CORPORATE GOVERNANCE IN PUBLIC INSTITUTIONS: A CASE STUDY ON THE REPUBLIC OF SLOVENIA

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Abstract

In the analysis, the author summarises the relationships between the founder of a public institution (i.e. the state or a municipality) and the public institution's bodies (i.e. the council of the institution, the director, and the expert council thereof) and proposes certain necessary changes to the relevant legal regulation.

Keywords: public institution, public sector, corporate governance, corporations, foundations, assets of the institution.

Resumen

«Relaciones entre el gobierno de las corporaciones públicas: un caso de Eslovenia». En este artículo el autor resume las relaciones entre el fundador de una institución pública (p. ej., el Estado o el municipio) y los órganos de la misma (consejo de dirección, director o consejo de expertos) y propone ciertos cambios en la legislación aplicable que estima necesarios.

Palabras clave: sector público, corporaciones, fundaciones, gobierno corporativo.

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INTRODUCTION

The *thema probandi* of this paper is to demonstrate that public institutions in Slovenia are, from a legal point of view, *sui generis* limited liability corporations and have a *sui generis* structure of corporate governance.

In terms of positive law, pursuant to the applicable Institutes Act (hereinafter: the IA)[1], public institutions are organisations established to provide public services relating to education, science, culture, sports, healthcare, social assistance, childcare, the protection of persons with disabilities, social insurance, or other activities, if they do not aim to make a profit from their activities. In fact, pursuant to the IA[2] it is not necessary that public institutions are legal entities. They can lack a legal personality.

A legal personality is a legal attribute of public institutions that are legal entities. A legal personality entails that public institutions become capable of having legal rights and duties following a final decision that the public institution has been entered in the court register.[3] For the definition of its legal personality it is essential that a public institution is capable of having property rights and duties in legal transactions. The state acknowledges such position of the public institutions in its legal order so that a public institution is defined by law as a separate legal person. A public institution is an organisation having legal capacity and an independent legal person in legal transactions. In order to become a legal person (i.e. to acquire a legal personality) certain fundamental conditions[4] must be fulfilled, namely, the specific purpose for establishing a legal person must be demonstrated (i.e. the necessary provision of a non-commercial public service *ex lege* and without a concession); funds for the accomplishment of such purpose must be ensured; management (and other bodies) necessary for the accomplishment of such purpose must be appointed; and a legally admissible organisational form must be determined.[5] The legal personality of the public institution further entails that the public institution can own movable property and real estate (regardless of the fact that, as a general rule, it only manages real estate of the founder, i.e. the state or a municipality), that it can acquire property rights and undertake obligations, that it can sue and be sued, and that it is liable for its obligations with all its assets.[6] An institution is not liable to creditors with assets that the institution manages but does not own.

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[1] Articles 1 and 3 of the Institutes Act (Zakon o zavodih – ZZ), Official Gazette RS, Nos. 12/91, 8/96, 36/00 – ZPDZC, and 127/06 – ZJZP.

[2] Article 4 of the IA.

[3] See: Dictionary of Law, Ed. Julian Webb, Penguin Reference Library, Penguin Books, 2009, p. 309.

[4] Retrieved from http://www.eracunovodstvo.org/blog/podjetnisko-pravo/kdo-so-pravni-subjekti/ (21 April 2016).

[5] See: Trstenjak, V. (2003), pp. 49-53.

[6] See: Bohinc, R. and Tičar, B. (2006), p. 113.

The concept of *corporate governance* in institutions derives from the presumption that public institutions are corporations. However, strictly speaking, in accordance with Ancient-Roman and contemporary Germanic understanding, public institutions are not corporations. Based on the theoretical view presented by *V. Trstenjak* in her book *Legal Entities* (*Pravne osebe*),[7] a public institution is a fictitious structure that represents assets bound for a certain purpose (*universitas bonorum; i.e. a foundation*). A public institution is not a membership organisation (*universitas personarum*, i.e. *a corporation*),[8] as it does not have members. A public institution is established either by the state or a municipality and is intended for providing a non-commercial public service. In legal transactions it acts through its bodies, especially individual members of its management (e.g. a director, principle, chancellor). A public institution acquires legal and contractual capacity following a final decision that it has been entered in the court register.[9]

However, the understanding of the concept of the *corporation* can also be different. For example, in 1910 the American writer *A.W. Machen*[10] connected the theoretical understanding of the concept of the corporation and the limited liability of a legal person for obligations. Such understanding was not compatible with the Roman law and contemporary continental European understanding. In the American context, corporations are understood to be fictitious legal persons whose liability for the obligations of their founder or founders is limited. The connection between the concept of the corporation and limited liability for obligations was illustrated by *J. Dewey* in 1926, as he wrote about the historical background of the develop-

[7] See: Trstenjak, V. (2003), pp. 49-53.

[8] The reasoning of this paper is based on the division of legal entities into corporations and foundations, as was presented by *V. Trstenjak* in her book *Legal Entities* (*Pravne osebe*) (2003), and as was later summarised and expanded by the author and *R. Bohinc* in the book *Administrative Law – General Provisions* (*Upravno pravo – splošni del*) (2005). The outlined reasoning therein is re-systemised and upgraded in this paper so that forms of legal entities in terms of their organisation are determined and placed in an organisational scheme of territorial, functional, and associative administrative systems, as understood by *G. Trpin* in the book *Regulations in the State Administration, Government, and Ministries with Introductory Remarks* (*Predpisi o državni upravi, vladi in ministrstvih z uvodnimi pojasnili*) (1995) and subsequently summarised by *B. Brezovnik* and *B. Grafenauer* in the book *Public Administration* (*Javna uprava*) (2006). The author and *I. Rakar* partly elaborated the above-mentioned in the book *Public Sector Law* (*Pravo javnega sektorja*) (2011). The presentation in this paper is a continuation of the above-mentioned analyses. See: Trstenjak, V. (2003). *Pravne osebe*. 1st Edition, GV Založba, Ljubljana. Bohinc, R., Tičar, B. (2006). *Upravno pravo – splošni del*. Fakulteta za varnostne vede, Ljubljana. *Predpisi o državni upravi, vladi in ministrstvih z uvodnimi pojasnili Gorazda Trpina* (1995). Uradni list, Ljubljana. Grafenauer, B., Brezovnik, B. (2006). *Javna uprava*. Pravna fakulteta, Maribor. Tičar, B., Rakar, I. (2011). *Pravo javnega sektorja*. Inštitut za lokalno samoupravo in javna naročila, Maribor.

[9] Certain legal entities are not entered in the court register, e.g. the state, municipalities, and the Slovenian Academy of Sciences and Arts. They are granted a legal personality by operation of the Constitution (e.g. the state) or by operation of law (*ex lege*).

[10] See: Machen, A.W. (1910).

ment of the corporate legal personality.[11] In his view, historically, the concept of the legal personality of legal entities was developed in medieval, Catholic ecclesiastic law. The author of this idea was Pope Innocent IV (1195-1254).[12] He gave certain Italian monasteries a legal personality so that the assets of the monasteries were separated from the assets of the monks and the Church. This was done mostly so that other connected legal entities and natural persons would no longer be liable to the creditors of the monasteries for the obligations that the monasteries undertook. A monastery with a legal personality was named a *persona ficta* or a person without a soul (*a persona sine anima*). The reason for the introduction of the concept of a *fictitious person* was originally economic, as a *persona ficta* did not have a soul and therefore could not be guilty of a delict, while the church and monks naturally were not liable for the obligations of other persons.

Similarly, due to economic reasons, a contemporary corporation is an artificially created legal person, while its founders are not liable for the corporation's obligations.

In the usual context, corporations are first of all companies limited by shares. However, in the Republic of Slovenia also public institutions are similar to companies limited by shares as regards their liability for obligations. Regardless of the fact that public institutions do not have equity, the founder thereof (i.e. the state or a municipality) is, as a general rule, not liable for the obligations of the institution, which is also entered in the court register upon the registration thereof. A public institution is, naturally, always liable with all its assets, whereas the founder of the institution is not liable to its creditors. In such a context, a public institution is a *sui generis* non-membership corporation that is in fact similar to a company in terms of the type of liability. The anomaly of the system lies in the fact that minimum equity, which would to a certain extent protect creditors, is not prescribed when establishing a public institution. In addition, the rules of lifting the corporate veil in cases of abusing the public institution also do not apply, and there is no case law supporting the idea that such rules apply.[13]

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[11] See: Dewey, J. (1926), p. 657. "The doctrine has been attributed to Pope Innocent IV, who seems at least to have helped spread the idea of persona ficta as it is called in Latin. In the early church, the doctrine of persona ficta allowed monasteries to have a legal existence that was apart from the monks, simplifying the difficulty in balancing the need for such groups to have infrastructure though the monks took vows of personal poverty. Another effect of this was that as a fictional person, a monastery could not be held guilty of delict due to not having a soul, helping to protect the organization from non-contractual obligations to surrounding communities. This effectively moved such liability to individuals acting within the organization while protecting the structure itself, since individuals were considered to have a soul and therefore capable of being guilty of negligence and excommunicated."

[12] See: Dewey, J. (1926), pp. 655-673.

[13] Today, the concept of a legal entity is naturally not absolute. In the majority of legal systems, the corporate law institution of lifting the corporate veil in case of companies or corporations enables creditors to direct their claims directly at shareholders, if they abuse a legal entity for their own benefit. See: Machen, A.W. (1910), p. 253: "Piercing the corporate veil or lifting the corporate

2. THE HISTORICAL DEVELOPMENT OF PUBLIC INSTITUTIONS IN TERMS OF THEIR ORGANISATIONAL FORM

The term *public institution* (German: *öffentliche Anstalt*) first appeared in Austrian legal texts in the 18th century. In the Austrian general national law of 1794, the term is defined as: "[...] *necessary institutes for maintaining public peace, safety, and order* [...]."[14] The term *institution* is used causally as a form of target-oriented activities of the state administration. In addition to the definition of a public institution, the term *public utility enterprise* (German: *öffentliche Unternehmung*) is still used as a synonym.[15]

At the end of the 19th century, *O. Mayer* defined a public institution as: "[...] *the certitude of means, proper as well as personal, which are intended to serve specific, public goals over time.*"[16]

Today, the regulation of public institutions in European countries varies considerably. The content thereof is to a great extent based on the traditional regulation of carrying out such activities, so that a clear answer to the question of what the European regulation of providers of public services is cannot be given. There is also no uniform European legislation that would regulate the legal organisation of public institutions in terms of their organisational form. There is no *aquis communatauire* as regards the regulation of the institutions in terms of their organisational form, so this field is left to the Member States of the European Union.

In Europe, a comparable legal form in terms of the organisation of public institutions can be found in the public as well as in the private sphere. In the Member States of the European Union there is in general no framework law that would regulate all institutions in a uniform manner, as is the case in Slovenia. The exception is Croatia, where the Slovenian model of a uniform law has been followed. The institutions are usually regulated in sectoral legislation by special laws. When regulating the provision of non-commercial public services in terms of the organisational form of the provider, particular emphasis is placed on the public interest, which is expressed at various levels of local self-government (e.g. provinces, regions, towns, municipalities, communities). Thus, in European countries, institutions, as a general rule, take such legal forms in terms of their organisation by which local communities can efficiently serve the public interest as an element of constitutionally guaranteed rights in the social state.[17]

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veil is a legal decision to treat the rights or duties of a corporation as the rights or liabilities of its shareholders. Usually a corporation is treated as a separate legal person, who is solely responsible for the debts it incurs and the sole beneficiary of the credit it is owed. Common law countries usually uphold this principle of separate personhood, but in exceptional situations may 'pierce' or 'lift' the corporate veil."

[14] See: Jecht, H. (1963), pp. 17-20.

[15] See: Bohinc, R. and Tičar, B. (2012), p. 132.

[16] Ibidem, p. 131.

[17] Ibidem, pp. 131-142.

Today, in part of continental Europe —the part that is under the influence of the Germanic legal system— social activities (e.g. education, healthcare, culture) are provided through public institutions. Public institutions are organisational forms that provide non-commercial goods or services intended for users. Institutions can be established as independent or non-independent institutions (German: *unselbständige Anstalten*). Independent institutions are legal entities of public law, while non-independent institutions do not have their own legal personality. Intermediate forms of institutions are also recognised, namely institutions that have a legal personality, however, such legal personality is limited to a certain extent. Regardless of the above-mentioned, neither Germany nor Austria has regulated public institutions with a systemic law. In lieu of a uniform law on public institutions, in both countries public service providers are instead regulated by laws that regulate a certain field (e.g. education); certain public institutions are also established on the basis of a special law when the public interest requires a specific regulation (e.g. the national television broadcaster ORF in Austria).

In the Federal Republic of Germany, the regulation of organisations that provide public services does not fall within the competence of the Federal Republic, but within the competence of individual federal states (German: *Bundesländer*). There are different regulations governing institutions in each federal state, in addition to institutions established at the federal level to provide services that fall within the competence of the Federal Republic (German: *Bundesanstalten*). There is a relatively small number of such federal institutions and they are formed on the basis of special laws that regulate each individual instance of the provision of certain services. In Austria, the competences of the central government are broader, so that the fundamental regulation of institutions providing public services falls within its competence, and consequently the regulation of public institutions in the country is more uniform.[18]

English theory is not based on the system of a legal entity and as a result public institutions as independent legal persons or non-independent organisational forms are established in a causal manner, with due consideration of the actual needs of the state and most of all the local communities. Generically, they are named *public institutions*. There is no umbrella regulation that regulates such institutions. In the private sphere, the provision of non-commercial activities is regulated in a functional manner by the Charity Act of 1992. Pursuant to this Act, a special commission decides whether a certain activity is a charity or not. The consequences of such distinction especially concern taxation, which is more favourable for charities.

In Slovenia a regulation similar to that in England is irrelevant for public institutions, as all legal entities must pay corporate income tax.[19] Persons liable for the 17% tax comprise all legal entities of domestic and foreign law, and also companies

[18] Ibidem, p. 135.

[19] Article 3 of the Corporate Income Tax Act (Zakon o davku od dohodkov pravnih oseb – ZDDPO-2), Official Gazette RS, No. 117/06.

and/or any associations of persons, including civil law companies subject to foreign law that do not have a legal personality and are not considered persons liable for tax subject to the Slovenian act regulating personal income tax. In short, the persons liable for this tax are all corporations and all other legal entities, which also include all public institutions that, in addition to public financing, generate income from the sale of services or goods.

As mentioned above, public institutions in Slovenia are regulated by the Institutes Act of 1991, which is already 25 years old. Until the adoption of this Act, the organisation of legal entities in terms of their organisational form in the field of social activities had been regulated by the Yugoslav Associated Labour Act of 1976.[20] Until the period just before the Republic of Slovenia declared independence, such activities were regulated in terms of their organisational form on the basis of different legal-economic and political foundations. The substantive foundation of the former organisational form was namely contained in the old political system of the free exchange of labour. In the context of the regulations adopted by the Republic of Slovenia just before declaring independence, the IA, which entered into force on 30 March 1991, transformed the former organisational form of the organisation of associated labour into an institution. With this move, the legislature relatively simply abolished the former systemic regulation and established a new one. It has persisted with little change until today. Despite its progressive nature at the time, the IA also left a number of questions open, especially regarding the assets of public institutions that were *ex lege* nationalised and the question of the appropriate organisation of public entities that were, due to the short (i.e. six-month) transitional period, left stranded in a relatively out-dated organisational form. Despite several attempts and drafts throughout the period after the adoption of the IA, a new institutes act has not yet been adopted.

3. THE MANAGEMENT STRUCTURE OF PUBLIC INSTITUTIONS *DE LEGE LATA*

The management structure of institutions is presented through an organic scheme determined by the IA. Public institutions must have the following bodies: the council of the institution, a director, and a council of experts. However, these bodies can have different names or a different structure if a special act determines such. In such case, the rule *lex specialis derogat legi generali* applies, whereby the IA is *lex generalis*. For example: a special act, i.e. the Higher Education Act,[21] regulates

[20] The Associated Labour Act (*Zakon o združenem delu – ZZD*), Official Gazette SFRY, Nos. 53/76, 63/79 – corr., 57/83, 85/87, 6/88 – corr., 11/88, 19/88 – corr., 38/88 – corr., 77/88 – ZPod, 40/89, 40/89, 60/89 – ZTPDR, and Official Gazette RS, No. 37/90.

[21] The Higher Education Act (*Zakon o visokem šolstvu – ZViS*), Official Gazette RS, Nos. 32/12 – official consolidated text, 40/12 – ZUJF, 57/12 – ZPCP-2D, 109/12, and 85/14. Article 20 reads as follows: "The bodies of a university shall be: the rector, the senate, the administrative board,

that the rector is the director or manager of the university, the university council is the administrative board, and the senate of the university is the expert body.

In large public institutions with a specific structure there can also be other bodies, such as a director general, a management board, and an assembly. The Health Insurance Institute of Slovenia is an example of such. In the Health Insurance Institute of Slovenia the assembly of the institute, the management board, and the director general independently adopt business decisions pursuant to the law, statutes, and other legal acts, while in some cases they must obtain the consent of the National Assembly, the Government, or the Ministry of Health.[22] The highest management body in the public institution is the council of the institution or some other collegiate body. It is always composed of the representatives of the founder, the representatives of the institution's employees, and the representatives of users or the interested public. The composition of the council, the manner of the appointment or election of council members, the length of the council's term of office, and its powers are determined by law (according to the *lex specialis* rule) or the memorandum of association, statutes, or rules of the institution.[23]

The council adopts the statutes, rules, or other general acts of the institution as well as programmes of the institution's work and development, monitors their implementation, defines a financial plan, adopts the annual financial statement of the institution, proposes any changes to the institution's activities or the broadening of the scope of its activities to the founder, and submits proposals and opinions about particular issues to the founder and the director of the institution.

The management of a public institution is the director or other individual management body. The director is appointed and dismissed by the founder unless the law or the institution's memorandum of association stipulates that the council of the institution is competent to do so. Where the council of the institution is competent to appoint and dismiss the director of the public institution, the founder gives consent to the appointment and dismissal of the director, unless otherwise provided by law. Where the management of the institution and the management of the expert work of the institution are not separate, the director is appointed and dismissed by the council of the institution with the consent of the founder. The director of an institution with the right to operate publicly (i.e. an institution that is privately owned and has a state concession to carry out a public service) is appointed

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and the student council. The bodies of a university member shall be: the dean, the senate, the academic assembly, and the student council. The body of other institutions that are members of a university shall be the director and possibly the professional council. The bodies of a higher education institution that is not a university member shall be: the senate, the academic assembly, the administrative board, the student council, and the dean. Higher education institutions and other institutions that are members of a university may have other bodies in accordance with their charter or statutes."

[22] The Health Insurance Institute of Slovenia is governed by an assembly composed of the elected representatives of employers (among which, the representatives of the Government of the Republic of Slovenia) and insured persons. Retrieved from http://www.zzzs.si/zzzs/info/egradiva.nsf/ (12 June 2016).

[23] Tičar, B. and Rakar, I. (2011), pp. 308-314.

or dismissed with the consent of the competent national body or local community body, if so provided by law or an ordinance issued by the municipality.[24]

The director organises and manages the work and operations of the institution, represents the institution, acts on its behalf, and is responsible for the legality of its work. The director manages the work of the institution and is responsible for the professionalism of the institution's work unless the law or the institution's memorandum of association provides that, given the nature of the activity performed and the scope of management duties, the management of the institution and the management of the institution's expert work are separate.

A candidate who meets the requirements provided by law or the memorandum of association, statutes, or rules of the institution may be appointed director of the institution. The length of the director's term of office is four years unless otherwise provided by law or the institution's memorandum of association. After the expiry of the director's term of office, the same person may be reappointed director. The director of the institution is appointed following a public call for applications, unless otherwise provided by law or the institution's memorandum of association; a public call for applications must be published in the media. The public call for applications must specify the requirements that a candidate should meet, the period for which he or she will be appointed, the time limit for the submission of the applications, and the time limit within which the candidates will be informed of the outcome of the selection process. The time limit for the submission of applications may not be shorter than 8 days, and the time limit by which candidates are informed of the outcome of the selection process may not exceed 30 days from the date of the publication of the call for applications.

The director of the public institution may be dismissed by a decision of the competent body before the expiry of the period for which he or she has been appointed. The competent body is obliged to dismiss the director in the following cases: if the director requests his or her dismissal; if any of the reasons for the termination of employment in accordance with the regulations governing employment relationships arises; if, in his or her work, the director fails to act in accordance with regulations and the general acts of the institution, or if he or she fails to implement the decisions of the institution's bodies without justification or acts contrary to these decisions; if, by failing to perform his or her work with due care or by performing it incorrectly, the director causes substantial damage to the institution; or if he or she neglects his or her duties or performs them negligently such that they cause or might cause a major disruption in the operation of the institution.[25]

The expert work of the institution is managed by the head of the expert work of the institution (hereinafter: the expert head) if such is provided by law or the institution's memorandum of association. The rights, duties, and responsibilities of the expert head are laid down in the statutes or rules of the institution in accordance

[24] Ibidem, p. 309.
[25] See: Article 38 of the IA.

with the law or the institution's memorandum of association. The expert head is appointed and dismissed by the council of the institution following the issuance of an opinion thereon by the council of experts, unless otherwise provided by law or the institution's memorandum of association. The provisions of the IA that apply to the appointment and dismissal of the director of the public institution apply, *mutatis mutandis*, to the appointment and dismissal of the expert head.

Institution shall have a council of experts or other collegiate expert body. The composition and manner of forming the council of experts and the tasks thereof are laid down in the statutes or rules of the institution in accordance with the law and the institution's memorandum of association. The council of experts deals with issues pertaining to the expert work of the institution, makes decisions with regard to expert issues within the limits of its competences laid down in the statutes or rules of the institution, determines the expert groundwork for the programmes of the institution's work and development, submits proposals and opinions to the council, the director, and the expert head with regard to the organisation of the institution's work and the conditions for the development of the institution's activities, and performs other tasks provided by law or the institution's memorandum of association, statutes, or rules.

The institution has its own *statutes* or *rules* that regulate the institution's organisation, bodies, and the powers thereof, the manner of their deciding, and other issues relevant to the performance of the institution's activities and operation in accordance with the law and the institution's memorandum of association. The institution may also have other general acts that regulate issues relevant to the institution's work and operation in accordance with its statutes or rules.

The statutes or rules of the institution are adopted by the council of the institution with the consent of the founder, whereas other general acts are adopted by the council of the institution, unless the statutes or rules of the institution provide that they are adopted by its director.

The organisation of the institution is laid down in the statutes or rules of the institution. Organisational units may be formed within the institution to perform a particular activity or a part of an activity, or to perform an activity in a particular area. The statutes or rules of the institution may determine that particular organisational units are competent to enter into legal transactions and that they may exercise these powers on behalf of and for the account of the institution.

The institution obtains funds for its work from the funds of the founder, with payment for the services it provides, the sale of goods and services on the market, and other sources in the manner and under the conditions provided by law or the institution's memorandum of association. The institution uses the surplus of revenue over expenditure solely for the purposes of carrying out and developing its activities unless otherwise provided by its memorandum of association.

The institution is liable for its obligations with all its available assets, while the founder is liable for the institution's obligations, unless otherwise provided by law or the institution's memorandum of association.

The IA in force[26] determines three types of supervision over the institution, namely: supervision of the legality of the institution's work, supervision of its financial operations, and supervision of the professional quality of the institution's work. Supervision of the legality of the institution's work is exercised by the competent state bodies; supervision of its financial operations is exercised by the competent state bodies or authorised organisations; while supervision of the professional quality of the institution's work is exercised by the expert bodies determined by law.

The IA allows a number of changes to institutions in terms of their organisational form. The founder may decide a) that the institution merges with another institution, that two or more institutions merge into a new institution, or that the institution is separated into two or more institutions, b) that an organisational unit of the institution is separated from the institution and merges with another institution or is organised as an independent institution, and c) that the institution or an organisational unit thereof is organised as a company.[27]

With the consent of the founder, institutions may merge to form associations of institutions in order to conduct their joint affairs. An association of institutions is a legal entity unless otherwise provided by its memorandum of association.

The public institution may, similar to all other legal entities, cease to exist. This may occur in the following cases: if it is established by way of a final decision that its entry in the court register is null and void; if a measure has been imposed on the institution prohibiting it from performing its activities as it does not satisfy the requirements for the performance of its activities, or the institution fails to fulfil these requirements within the time limit determined in the measure; if the founder adopts a decision on the dissolution of the institution, as the need or conditions for the performance of the activity for which the institution has been established have ceased; if it merges with another institution or merges with another institution to form a new institution or is separated into two or more institutions; if it is organised as a company; and in other cases provided by law or its memorandum of association.

4. THE ELEMENTS OF CORPORATE GOVERNANCE IN PUBLIC INSTITUTIONS

In general, the term *governance* entails a process of planning, organising, managing, and supervising.[28] As an economic and organisational scientific discipline, the concept of governance was first described by *H. Fayol* in the 1920s.[29] Corporate governance in the contemporary sense entails the structure of supervisory mechanisms by means of which those who provide financial resources (equity) for

[26] See: Article 50 of the IA.

[27] Ibidem.

[28] See: Gregorič Rogelj, E. Retrieved from http://uprava.fu.uni-lj.si/index.php/IPAR/article/view/142 (20 August 2016).

[29] Ibidem.

corporations ensure that they gain a return on their investment. At the same time, they must not jeopardise the long-term development and existence of the business system of the corporation at issue.

The legal foundation of corporate governance is, as a general rule, derived from majority ownership equity in the corporation. This is transparent as regards public limited companies and some other types of companies.[30] The hypothesis is that public institutions are also corporations and that, in general, they do not have their own funds. Equity is an accounting category that is common in companies and is a basis for corporate governance. Law determines the amount of equity. In the case of institutions, this is not regulated in the same manner. In this paper the basis for the corporate governance of institutions will therefore be expanded to majority control of a corporation/institution that is legally ensured by the memorandum of association of the corporation/institution (e.g. by a decision or act establishing a public institution).

The concept of corporate governance first appeared in the 1930s in the USA. A pioneering work in this field is the book *The Modern Corporation* by *Bearl* and *Means* (1932). As mentioned above, the purpose of corporate governance is that the owners (i.e. shareholders) of large corporations no longer run the corporations themselves but they assign this task to experts (i.e. managers) who are not owners. Thus, the separation of ownership and control is implemented.[31] A core issue of corporate governance is the *principal-agent* relationship. This relationship derives from the problem as to how owners (i.e. the *principals*) can ensure that their corporation, which is run by managers (i.e. *agents*), is truly managed or governed to their benefit. Herein, this question will also be applied to the governance scheme of public institutions.

The following comprise the broader tasks of the founders of public institutions (i.e. the state and municipalities) in Slovenia; these are authoritative and regulatory and exceed the scope of corporate governance, even though they significantly influence such:[32]

– The regulation of a non-commercial public service provided by an institution at the general and abstract levels. The founder determines in a general and abstract manner what the activity of the public institution shall be. Usually this is regulated by compulsory regulations, as a non-commercial public service is always carried out in the public interest.
– Annual financing —by concluding annual contracts between the founder and the institution— for the institution to provide a specific public service in a

[30] By means of the articles of association concluded between the members of a limited liability company, the members may change the system of governance and regulate such system regardless of the amount of their equity investment. This is unusual, but legally admissible.

[31] See: Bohinc, R. (2011). Podjetje in delo, No. 6/7-2011.

[32] These tasks were also similarly summarised by Kamnar, H. (1999). Javni zavodi med državo in trgom. Znanstveno in publicistično središče, Ljubljana.

certain geographical area and field of activity. Through such financing, each year the founder significantly influences the scope and quality of the provision of the public service that is the main activity of the public institution.

– Making investments, as the assets that institutions manage are, as a general rule, legally owned by the founder. The only exception are public universities in the cases determined by the Act Amending the Higher Education Act,[33] which is a *lex specialis*, where assets of the state are transferred to these institutions. However, also in the case of investments by universities, the state must provide the majority of the funds for investments (e.g. for new buildings, research equipment), as the public service cannot be ensured otherwise.
– Exercising administrative supervision over public institutions regarding the provision of a public service. This refers to administrative inspection in the field of operation of the institution, supervision of the rational management of the funds of the institution by the Court of Audit of the Republic of Slovenia, and supervision of its financial operations by line ministries in cases in which an institution decides on public matters on the basis of having been granted appropriate public authority (according to the rules of general and/or special administrative procedures).

The above-mentioned tasks of the founders (i.e. the state and municipalities) of public institutions importantly influence corporate governance, however, they are not corporate governance itself. They represent a *sui generis* legal framework, which is characteristic only of public institutions. In a broader sense, these tasks are therefore also an instrument of governance by which the state and municipalities exert influence on the functioning of public institutions.

Governance is a continuous process of adopting relevant decisions in an institution. Considering the large number of institutions founded by the state and municipalities, the state and municipalities simply cannot handle this task themselves. They are not appropriately organised to do so, as their primary function is authoritative social regulation and not to directly govern entities of public law. Thus, in public institutions a governance system that is unique to the structure thereof has been developed, a structure composed of the management bodies of the institution, whereas the corporate rights of the founders are directed primarily at forming the

[33] See: Article 13 of the Higher Education Act (ZviS) and Article 38 of the Act Amending the Higher Education Act (ZViS-A). The content of these provisions can also be understood from Supreme Court Judgment No. II Ips 65/2013, dated 14 August 2015, where the Court explicitly stated that ownership of real estate that a university acquired from public and other sources changed with the amended Higher Education Act (ZViS-A): the owner of such assets (with a limited capacity to dispose of such) became the university (Article 4 of the Act Amending the Higher Education Act) and the transfer of the ownership right thereto should have been regulated by a contract no later than three years after the entry into force of the amended Act, as per the situation on 1 March 2000. The above-described amendment is a consequence of an amendment adopted on 20 October 1999, the explanation of which eliminates any doubt as to its intended meaning and the legislature's aim that the ownership of assets that had already been managed by universities was transferred to them.

institution's bodies, adopting fundamental strategic guidelines, and deciding on changes in the public institution in terms of its organisational form.[34]

A corporate legal relationship within a public institution between the state or a municipality and the public institution itself is implemented within the scope of the right of the public founder of the public institution (i.e. the state or a municipality), in general, to directly appoint the majority of the members of the council of the institution. Due to their inability to directly manage the institution, the state or municipality transfers the authority to manage such to its members in the council of the institution, who exercise this power on their behalf. In doing so, the members of the council of the institution must act in accordance with the guidelines and instructions of the founder, however, they do not have an imperative mandate.[35] This applies to both state-founded and municipality-founded public institutions.

Furthermore, this entails that the members of the council of the institution who were appointed by the founder participate in adopting the collective decisions of the council with legally binding effect even if their decision is contrary to the directions and instructions of the founder. At first sight, such regulation might seem unusual, but it is entirely logical, as otherwise it would be impossible to know when a decision of the body is legally binding and when it is not. Founders could namely challenge the decisions of the council any time, stating that an individual member of the council did not vote in accordance with their guidelines and instructions. This would result in complete confusion within the legal order and significantly diminish general legal certainty.

However, such regulation does not entail that a member who was appointed by the state or a municipality is not accountable to the founder, i.e. the state or a municipality. The founder may dismiss a member appointed thereby at any time and replace him or her without having to demonstrate the member's wrongdoing or stating any reasons for such dismissal. The ability to appoint or dismiss members of the council of the institution is a right enjoyed by the founder that ensures that it can efficiently exert its influence on the functioning of the public institution.

Within the scope of the founder's rights, there is another relationship between the public institution and the state or municipality as the founder, namely the question of operational decision-making, i.e. the relationship between the founder and the director. In certain public institutions the founder may directly appoint and dismiss the management body. In other public institutions, the state or municipality leaves the appointment of the management body most often to the council of the institution, in which the founder in fact has a decisive influence through the members appointed by the founder (e.g. in hospitals, medical centres, primary and secondary schools). The latter possibility is in general better than the first, as it ensures a better line of accountability within the institution and greater latitude for the council of

[34] Trpin, G. (2009), pp. 1-2.
[35] Trpin, G. (2009), pp. 3-4.

the institution to exert its influence. The council is namely better informed than the founder as regards issues concerning the management of the institution.

Finally, the founder's rights are also reflected in the fundamental documents and acts of a public institution that provides a non-commercial public service, which are adopted directly by the founder. As a general rule, these include the programmes of the institution's work, financial plans, and annual financial statements. Similarly as with the appointment and dismissal of the management body, also these tasks can be entrusted to the council of the institution. In addition, the founder also decides on changes to the public institution in terms of its organisational form; as a general rule, it reserves this right for itself and does not transfer it to the council.

5. CONCLUSION

In the IA of 1991[36] it was determined that all activities that as of 1 April 1991 were defined as activities or affairs of particular importance to society were deemed to be public services; consequently, all organisations that performed these activities up until the above-mentioned date were transformed into public institutions if they were founded by the state or self-governing local communities. Thus, 25 years ago the specific legal regulation of the public institution as a *sui generis* organisational form of a legal entity of public law was introduced. Sectoral legislation later supplemented this regulation; however, the fields of the public services determined by the IA (e.g. education, science, culture, sports, healthcare, childcare, social assistance) remained more or less unchanged.

The IA, as an act that regulates the organisational forms of public institutions, also regulates the bodies of public institutions.[37] The council of the institution is the main body composed of representatives of the founder, the representatives of the institution's employees, and the representatives of users or the interested public. The IA does not determine a ratio in this tripartite composition of the council, but leaves this question, as well as questions regarding the manner of the appointment or election of the members of the council, the duration of their term of office, and the special powers of the council, to sectoral laws, or the memorandum of association or statutes of the institution.

The general competences of the council of a public institution are defined in Article 30 of the IA, namely the following: the council adopts the statutes, rules, or other general acts of the institution as well as the programmes of the institution's work and development, monitors the implementation thereof, defines the financial plan and adopts the annual financial statement of the institution, proposes any changes to the institution's activities or the broadening of the scope of its activities

[36] See: Article 64 of the IA.

[37] Article 29 of the IA determines that a council or some other collegiate body shall be the strategic management body of the institution.

to the founder, submits proposals and opinions about particular issues to the founder and director of the institution, and performs other tasks specified by law, or the memorandum of association, statutes, or rules of the institution.

It can be established from the above-mentioned that the IA transferred the corporate governance of the institution to the council. This does not entail, however, that the council may also manage the institution in the operational sense. The council's task is only to set appropriate normative frameworks for the operation of the institution and adopt key financial and programming documents. The council also may not decide on changes to the institution in terms of its organisational form, as pursuant to Article 51 of the IA this right is explicitly reserved for the founder (i.e. the state or municipality).

With reference to the implementation of the business decisions of the institution, a question is raised regarding the supervision that the council exercises over the director. As regards the appointment and dismissal of the director, the IA provides two alternatives, namely that the director is appointed and dismissed by the founder, unless it is determined by law or the memorandum of association of the institution that the council thereof is authorised to do so. There is a specific situation in the case of public universities, where the rector (who is in fact the director) is elected in a public election by higher education teachers, academic staff, higher education staff employed at the university, and the students thereof. This is regulated by the Higher Education Act and the statutes of the university.

However, in other public institutions, also in instances in which the council of the institution appoints and dismisses the director, the founder, as a general rule, must give its consent to such appointments or dismissals; this right of the founder may only be changed by law and not by the institution's memorandum of association.

The director of the public institution is, in general, accountable for his or her work to the council of the institution, which, within the framework of this competence, also exercises supervision over the director's work. Such supervision, however, does not entail that the council may directly supervise the management of the institution, but it may only supervise the legality of the director's work and whether the set goals have been achieved. The council cannot impose sanctions in order to influence the management of the daily activities of the institution, as the only available sanction is to propose that the founder dismiss the director or for the council to dismiss the director itself with the consent of the founder if it is authorised to do so (which is not the case in public universities). Such sanction may naturally be considered only after a comprehensive evaluation of the director's work from the viewpoint of its lawfulness and the level of success of the operations of the institution.

There is a similar relationship between the council of the institution and the expert head thereof in cases in which the tasks of the management and the management of the expert work of the institution are separate. As a general rule, in public institutions the expert head is appointed and dismissed by the council of the institution following the prior opinion of the council of experts, unless otherwise provided by law or the institution's memorandum of association. This solution is not the best as the council, as the body of strategic deciding, is not suited to deciding on expert issues, which the selection of the expert head of the institution undoubtedly

is. However, the law left open the possibility that this question be regulated differently by the institution's memorandum of association, which entails that it can be, for example, determined in the memorandum of association that the expert head is appointed and dismissed by the expert council of the institution.

These are the most important corporate governance relationships that define the position of the council of a public institution in the system of its governing bodies. From this there follows the requirement that the members of this body should posses a certain type of knowledge. Considering the fact that the council is a body of strategic deciding,[38] the members must be familiar with general issues relating to public institutions as well as issues concerning the field in which the institution pursues its activities. The latter exceeds the scope of this paper, thus in the remaining paragraphs the focus will primarily be on the general issues of public institutions, or rather on the issues that influence the functioning of each public institution.

It the future, it would be reasonable for the founders (i.e. the state or municipalities) to provide funds for the provision of the relevant public service to all public institutions. Thereby, the public institutions would legally own such funds. This would be reasonable for all funds needed by the public institutions for the provision of the public services, but not for infrastructure equipment and facilities that, due to their specific economic characteristics, could remain in the ownership of the founder. Public universities, as public institutions to which the state transferred such equipment and facilities, have had, in 16 years of experience, substantial problems maintaining such and ensuring normal infrastructure conditions for the provision of the public service of research and education.

The transfer of only the assets required for the provision of the public service at issue would result in more rational use of public funds. In addition, the independence and accountability of public institutions regarding the provision of public services and carrying out additional, commercial activities would increase.

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[38] Trpin, G. (2009), pp. 3-4.

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