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

Matías F. Travieso-Díaz

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

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

This paper seeks to address this question. To assist in the analysis, the paper provides a comparison of Cuba’s EOP with steps taken in the early stages of the privatization programs of some other countries that have undertaken, to some degree or another, the privatization of SOEs. Thus, the first part of the paper provides by way of background a summary of the actions that are generally required to prepare an SOE for its privatization. The second section describes the genesis, framework and current status of the EOP. The third section presents a summary of the actions taken by the governments of China and Eastern Germany in the early stages of their respective privatization programs. (Those countries were selected because they represent opposite poles in the range of potential approaches to SOE privatization.) The fourth section compares Cuba’s EOP with the methods adopted by the comparison countries in an effort to determine whether Cuba’s EOP is consistent with the processes utilized elsewhere in moving towards privatization. Finally, the fifth section offers the author’s conclusions as to whether the EOP is a meaningful step towards the implementation of a privatization program in the island.

1. The author gratefully acknowledges the assistance of Luis Marini, Charles P. Trumbull IV and Sima Chowdhury in the research and preparation of this paper.
3. The literal translation of “perfeccionamiento empresarial” is “enterprise perfecting.”
**STEPS IN PREPARING AN ENTERPRISE FOR PRIVATIZATION**

This section provides, as necessary background to the discussion that follows, a brief summary of the actions that are generally required to prepare an SOE for privatization. The discussion does not include addressing external conditions, such as outstanding judgments, liens or claims against the enterprise. Clearly, such “clouds on the title” of the State to the enterprise need to be removed before the SOE can be sold. In the case of Cuba, a factor that may complicate the prospects for privatization is the existence of a large number of claims by U.S. nationals, Cuban Americans, and Cubans living in the island for the expropriation of their assets after the Cuban Revolution. Cuba has failed to provide compensation to any of these groups, thus they all have outstanding claims against the State, and may seek restitution of the confiscated assets in lieu of compensation or other remedies. The outstanding expropriation claims will need to be addressed early in Cuba’s transition to a free-market society in order, not only to make possible the privatization of SOEs, but also to restore full relations with the United States, foster political stability, and encourage foreign investment. To the extent that any expropriation claims are resolved through restitution of the assets to their former owners, privatization of those properties will automatically occur.

A frequently used privatization technique is to sell the SOE as an ongoing concern. Frequently, however, SOEs are not salable on an “as is” basis, and a wide array of preparatory restructuring measures may be required to allow them to be privatized. These measures seek the transformation and reorganization of poorly performing SOEs into profitable, self-sufficient business concerns that may be attractive investments for the private sector. Specifically, the following preparatory actions are required in most cases:

- A feasibility study should be conducted to determine whether the enterprise can be sold as an ongoing concern or should be liquidated.

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

- The enterprise may also have to be restructured to make it more attractive to potential purchasers. First, if this has not been done, the enterprise should be transformed into a corporation, so that there is flexibility in the format of the subsequent sale, which may proceed through the sale of the enterprise’s assets or of its corporate stock.

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11. Id. at 43.
Other necessary structural changes may include refinancing or writing off debt, eliminating unprofitable lines of business, reducing the number of employees, hiring new managers, and disposing of assets and liabilities that make the enterprise more difficult to sell.12

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

CUBA’S ENTERPRISE OPTIMIZATION PROGRAM

Background

The management of SOEs in state-dominated economies, such as Cuba’s, suffers from a number of shortcomings that prevent the effective operation of the enterprises.14 Basically, SOEs are used by the government to further its social and political goals. The State’s lack of concern for their efficient operation renders the SOEs uneconomical and, in most cases, incapable of functioning without financial aid.15 As a result, SOEs became a burden on the State’s finances and may cause imbalances of the country’s economy.

In Cuba, the inefficiencies in the operation of SOEs were first addressed by the country’s armed forces (“FAR” or “Fuerzas Armadas Revolucionarias”) through a program initiated in 1987 to improve the operation of the numerous enterprises managed by the FAR.16 The FAR program progressed gradually from four firms in September 1987 to essentially all FAR-operated enterprises ten years later.17 However, the FAR enterprise upgrading remains incomplete after fourteen years.18

Cuba’s EOP, as instituted by Law 187, is an expansion to the entire SOE apparatus of the FAR EOP, which was judged to be a success by the country’s leadership. The Fifth Congress of the Cuban Communist Party adopted in October 1997 an Economic Resolution that praised the FAR experiment as “particularly relevant” to improving the performance of the Cuban economy and called for the “extension to other areas of the economy of the principles followed by the Armed Forces towards the perfecting of their enterprise system, to be carried out to the fullest extent, in an orderly and programmed manner, taking into account the characteristics of each activity.”20

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13. Private ownership of income-producing property in Cuba is limited to small plots of land in the hands of farmers, and the assets of joint ventures between state enterprises and foreign venturers. CONSTITUCIÓN DE LA REPÚBLICA DE CUBA (1992), published in Gaceta Oficial (August 1, 1992), art. 19-23.


16. The FAR operate a number of enterprises in several segments of the economy, including tourism. For example, Gaviota S.A., organized in 1990, owns resort hotel properties that at the end of 1998 accounted for 7% of Cuba’s hotel rooms and accommodated 10% of the visitors to the island. See http://www.gaviota.cubaweb.cu/espanol/index.html.

17. Jose A. Massip, Ernesto Hernández García and Boris Nerey Obregón, La Empresa Estatal Cubana y el Proceso de Perfeccionamiento Empresarial, CUBA SIGLO XXI (February 2001), available online at http://www.cubaxxi.f2s.com/economia/ (hereinafter “EMPRESA ESTATAL”).

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

19. Enterprises wholly owned by the State currently provide employment to over 70% of the Cuban workforce. VASCOs, supra.

suance of Law 187 followed, after “a broad process of consultation.”

Framework Created by Law 187

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

Another fundamental principle of Law 187, proclaimed in the General Bases, is that the SOEs should become economically self-sufficient. Since labor costs are a crucial component of enterprise operating expenses, a related principle is that the labor costs should be commensurate to the enterprises’ economic performance. To accomplish this, salaries are not to be fixed, but pegged to productivity. After-tax earnings may, if authorized, be retained by the enterprise as capital reserves.

Another principle, which is a corollary to the granting of administrative autonomy to the SOEs, is that each enterprise can propose and implement its own “tailor-made” approach for implementing its version of the EOP—subject to approval by several layers of bureaucracy.

Other fundamental principles are also set out in the General Bases.

Organizational Framework: As provided by Law 187, the main instruments in the implementation of the EOP are the Government Group and its Executive Secretary, both part of the Executive Committee of the Council of Ministers. Below the Government Group are overseeing organizations known as “Higher Organizations of Enterprise Direction” (Organizaciones Superiores de Dirección Empresarial) (“OSDEs”). The OSDEs are set up by the Ministry of

22. Law 187 is a very short (less than half a page) document, consisting of an introduction, two articles, one special provision, and two final provisions. Art. 1 approves the General Bases which are “an annex” to the law, but which are not included in the copy published in the Gaceta Oficial. (The General Bases are available online at http://www.nuevaempresa.cu/01_5.htm.) Art. 2 of the law authorizes the establishment, by the Executive Committee of the Council of Ministers, of a temporary Government Group headed by the Secretary of the Executive Committee of the Council of Ministers and comprised of five ministers and the head of the Central Bank. The Government Group, assisted by an Executive Secretary, is charged with the review of optimization proposals submitted by SOEs in accordance with the General Bases. The proposals are not to be submitted by the SOEs directly, but through the Organizaciones Superiores de Dirección Empresarial, described below.
24. See EMPRESA ESTATAL, supra.
25. “Enterprise optimization is based on enterprise self-financing, which requires that the enterprise its costs out of revenues and generate a profit.” General Bases, Section 1.1.
26. Id. The General Bases declare bluntly: “Rewards will be given to results, not efforts.”
27. General Bases, Section 1.1.
28. For example, the management of each enterprise is to have the authority to develop annual plans and budgets, and to manage the enterprise’s physical and financial assets, as well as the labor force. Id.
29. The discussion in this section is based on Sections 1.2 and 2 of the General Bases.
Finance for the purposes, among others, of coordinating the EOP efforts of the various enterprises in the same area of business, overseeing the preparation of each enterprise’s EOP, business plan and budget, and submitting and defending these documents before the enterprise’s governing board and before the Ministry responsible for the enterprise’s economic activity.30 Within each OSDE, there is a “governing board” consisting of five members chosen by the Executive Committee of the Council of Ministers. The board oversees each enterprise’s business plan and budget and the execution of the plan execution, and approves new lines of business.31 This structure is similar to those of the board of directors of a corporation in a capitalist country, except that under the Cuban program, the board’s sole shareholder—whose interests are represented by the board—is the State.

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

Stages in the EOP:33 The EOP is to be implemented in seven stages. First, the workforce and the labor unions must be trained to accept and support the process, and become active participants in it.34 This stage focuses on explaining to the workforce the general principles of the EOP and how they are accomplished, and securing through persuasion the workers’ active cooperation.

The second stage is to conduct an initial diagnostic analysis of the enterprise. This analysis is performed either by the SOE or “an external group,” depending on the condition of the enterprise. The analysis evaluates the enterprise’s history, its current status, its future prospects, and the state of its resources, its internal culture, and its technical and managerial functions. The main purpose of the analysis is to identify internal and external problems and determine in which respects the enterprise is not being efficient.35

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

The fourth step is to have each enterprise selected for participation in the EOP develop an optimization proposal (designated as “expediente de perfeccionamiento empresarial” or “EPE”). The EPE is in reality a detailed business plan that summarizes how the enterprise proposes to optimize its operations. The EPE

30. General Bases, Section 2.1.
31. Id., Section 3.1.2.
32. Id., Section 3.2.
33. These stages are described in Section 1.2 of the General Bases.
34. The possibility that increased enterprise efficiency will result in employee layoffs is addressed quite obliquely, as follows: “As workers become available, the most appropriate measures will be taken (in coordination with the organizations in the sector and the local labor oversight authorities) so that no worker is left unprotected.” General Bases, Section 1.2.4.1.
35. Id., Section 1.2.4.2.
36. Id., Section 1.2.4.3. The General Bases do not specify the consequences of a finding that an enterprise does not qualify for the EOP. Presumably, however, since the Cuban Government has placed great emphasis on the implementation of the EOP, those enterprises that are deemed unqualified to participate in the program may be candidates for eventual dissolution.
is required to address, among other subjects, the enterprise’s business objectives, its functions, its organizational structure, the proposed changes in the manner in which the production of goods and services is accomplished, and the methods to implement internal controls, planning, contracting, human resource management, marketing, and information systems. Each proposed change to the SOE is to be evaluated in terms of cost and anticipated economic results. The EPE is to set forth proposed economic performance objectives and compare them to the enterprise’s performance prior to implementation of the EOP. The EPE must also include an implementation schedule.

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

The sixth stage is the implementation of the EPE by the enterprise. The seventh stage is described as a continuous process of increased optimization, to be undertaken once the initial EPE objectives are accomplished.

**Functional Areas to be Addressed in the EOP**

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

- General Organization
- Management methods and styles
- Organization of the production of goods and services
- Organization and oversight of the work processes
- Quality assurance
- Labor and salary policies
- Planning
- Contracting
- Accounting
- Cost accounting
- Internal controls
- Taxes and internal finances
- Outside contracting
- Internal communications
- Prices
- Human relations
- Marketing

Each of these subsystems is addressed in a separate section of the General Bases. The level of discussion is, in most instances, non-specific: the General Bases only provide broad concepts without the accompanying performance standards. For example, Section 8.3 describes the “Valuation and Data Presentation Principles” applicable to enterprise accounting systems as follows:

The financial statements issued by an enterprise must be prepared using adequate and uniform techniques.

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

The accounting norms must be uniform, appropriate and explicit, with the objective of presenting information that is adequate, correct and timely. They must also be easy to interpret and useful to all their users.

37. *Id.*, Section 1.2.4.4.
38. *Id.*, Section 1.2.4.5.
39. *Id.*, Section 1.2.4.6.
40. *Id.*, Section 1.2.4.7.
The rest of the accounting section (Section 8) of the General Bases sets forth equally non-specific standards. Not all sections of the General Bases, however, are devoid of specific content. Some sections provide detailed insights into how the enterprise is expected to conduct its business. Of particular interest is the discussion of internal finances, which establishes provisions for the uses that can be made of enterprise profits. These uses include payment of taxes, establishment of reserves against contingencies, making capital contributions to the State, and establishing other types of authorized reserves (e.g., reserves for research and development). After these obligations have been funded, the remainder of the enterprise profits (if certified as such by outside accountants) can be treated as retained earnings and, if so decided by the management of the enterprise, distributed to the employees as “material incentives.”

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

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

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

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

As noted above, incentive payments may be provided to workers (based on retained earnings) up to 30% of their base salary; on the other hand, when the projected after tax profits are not met, salary reductions of up to 20% of the base salary may be assessed.

**Internal Controls:** Each enterprise must set up an internal controls program to protect the enterprises’s resources from “waste, fraud and inefficient use.” The internal controls are to include establishing procedures for the control of each enterprise activity, which must be “authorized, approved, carried out, and recorded.” Another required control mechanism is the functional separation between the accounting and operation functions and between assets and their accounting records. Also required are internal and external audits, with the external audits being conducted only by independent accounting firms approved by the State. Other internal control measures identified in the General Bases include, among others, (1) keeping cash in safes to which only the cash-
ier has access; (2) performing unscheduled audits of the cash at hand; (3) requiring petty cash vouchers to be countersigned by the requiring petty cash cashier and the cash recipient; (4) requiring daily deposit of sale proceeds; (5) requiring that different people authorize and issue checks, on the one hand, and reconcile bank statements; (6) keeping control of warehouse inventories and transfers of warehoused materials; (7) requiring that the person receiving goods at the warehouse be different from the one receiving the invoices for the goods; (8) requiring periodic inventories of 10% of the stored goods (a) maintaining controls over the issuance of tools and materials; (9) separating the functions of sale or delivery of goods from the invoicing and collection for such sales; (10) keeping control over the supply of blank invoices and requiring that such invoices be pre-numbered.

**Status of Enterprise Perfecting Program**

Currently, there are 1,004 SOEs (31% of all Cuban firms) undergoing the EOP. In 1998, over 1,400 SOEs were selected for transformation under the EOP; however, 400 had to abandon the process due to serious deficiencies in internal accounting. The majority of the firms chosen for upgrading are in key industries that Cuba hopes to develop. Nearly all nickel exploration companies, petroleum refineries, power companies, and many agriculture companies are candidates for reform. Although the government hopes to eventually reform all of Cuba’s 3,000 SOE, the firms in these fields are the most significant for Cuba’s economy.

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

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

In March 2001, Carlos Lage, Secretary of the Executive Committee of the Council of Ministers and Vice President of the Council of State, announced the cre-
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The first 26 OSDEs, an important step in the advancement of the EOP. As discussed earlier, the OSDEs, which are comprised of ministers, vice-ministers, and other high functionaries of the Cuban government, serve as a direct intermediaries between the SOEs and the Council of Ministers and are responsible for monitoring and assessing the progress of the various firms in the implementation of the EOP.\(^{53}\)

Despite claims that the EOP is moving too slowly, government officials claim to be satisfied with its progress. Armando Pérez Betancourt, executive secretary of the Government Group, claims that the process appears to move slowly because the Cuban population is anxious to see results. However, positive results cannot be expected to instantly materialize.\(^{54}\) Still, he points several to signs that the EOP is working:

- Government subsidies to failing SOEs have decreased. These subsidies placed a great strain on the Cuban budget. In 1994, for example, the government paid 5,750,000,000 pesos in subsidies to SOEs. In 2001, the government plans to reduce this amount to 300,000,000 pesos.\(^{55}\)

- Enterprises that have already implemented the EPEs are growing at a quicker rate than the overall economy. Last year, SOEs that implemented structural reforms reported a 9.5% increase in sales over 1999 levels.\(^{56}\)

- The petroleum industry, which was almost non-existent before the collapse of the USSR, has also made substantial economic improvements. In 2000, Cuban refineries produced a record high 3 million tons of petroleum, a 50% increase over the 1999 output.\(^{57}\)

Despite these signs of success, many people remain skeptical of the EOP, and in some SOEs the optimization process has been delayed by workers’ concerns over salaries and monetary incentives. Currently, a sixth of Cuba’s work force receives monetary rewards for increased production, which are awarded if the enterprise exceeds some production goal.\(^{58}\) As noted earlier, the EOP links individual salaries to individual output, not the output of the entire enterprise. This system is criticized as inequitable.\(^{59}\)

Workers also worry that they may be fired from their jobs, an inevitable step from the restructuring of inefficient SOEs. The first sixty-four SOEs to implement reforms laid off 2.5% of their workers.\(^{60}\) Cuban law guarantees these workers 60% of their income while they look for new jobs. However, implementation of the EOP is feared to ultimately lead to massive unemployment.\(^{61}\)

Another obstacle to the success of the EOP is the lack of accountability in Cuban corporations. Except for the few corporations that have entered the final stage of the EOP, Cuban businesses operate under “soft-budget constraints.” Since bankruptcy is not a threat, SOEs are not confined to their budgets as capitalist enterprises.

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54. TORTUGA, supra.
56. TORTUGA, supra.
59. SILBERMAN, supra.
60. CAMBIO, supra.
businesses are. The lack of business accountability and the poor accounting practices has made it extremely easy to embezzle money or commodities from one’s place of employment. In March of 2001, the Ministry of Prices and Finance declared that only 675 of over 3000 SOEs possessed adequate accounting measures.

In many cases, there is no incentive for managers and workers to reform the SOEs, since they can make more money by under-reporting earnings or stealing unaccounted-for products than they could earn from productivity bonuses. An independent Cuban economist states: “the lack of control in the management of public goods and the corruption constitute the gravest problems that society has faced over the past years. These phenomena not only produce immeasurable losses, but degrade society as a whole.”

Thus, the EOP appears to be facing, as its most serious challenge, changing the way that enterprises and their managers do business.

ENTERPRISE REFORM CASE STUDIES

Introduction

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

A rapid privatization program is one whose goal is to turn SOEs over to the private sector as quickly as practicable. Rapid privatization methods attract private investors and foster the re-emergence of a domestic enterprise sector. They are, therefore, the most appropriate methods for handling the transition from a state-controlled to a free-market economy. As discussed below, rapid privatization was the method used in East Germany after Germany was reunified in 1989.

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

The Chinese Experience

Initial SOE Reforms in China: China is a self-proclaimed socialist country that continues to retain its allegiance to a command economy. Yet, it has gradually become marketized, through a process that in-

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62. Interview with Oscar Espinosa Chepe, En Crítica Situación la Economía Cubana, BURÓ DE INFORMACION DE DERECHOS HUMANOS, October 24, 2000 (“CHEPE”).


64. See CAMBIO, supra.

65. See CHEPE, supra.


67. China has coupled the limited opening of SOEs to private ownership through the sale of enterprise stock to the public with a grant of increased operational autonomy to its SOEs. BARBARA LEE & JOHN NELLIS, ENTERPRISE REFORM AND PRIVATIZATION IN SOCIALIST ECONOMIES 7-9 (1990). As discussed earlier, the second half of that equation is analogous to an stated objective of the EOP in Cuba.
volved, among other things, a reform of the state enterprise system.68 The main objective of SOE reform was to provide incentives for enterprises and individuals to be more effective through profit retention, a dual-price system, and the contract responsibility system described below.69 All these measures were designed to reduce price distortion, increase SOE competitiveness, and reap the profit generated by free markets.70

To bring SOEs within the market’s orbit without relinquishing State ownership, China created a framework aimed at separating the government’s ownership of an enterprise from its management and administration.71 Reforms began in the rural areas, where people’s communes were disbanded and replaced by a “household responsibility system.”72 The land remained communally owned, but households were allowed to contract to cultivate the plots and were given incentives to increase productivity: the communes’ assets needed for production were sold to the households at low prices, and a type of contractual arrangement was instituted under which farmers organized by “household unit” contracted with the State to sell a set quantity of products at a government-set price, but any surplus above the established quota could be sold in the open market at open-market prices. This initial, limited reshaping of the SOE system led to improvements in the performance in the agricultural sector, especially in the production of grain.73

The Chinese government expanded in 1984 the agricultural sector reforms to other SOEs.74 The concept of “responsibility contracts” was made applicable to all SOEs and all levels of the production and distribution chain. Under the reformed system, SOEs enter into contracts with the State which set production targets for the enterprise to meet within a specified period of time.75 After the targeted performance goals are met, the enterprise is allowed to retain any excess profit for use as its management deems necessary, thus giving management limited rights over production, marketing, labor, procurement, investment, and asset disposition.76

Subsequently, in 1992, regulations were issued that expressly conferred upon an SOE a number of powers, including those to: (1) make decisions with respect to production and operation; (2) fix prices for

68. Lan Cao, Public Perspectives on Privatization: Chinese Privatization: Between Plan and Market, 63 LAW & CONTEMP. PROB. 13 (2000). (hereinafter "PERSPECTIVES"). Since the beginning of market reforms, however, Chinese officials have drawn a distinction between marketization (which they favor) and SOE privatization (which they oppose). As will be further discussed below, parallel with the institution of SOE reforms, the Chinese government has also allowed the development of a non-state sector side by side with the state sector. See Lan Cao, The Cat that Catches Mice: China's Challenge to the Dominant Privatization Model, 21 Brooklyn J. Int’l L. 97, 100 (1995) (hereinafter "CAT").
69. See id.
70. See id.
73. PERSPECTIVES, supra, at 29–30. Cuba copied the Chinese model when it instituted the Unidades Básicas de Producción Cooperativa (UBPCs) in 1993 and subsequently established the mercados agropecuarios, that is, agricultural markets in which agricultural products are sold by farmers to the public at free-market prices. See, e.g., Hans-Jurgen Burchadt, La Descentralización de las Granjas Estatales en Cuba: ¿Gérmen Para una Reforma Empresarial Pendiente?, in CUBA IN TRANSITION—VOLUME 10, PAPERS AND PROCEEDINGS OF THE TENTH ANNUAL MEETING OF THE ASSOCIATION FOR THE STUDY OF THE CUBAN ECONOMY 64 (Aug. 2000).
74. SUN, supra, at 20–21.
their products and services; (3) purchase materials; (4) import and export; (5) make investment decisions; (6) dispose of reserved funds; (7) dispose of assets; (8) form a joint venture, or merge, with another enterprise; (9) hire employees; (10) sell its products; (11) manage its personnel; (12) decide wages, salaries and bonuses; (13) set up internal offices; and (14) resist or reject resources offered by the State, including human, material and financial resources. Under the regulations, SOEs are expected “to become, under the law, units for commodity production and management with autonomy, sole responsibility for their own profits and losses, self-development and self-command, and to become legal persons competent to enjoy civil rights and to assume civil responsibilities independently.”

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

The “Modern Enterprise System”: Another solution was needed, and China instituted the “modern enterprise system” program in 1995 with the goal of “corporatization” of the SOEs. Selected SOEs were reorganized into corporate entities having ownership rights, property rights, and clearly defined managerial responsibilities. The government established two stock exchanges to promote the development and expansion of the enterprise transformation program. Only a small portion of the SOEs have participated in this program, and most of the enterprises participating are small or medium size SOEs. This is due to the government’s reluctance to introduce private ownership into large and super-large state-owned enterprises. Many small enterprises were left to fend for themselves, and either succeeded, sold out or merged.

The major features of the Chinese enterprise reform program included:

- Transforming the SOEs into corporations by a re-definition of their ownership.
- Allowing individuals to buy shares in the SOEs in the stock markets and become minority owners of the enterprises.
- Requiring the corporatized SOEs to set up boards of directors that represent all owners’ interests.

78. Id., Art. 2.
79. See CAT, supra, at 102.
80. Id. at 103.
81. See SUN, supra at 21.
83. See SUN, supra, at 28.
84. See id.
85. Of the 380,000 SOEs in China, only 1 ½ percent have become joint stock companies. They represent, however, six percent of the production and account for thirteen percent of the profits of the Chinese SOE system. Id. at 21, 28-29.
87. See SUN, supra, at 35.
88. See id.
• Establishing separate entities (supervisory boards) that supervise the management of each enterprise.

• Requiring that the supervisory boards include outside specialists in business management.

The expectation which underlay the initiation of the modern enterprise system was that it would help separate the government’s regulatory duties from the commercial functions of the SOEs.Experts have concluded, however, that the “modern enterprise system” has had only limited impact on improving the SOEs’ efficiency, and that there are still serious organizational problems in the SOEs from the standpoint of corporate governance.

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

There are also structural problems with the modern enterprise system in that there are functional overlaps between the general managers and the director of the board, and in the administrative appointment of SOE managers. Furthermore, three pre-reform committees, party committee, trade union, and the congress of workers representatives, co-exist with the three new ones, the shareholders congress, the board of directors, and the supervisory board. There seems to be a lack of clear definition of the responsibilities of these entities and the relationships among them causes internal conflicts and inefficiency in decision-making.

The implementation of the modern enterprise system has also not resulted in a change of the internal structure of the SOEs. According to the results of a study that examined the composition of the board of directors and the supervisory committee in the corporatized SOEs, members of the board and the supervisory committee in the corporatized SOEs, members of the board and the supervisory committee in the corporatized SOEs, members of the board and the supervisory committee in the corporatized SOEs, members of the board and the supervisory committee in the corporatized SOEs, members of the board and the supervisory committee in the corporatized SOEs, members of the board and the supervisory committee in the corporatized SOEs, members of the board and the supervisory committee in the corporatized SOEs, members of the board and the supervisory committee in the corporatized SOEs. This is true even though the law prohibits govern-
ment officials from remaining entrenched in company management.99

Despite these deficiencies, the results of China’s enterprise reform initiatives have been generally positive. Reported data reveals that the gross output value of state enterprises increased from 342.1 billion yuan in 1978 to 1.35 trillion yuan in 1988.100 The total factor of productivity in state-owned industries also increased during the 1980s at an annual average of 2.4%. After enterprise reform, joint-stock companies have demonstrated greater vitality and performed better in the market than traditional SOEs, even though they make up only 1.5% of all SOEs in China.101

**Flaws in the Chinese SOE Reform Model:** As just described, since the Chinese Government undertook to improve the SOE apparatus to make it more competitive with the alternative property modes being allowed to develop in the country, the SOEs that have been allowed to institute the “modern enterprise system” have exhibited operational improvements. However, the progress of SOEs towards optimization has been impeded by a number of constraints and problems, which are strongly reminiscent of those already reported in Cuba under the EOP:

- Lack of separation between enterprise ownership and management.102 This is at the same time ironic (because, like in Cuba, the fundamental tenet of SOE reform in China is to allow a greater degree of enterprise self-government) and predictable. As in Cuba, multiple layers of Chinese bureaucracy exist at the national, provincial, and local level, all with entrenched powers over the SOE, which they are unwilling to give up.103 The SOE management is powerless to raise objections to the government’s meddling in the internal affairs of the enterprise, since the State is both owner and regulator, and SOE managers who oppose government directives risk transfer or removal.104 The most effective way to accomplish this separation, and the one that is being now instituted to a limited extent in China (but not in Cuba) is the privatization of at least the small- and medium-sized SOEs.105

- Corruption, particularly among managers. As their powers increase, managers have more opportunity (which they often seize) to appropriate to themselves an increasing share of the corporate resources.106

- Enterprise asset stripping by managers acting in collusion with workers.107

99. See SUN, supra, at 32.


101. See SUN, supra, at 28.

102. SUN, supra, at 38-39.

103. Id. at 40-43. The problem has been characterized as follows: “Various administrative agencies at both the national and local levels invested in an enterprise vie to exercise control over it, thereby subjecting the enterprise to overlapping and often conflicting vertical – usually one of the industrial administrative bodies attached to a central ministry – as well as horizontal – usually the local people’s government or their agencies – lines of authority.” PERSPECTIVES, supra, at 37.

104. SUN, supra, at 39-40.

105. Privatization is not always feasible, however, because many Chinese SOEs are unsalable, either because of their poor financial condition or because there are few Chinese nationals who can afford to buy them. With respect to SOEs engaged in important industries, such as transportation, telecommunications, and national defense, it would be politically unacceptable to sell to foreign nationals. Id. at 43.

106. Id. at 44-45. Potential ways to address the corruption problem include external auditing, formal control systems, budget restrictions, the establishment of suitable incentive compensation systems, and reforming the State employment system so that managers have a real risk of unemployment if the enterprise is not successful. Id. at 45-46.

107. PERSPECTIVES, supra, at 42.
- Misuse of public resources through the purchase of commodities at lower, official prices and subsequent resale at a higher price on the non-state market.  
- Informational uncertainties, unreliable accounting, and inconsistent financial data.  
- Arbitrary and excessive taxation.  
- Overproduction and reckless investment in plant capacity.  
- Asset inflation due to measures by managers to show profits, whether true or not. Such measures include unwillingness to recognize bad debts, inflation of receivables and credits, and underestimation of depreciation and costs.  
- Siphoning of public resources towards weaker SOEs through improvident loans by state banks and state infusions of cash to stem potential layoffs by failing enterprises.

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

... Within the [SOE] itself, governmental decentralization, the downward transfer of rights, and the separation of the firm from the state have resulted in more autonomy for managers as intended, but they also set in motion a web of causally linked and distorted incentives that are difficult to rectify because of the absence of internal and external controls.

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

The East German Model

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

The transformation to a private property system was initiated by the GDR’s enactment of the Treuhandgesetz (Trust Law). The law created the Treuhand which instantly became the largest holding

108. Id.  
109. Id. at 37.  
110. Id. at 38.  
111. Id. at 41.  
112. Id. at 41.  
113. Id. at 42.  
114. Id. at 42-43.  
115. Privatization of small SOEs is no longer a problem. Government regulations issued jointly in 1998 by the State Commission of Economy and Trade, the Treasury Department, and the Central Bank establish guidelines for the sale and purchase of small SOEs. Such sales are well under way in China, although the process is not officially acknowledged as privatization. SUN, supra, at 35.  
116. Id. at 36.  
119. TRUST LAW, v. 22.6.1990 (GBL. I at S.300).
company in the world with control over 12,370 businesses.\textsuperscript{120} The first words of the Trust Law declared emphatically that privatization was to occur “as quickly and as comprehensively as possible.”\textsuperscript{121}

The Treuhand, in turn, became the owner of all of the shares of these companies and was responsible for preparing them for sale to the private sector.\textsuperscript{122} The Treuhand was required by law to evaluate the economic positions of these companies; it determined which enterprises were competitive enough to be privatized, which should be dismantled, and which should be liquidated.\textsuperscript{123} In all companies with over 500 employees the Treuhand established advisory boards. These boards, consisting mainly of representatives from West Germany’s government, businesses, and banks were responsible for drawing up plans to restructure the corporation, contract short term managers, and make other necessary changes.\textsuperscript{124}

The sale of the companies was the most important part of the privatization process. Before the Treuhand could sell interests in the formerly state-owned enterprises, it first needed reliable valuations of them.\textsuperscript{125} The Financial Statement Law required enterprises considered for privatization to prepare financial statements using D-Mark valuations.\textsuperscript{126} If the prospects for survival were questionable, the Treuhand decided against privatization and liquidated the company.\textsuperscript{127} If, however, the company’s prospects for survival were promising, the Treuhand would fund the company up to the amount of its debt.\textsuperscript{128} The company would then be made ready for direct sale into the private sector.

The strategy of rapid privatization was grounded on the assumption that the costs of rehabilitation faced by private investors would be considerably lower than those of the Treuhand.\textsuperscript{129} Aside from the transfer of economic and technical knowledge and the mobilization of private capital, what the Treuhand expected from a rapid privatization was above all the chance for East German enterprises to overcome barriers to market entry.\textsuperscript{130} The survival of East German firms could be ensured only by making them competitive, which could be accomplished only by investing substantial sums into their rehabilitation.\textsuperscript{131} The Treuhand for the most part decided against financing rehabilitation itself, opting instead for a “privatization of rehabilitation.”\textsuperscript{132}

Many East German companies, however, were unattractive to private investors. Although the Deutschemark was valued 1:4 to the Ostmark, the two currencies were officially united at a 1:1 ratio. Subsequently, eastern Germany’s labor force became grossly overpaid, and capital stock devalued by

\textsuperscript{120} The Treuhand was created by the GDR prior to reunification and was integrated into the government of the Federal Republic in the Treaty on Unification, where it became a federal agency overseen by the minister of finance. Unification Treaty art. 25, v. 28.9.1990 (BGBl. II at S.897), 30 I.L.M. at 481.
\textsuperscript{121} TRUST LAW, v. 22.6.1990 (GBl. I at S.300).
\textsuperscript{122} See id.
\textsuperscript{123} See id.
\textsuperscript{124} The Economist, “Is Germany’s Treuhand a good thing?” March 21, 1992
\textsuperscript{125} See COLONIZATION, supra
\textsuperscript{126} See Besondere Bestimmungen fumur Fortgeltendes Recht der Deutschen Demokratischen Republik, ch. III, 1(2), v. 28.9.1990 (BGBl. II S.1173) [hereinafter “Financial Statement Law”].
\textsuperscript{127} Id.
\textsuperscript{129} Herbert Brucker, PRIVATIZATION IN EASTERN GERMANY, Frank Cass (1997).
\textsuperscript{130} See id.
\textsuperscript{131} See id.
\textsuperscript{132} See id.
50%. These factors, combined with the poor state of east German companies and resources, discouraged many investors.

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

Other than initial evaluations and limited restructuring in larger companies, the Treuhand did little to prepare former SOEs for privatization. Many critics claim that the Treuhand should have restructured these companies and sold them at competitive prices and at a time when the economy was stronger. Instead, after four years the Treuhand incurred a DM270 billion debt which must be financed by the German state. The desire to quickly dump these companies on the world market led the Treuhand to sell them at only 10% of what they had formerly expected to raise.

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

The effect of eastern Germany’s rapid privatization has had mixed effects on the economy. Unemployment initially skyrocketed as managers downsized the overpaid workforce that was draining capital reserves. About half of the workers in the former GDR lost their job and 600,000 migrated to western Germany. Nevertheless, eastern Germany’s economy grew about 9% in 1994. GDP, per capita income, and productivity have all increased relative to western Germany. Still, unemployment remains a problem in eastern Germany. This is due to the Treuhand’s efforts to provide “equal pay for equal work” in the former GDR and West Germany. Companies agreed to boost wages 11-fold by 1996, rendering many companies inefficient and struggling to compete.

Although Germany’s method of privatization has had mostly desirable effects, it may not be a suitable model for other countries to follow. The GDR had the advantage of unification with an economic superpower that could finance the debt incurred by the privatization of inefficient companies. Furthermore, unification with Germany provided the economic and political stability needed to attract foreign investment. Finally, the well educated east German work force, and a strong service sector offered insurance that the privatization process would eventually be profitable, even if it would suffer in the short run.

133. See COIN
134. The Economist, “Privatisation; farewell, sweet Treuhand,” December 24, 1994 (Hereafter, PRIVATIZATION)
135. See PRIVATIZATION.
136. The Economist, “East German privatisation: Fast and loose,” April 30, 1994 (Hereafter FAST)
137. See PRIVATIZATION.
138. See Id.
140. See Id.
141. Lucjan Orlowski, “Present Stages of Economic Reforms and Privatization Programs in Eastern Europe,” University of Notre Dame April 1991
Thus, East Germany’s transition cannot be evaluated or applied to other scenarios without carefully considering the surrounding factors.

**IS CUBA’S PERFECCIONAMIENTO EMPRESARIAL LAW A STEP TOWARDS PRIVATIZATION?**

**Actions Contemplated in the EOP That Would Aid in the Preparation of Cuban SOEs for Eventual Sale**

As noted above, a first step in privatization is a thorough examination of the SOE’s finances and operations. Cuba’s EOP program ostensibly accomplishes step through the performance of the initial diagnostic analysis of the enterprise. To the extent a thorough evaluation is performed, it will be a valuable first step towards a possible privatization.\(^\text{142}\) If the assessment is based on proper accounting methods and if it provides an adequate disclosure of the company’s finances, the program will give potential investors a good sense of how much an enterprise is worth. In addition, if the valuation is performed competently, it will serve (as was the case in East Germany) as a triage tool to allow the State to determine which enterprises can be sold and which need to be liquidated.\(^\text{143}\)

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

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

**Comparative Outlook Based on Reference Countries’ Experience**

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

With the adoption of the modern enterprise system, China went a step further as it sought to achieve structural reforms within its SOEs. The specific strategies of the program are very similar to those in Cuba’s EOP. Both countries have sought to establish in-

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\(^{142}\) Depending on how far into the future the actual privatization takes place, this evaluation may need to be updated or repeated, but the initial exercise should provide a good starting point in any instance.

\(^{143}\) Although Cuba has yet to take steps to liquidate unprofitable enterprises, the initial selection of SOEs to be included in the EOP, and the subsequent culling of some enterprises based on the results of the valuation, suggests that Cuba has already indirectly made the cut as to what SOEs will be supported towards possible solvency and which will be eliminated by some method or another.
dependent management structures through the establishment of boards of directors, and have tried to make their SOEs closer in operational freedom to Western business organizations. However, while Chinese corporate law nominally seeks to extricate the State from the day-to-day business of the SOEs, the actual composition of boards and key offices is still directed and peopled by government actors. Cuba’s EOP does not even make such an attempt, since the program specifically requires that the majority of the members of outside governing boards be State officials. It also subjects enterprise management to the authority of both the OSDEs and the Cabinet-level Government Group. In this sense, Cuba has made even less progress in removing the State’s control over the enterprise than the Chinese approach. Perhaps China’s more liberalized system reflects its acknowledgment of past failures with enterprise reform, an experience likely to be repeated in Cuba.

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

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

**CONCLUSIONS**

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

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

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144. See CAT, supra, at 104.