have been almost impossible.

In other cases, however, hidden goals were less "honest." For example, they appeared in the course of formation of entrenched interest groups which were interested in privatization (or more often lack of privatization, e.g. in the sectors where privatization would mean discontinuance of public financial support), or some specific method of privatization of enterprises or whole branches, primarily in view of the gains they expected to reap as a result. Members of these groups rather seldom occupied the highest positions in the government or administration; they were influential mostly as lobbyists or voters.

The problem is that at least some of the goals may be contradictory. For example, pursuing the fiscal goals may jeopardize the goal of increasing of microeconomic efficiency (the more an investor must pay to the budget, the less he may invest in a company[16]). In addition, maximizing global revenues from privatization would require a gradual approach (because glutting the market with privatization offers would reduce the market prices of enterprises), while the tactical goal of reduction of the budget deficit in a given year could lead to just such an attempt to maximize privatization revenues in a given year, thus lowering the total revenues to be achieved from privatization. Excessive attention to the social obligations of an investor may lead to inadequate investments in the company (an excessively high wage bill reduces funds available for investment). The goals related to "social justice" (e.g., "enterprises should belong to their employees" or "enterprises should belong to the whole society") may contradict the need to find efficient owners for privatized enterprises.

It is quite obvious that contradictions between official and hidden goals can be highly destructive for the privatization process, especially in the case of "dishonest" goals. Their pursuit not only leads to slowdown and distortions in the privatization process, but has severe political consequences related to the corruption of the state apparatus, deceleration of the construction of institutions of the market economy, and growing disappointment of population.

A set of goals on the enterprise level also existed. These were the group and individual goals of the managers and employees of state-owned enterprises. Quite often

16 In fact, Krzysztof Lis, who at that time was government plenipotentiary for ownership transformation, claimed that enterprises were intentionally left without investors' money because the scarcity of funds was seen as a source of pressure on the firms to carry out restructuring.

such goals were not in line with the privatization policy conducted by the government. This problem is of a special importance in Poland, where insiders have very substantial impact on privatization of "their" enterprises. At this level, too, we observe openly proclaimed and hidden goals, the latter often connected with enfranchisement of certain enterprise actors (primarily managers).

Another important feature of Polish privatization (and the whole enterprise sector reform) is its gradualist, highly consensual character. Its authors were aware of a trade-off between the speed and quality of transformation processes. They believed that lower speed resulting from careful preparation of privatization deals (both in the technical and social dimensions) is much more important than massive and rapid formal change of owners, because the reformed market environment would exert strong pressure on state-owned enterprises and force them to adapt and restructure, thus making their privatization less urgent, although still necessary. The gradual character of Polish privatization also reflected a choice made in the discussion of what should come first: privatization (which would create demand for further reforms)[17] or regulation and institutional constraints (in order to create a framework for actors' behavior and prevent tunneling)[18]. The gradualism reflected a choice in favor of the latter solution.

The main features of Polish privatization (multiplicity of goals and its low-pace consensual character) were reflected in the privatization law, which envisaged a wide range of possible methods and paths of ownership transformation: sale both to strategic investors and via the stock market, management-employee buyouts and even a unique kind of mass privatization that had been designed not only to transfer a significant (albeit limited in comparison with other post-Communist countries) part of the state's sectors assets to Polish citizens, but also to create a mechanism for actively restructuring the companies participating in mass privatization. All methods and paths of privatization are equivalent (buyers pay the market price or a price based on valuation), except the NIF program, where certificates of ownership were distributed among the population for a nominal fee.

To govern the privatization processes, a brand new special structure within public administration had do be set up. The Ministry of Privatization (reconstituted in 1996 as the Ministry of the State Treasury) had to perform functions which had not existed before, which for the reformers meant that it had to be organized in a way differing significantly from the established culture of public administration in Poland. Moreover, its functions, as originally conceived, were limited in time (meaning that it was to be

[17] See Frydman and Rapaczynski (1995); Boycko, Schleifer and Vishny (1995).
[18] For example, see Murrell and Wang (1993).

liquidated after privatization ended). Thus the ministry had to create its patterns of behavior, internal structure etc. in a new and uncertain environment, and be very task-oriented (not to form another interest group interested in perpetuation of the transition period or, if the end of transition becomes inevitable, adopt "end-game" behavior trying to convert its authority into another, more liquid form). This was, moreover, the problem of all new agencies created to serve the process of post-Communist transformation.

Creation of conditions for private sector development

Liberalization and deregulation measures intended to facilitate new entries were started by the last Communist government under Prime Minister Mieczysław Rakowski, which adopted the Law on Economic Activity (December 1988). Limited liberalization of foreign trade and FDI was also introduced at this time. But the real breakthrough was made by the first two post-Communist governments (Mazowiecki's and Bielecki's), which made development of the private sector (privatization in a "broad sense") a cornerstone of economic policy, privatization of state-owned enterprises being only a part of this larger process. These governments implemented a wide range of measures aimed at radical facilitation of new entries and liquidation of obstacles for market competition (including opening to competition of foreign entities), in particular:

- creation of uniform tax policy for all ownership sectors (although SOEs for some time were subject to two additional taxes – a kind of a capital tax and a tax on excessive wage increases);
- acceptance of a new anti-monopoly legislation, deconcentration of some sectors of industry (see section 5.2.1 below);
- liquidation of all federations of cooperatives;
- introduction of a customs law corresponding to European Community standards;
- abolition of all remaining forms of trade not based on free market principles;
- price liberalization;
- ending of traditional central planning, granting greater independence and responsibility to state-owned enterprises;
- creation of a securities market;
- acceptation of the new Foreign Investment Law eliminating most licensing requirements and allowing the free repatriation of profit and invested capital;
- introduction of current account convertibility of the Polish currency (Dąbrowski, 1995).

Implementation of such a wide range of very radical measures (as well as other components of stabilization, liberalization and institutional reform) was inevitably in conflict with many existing interests. It was possible only in the "extraordinary" situation of the early years of reforms, when the government enjoyed an exceptional "credibility credit" from the society that supported the changes not being aware of their real meaning and burden, as well as the political support (so-called "umbrella") of "Solidarity" trade union. Old interest groups were in a sense taken by surprise and scattered, and new interest groups were only forming and too weak to exert strong pressure on the reformers' team. This created a window of opportunity for implementing difficult reforms in the forceful and credible fashion. This period is sometimes referred to as period of "extraordinary politics" (Balcerowicz 1995).

Quantitative effects of privatization

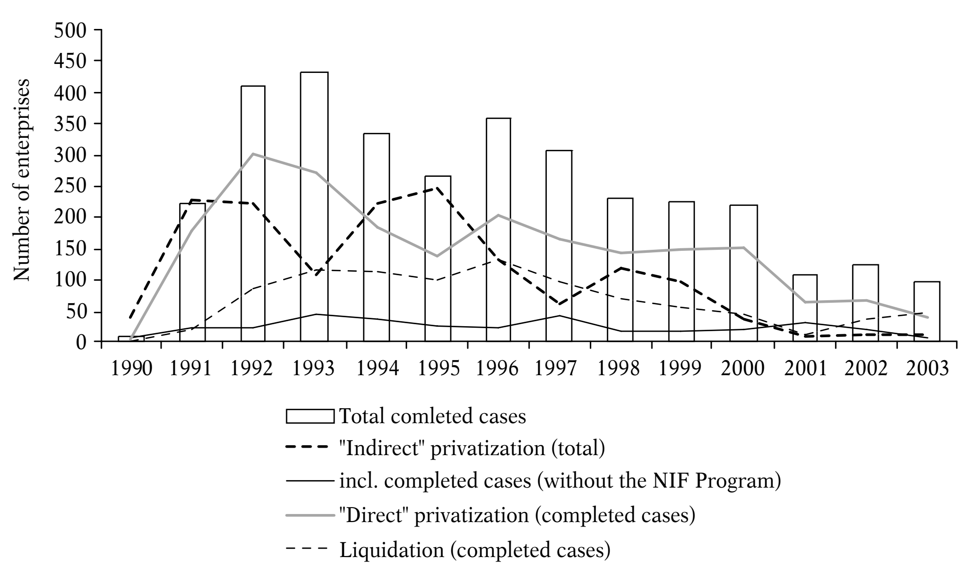
The most striking, and arguably most important quantitative result of the process of privatization of the Polish economy has been the creation of nearly 200,000 new private companies (and about 2.5 million private one-person and family businesses) since 1989, which make up more than 97% of all registered firms, employ 70% of the work force and are responsible for 75% of GDP (Central Statistical Office, 2003; EBRD, 2003).

In Poland, the so-called small privatization, affecting the retail, catering and service sectors, was conducted very rapidly: by the end of 1992, 97% of all units in these sectors had been privatized. This was a decentralized, "grassroots" process led by thousands of local authorities, virtually without any intervention from the central government.

Decentralization of initiation of privatization deals in enterprise sector and the high role of insiders in this process, together with possibility of establishing management-employee ownership, acted as a catalyst of privatization of SOEs. During the first years, MEBOs and other forms of decentralized, "participatory" privatization greatly outnumbered centralized, government-led sales of enterprises. At the same time, the overall pace of privatization of the enterprise sector was much slower than had been anticipated. Besides, since the mid-1990s we have witnessed a substantial slowdown of the privatization process, which occurred due to two main reasons: the stock of "easy to privatize" enterprises was rapidly depleted, and political pressure for privatization slowdown increased (Figure 5.1).

The speed of ownership transformation depended mainly on the industry, size, organizational structure and profitability of an enterprise. The privatization of small and medium-sized enterprises (SMEs) in manufacturing, trade and construction was

Figure 5.1. Dynamics of privatization (number of enterprises by years, 1990-2003)



Source: Ministry of the Treasury (2004).

usually accomplished relatively quickly (as technically and politically less complicated – more than half of them were bought by managers and employees). The other pole was represented by the largest enterprises, especially from infrastructural sectors, mining and metallurgy. Obstacles of a political nature started to appear as well (i.e., powerful interest groups which defended the status quo and created pressure on the government to slow down privatization; this will be discussed further below). Apart form "re-consolidating" sectoral programs described in the next section, the 1993 Law on the Ownership Transformation of Certain SOEs of Special Importance for the National Economy was passed, which in fact excluded a large number of enterprises from the privatization process. Additionally, the 1996 Privatization Law in practice lifted the obligation to privatize commercialized state-owned enterprises. As a result, by 2003, privatization was completed only in the case of 66% of state-owned enterprises (Nawrot, 2003), and state-controlled firms still produce about 25% of the GDP (Central Statistical Office, 2003).

As a result, the characteristic feature of Polish privatization is quite a large number of cases of "unfinished privatization" in the form of more than 500 predominantly large companies that were only commercialized, but never privatized (the so-called sole-shareholder company of the Treasury, Polish acronym: JSSP), and about 100 companies where the Treasury has stakes of more than 50% (Nawrot, 2003). Moreover, in the National Registry of Business Entities (REGON) there are still more than 1700 state-owned enterprises[19] (out of the total number of 8453 SOEs at the beginning of transition) (Central Statistical Office 1991, 2004).

Table 5.1. Selected data on privatization of state-owned enterprises

Methods of privatization	Number of companies (end 2003)	Total employment, thousands (end 2002)	Performance (2002)		
			Cost level indicator	Turnover profitability rate	
				gross	net
"Indirect" privatization:	1539				
JSSP	541	352.6	101.9	-1.8	-2.4
completed cases[a]	277	242.3	97.9	2.1	0.5
- with participation of foreign investors	90	81.5	97.0	3.0	1.7
companies included in NIF Program	512	124.9	101.8	-1.7	-2.4
Debt conversion	17	1.9	118.9	-18.9	-18.9
"Direct" privatization:	2062				
MEBO	1357	151.2	98.0	2.0	0.9
in-kind contribution	232	44.1	99.7	0.3	-0.3
other forms of "direct" privatization	508	2.5	103.3	-3.3	-3.5
Liquidation (completed cases)	932				
TOTAL	4550	982.8	99.9	0.1	-0.9

[a] The share of the Treasury is less than 50%. Without the NIF program.
Source: Central Statistical Office (2003), Ministry of the Treasury (2003, 2004).

5.2. Enterprise restructuring

The need for a policy on an enterprise restructuring

The gradualist privatization model led to the necessity of a special approach towards enterprise restructuring. In fast models, deep restructuring is expected to happen after privatization and is the new owners' responsibility (except some superficial restructuring made in order to speed up privatization process, such as splitting up of enterprises etc.). In the gradualist model of ownership transformation adopted in Poland, where deep restructuring is often postponed, the problem of government-led restructuring arises. There were two main tasks of such restructuring efforts:

– to prepare large enterprises that were still under state control for privatization by increasing their value and making them more attractive for potential investors;
– to make them viable and able to adapt to rapid changes in their environment for the period when they were still state-controlled.

The first task was realized through various methods, including stripping the enterprises of their social assets (such as kindergartens, holiday homes, medical services, sport centers etc.), as well as through recapitalization, downsizing, etc.

[19] However, the real number of still existing SOEs may be lower, because of problems with updating the registry.

At the same time, at the beginning of transition in Poland, the need for the implementation of the second task was not fully appreciated. A large-scale demonopolization and deconcentration of Polish economy have been carried out in the form of breakup of state-owned enterprises in a number of industries (meat, sugar, grain, cement, coal, energy, energy generating machine, mining, internal trade, construction, commodity transport, public utilities and other), and the common opinion was that the emerging market would force changes in state-owned enterprises' behavior and necessary restructuring. In fact, only one instrument of external pressure was used at that time: the *popiwek* (introduced in the 1980s and lifted in 1995), whose goal, as discussed in Section 3, was to decrease the inflationary pressure of wages in the state-owned sector. However, in 1990 and especially 1991, negative factors in SOE operations became apparent: there was a sharp decline in production, increase in enterprises' debts and tax and wage arrears.

Since then, many restructuring programs have been adopted, with only a few being successful. Here, we discuss some of most important programs. We start with the relatively successful enterprise and bank restructuring program.

The Enterprise and Bank Restructuring Program

The government became aware of the inadequacy of its *laissez-faire* approach towards these processes only when the steadily growing bad debts of the state-owned sector towards the banks began to seriously threaten the stability of Polish banking system, after foreign experts alarmed the government about the rapidly growing bad loan portfolios of a number of state-owned commercial banks in 1991. In 1992-1993 a group of enterprises (mostly state-owned industrial enterprises and housing cooperatives) representing one tenth of the enterprise sector (in terms of sales) had accumulated enormous debts to banks, the government and other enterprises. (It is also worth noting, however, that the remaining 90% of the enterprise sector was almost debt-free.) By mid-1991 bad debts were found to represent a weighted average of 42% of the credit portfolios of the nine commercial banks hived off of the NBP in 1988 (Gomułka, 1993).

Experts from the World Bank recommended the implementation of a standard procedure for cleaning up banks' bad loan portfolios, applied in Spain and some countries of Latin America, which envisaged first transferring bad debts from banks' portfolios to a specially created restructuring agency responsible for work-outs (a so-called "bank hospital"), and then recapitalizing the banks.

However, the Polish government (Finance Ministry officials) did not believe in the efficacy of this procedure, because, in Polish conditions, it would not address the cause of the problem, which lay primarily in the lack of experience and expertise of the banks in assessing credit risks and of enterprises in proper governance in the market environment. Nor did they believe in the efficient functioning of a centralized, government-run "bank hospital" and its ability to resist political pressure. The idea was that the restructuring of banks with bad loans portfolios and indebted enterprises should force a change in the way they operate: banks should learn risk assessment and management by dealing with the bad debt problem themselves, and the management of enterprises would be improved and capable of coping with challenges of the market. Thus, contrary to the suggestions of foreign experts, the Polish government applied a participatory approach that envisaged decentralized learning of the main actors involved.

Under the 1993 Law on Financial Restructuring of Enterprises and Banks, each participating state-owned bank created a special department to manage its bad loan portfolio, and could use a number of methods for restructuring that portfolio, including debt-to-equity swaps and the innovative bank conciliation procedure, under which banks holding at least 50% of the total claims against a given debtor had to reach an agreement on debt restructuring with that debtor enterprise. After the initial assessment of the costs (e.g., in terms of written-off debt), but prior to carrying out the restructuring operations, the banks were subject to a one-off recapitalization. After having cleaned up their portfolios, banks were to be privatized.

The process of preparing the law and its implementation did not encounter any significant political resistance, because of appropriate PR activity (in fact, the main goal of the law was to prevent a banking sector crisis, but in order to make the whole process politically palatable, the need to help indebted enterprises was stressed) and the fact that it reconciled the interests of all the main actors involved: policy makers, bank management, enterprise management and employee organizations. The program was supported by international and foreign funding, primarily from the EU Phare program and the British Know-How Fund.

The success list on the side of enterprises was rather short. The program was indeed successful in selecting and keeping alive the best state-owned enterprises while the worst were pushed towards exit. But there was no significant overall improvement in enterprises' performance, the main impact of conciliation simply being a "breathing room" for them (Gray and Holle, 1996). Banks proved to be rather weak in promoting the needed restructuring and/or privatization of enterprises (for example, they seldom took advantage of the opportunity, provided for in the law, to take over enterprises through debt-equity swaps).

But the main goal of the program was achieved: a banking crisis was prevented and today the Polish bank system is very sound and, unlike in most other post-Communist countries, in Poland there were no banking or financial crises during the whole transition period. Bank solvency was restored, banks changed their behavior from uncritical funding of enterprise losses to making decisions on the basis of profitability concerns.

Enterprise restructuring in other sectors

Trying to overcome negative tendencies in the state-owned sector, in 1992-1993 the government started to prepare and implement sectoral restructuring programs involving the re-consolidation of the previously deconcentrated sectors. At the first stage of this process, the main goal of such re-consolidation was prevention of the collapse of those sectors of economy where state-owned enterprises still prevailed, increasing their competitiveness and thereby making possible their future privatization. It was believed that re-consolidation would lead to:

- cost reduction due to economies of scale;
- optimization of investments;
- optimization of production processes;
- improved competitiveness with foreign companies due to increase in companies' scale;
- increase in the value of the companies, which would lead to higher revenues from their privatization.

In fact, since then almost all restructuring programs have envisaged a greater or lesser degree of consolidation of the remaining state-owned enterprises. In 1993-2003, big state-controlled companies and/or holding structures were created in coal mining, sugar, petrol, ferrous metallurgy, and banking. At the same time, some sectors were not even deconcentrated, or such a deconcentration had only formal character (for example, in railway transport and telecommunications – in the latter case, the national telecom company remained a monopolist even after privatization). In some sectors, restructuring through re-consolidation indeed gave some positive effects (for example in downsizing both in terms of production and employment, raise in labor productivity etc.), but it is hard to tell whether these improvements wouldn't have been more widespread and deep without re-consolidation. Certainly this policy helped to keep alive a lot of firms that otherwise would have gone bankrupt, but this in fact extended the death throes of the inefficient state-owned sector and forced the government to keep subsidizing these firms in more or less open form (e.g., through recapitalization, write-off of tax arrears, etc.). Another cause for slow restructuring at lest of some these sectors (e.g., coal mining, railways) was its highly negotiated, participatory character, allowing the interest groups threatened by restructuring to exert influence on its speed. Nevertheless, our interviewee who had studied the problems of privatization and enterprise restructuring since the very beginning of transition has strong doubts whether in the given political circumstances a more technocratic approach would have been more efficient.

But not only the "technical" inefficiency of this kind of restructuring presented a threat to the reforms. As it turned out, the social and political dimension of concentration of the state-controlled sector was much more dangerous. This policy led to the creation or consolidation of powerful interest groups both within sectors (employees, managers, trade unions, often constituting powerful coalitions placing demands on the government) and among the political elites of the country. Emergence of these interest groups led to strong political bargaining with the government, which in many cases stopped both real restructuring of state-owned enterprises and their subsequent privatization. Since the establishment of these entrenched groups, whose positions were largely consolidated by the mid-1990s, almost all sectoral restructuring programs of the government reflected more the interests of those groups than the goal of genuine restructuring. This effect has been intensified by the mentality of the left-wing ruling coalitions (which proved to be more prone to tighten state control over the economy than right-wing coalitions – not only in enterprise restructuring, but also in other spheres of economic policy), originating perhaps not so much from leftist ideology as from the habits inherited from the central planning era (many left-wing politicians were already active in Communist party and state administration in the 1980s).

5.3. Building corporate governance mechanisms

Intellectual background and political context

At the microeconomic level, one of the main tasks of both privatization and enterprise restructuring was the building of efficient corporate governance mechanisms that would help to overcome the governance problems which in Communist times were one of the main obstacles to raising the efficiency and productivity of the enterprise sector.

The choice of the right corporate governance model was not an easy task, however.

First, there was a question what corporate governance model would be the best for the Polish enterprise sector. In developed market economies, two main models existed (Anglo-Saxon and Continental) that reflected different philosophies of corporate governance, especially in the field of corporate control mechanisms and company mission.

Pragmatically speaking, the Continental model was more suitable for Poland (as well as other post-Communist countries) for a number of reasons:

(1) The influence of external control (in the form of commodity, financial, take-over and other markets) did not exist or was not sufficiently effective. In such conditions, the efficient functioning of internal supervision was of fundamental importance.

(2) The investment potential of the Polish population was weak, therefore the main sources of capital had to be looked for elsewhere. The Continental model assumed the significant role of a strategic investor, in Polish circumstances – most likely foreign (and, later, also domestic industrial and institutional).

(3) Both the managerial skills and technical assets of Polish enterprises were archaic and not adapted to the new challenges of the emerging market environment. Strategic investors, especially foreign ones, were able to bring to a company not only capital, but also a new culture of management, of company behavior towards its environment, new technology etc.

Second, the corporate governance model was expected not only to meet enterprises' needs (i.e., their efficient operation), but also serve the transition in Poland in general, being a part of the new political, social and economic model. Therefore, the choice of a model depended on social and political considerations as well. Here, the choice between Anglo-Saxon and Continental model was not so obvious, because the Anglo-Saxon idea of shareholder value suited the ideas of mass enfranchisement of population. On the other hand, the Continental model was of a more participatory character, which suited the advocates of employee self-management and participation.

Third, unlike green-field companies, privatized enterprises did not emerge out of the blue. They represent a continuation (in economic, organizational, social and other ways) of the former SOE. The "legacy" of SOEs has several aspects, including the following:

- the state-owned enterprise had its own organizational structure, with each body having its own competencies to which all actors had become accustomed;
- in most state-owned enterprises, stable structures of power and influence had been established, and many insider actors were afraid of losing them after privatization;

– the mentality and behavior of the main insider actors were to a great extent determined by their previous experience in the state-owned enterprise.

Here, a real threat was that entrenched insiders would resist any attempt to change the internal *status quo*. Therefore, there was a popular view that strong owner control must be imposed, while taking insiders' concerns into account. Under such circumstances, the Continental model seemed to be a good solution (Jarosz, Kozarzewski, 2002; Kozarzewski, 2003).

The legal background

So, the Continental model of corporate governance was chosen, with slight inconsistencies and alterations caused by ideological and political considerations, as well as pressure exerted by the main actors on the Polish corporate governance scene.

It is worth noting, that in most cases Polish legislation does not take the concerns of stakeholders into account in corporate governance structures. For example, there is no general requirement to include the representatives of stakeholders (e.g., employees) on the supervisory board (although such a requirement exists in JSSPs). The peculiarity of the Polish legal system is that the main vehicle for representation of stakeholder interests in Poland is privatization legislation, rather than regulations affecting the enterprise sector in general. Thus, there are fundamental differences in the corporate governance regime depending on whether an enterprise originated in the state sector or the *de novo* private sector – a situation which is, to our knowledge, not found in any other European country.

The Polish legal background for corporate governance can be assessed as good, with strong disclosure and transparency requirements (especially for publicly listed companies) – but not flawless. First, it is not instructive enough, too often giving general ideas and principles rather than concrete solutions, which is insufficient in the country with no previous experience in market economy behavior. Second, the system of rights and safeguards that regulates corporate governance within companies is imperfect. It makes possible the abuse of minority interests, and recently we have seen cases of abuses of the majority by a minority representing powerful industrial interests. In many cases, there are no efficient safeguards against opportunistic behavior of managers. Third, legal acts sometimes contradict each other and overlap; the most important such cases include the Company Code, the Act on Public Securities Trading, and the Act on Commercialization and Privatization of State-owned Enterprises (Tamowicz, Dzierżanowski, 2002; Kozarzewski, 2003).

5.4. Effects of enterprise sector reform

Corporate governance

It should be noted that the patterns of corporate governance emerging in Polish companies depend on a number of factors, and not on corporate law alone. Other factors include: the privatization law and practice; the law on the securities market and its development in practice; the pace, scope, and effects of restructuring programs; the process of re-configuration of enterprise goals and main actors' interests in the course of transition, and the type of dominant owner.

The heterogeneous character of Polish privatization, peculiarities of regulation and real processes of enterprise privatization and restructuring resulted in the emergence of heterogeneous patterns of corporate governance in privatized enterprises, although all of them formally stay within the Continental model. Among those patterns, at least three deserve special attention.

The first pattern is represented by the largest companies which went through "indirect" privatization and have concentrated ownership structures, often dominated by foreign investors. In the sector of former SOEs, they are unquestionable leaders in post-privatization restructuring and creation of highly efficient corporate governance structures and behavior.

The ownership structure of this group of companies is highly concentrated (and the concentration level is still growing), and insiders' participation is very limited, unlike in privatized SMEs and in spite of the pro-insider provisions of Polish privatization law (half-price and free shares for employees in the case of indirect privatization).

In almost all companies we have studied in a separate project on corporate governance (Kozarzewski, 2002), deep changes in corporate governance structures have been introduced, and the "legacy" of the state-owned past has already been overcome. Thus, the processes of post-communist corporate governance transformation are complete. However, changes in corporate control mechanisms appear to be conditional on the characteristics of the controlling shareholder(s). The companies with the highest levels of ownership concentration, especially those dominated by foreign investors, have more coherent corporate governance structures. In the companies with the lowest levels of ownership concentration, the shareholders' majority is often rather formal and does not ensure full real control over the company.

Within the pattern in question, companies with foreign investor domination deserve special attention. Corporate governance structures in most of these companies are very transparent with clear division of powers among the executive board, supervisory board, and general assembly of shareholders. At the same time, the foreign investor keeps tight and efficient control over the firm. An important feature of corporate governance policy in foreign dominated companies is the introduction of incentives for insiders (primarily managers), in the form of small blocks of shares and/or seats on the supervisory board.

The second pattern is found in companies privatized by management-employee buyouts (MEBO). Most of them used the leasing path of direct privatization, although a significant number of such companies emerged as a result of direct sale and even "indirect" privatization. There were two main trends of ownership transformation: towards concentration of shares and toward their "outsiderization." These processes had varying intensity in different groups of companies, and three patterns of ownership structure have emerged:

- management-employee pattern (large blocks of shares in the hands of managers, the rest dispersed among non-managerial employees);
- dispersed insider ownership;
- ownership concentrated in the hands of an outside investor.

The most important factor that influenced the direction and dynamics of ownership changes was the economic performance of the company, which favors concentration and "outsiderization" of ownership when very poor or very good. In the former case, this can be seen as a trade-off between the power of insiders and the firm's chances for continued existence. In the latter case, it reflects the opportunity of insiders to reap significant gains by selling their shares to outside investors. By the end of the 1990s, the post-privatization processes of property redistribution have been completed in most MEBO companies, and now only minor changes can be seen (Kozarzewski, Woodward, 2003).

Compared with enterprises that have been privatized through indirect methods, corporate governance structures in MEBO companies seem to be to a great extent dysfunctional. A problematic division of powers and functions can be seen in many companies, which is caused by unclear principal-agent relations.

Besides, MEBO companies are characterized by a very high inertia of the authority and influence structures which emerged already during the Communist period. Reproduction of the managerial elites in these companies (especially with respect to SOE directors and the executive boards of the privatized companies) as a rule takes the form of internal "direct reproduction" (Wasilewski, Wnuk-Lipinski, 1995); i.e., one that does not entail shifts of individuals within the hierarchy of authority.

As to the ideological underpinnings of this path of privatization, it turned out that claims regarding workers' aspirations for employee participation had been exaggerated. As a rule, they did not express a desire to participate in management of their firms, and shares with no dividends were as a rule of no use for them (Kozarzewski, 1999). The main motivation for workers to retain shares was the fear of unwelcome changes that an external investor might cause (lay-offs, worsening labor conditions, etc). The popular idea of capitalism based on employee ownership collapsed, but this collapse gave room for the development of corporate governance mechanisms based on clearly defined property rights and a strict distinction between ownership, supervisory and managerial functions.

The third pattern is represented by the JSSPs, companies wholly owned by the state. Initially, JSSPs were intended to be a transition entity between the SOE and a private company (with this stage lasting no longer than two years). However, in practice, for every third enterprise which entered "indirect" privatization, ownership transformation stopped at this stage indefinitely. At the beginning, the main cause for this delay were problems with entering the next stage of privatization: technical difficulties related to restructuring and preparing a privatization deal, lack of appropriate buyers, etc. Later on, however, strong lobbies emerged which were interested in keeping enterprises in this intermediate stage. At the enterprise and branch levels, these included trade unions and other organized groups of employees who were not interested in privatization because it would lead to deep restructuring followed by shutdowns of loss-making enterprises, lay-offs, and liquidation of branch privileges. A separate category of insiders not interested in future privatization consisted of the Treasury representatives on the supervisory boards. For them, privatization meant the loss of their positions. Simultaneously, after a significant slowdown of the entire reform process in Poland beginning in 1992, and increase in clientelist behavior of the political elite, JSSPs began to be regarded as a significant asset in the hands of politicians and governmental bureaucracy. The Ministry of Ownership Transformation (later renamed the Ministry of the State Treasury) proved to be to a large extent incapable of staying within the boundaries of a task-oriented organization set up for organizing the process of transition. It suffered a growing conflict between its owner's and seller's functions: the fewer assets under control of the ministry, the less its political weight. This attitude was strengthened by winning political parties, which started to treat state assets as spoils that belong to the victors. One of the most attractive parts of this "loot" were the seats on the supervisory boards of the JSSPs, and for a long period of time the Ministry used them as an instrument of preserving its political importance and stability regardless of the changes of governments (Błaszczyk et al., 2001; Jarosz, 2001). Thus, the Ministry became one of the interest groups working to slow down the reforms.

Although JSSPs are regarded as a highly valuable asset in political struggles, at the enterprise level the role of the Treasury Ministry as an owner is in most cases extremely weak: the real priority is to keep this property and extract material gains from this possession, and not to manage it in a microeconomically efficient way. It is therefore not surprising that in terms of corporate governance and enterprise performance JSSPs have become the most dysfunctional group of companies included in the privatization process. Most JSSPs were for a long period of time left in an intermediate state, being neither a "regular" SOE nor a private company, without any concrete prospects or priorities for further ownership transformation, restructuring, etc. Therefore, in practice, existing corporate governance structures are characterized by a high degree of influence of managers and trade unions and the very weak role of the representatives of the Treasury. Additionally, in many JSSPs the spheres of influence of the main actors have not stabilized, which gives ground for perpetual conflicts (Kozarzewski, 2003a).

The state is not the only institutional actor on the corporate scene whose ineffectiveness in its corporate governance role has disappointed the hopes and expectations of the reformers. The role of **other institutional actors**, such as banks, insurance companies, pension funds and investment funds is rather sub-optimal, although their activity (or lack of thereof) is not so dangerous for the outcome of enterprise sector reform as that of the agencies of the state. The weak role of these non-state institutional actors has many causes, including lack of experience and proper governance, conflicts of interests, insufficient motivations to pursue the goals envisaged for these actors by legislators, etc.

However, perhaps the most important reason is the lack of proper infrastructure, including most importantly the **weakness and shallowness of the capital market**. The organized segment of the market represented by the Warsaw Stock Exchange (WSE) does not properly perform two basic functions of a stock exchange: valuation and a source of capital for private sector. Ironically, the Treasury is the largest beneficiary of capital inflow through the WSE: it was established mainly to serve initial public offerings in the course of indirect privatization. The dominance of privatized enterprises (61% companies listed are former SOEs) is a barrier for further development of the WSE, because the main task of indirect privatization is to find strategic investors for SOEs, and many such investors are not interested in keeping the companies public (Tamowicz, Dzierżanowski, 2002) because of various reasons, among others the less stringent prudent disclosure regulations for non-listed companies. Moreover, the declining pace of privatization contributes to a further fall on the supply side. The situation is additionally complicated by the entry of new players (e.g., pension funds) on the market, which produces additional demand. The WSE has never obtained a proper balance on the demand and supply sides. During the first years of its existence, the supply of shares of the largest privatized companies was huge in comparison with demand. Now, the situation is reversed: the stagnant market has not expanded rapidly enough to satisfy the needs of institutional investors. As a result, the WSE is a very small market with a contracting tendency: the total number of companies listed is falling (from 230 at the end of 2001 to 203 by the end of 2003)[20].

In recent years, attempts have been made to strengthen corporate governance by elaborating and introducing **best practices of corporate governance**. The main idea behind this approach was that because legal regulations themselves are incapable of dealing with all the problems of corporate governance, a set of principles should be prepared which would serve both as instructions on how to behave correctly and as a form of moral pressure on companies to introduce these principles. In 2002, the Warsaw Stock Exchange adopted a Best Practices Code for listed companies, which presented both the general ideas and concrete solutions aimed at improving corporate governance in companies. Although this document is indeed rather a kind of moral obligation imposed on companies than a strict regulation (because there are no effective sanctions for not introducing those measures into companies' charters and everyday behavior), almost all companies declared that they were going to comply with it. Nevertheless, none has declared compliance to every provision of the Code so far. It is still too early to assess the impact of the Code on the governance of companies.

Changes in enterprise behavior and performance

There were at least two distinct phases, or periods, of changes in enterprises behavior and performance.

The main feature of **the first period**, which started in 1990 and ended in the mid-1990s, was adjustment to the emerging market environment, first of all hardening budget constraints and increasing competition. In that period, all types of enterprises showed many similarities in their behavior. Privatization, not to mention its specific methods and paths, seemed to have little influence on the adjustment patterns of enterprises. There where three stages of this adjustment (Błaszczyk and Woodward, 1999; Mączyńska, 2001):

The first stage (1990-1991) was a period of severe crisis caused by external shocks linked with the systemic change. While in 1990 many enterprises could still allow themselves a "wait and see approach" because of accumulated financial and other

[20] WSE data: http://www.gpw.pl

reserves, 1991 was a year of sharp decline. At this time enterprises made intensive efforts to find short-term survival strategies, mostly by employment cuts, sale of non-productive assets etc., as well as by attempts to find new markets for their goods. Production and sales, as well as other economic indicators, fell sharply. The real indebtedness of enterprises was growing.

The second stage of adjustment was in the years 1992-1993, when enterprises tried to halt the decreasing trend of production and sales. In this stage, they introduced new sales strategies. The first sign of recovery was the rise of labor productivity in 1992, accompanied by a production increase, but the profitability indicators of enterprises were still decreasing and investment stagnating. 1993 was the first year when the financial performance of enterprises recovered and investment rose (although net profitability was still negative).

The third stage of adjustment, starting in 1994, was characterized by steady production growth, improvement of profitability, rising net profitability and investment spending.

By the mid-1990s, adjustment processes in most enterprises were completed, which marked the beginning of **the second period**. Since then, a gradual differentiation between the restructuring patterns of various groups of enterprises has become more and more visible. In turn, those emerging patterns began to differentiate changes in enterprises' performance. One of the most important vehicles of changes in enterprises were changes (or lack of thereof) in their ownership structure, although the problem of exogeneity vs. endogeneity of ownership structure vis-à-vis companies' performance is still not resolved. Privatization was characterized by a very strong selection bias, especially in the case of management-employee buyouts and completed cases of indirect (capital) privatization (these were generally the best-performing SOEs), but there is strong evidence that ownership matters (although it is rather the type of dominant owner than the level of concentration that is important).

Three types of enterprises (differentiated with respect to ownership) are of special interest in Poland.

Privatized enterprises with dominant foreign investors. Here we observe the deepest strategic restructuring, involving large investments and innovative technological changes, which leads to the high economic performance of such companies.

Enterprises privatized to managers and employees. Most of these were viable profitable small and medium-size enterprises at the beginning of privatization, many of them already having their niches on the emerging market. This situation made immediate restructuring measures less urgent, so many companies limited their efforts to shallow and simple restructuring measures. A real motivation for deep restructuring appeared only when there was a real threat to the company's further existence. During the better part of the 1990s, this led to a gradually falling (albeit still favorable) trend in MEBO companies' economic indices, in contrast to the rising trend in companies privatized through sales to strategic (especially foreign) investors. By the end of the decade, a large number of MEBO companies seemed to realize that lack of restructuring measures might jeopardize their future, and tried to change their behavior, i.e., to start investment programs and deep technical restructuring.

Enterprises in practice exempt from privatization for some social, political or lobbyist reasons. This group consists primarily of JSSPs and state-owned enterprises in "sensitive" sectors such as infrastructure, mining etc. This group of companies demonstrates the worst economic performance and a lack of deep and efficient restructuring. The differences between these companies and privatized firms are becoming more and more striking, the former showing not only worse economic indices, but also no will or capabilities to perform deep restructuring, because of the lack of incentives to change their rent-seeking behavior. Nevertheless, some managers of such companies are longing for privatization (on their terms, i.e. that would preserve their power) because they expect higher gains if their companies would be freed from the government's intervention.

5.5. Assessment

The processes of privatization and enterprise restructuring are marked by both successes and failures. The most spectacular success is privatization in the "broad sense" which boosted the growth of new private businesses and the share of the private sector in the national economy. Privatization in the "narrow sense" (ownership transformation of state-owned enterprises) was only a partial success, both in terms of quantity and quality. Some methods of privatization proved to be more "permeable," easier to implement for a number of social, political and technical reasons than the others; thus, the progress of privatization was very uneven across sectors, and some of them (infrastructure, extractive industries and some others) remain predominantly state-owned. There were two reasons for this situation: the highly gradualist, consensual character of Polish privatization procedures and the emergence of interest groups not interested in privatization of remaining state-controlled companies.

The outcome of enterprise restructuring processes is even more ambiguous. It should be noted that two totally different types of restructuring exist in Poland. The first one is led by new owners of privatized companies, and the success of such restructuring to a great extent depends on the type of owner (restructuring efforts led by foreign investors being among most successful). Adoption of the Continental model of corporate governance also contributed significantly to successes of post-privatization restructuring of enterprises. On the other hand, there are restructuring programs led by the government which apply to the sectors that are still under state control. During the whole period of post-Communist transformation, only one such program can be regarded as a success, although not all of its declared goals have been met (Enterprise and Bank Restructuring Program). Restructuring efforts of the government were effectively blocked by newly emerging powerful interest groups of "early winners" supported by employees of the state-owned sector; moreover, quite often restructuring programs themselves contributed to consolidation of these groups.

The analysis of the enterprise sector reform supports most of our initial hypotheses, and additionally allows us to refine some of them.

In particular, it corroborates our hypothesis #1: enterprise sector reforms require a highly participatory approach, because their success depends not only on efficient construction of new institutions, but also on ability to make the main actors behave in post-reform environment in line with the goals of the reforms. On the other hand, technical aspects of reforms must not be neglected, otherwise even highly relevant set of actors involved will not be able to ensure the success of a program.

It also supports the hypothesis #2: the most successful reforms involved the main actors in looking for the best organizational and behavioral solutions, while the most drastic cases of reform failure are connected with the State acting as a distributor of public goods and rents.

Our analysis supports hypothesis set #4: the most successful reforms were elaborated or at least thoroughly fine-tuned by Poles themselves, so local conditions had been taken into account and "ownership" of the reform was local. Besides, interests of potential allies of the reformers were taken into account, and the opponents were in some way "neutralized." In the spheres where the reformers failed to do this, strong interest groups emerged that opposed the continuation of the reform course. These groups consist of both "early winners" and actors associated with the state-owned past of privatized enterprises. From this perspective, "local ownership" of reform failures can be regarded as a disadvantage, because it leads to very strong and stable dysfunctionalities embedded in the local cultural and political context.

The analysis supports the hypothesis set #5, contributing to the creation of a model which describes the influence of the three main groups of actors ("reform advocates," "early winners" and "transformation losers" associated with the state-owned sector) on the reform process, as well as conditions under which reforms pass through the two critical points (see Section 2).

In Poland, external factors have been important in shaping the enterprise reform process, foreign experts helping in identifying the problems that had arisen in the course of transformation (hypothesis #6b), and foreign firms and foreign direct investments having a highly positive impact on enterprise reform. But the role that international institutions have played in constraining the actions of policy makers and in shaping their thinking about the enterprise sector reforms was far from crucial, mostly due to the very high degree of their local "ownership."

6. Pension reform

The pension reform was introduced, through a succession of laws, in 1997 and 1998. It was an almost unique example of a political consensus of two successive governments – SLD and AWS, as the reform was started under the former and was ultimately implemented under the latter government. It is also an example of reform motivated not by pressing current concerns and issues, but rather by the consideration of long-term prospects, and also very thoroughly designed and carefully guided through the political process. As such it can be treated as successful, although various problems inevitably arose during its implementation. In our discussion we consider the success of this reform purely in the sphere of political economy – i.e., the ability of reformers to win support for the reform and ensure its passage in the legislature and implementation in practice, and the fact that the reform has not been reversed by later governments – abstracting from economic and technical questions concerning difficulties (discussed briefly in section 6.3) arising in computerization, the fiscal transition costs of partial privatization, etc..

6.1. Legacy

Since the 1950s, Poland had had a comprehensive pension system of the pay-as-you-go (PAYGO) type (Czepulis-Rutkowska, 1997). Until the late 1980s, the system retained basic financial stability. However, over time, it acquired sizable deficiencies, particularly in the form of so-called "branch privileges," granted to certain professional groups (army, police, miners, etc.). These were the outcome of the tacit political pressure of interest groups and the co-opting policies of the authorities. The privileged groups benefited from earlier retirement age and/or better pension-to-pay ratios. All other members of the system financed these benefits. During the 1970s, pensions had also been granted to the farmers, a sizable part of the population, but who did not pay into the system. Poland also developed a widespread system of disability pensions. Since it has been easy to obtain such pensions, they constitute a much larger share of the whole pension scheme than in most European countries. The whole system has been administered by the Agency for Social Insurance (ZUS), responsible to the Ministry of Labor. In 1991, the farmers' pension program was moved to a separate Fund for Farmers' Social Insurance (KRUS). This system is in constant financial strain and has to be additionally funded by the budget, as many farmers routinely are arrears with their contributions.

Already at the late 1980s problems of the liquidity of the whole system started to show, which prompted to the gradual increase of social security contributions, from 15% of pay in the 1950s to over 35% in the late 1980s (Hausner, 1998). In the early stages of the transformation, the problems of the pension system became aggravated by two factors: by inflation and by the policy, described in section 4.4, of massive early retirement. The situation was aggravated by costly solutions to problems caused by inflation. They involved indexing and revaluation of pensions granted long before and thus having smaller real value than pensions received by workers retiring from the same jobs at later dates. Such was the context the initiative for reform of the system was born in the mid-1990s.

The first suggestions for radical reforms – in fact, a shift from a PAYGO to a funded system – were put forward as early as 1991 (Topiński, Wiśniewski, 1995). One of the initiators, Wojciech Topiński, in his capacity as head of ZUS, visited Chile, was impressed by the Chilean solutions and tried to promote them at home, but without success. The debate took off once again a few years later. By then, the overall economic change was more advanced. Additionally, the World Bank, which played a considerable role in Poland, became engaged with promoting the change to the funded model all over the world (World Bank, 1994).

At this stage, the participants of the debate concentrated not on the immediate problems of the pension system, but rather on its long-term prospects, related to declining ratios of working to non-working population, caused in particular by declining fertility (Golinowska, 1997; Szumlicz, 1999). According to a number of demographic scenarios, the existing PAYGO system would accumulate problems and ultimately collapse at the end of the first decade of the 21st century. The idea that it was necessary to introduce funded systems instead of or in addition to the PAYGO solutions gained acceptance among social policy experts. As a result, several developed proposals were put forward, ranging from the radical projects of Finance Ministry experts to more conservative proposals of Labor Ministry experts (for comparisons, see Golinowska, 1998).

6.2. The Reform

The political decision to go on with the reform was made by the SLD government in 1996, largely on the initiative of the Finance Minister, Grzegorz Kołodko. The most important personality behind the efforts to start the reform was the Minister of Labor, Andrzej Bączkowski, who put unusual effort and commitment into the reform of the social security system. A lawyer by profession and a Solidarity activist since 1980, he became Deputy Minister of Labor in 1991, stayed in several cabinets, became chairman of the Tripartite Commission and acquired considerable prestige as an exemplary public servant and good negotiator (Hausner, 1998, 37). He became Minister in February 1996 and at the same time Government Plenipotentiary for the Reform of Social Security. After his premature death in November 1996, Jerzy Hausner, a well-known economist with a record of publications on transformation and a liberal-minded intellectual-politician close to the SLD, replaced him in this capacity. (With the AWS-UW coalition victory, Hausner was in turn replaced by Ewa Lewicka.)

The actual work on the design of the reform was done, between October 1, 1996 and June 1997, by the specially constituted Office of the Government Plenipotentiary for the Reform of Social Security (Biuro Pełnomocnika Rządu 1997). The way it acted was unusual for the Polish bureaucracy, and the character of its operation is a factor explaining the high quality of the design[21]. It was a hand-picked *ad hoc* team of economists and social policy experts, led by Michał Rutkowski, "on loan" from the World Bank to the Polish government. They were administratively attached to the Ministry of Labor, but in fact worked without the usual everyday constraints the permanent members of any bureaucracy feel. Hausner, who both in his theoretical work on the transformation and in his political activity stresses negotiation and the "institutionalized cooperation" of opposing interests, provided a political shield (cf. Hausner, 1995, 324, for the concept of institutionalized cooperation). In the design of the reform, the team members did not confine themselves to arguing for the necessity of change and the construction of the new models, but went further, preparing (with the cooperation of legal advisers) drafts of the necessary new regulations. Moreover, they did not work in isolation, but – relying on the communication talents of both Hausner and Rutkowski – were active in preparing ground for understanding of the new system among the government bureaucracy (particularly ZUS), the parliamentarians, and even the wider public (cf. Hausner, 2004).

[21] The authors of this report express their thanks to Irena Topińska, a member of this team, for sharing information about the ways it operated and the climate of its work.

The proposed system consisted of three pillars: a reformed PAYGO pillar, a privately funded pillar which was to become universal and mandatory over time, and a voluntary privately funded pillar. In the new system, part of the future pension would come from the reformed PAYGO, and part from the private fund. The choice of the private fund would be free, and it would be possible to change from one to another. The change from the old to the new system was supposed to be gradual. Persons over 50 were to stay in the old one (i.e., they participated exclusively in the first pillar), persons under 30 were required to switch to the new one (i.e., to participate in the second pillar), and persons in between had a choice between either staying in the old system and moving to the new system. There were two main arguments in favor of the new system: it would avoid the type of financial traps characteristic of PAYGO systems, and it would provide incentives for saving and facilitate the development of financial markets. There would be, on the other hand, a cost of transition, as there would be a necessity of both financing the current pensioners (through the old PAYGO system, until its phasing out) and paying contributions related for the second pillar. These additional costs were to be financed from privatization revenues.

The work of pushing the project through the Council of Ministers (cabinet) and through the parliamentary process was done mostly by Hausner. In early 1997, the Plenipotentiary was placed directly under the authority of the Prime Minister. This gave Hausner more leeway, as his responsibilities were now solely for the reform, and not for the current operation of the social security apparatus. He was also made chairman of an inter-ministerial task force for the implementation of the reform, which allowed him to set the intensive pace of work on the final legislation to be processed by the government and the Sejm. An important part of his activities consisted in winning the trade unions – and particularly, Solidarity, which was the main component of the AWS – over to the reform (Hausner, 1999, 40ff.; Hausner, 2004).

Four of the laws necessary to implement the reform (related mostly to the use of the funds from privatization) were passed between June and September 1997, still under the SLD government. The key law on the system of social security was passed under the AWS-UW coalition, in October 1998.

6.3. Assessment

It is too early for an assessment of long-term effects of the pension reform, either in terms of its contribution to the solution of social security problems, or of its influence on the development of capital markets. It also has to be noted that, at the early stages of implementation it stumbled because of logistical problems. The implementation required setting up individual accounts for every member of the system in the ZUS and smooth data processing, including transfers of money between the ZUS and the various private retirement funds. For that, the ZUS needed to improve radically its IT capacities. It contracted a large Polish company, which for years failed to succeed in developing the necessary software. Also, more people from the age group of 20-50 decided to join the new system than had been predicted by the authors of the reform, which put additional financial strain on the ZUS. Finally, it is necessary to add that the reform did not touch two segments of the social security system which are sources of constant problems, namely those of disability pensions and farmers' pensions. Hausner (2004) says that – given the strength of the Peasant Party (PSL) establishment – any attempt to deal with the farmers' pensions was doomed to failure. Leaving these problems aside, however, it is possible to say that the pension reform was a success, particularly in comparison with two other major reform efforts of the same period, those of health and of education, which were reversed by the succeeding governments.

We can point to several factors to explain this relative success:

- Good design. This in itself was a coincidence of several factors. One of them was a clear model, due to an on-going debate at that time (promoted by the World Bank in particular) on the desirability and advantages of funded, as opposed to PAYGO, pension systems. This was in marked contrast to, for example, the health reform, where no such clear models were at hand. The second factor was the talent and commitment of the leadership of Polish reforms, particularly of Bączkowski, Hausner, and Rutkowski. In addition to their personal commitment, they were able to organize a good team and to persuasively communicate their ideas to other actors and to the wider public. The third factor was the design of the working team itself, created as a task force independent, in practice, from the government bureaucracy, and also having a clear "exit strategy," as they were supposed to terminate their work quickly upon the completion of the program. Incidentally, this sheds a certain light upon the effectiveness of the Polish public administration, the topic of section 3.1, as the pension reform – in a way similar to the macroeconomic reform, also a successful one – was designed not by a standing bureaucracy, but by experts who were, to a large extent, outside both the bureaucracy and the party system.
- Coalition of supporters and allies. There were a number of actors who had a stake in the success of reforms (Golinowska, 1998). They included the local experts, the foreign experts, the international financial institutions (World Bank, the IMF) and

– last but not least – the emerging private pension funds. The latter, through their aggressive (and probably very costly) promotional campaigns, took upon themselves the task of accustoming the wider public to the new system.

- Lack of powerful opponents. Although the pensioners were a powerful political force in Poland, their immediate interests were in no way threatened by the reform. Also, contrary to the health reform and the education reform, in the case of pensions there were no lobbies of service providers blocking the reform process in the name of status quo (Nelson, 1998). The ZUS administration was not particularly enthusiastic about the project, but it did not oppose it (Golinowska, 1998). There was some opposition among legal circles, who saw funded systems as "not social security" – but the views of the economists prevailed (Golinowska, 1998, 21; Hausner, 1998, 37).

7. Conclusions

Hypothesis 1. Participatory vs. technocratic approaches: importance of "match" or "balance"

We hypothesized that one of the key factors in the political economy of reform success is the degree of match between technocratic or participatory approach compatibility and the degree to which it is in fact implemented using either a technocratic or participatory approach, and that reforms are successful where there is a good match. This occurs when, for example, reforms of a largely technical nature are carried out in a technocratic manner, and reforms requiring a more participatory approach are implemented as decentralized learning processes on the basis of negotiation, with the participation of various social actors. Unsuccessful reforms, on the other hand, are observed where there is a mismatch or an improper balance between the role of technocratic concerns and the role of the interests of various social actors.

We have argued that the successful Polish experience with the initial stabilization and liberalization reform package is evidence in favor of our first hypothesis – that it represents a success of the "technocratic" process in preparing a reform of a very technical nature. On the other hand, we have also noted that it was unfortunate that a greater effort to educate Polish society about the goals of the reforms and the nature of the market economy was not undertaken.

While reforms of a largely technical nature, such as macroeconomic stabilization and liberalization, consist of parameter setting by a small group of central institutions such as the finance ministry or the central bank, successful enterprise sector reforms require a highly participatory and decentralized approach, because the actors involved are very numerous and located throughout the economy[22]. Such an approach was

[22] Of course, mass privatization can and has been carried out in a centralized manner (e.g., in the Czech Republic), but the consensus seems to be that this has been the least successful method of privatization in the post-Communist countries. See, for example, Błaszczyk et al. (eds., 2003).

crucial for the progress made in the first five years of the Polish transformation in the area of privatization, when the vast majority of privatizations were management-employee buyouts (privileged employee access to shares was also important in winning employee approval for privatization by trade sales and IPOs). It was similarly crucial for the success of the Polish program for restructuring of banks' bad loan portfolios, in which banks and enterprises were the main actors and participated in a learning process, as opposed to the centralized, and much less successful, approach adopted in the Czech Republic and Hungary. Failure to achieve a proper degree, scope and character of participation led, for example, to suboptimal results of some privatization paths and methods (the most drastic example are numerous unfinished cases of indirect privatization) and most of the restructuring programs. On the other hand, technical aspects of reforms must not be neglected, otherwise the involvement of even highly relevant sets of actors will not be able to ensure the success of a program. Technical inadequacy was one of the main causes for sub-optimal results of some methods and paths of privatization (mainly indirect ones, such as the failure to resolve a number of technical questions in the course of privatization of largest enterprises and flaws in the NIF mass privatization program), as well as of certain restructuring programs.

The success[23] of the pension reform was due in large measure to the ability to find the appropriate balance between technocratic and participatory approaches. The pension reform, although technically complicated, had a strong participatory aspect, as major attention was devoted by the reformers to involving a large number of groups in the preparation of the reforms (so that large numbers of parliamentarians, ministers and trade unionists felt themselves to be "co-owners" of the reform) and in the creation of new groups of social actors (private pension funds); of course, the population was empowered as well (by being given the opportunity to make choices about their funds and, in the case of persons aged 30-50, to make a choice whether to join the new system or not). However, the reform also included a large, effectively organized "technocratic" component which was crucial in assuring the quality of reform design.

Thus, with respect to the first hypothesis, we conclude that it should be reformulated: it is not a question of "matching" a given approach (participatory or technocratic) with a given reform, as reforms are generally of a complex nature, and various aspects of any given reform require various approaches. Thus, for any given reform, an appropriate "mix" or "balance" of the two approaches would seem to be necessary for success.

[23] This success was a political success. It is too early to judge the degree of success of this reform in economic terms.

Hypothesis 2. The successful participatory approach as a learning process

Our analysis of reforms in the enterprise sector shows how the most spectacular successes and failures in this area in Poland support this hypothesis. The most successful reforms engaged the main actors in looking for the best organizational and behavioral solutions, while the state limited its role to setting of the general framework of learning activity and acted as a referee (as in the bank and enterprises restructuring program and many cases of consensual privatization). The most drastic cases of reform failure are connected with the state acting as a distributor of public goods and rents (as in the JSSPs or sectoral restructuring programs). At the same time, in order to meet the goals of the reforms, the proper set of actors must be chosen and they must be forced to act within a certain institutionalized framework. Otherwise, interest groups emerge whose goals often contradict the goals of the reforms. This can be seen, for example, in the case of entrenched managers in many management-employee owned companies, and members of the supervisory boards of the JSSPs. The worst situation occurs when an improper choice of actors is combined with the highly distributive role of the State. In such situations, clientelism and the entrenchment of actors reach their apogee (e.g., JSSPs; the role of the Ministry of the Treasury in privatization and enterprise restructuring during the last few years; failure to restructure some sectors, e.g., mining).

The case of reform of the judiciary also supports this hypothesis. Here, role of the social actors (in this case, judges) was not construed at the beginning of the reform process as a learning one within a partnership relationship, but rather as one in which they would simply use their "voice" to make demands. As a result, these actors have blocked further reform in this area.

Hypothesis 3. The missing link: Early public sector reform

Our analysis of the civil service reform and the justice system reform supports our hypothesis # 3, namely that the failure of reformers in the early stage to appreciate the importance of public sector reform led to stagnation later. Failure to develop a civil service and an effective administration of justice seriously diminished state capacity (including its market supporting role) in terms of its ability to reconstruct institutions through the introduction of new regulations, as well as to effectively monitor and enforce the functioning of existing institutions.

Many of the problems of the Polish privatization process can also be linked to the failure to create a well-paid, apolitical and professional civil service which could have managed the process in the ministry. The high rate of turnover of ministry personnel and the high level of politicization of that personnel have led to many delays in the privatization of large, valuable enterprises, which have often been held in limbo in the intermediate JSSP stage, where political appointees have been able to hold lucrative posts on both supervisory and executive boards. The lack of continuity has also been partially responsible for a stop-and-go dynamic which has been observable in the pace of privatization, as during long periods following each new government's taking office privatization comes to a virtual halt.

Hypothesis 4a. The importance of "local ownership"

One of the key factors of mostly successful general course of Polish transition (especially when compared to most other post-Communist countries) is the fact that almost every reform was elaborated or at least thoroughly fine-tuned by Poles themselves, so local conditions had been taken into account and "ownership" of the reform was local. In spite of the important role played by foreign advisers including Jeffrey Sachs and representatives of international financial institutions, the Polish stabilization and liberalization reform package was a Polish product. This fact constitutes a great success whose importance cannot be overestimated, because part of the initial conditions and inherited baggage of the past referred to in our formulation of the hypothesis was the post-Communist countries' shortage of trained professionals competent to understand the issues involved and design and implement such a program (a shortage which was much more severe – in some cases amounting to a complete lack of such persons – in many countries of the former Soviet Union).

In the area of enterprise reforms, not only did Poland elaborate its own original privatization concepts, but sometimes (as in the case of bank and enterprises restructuring program) foreign solutions were rejected in favor of locally designed solutions (moreover, in this case, we would argue that this locally designed solution was in fact superior to the foreign solution). Similarly, the fact that "local ownership" of the reform was clearly maintained was a key factor in the success of the social security system reform.

Hypothesis 4b. The policy maker's need for allies

The whole privatization concept in Poland was build on the understanding the necessity to take into account interests of potential allies of the reformers (or at least "neutralize" potential "enemies"). One country-specific feature consisted in the important role of trade unions and employee self-management. Where these institutions acted as allies of the restructuring and privatization process, the reforms were faster and smoother (as in MEBO companies and other successful privatization deals as well as the bank and enterprises restructuring program) than in cases where their interests contradicted the goals of the reform programs (i.e., most restructuring programs, JSSPs).

In the case of the pension reform, we observed the emphasis the reformers put on taking into account the interests of potential allies and winning them over to the reform. One very important such ally was in the financial sector, which was responsible for the creation of the private pension funds making up the second and third pillars (trade unions also enjoyed the possibility of participating in the creation of pension funds).

Hypothesis 4c. Reforms must be compatible with the local context

We have observed difficulties in reform implementation when efforts have been made to transplant foreign solutions without taking the conditions of the Polish context sufficiently into account. In the case of civil service, introducing legal-rational structures based on professional skills and merit was difficult given the inadequate pool of potential personnel and in view of the entrenched habits of social interaction based upon personal relations. In the case of the administration of justice, the introduction of a far-fledged independence of judges, based on the Anglo-Saxon model, did not take into account the fact that the traditions and institutions were not in place which would safeguard the responsibility of the judges.

On the other hand, we also have to note that two of the most positive developments in the area of enterprise reform have occurred where it proved possible to successfully transplant foreign models and experience into the Polish economy. These were the cases of privatization by commercial methods in which enterprises were sold to foreign investors (in such cases, restructuring and investment has been carried out with much greater intensity than in any other group of Polish enterprises) and the overall process of implementation of the Continental model of corporate governance.

Hypothesis 4d. The danger of re-constitution of old interest groups

Socialist industry and the planning apparatus which ran it were characterized by branch interest groups whose structure (even if sometimes informal) was a corporatist nature. This was particularly true of mining and heavy industry (but also, for example, the textile industry), where enterprise directors, the official trade unions and ministry officials together formed powerful lobbies which exerted great influence on the resource allocation decisions of the central authorities. While these interest groups disintegrated in the initial shock of the end of the central planning system, we have observed a tendency in all post-Communist countries for them to reconstitute themselves. This poses a threat to the reform process. Overcoming them is crucial for development of efficient corporate governance and market behavior of enterprises, optimal goals and priorities setting.

Hypothesis 5. The importance of keeping "early winners" at bay

In Poland, a large number of powerful "early winner" interest groups emerged (especially after the reform slowdown of the mid-1990s), many of which are interested in defending their privileged positions (e.g., by controlling the legislative and decision-making processes at the parliament and government level, creating and keeping monopolies, etc.) rather than the level playing field of a liberal market economy. These groups include, for example, entrenched groups of politicians and bureaucrats, trade union leaders (at the national level) etc. Another important group consists of certain very rich businessmen who have obtained their status due to good political connections, fierce lobbying and even criminal activity. At the level of enterprises (especially state-owned ones or where there was no substantial progress in corporate governance restructuring, such as JSSPs and some MEBO companies), the most important such group consists of managers, for whom further reforms may mean deterioration of their opportunities for asset stripping and tunneling. In the public sector, judges constitute a good example of this group, having one extraordinarily far-reaching independence at the outset of the transition. Similarly, judges, as a result of their gains (with respect to independence) in the early reform period, were able to organize themselves as a rent-seeking group which was successful in blocking further reform. (This is related to hypothesis # 2 as well, since the role of the social actors – in this case, judges – was not construed as a learning one within a partnership relationship, but rather as one in which they would simply use their "voice" to make demands.) As a result of their gains in the early reform period, such groups have been able to organize themselves as a rent-seeking group which was successful in blocking further reform. On the one hand, the existence of these groups is a guarantee that there can be no return to the classic socialist economy with state ownership and central planning. However, these groups tend to block reform progress which would bring the country to the "critical mass" at which those interested in a liberal and competitive economy and rule of law are stronger than those favoring "crony capitalism" and similar syndromes that tend to characterize most transition economies.

In Poland, transformation losers consisted of groups linked with the state sector, such as employees of SOEs in the "sensitive" sectors, and those employee council members and trade union functionaries who were unable to find places for themselves in privatized companies.

None of the transition countries, including Poland, seems to have been able to overcome the low level equilibrium described in section 2.2 and move beyond the R_2 point (although apparently Poland is much closer to the R_3 point than many other post-Communist countries, especially FSU states), which is the real "critical mass" point of post-Communist reforms.

These observations lead us to the tentative conclusion that rather than a breakthrough taking a country rapidly from the R_2 equilibrium to the R_3 equilibrium, we should expect at best a set of incremental changes in the balance of powers between the three groups (mostly changes in the composition and behavior of the early winners group) which permit a gradual move in this direction. There will be no more "windows of opportunity" or "extraordinary politics" in the transition countries, barring unforeseeable extraordinary circumstances. Thus, the only option available is gradual progress, which can be attained by pursuing two strategies simultaneously. One is a "stick" approach consisting of constant pressure on the interest groups blocking reforms (both the "early winners" of the transition period and the re-constituted corporatist groups of the *ancien regime*), in an attempt to contain their advances or even roll them back to some extent when it is possible. The other is a "carrot," consisting of efforts to find ways to link the interests of small groups of the reform-blocking coalition with a reform agenda and bring them into the reform camp, enlarging it and diminishing the anti-reform coalition at the same time.

Hypothesis 6a. Diminishing role of EU and NATO membership prospects over time

Unfortunately, the reform areas covered by our research have been practically unaffected by EU and NATO membership prospects, and thus we were unable to test this hypothesis. The exception is in the area of monetary policy. The fact that monetary policy has remained on a more or less restrictive course and the independence of the monetary authorities not seriously challenged is probably due in large measure to the constraints imposed by the international environment, in which Poland's status as a borrower and candidate for EU membership would have been threatened by serious policy reversals in this area.

Hypothesis 6b. The role of international institutions

We have seen that in the sphere of public administration (civil service) and the administration of justice, the failure to reform was linked to the low level of pressure or advice from international institutions to reform existing institutions. In contrast, the very active role of the World Bank was critical in the success of the social security system reform (at the same time, "local ownership" of the reform was clearly maintained, in support of hypothesis 4a).

International institutions have also played an important role in constraining the actions of policy makers as well as in shaping their thinking about both the content of the enterprise sector reforms and the manner of their implementation (sequencing, methods applied, etc.). The research showed that foreign experts also helped a lot in identifying the problems that had arisen in the course of transformation and had been caused by reforms themselves (as in the case of the restructuring of banks' bad debt portfolios).

Hypothesis 6c. The role of the international business cycle

Poland's transformational recession at the outset of the 1990s was deeper and longer than the reformers had expected, largely due to unforeseen external circumstances such as the collapse of the CMEA and the Soviet Union in prolonging the recession, but also because this period was not a favorable one in the world economy, with both the United States and Japan moving into recession. A better situation in the world economy would have probably helped Poland's economy recover faster and make the reforms more popular. This seems to have been the case for Turgut Özal in Turkey and Viktor Yushchenko in Ukraine – their reforms, carried out in the early 1980s and the late 1990s, respectively, were accompanied by favorable external conditions and their popularity was much greater than that of Leszek Balcerowicz.

Additional conclusions suggested by the analysis

Our research points to a number of conclusions concerning issues which were not touched on in our hypotheses. We would like to deal with these briefly at this point.

Our research suggests that the impulse for reform initiatives often comes from the presence of a crisis situation. Thus, for example, near-hyperinflation seems to have been a necessary condition for Balcerowicz package, and the bank loan portfolio crisis a necessary condition for the enterprise and bank restructuring program. Similarly, the lack of tangible crisis could be seen as a reason for the lack of civil service reform. There are, however, exceptions, for example in the justice system, which is certainly in crisis, but in which reform is nevertheless blocked by the judges' lobby and the fact that the current fiscal crisis limits the funding available for investments (e.g., in computerization of courts and police). Also, in this case, the logic of collective action described by Mancur Olson seems to be relevant: the small lobby of judges has a stronger incentive to retain the status quo than the large body of citizens that would benefit from reform has to actively work for reform. Another exception can be found in the pension reform, which was undertaken despite the fact that a crisis situation, while inevitable if the pay-as-you-go system had remained unreformed, was still in the distant future at the time.

Regarding the role of various actors in the reform process, our observations of reform opponents suggest that it is important to distinguish between rhetoric and action. The former is usually much more radical than the latter. To date, no one in power has ever radically revised the reforms undertaken at the beginning of the Polish transition. In general, there seems to be rather a gradual erosion than a "counterrevolution" (this should have implications for the theory of the "critical mass" or "point of no return").

On a related subject, political instability seems to be more important for the implementation (especially the pace) of reforms than for their content (design). People have often come into office intending to implement new policies and programs but ended up implementing ones that had been elaborated by the previous administration. The effect of this has been to slow the pace rather than alter the content of the reforms.

Another interesting observation is that a change in the ruling party is not necessary for reform reversals, which have sometimes been initiated by the same groups earlier responsible for reform policies.

Finally, a factor that seems to underlie the success or failure of the reforms examined here is the quality of leadership. We cannot find an example of a successful Polish reform without a leader who pushed it through. Such a leader must have a vision of change and a commitment to that change and be able to convince the appropriate parties to support, or at least not hinder, the reform. The strengths and weaknesses of such leaders are crucial. Balcerowicz, at the time of the initial stabilization and liberalization package, lacked a talent for communicating his vision to the society, but had the necessary vision and was able to pick a team which operationalized and implemented it. The strengths and weaknesses of later reform leaders differed to a greater or lesser extent, but the common denominator is their presence as the *spiritus movens* of the reform effort.

Suggestions for further research

One question which we believe would be interesting for further research concerns the importance of good institutions for reform success. On the basis of the Polish experience, there seems to be reason to believe that this importance may differ with respect to the stage of the reform process at which a country finds itself. Institutions may be more important for sustainability than for the quality of reform package content at an early stage (as in the case of the Polish stabilization and liberalization reforms, which succeeded in spite of the very low level of development of market institutions at the outset of the Polish transition), but become more important for the quality of reform packages in later stages.

As we have discussed above, all post-Communist countries face the problem of breaking the low-level equilibrium represented by the R_2 point in Figure 2.1. An interesting question relates to the policy measures that may be most effective in dealing with this problem, including a wide range of measures aimed at improving the government's credibility and support for reforms. Among the reforms that may be of particular importance here we can list improvements in the conditions for the private sector of economy, especially small and medium sized new entrants; improvements in the legal system in order to minimize the illegitimate gains of early winners, and reallocation of public expenditures to raise the efficiency of social programs and safety nets (thus better compensating losers). The problem is, however, that the early winners' influence on the government and the parliament is so strong (those institutions being to a large extent captured by these groups) that by the time policy makers begin to consider these measures, it may be too late.

Additionally, one might want to identify factors whose presence could reduce the gains of the early winners who capture and thwart the reform process, possibly encouraging some of them to transfer to the "reform advocates" group. These factors could include:

– economic crisis caused by insufficient or ill-designed reforms or a shock from external markets, which threatens the gains of the early winners and may produce a situation in which at least some actors can defend their gains by supporting the reform continuation (at least to some extent);

– external pressure exerted by international financial institutions and membership in international organizations (WTO, NATO, EU etc. – both at the stage of seeking for membership and membership itself), which may force the government to introduce some reforms against the will of the early winners, which may force the latter to adapt to the new situation, among others looking for gains by switching to the reform advocates group;

– evolutionary changes of opportunity costs for early winners, when the reform hold-up becomes less promising than reform continuation (at least to some extent); for example, entrenched entrepreneurs, who benefit from special treatment from the government, may expect gains from freeing themselves from its intervention which exceed the losses caused by withdrawal of the special treatment they enjoy under a less liberal regime.

7. References

Amsden, Alice H.; Kochanowicz, Jacek; Taylor, Lance (1994), *The Market Meets Its Match: Restructuring the Economies of Eastern Europe*. Cambridge, MA: Harvard University Press.

Balcerowicz, Leszek (1995), *Socialism, Capitalism, Transformation*, Budapest, London, New York: CEU Press.

Balcerowicz, Leszek (2000), Interview with Public Broadcasting Service, November 12, http://www.pbs.org/wgbh/commandingheights/shared/minitextlo/int_leszekbalcerowicz.html.

Barbone, Luca; Marchetti, Domenico Junior (1995), Transition and the Fiscal Crisis in Central Europe, *Studies and Analyses* 40, Warsaw: CASE.

Biuro Pełnomocnika Rządu ds. Reformy Zabezpieczenia Społecznego [Government Plenipotentiary for the Reform of Social Security] (1997), *Bezpieczeństwo dzięki różnorodności. Reforma systemu emerytalno-rentowego w Polsce [Security through Diversity: Reform of the Pension System in Poland]*, Warsaw, mimeo.

Błaszczyk, Barbara (1993), Pierwsze lata prywatyzacji w Polsce (1989-1991). Dylematy koncepcji i realizacji [The First Years of Privatization in Poland. Dilemmas of Conception and Implementation], *Studia Ekonomiczne* 30, Warsaw: INE PAN.

Błaszczyk, Barbara; Górzyński, Michał; Kamiński, Tytus; Paczóski, Bartosz (2001), Secondary Privatization in Poland (Part II): Evolution of Ownership Structure and Per-formance in National Investment Funds and their Portfolio Companies, *CASE Reports* 48, Warsaw.

Błaszczyk, Barbara; Woodward, Richard (eds.) (1999), Privatization and Company Restructuring in Poland, *CASE Reports* 18, Warsaw.

Borowski, Marek (2000), Kto trafi, dostanie kryształową [A crystal ball for the one who gets it right], *Gazeta Wyborcza*, 24 May.

Borowski, Marek (2001), Rok niebezpiecznego knota [The Year of Bungling Dangerous], *Gazeta Wyborcza*, 23 May.

Borowski, Marek (2002), Kompletna klapa, czyli dobrego prognostę poznaje się w biedzie [Total Failure, or a Good Forecaster in Deed], *Gazeta Wyborcza*, 29 April.

Boycko, Maxim; Schleifer, Andrei; Vishny, Robert (1995), *Privatizing Russia*, Cambridge: The MIT Press.

Bratkowski, Andrzej S. (1993), Sytuacja budżetu w Polsce w okresie transformacji [Budget Situation of Poland in Transition], *Studies and Analyses* 10, Warsaw: CASE.

Bratkowski, Andrzej S. (1995a), Macroeconomic Performance, in Andrzej S. Bratkowski (ed.), Fiscal Policy in Poland under Transition, *Studies and Analyses* 49, Warsaw: CASE.

Bratkowski, Andrzej S. (1995b), Manner of Financing Budget Deficit and Its Implications for the Monetary Policy and Inflation, in Andrzej S. Bratkowski (ed.), Fiscal Policy in Poland under Transition, *Studies and Analyses* 49, Warsaw: CASE.

Brunetko, Krzysztof. (2003), *Służba cywilna w III RP. Punkty krytyczne [Civil Service in the 3rd RP: Critical Points]*, Warsaw: Fundacja Batorego, mimeo.

Central Statistical Office (1991), *Statistical Bulletin* 11, Warsaw.

Central Statistical Office (1992), *Statistical Yearbook of the Republic of Poland 1992*, Warsaw.

Central Statistical Office (1994), *Statistical Yearbook of the Republic of Poland 1994*, Warsaw.

Central Statistical Office (1995), *Statistical Yearbook of the Republic of Poland 1995*, Warsaw.

Central Statistical Office (1996), *Statistical Yearbook of the Republic of Poland 1996*, Warsaw.

Central Statistical Office (1998), *Statistical Yearbook of the Republic of Poland 1998*, Warsaw.

Central Statistical Office (1999), *Statistical Yearbook of the Republic of Poland 1991*, Warsaw.

Central Statistical Office (2000), *Statistical Yearbook of the Republic of Poland 2000*, Warsaw.

Central Statistical Office (2001), *Statistical Yearbook of the Republic of Poland 2001*, Warsaw.

Central Statistical Office (2002), *Statistical Yearbook of the Republic of Poland 2002*, Warsaw.

Central Statistical Office (2003), *Statistical Yearbook of the Republic of Poland 2003*, Warsaw.

Central Statistical Office (2004), *Statistical Bulletin* 12, Warsaw.

Cichocka, Elżbieta (2001), Reforma na manowcach [The Reform Gone Astray] (interview with Aleksandra Wiktorow), *Gazeta Wyborcza*, 30 March.

Crombrugghe, Alain de (1995), *Budżet państwa – jego stabilizacja i trwałość [The Polish Government Budget: Stabilization and Sustainability]*, Warsaw: CASE and Wydwanictwo Naukowe PWN.

Czepulis-Rutkowska, Zofia (1997), Analiza obecnego systemu [The Analysis of the Present System], in: Stanisława Golinowska (ed.), Reforma systemu emerytalno-rentowego [Reform of the Pension System], *CASE Reports* 6, Warsaw.

Dąbrowski, Janusz M.; Federowicz, Michał; Levitas, Anthony (1991), Polish State Enterprises and the Properties of Performance: Stabilization, Privatization, Marketization, *Politics and Society* 19, No. 4.

Dąbrowski, Marek (1995), Short History of Economic Transition in Poland, in: Andrzej S. Bratkowski (ed.), Fiscal Policy in Poland under Transition, *Studies and Analyses* 49, Warsaw: CASE.

Dąbrowski, Marek (2003), Currency Crises in Emerging-market Economies: An Overview, in Marek Dąbrowski (ed.), *Currency Crises in Emerging Markets*, Dordrecht: Kluwer Academic Publishers.

Dobrowolski, Paweł; Kurek, Piotr; Rymaszewski, Piotr (2004), Reformy procesu stanowienia prawa [Reforms of the Legislative Process], *Zeszyty BRE-CASE 72*, Warsaw: CASE.

EBRD (2001), *Transition Report 2001: Energy in Transition*, London.

EBRD (2002), *Transition Report 2002*, London.

EBRD (2003), *Transition Report 2003: Integration and Regional Cooperation*, London.

Fischer, Stanley (1989), The Economics of the Government Budget Constraint, *World Bank Policy, Planning and Research Working Papers*, May.

Frydman, Roman; Rapaczynski, Andrzej (1994), *Privatization in Eastern Europe: Is the State Withering Away?* London: Central University Press.

Gach, Zbigniew (1993), *Leszek Balcerowicz: Wytrwać [Leszek Balcerowicz: To Endure]*, Warsaw: Oficyna Wydawnicza Interim.

Gadomski, Witold (2000), Rezygnuję [I Resign] (interview with Witold Skrok), *Gazeta Wyborcza*, 7 July.

Gardawski, Juliusz (2003), Difficulties with Restructuring of the Polish Mining Industry, *EIROnline*, http://www.eiro.eurofound.eu.int/2003/09/feature/pl0309101f.html.

Gilejko, Leszek (ed.) (1995), *Partycypacja i akcjonariat pracowniczy w Polsce [Employee Participation and Employee Ownership in Poland]*, Warsaw: ISP PAN, SGH.

Golinowska, Stanisława. (1997), Cele reformy systemu emerytalno-rentowego [The Aims of the Reform of the Pension System], in: Stanisława Golinowska (ed.), Reforma systemu emerytalno-rentowego [Reform of the Pension System], *CASE Reports* 6, Warsaw.

Golinowska, Stanisława (ed.) (1998), O reformie emerytalno-rentowej w kategoriach ekonomii politycznej [The Pension Reform in Terms of Political Economy], in: Jerzy Hausner and Stanisława Golinowska, Ekonomia polityczna reformy emerytalnej [The Political Economy of the Pension Reform], *CASE Reports* 16, Warsaw.

Golinowska, Stanisława; Kurowski, Piotr (eds.) (2000), Rational Pension Supervision, *CASE Reports* 36, Warsaw.

Gomułka, Stanisław (1993), The Financial Situation of Polish Enterprises 1992-1993 and Its Impact on Monetary and Fiscal Policies, *Studies and Analyses* 6, Warsaw: CASE.

Gomułka, Stanisław (1995), The IMF-Supported Programs of Poland and Russia, 1990-1994: Principles, Errors and Results, *Studies and Analyses* 36, Warsaw: CASE.

Górski, Artur (2001-2002), *Civil servants* czy *politicus servants* – w okresie międzywojennym i obecnie [*Civil Servants* or *Politicus Servants* in the Interwar Period and Now), *Służba Cywilna* 3, Fall-Winter, pp. 70-97.

Grabowska, Mirosława; Szawiel Tadeusz (2001), *Budowanie demokracji. Podziały społeczne, partie polityczne i społeczeństwo obywatelskie w postkomunistycznej Polsce [Constructing democracy: social divisions, political parties and civil society in postcommunist Poland]*, Warsaw: PWN.

Gray, Cheryl W.; Holle, Arnold (1996), Bank-led Restructuring in Poland: An Empirical Look at the Bank Conciliation Process, *Policy Research Working Paper 1650*, World Bank.

Greskovits, Bela (1998), *The Political Economy of Protest and Patience*, Budapest: Central European University Press.

Grosse, Tomasz Grzegorz (2001), Służba cywilna w Polsce i możliwości jej rozwoju [The Civil Service in Poland and the Possibilities of Its Development], *Służba Cywilna* 2, Spring-Summer, pp. 79-113.

Hausner, Jerzy (1995), Imperative vs. Interactive Strategy of Systematic Change in Central and Eastern Europe, *Review of International Political Economy*, 2:2, pp. 249-266.

Hausner, Jerzy (1995a), Modele systemu reprezentacji interesów w społeczeństwach postsocjalistycznych [Models of Interest Representation in Post-Socialist Societies], in: Jerzy Hausner (ed.), Narodziny demokratycznych instytucji [The Beginnings of Democratic Institutions], *Studia nad Reprezentacją Interesów [Studies on the Representation of Interests]* 3, Krakow: Akademia Ekonomiczna and Fundacja Polska Praca.

Hausner, Jerzy (1998), Reformowanie systemu emerytalnego według programu "Bezpieczeństwo dzięki różnorodności" [Reforming the Pension System According to the "Security Through Diversity" Program], in: Jerzy Hausner and Stanisława Golinowska, Ekonomia polityczna reformy emerytalnej [The Political Economy of the Pension Reform], *CASE Reports* 16, Warsaw.

Hayek, Friedrich A. (1945), The Use of Knowledge in Society, *American Economic Review* XXV, 4.

Hellman, Joel S. (1998), Winners Take All: The Politics of Partial Reform in Postcommunist Transition, *World Politics*, 50.2.

Hoff, Karla (2000), *The Logic of Political Constraints and Reform with Applications to Strategies for Privatization*, preliminary draft, World Bank, 4 December.

Instytut Wymiaru Sprawiedliwości (1998), *Założenia zmian w ustawie z dnia 20 czerwca 1985 r. Prawo o ustroju sądów powszechnych [Directions of Changes in the Law on Common Courts of June 20, 1983]*, Warsaw: Instytut Wymiaru Sprawiedliwości, mimeo.

Instytut Wymiaru Sprawiedliwości (2001), *Informacja o stanie sądownictwa powszechnego w 2000 r. [Information on the situation of the common court system]*, Warsaw: Instytut Wymiaru Sprawiedliwości, mimeo.

Jankowski, Michał; Siemaszko, Andrzej (1999), *Administration of Justice in Poland*, Warsaw: Oficyna Naukowa.

Janos, Andrew C. (2000), *East Central Europe in the Modern World: The Politics of the Borderlands from Pre- to Postcommunism*, Stanford.

Jarosz, Maria (2001), Rady nadzorcze w kleszczach interesów partyjnych i grupowych [Supervisory Boards in the Grip of Party and Group Interests], in: Maria Jarosz (ed.), *Manowce polskiej prywatyzacji [Polish Privatization – Where Did It Go Astray?]*, Warsaw: PWN, ISP PAN.

Jarosz, Maria; Kozarzewski, Piotr (2002), *Sukcesy i klęski prywatyzacji w krajach postkomunistycznych [Successes and Failures of Privatization in Post-Communist Countries]*, Warsaw: ISP PAN.

Jędrzejewska, Katarzyna (2000), Rząd musi szukać oszczędności [The Government Must Look for Savings], *Rzeczpospolita* 23, November.

Kochanowicz, Jacek (1994), Reforming Weak States and Deficient Bureaucracies, in: Joan Nelson and contributors (ed.), *Intricate Links: Democratization and Market Reforms in Latin America and Eastern Europe*, New Brunswick and Oxford: Transaction Publishers.

Kochanowicz, Jacek (2004), Trust and Social Capital in Poland: A Historical Perspective, in: Ivana Marková (ed.), *Trust and Democratic Transition in Post-Communist Europe*, Oxford University Press/The British Academy.

Kolarska-Bobińska, Lena (ed.) (1999), *Druga fala polskich reform [The Second Wave of Polish Reforms]*, Warsaw: Instytut Spraw Publicznych.

Kołodko, Grzegorz; Nuti, D. Mario (1997), *The Polish Alternative: Old Myths, Hard Facts and New Strategies in the Successful Transformation of the Polish Economy*, Helsinki: UNU World Institute for Development Economics Research.

Kornai, Janos (1995), Transformational Recession: A General Phenomenon Examined through the Example of Hungary's Development, in: Janos Kornai, *Highways and Byways: Studies on Reform and Postcommunist Transition*, Cambridge: MIT Press.

Kozarzewski, Piotr (1999), *Elity kierownicze spółek pracowniczych: własność – zarządzanie – świadomość [Elites of Employee-owned Companies: Ownership – Management – Mentality]*, Warsaw: ISP PAN.

Kozarzewski, Piotr (2002), Changes in Corporate Governance Structures in Polish Privatised Companies, *Working Papers* 8, London: SSEES UCL.

Kozarzewski, Piotr (2003), Corporate Governance and Secondary Privatisation in Poland: Legal Framework and Changes in Ownership Structure, *Studies and Analyses* 263, Warsaw: CASE.

Kozarzewski, Piotr (2003a), Nadzór właścicielski, kontrola i zarządzanie [Ownership Supervision, Control and Management], in: Maria Jarosz (ed.), *Pułapki prywatyzacji [Privatization Traps]*, Warsaw: ISP PAN.

Kozarzewski, Piotr; Woodward, Richard (2003): Poland I: Ownership and Performance of Firms Privatised by Management-Employee Buyouts, in: Barbara Błaszczyk, Iraj Hoshi, Richard Woodward (ed.), *Secondary Privatisation Transition Economies: The Evolution of Enterprise Ownership in the Czech Republic, Poland and Slovenia*, Hampshire and New York: Palgrave Macmillan.

Kubuj, Katarzyna (1999), Reformowanie sądownictwa i prokuratury [Reforming the Courts and the Prosecution Service], in: Lena Kolarska-Bobińska (ed.), *Druga fala polskich reform [The Second Wave of Polish Reforms]*, Warsaw: Instytut Spraw Publicznych.

Kuroń, Jacek; Żakowski, Jacek (1997), *Siedmiolatka, czyli kto ukradł Polskę? [Seven Yeas, or Who Stole Poland?]*, Wroclaw: Wydawnictwo Dolnośląskie.

Łagowski, Bronisław (2004), Naród bezpaństwowy i apolityczny [Stateless and Apolitical Nation], *Europa*, 5 May.

Linz, Juan L., Alfred Stepan (1996), *Problems of Democratic Transition and Consolidation: Southern Europe, South America, and Post-Communist Europe*, Baltimore and London: The Johns Hopkins University Press.

Lora, Eduardo; Panizza, Ugo; Quispe-Agnoli, Myriam (2003), Reform Fatigue: Symptoms, Reasons, Implications, paper for a conference Rethinking Structural Reform in Latin America, sponsored by The Federal Reserve Bank of Atlanta and the Inter-American Development Bank, Atlanta, G.A., October.

Mackiewicz, Anna (2000), Odyseja 2001 [Odyssey 2001] (interview with Stanisław Gomułka), *Gazeta Wyborcza*, 7 July.

Mączak, Antoni (1994), *Klientela [Clientele]*, Warsaw: Semper.

Mączyńska, Elżbieta (ed.) (2001), *Restrukturyzacja przedsiębiorstw w procesie transformacji gospodarki polskiej [Enterprise Restructuring in the Course of Transformation of Polish Economy]*, Warsaw: INE PAN, Wydawnictwo DiG.

Ministry of the Treasury (2003), *Dynamika przekształceń własnościowych [Dynamics of Ownership Transformation]* 57, December.

Ministry of the Treasury (2004), *Privatization quarterly. January – December 2003*, Warsaw.

Mitra, Pradeep K.; Selowsky, Marcelo (2002), Lessons from Decade of Transition in Eastern Europe and the Former Soviet Union, *Finance & Development* XXXIX, 2 (June).

Montes-Negret, Fernando; Papi, Luca (1996), The Polish Experience in Bank and Enterprise Restructuring, *Policy Research Working Paper* 1705, World Bank.

Murrell, Peter; Wang, Yijiang (1993), When Privatization Should Be Delayed: The Effect of Communist Legacies on Organizational and Institutional Reforms, *Journal of Comparative Economics* 17.

Naím, Moisés (1994), Latin America's Journey to the Market: From Macroeconomic Shocks to Institutional Therapy, Paper prepared for the Ninth Plenary Meeting of the Inter-American Dialogue, Wye, M.D., April, mimeo.

Nawrot, Wioletta (2003), Postęp prywatyzacji w Polsce i potencjalny zasób "prywatyzacyjny" [Progress of Privatization in Poland and Potential Privatization Resources], Warszawa: CASE, mimeo.

Nelson, Joan (1998), The Politics of Pension and Health Care Delivery Reforms in Hungary and Poland, *Discussion Paper* 52, Budapest: Collegium Budapest.

Nunberg, Barbara (1992), Making the Civil Service: What LDCs Can Learn from Developed Country Reforms, *Policy Research Working Paper* 945, Country Economics Department, The World Bank, August.

Nunberg, Barbara; Barbone, Luca (1994), Transforming the State: Issues in Public Administration Reform in Poland, in: Shahid Amjad Chaudhry, Gary James Reid, and Waleed Haider Malik (eds.), *Civil Service Reform in Latin America and the Caribbean*, Washington, D.C.: World Bank.

Nunberg, Barbara; Nellis, John (1990), Civil Service Reform and the World Bank, *Policy, Research and External Affairs Working Paper* 442, Country Economics Department, The World Bank, April.

OECD (1999), *OECD Principles of Corporate Governance*, Paris: OECD Publications.

Office of the Council of Ministers (1995), Służba Cywilna w wybranych krajach Europy [The Civil Service in Selected European Countries], conference proceedings, Warsaw: Office of the Council of Ministers, mimeo.

Olson, Mancur (1971), *The Logic of Collective Action: Public Goods and the Theory of Groups*, Cambridge, M.A.: Harvard University Press.

Olson, Mancur (1984), *The Rise and Decline of Nations: Economic Growth, Stagflation, and Social Rigidities,* New Haven, C.T.: Yale University Press.

Olson, Mancur (2000), *Power and Prosperity: Outgrowing Communist and Capitalist Dictatorships*, New York: Basic Books.

Osiatyński, Wiktor (2003a), Interview by Jacek Kochanowicz, November 19.

Osiatyński, Wiktor (2003b), *O zbrodniach i karach [On Crimes and Punishments],* Poznań: Media Rodzina.

Piętka, Katarzyna; Antczak, Rafał (2001), *Stabilisation Programs in Poland, 1990-1995: The Role of IMF Programs*, Warsaw: CASE.

Pinto, Brian; van Wijnbergen, Sweder (1995), Ownership and Corporate Control in Poland: Why State Firms Defied the Odds, *CEPR Discussion Paper* 1273, December.

Polanyi, Karl (1957), *The Great Transformation: Economic and Political Origins of Our Time,* Boston: Beacon Press.

Rydlewski, Grzegorz (2001), *Służba cywilna w Polsce [The Civil Service in Poland],* Warsaw: Scholar.

Rządowe Centrum Studiów Strategicznych [The Government Center for Strategic Studies] (2002), *Transformacja społeczno-gospodarcza w Polsce [The Social and Economic Transformation in Poland],* Warsaw.

Siemaszko, Andrzej (1998), *Dostęp do sądu a przewlekłość postępowania [Access to Courts and the Protractedness of Trials],* Warsaw: Instytut Wymiaru Sprawiedliwości, mimeo.

Siemaszko, Andrzej (1999), Interview by Ewa Siedlecka, *Gazeta Wyborcza,* June 19-20.

Siemaszko, Andrzej (2002), Interview by Jarosław Kurski, *Gazeta Wyborcza,* July 9.

Siemaszko, Andrzej (2002a), *Kogo biją, komu kradną. Przestępczość nie rejestrowana w Polsce i na świecie [Who Is Beaten, Who Is Robbed. Unreported Crime in Poland and in the World]*, Warsaw, Oficyna Naukowa.

Siemaszko, Andrzej (2003), Interview by Jacek Kochanowicz, November 1.

Siemaszko, Andrzej (n.d.), *Quo vadis iustitia? Stan i perspektywy wymiaru sprawiedliwości w Polsce [Quo Vadis Iustitia? The Current State and Development Prospects of the Administration of Justice in Poland],* Warsaw: Instytut Wymiaru Sprawiedliwości, mimeo.

Stasik, Dariusz (1999a), Małe czerwone światełko [Little Red Light], *Gazeta Wyborcza*, 16 March.

Stasik, Dariusz (1999b), Budżet z sufitu? [Budget Out of Thin Air?] (and commentary by Andrzej S. Bratkowski), *Gazeta Wyborcza*, 20 September.

Stasik, Dariusz (2000), Miliardy z kapelusza [Billions Out of a Hat], *Gazeta Wyborcza*, 6 July.

Stasik, Dariusz (2001), Groźne 73 proc. [Dangerous 73%], *Gazeta Wyborcza*, 19 April.

Stec, Andrzej (2003), Obligacje dla emerytów [Bonds for Pensioners], *Gazeta Wyborcza*, 9 July.

Stiglitz, Joseph (1987), Learning to Learn, Localized Learning and Technological Progress, in Dasgupta and Stoneman (eds.), *Economic Policy and Technological Performance*, Cambridge University Press, pp. 125-153.

Stiglitz, Joseph (1999), Scan Globally, Reinvent Locally: Knowledge Infrastructure and the Localization of Knowledge, Keynote address, First Global Development Network Conference, Bonn, Germany, December.

Szumlicz, Tadeusz (1999), Reforma zabezpieczenia emerytalno-rentowego [Reform of the Pension System], in: Lena Kolarska-Bobińska (ed.), *Druga fala polskich reform [The Second Wave of Polish Reforms]*, Warsaw: Instytut Spraw Publicznych.

Tamowicz, Piotr; Dzierżanowski, Maciej (2002), *Biała księga nadzoru korporacyjnego [The White Book on Corporate Governance]*, Gdańsk: IBnGR.

Tarkowski, Jacek (1994), Patroni i klienci [Patrons and Clients], in: Jacek Tarkowski, *Socjologia świata polityki [Sociology of the Political World]*, Vol. 2, Warsaw: ISP PAN.

Topiński, Wojciech; Wiśniewski, Marian (1995), Prywatne programy emerytalne [Private Pension Programs], in: J. Fougerolles and S. Golinowska (eds.), Tworzenie prywatnych funduszy emerytalnych w Polsce [Creating Private Pension Funds in Poland], *Studia i Materiały IPiSS*, Warsaw: IPiSS.

Wasilewski, Jacek; Wnuk-Lipinski, Edmund (1995), Poland: Winding Road from the Communist to the Post-Solidarity Elite, *Theory and Society* 24, Kluwer Academic Publishers.

Wayne, Leslie (1989), A Doctor for Struggling Economies, *The New York Times*, 1 October.

Wellisz, Stanislaw (1994), *Wolny handel czy ochrona rynku krajowego? [Free Trade or Defense of a Domestic Market?]*, Warsaw: CASE and Wydawnictwo Naukowe PWN.

Włodarczyk, Cezary (1999), Reforma opieki zdrowotnej [Health Care Reform], in: Lena Kolarska-Bobińska (ed.), *Druga fala polskich reform [The Second wave of Polish reforms]*, Warsaw: Instytut Spraw Publicznych.

World Bank (1994), *Averting the Old Age Crisis*, Oxford: Oxford University Press.

World Bank (1997), *World Development Report 1997: The State in a Changing World*, Oxford: Oxford University Press.

World Bank (1999), *Korupcja w Polsce: Przegląd obszarów priorytetowych i propozycji przeciwdziałania zjawisku [Corruption in Poland: A Review of a Priority Areas and Proposals of Preventive Measures]*, Warsaw: World Bank, Warsaw Office, mimeo.

World Bank (2002), *World Development Report 2002: Building Institutions for Markets*. Oxford: Oxford University Press.

World Bank (2002a), *Transition. The First Ten Years. Analysis and Lessons for Eastern Europe and the Former Soviet Union*.

Zieliński, Adam; Zubik, Marek (eds.) (2002), *Przyszłość polskiego wymiaru sprawiedliwości [The Future of the Administration of Justice in Poland]*, Warsaw: Instytut Spraw Publicznych.

Zubik, Marek (ed.) (2001), *Niedostatki wymiaru sprawiedliwości [Shortcomings of the Administration of Justice in Poland]*, Warsaw: Instytut Spraw Publicznych.

List of interviews

Bratkowski, Andrzej. Interview with Andrzej Bratkowski, leader of macroeconomic advisory team for economic strategy in the Ministry of Finance, 1991, and Vice President of the Polish National Bank, 2001-2004, by Piotr Kozarzewski and Richard Woodward, 12 September, 2003.

Bukowski, Jacek. Interview with Jacek Bukowski, director of department of privatization of small and medium-sized enterprises, Ministry of Ownership Transformation, 1990-1996, by Piotr Kozarzewski and Richard Woodward, 8 July, 2004.

Gardawski, Juliusz. Interview with Juliusz Gardawski, Polish sociologist and industrial relations specialist, professor at the Warsaw School of Economics, by Piotr Kozarzewski and Richard Woodward, 16 July, 2004.

Hausner, Jerzy (2004). Interview with Jerzy Hausner, the Government Plenipotentiary for Pension Reform in 1997 and Deputy Prime Minister in 2003-2005, by Jacek Kochanowicz, Piotr Kozarzewski and Richard Woodward, October 7.

Koźmiński, Jerzy. Interview with Jerzy Koźmiński, director general and undersecretary of state in the office of the cabinet, 1989-1991, by Richard Woodward, 9 July, 2004.

Kloc, Kazimierz. Interview with Kazimierz Kloc, Polish specialist on industrial conflicts and professor at the Warsaw School of Economics, by Piotr Kozarzewski and Richard Woodward, 14 and 22 October, 2003.

Kawalec, Stefan. Interview with Stefan Kawalec, deputy finance minister, 1989-1994, and director of strategy for the PZU insurance group since July 2003, by Piotr Kozarzewski and Richard Woodward, 16 September, 2003.

Lis, Krzysztof. Interview with Krzysztof Lis, the Government Plenipotentiary for Ownership Transformation, 1989-1990, by Piotr Kozarzewski and Richard Woodward, 17 October, 2003.

Osiatyński, Wiktor (2003a), Interview with Wiktor Osiatyński, constitutional expert, author of books and comments on legal reform and a member of Constitutional Commission in the early 1990s, by Jacek Kochanowicz, November 19.

Rychard, Andrzej. Interview with Andrzej Rychard, Polish sociologist, Institute of Philosophy and Sociology of the Polish Academy of Sciences, by Piotr Kozarzewski and Richard Woodward, 2 June, 2004.

Siemaszko, Andrzej (2003), Interview with Andrzej Siemaszko, author of books on criminal law and head of the Institute of the Administration of Justice, by Jacek Kochanowicz, November 1.

Wnuk-Lipiński, Edmund. Interview with Edmund Wnuk-Lipiński, Polish political scientist, Institute of Political Studies of the Polish Academy of Sciences, by Piotr Kozarzewski and Richard Woodward, 14 September, 2004.