8th International OFEL Conference on Governance, Management and Entrepreneurship

17th - 18th April 2020 / Dubrovnik, Croatia

From Corporations to Social Entrepreneurs: Exploring the Different Faces of Social Innovation

CONFERENCE PROCEEDINGS

Edited by:
Darko Tipurić and Mislav Radić

OFEL
INTERNATIONAL CONFERENCE

Under the patronage of
Croatian Ministry of Science and Education

CIRU

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UNIVERSITY OF DUBROVNIK
DEPARTMENT OF ECONOMICS
AND BUSINESS

Under the patronage of Croatian Ministry of Science and Education

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All papers are subject to anonymous double-blind peer review

From the Editors

We are delighted to welcome you to the eighth International OFEL Conference on Governance, Management and Entrepreneurship. This year's OFEL Conference featured theme is *From Corporation to Social Entrepreneurs: Exploring the Many Faces of Social Innovation*.

The conception of the International OFEL 2020 Conference is in adding value through the fields of corporate governance, management, leadership, entrepreneurship, and education. We are very pleased to have a distinguished keynote speaker, professor Nelson Phillips from Imperial College Business School, Imperial College London.

This year's conference has a particular focus on social innovation and the ways that different types of actors can engage in it. This creates a special opportunity for scholars, practitioners' and policy makers alike, to share and discuss their latest research findings. At the time that we are writing this letter, the world is facing a crisis due to the outbreak of the COVID 19 virus, a situation that little of us even imagined possible. As the current crisis is demonstrating, we are in desperate need for social innovation, which can only be achieved through the cooperation of different types of actors.

This years' conference connects authors from more than 25 countries from across the world. The topics of papers include social entrepreneurship, corporate social responsibility, digitization, platform governance, sustainable development and other.

Our collaboration with the Academy of Management Organization and Management Theory (OMT) division continues through a doctoral student and junior faculty workshop. The workshop enables participant to learn from leading scholars in the field, and to receive feedback on their respective work.

On behalf of the Scientific and Organizing Committee, we would like to express our deep gratitude to contributing authors, reviewers and conference participants for their time and effort in finding answers to present challenges and fostering change. We hope that conference papers and events are interesting and beneficial for those engaged in the areas of governance, management, leadership, entrepreneurship, and education from academia and the corporate world.

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Faculty of Economics and Business
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OFEL 2020 KEYNOTE ADRESS

Nelson Phillips, Ph.D., *Abu Dhabi Chamber Chair in Innovation and Strategy at Imperial College Business School*

Professor Phillips' research interests lie in four main areas. First, he has become increasingly engaged in a program of research looking at a range of different but related issues in entrepreneurship. He is also interested in how new ventures "pivot" as this activity remains highly undertheorized. When studying entrepreneurship, Professor Phillips often uses ideas from organization theory to help him theorize and he has found this approach to be particularly fruitful. Second, Professor Phillips has been working for the last several years on various aspects of technology strategy and innovation. In particular, he is interested in the social dynamics of technology adoption and the ramifications of these dynamics for technology, strategy, and innovation. Third, Professor Phillips has a general interest in organization theory. Much of his work in this area has focused on connecting conventional approaches to understanding institutional processes to other theoretical perspectives such as identity or to new empirical areas of study such as stigma. Finally, Professor Phillips has a strong interest in qualitative research methods and he has published a number of papers, books, and book chapters on various topics in this area. In particular, he is interested in the application of discourse analysis, narrative analysis and other related linguistic methods in the study of organizations. Professor Phillips has published more than 100 academic articles and book chapters. Professor Phillips is currently the Editor-in-Chief of Innovation: Organization & Management and the Editor of the Cambridge Elements Series in Organizational Theory. He is also on the editorial board of the Academy of Management Journal and is the Past Division Chair of the OMT Division of the Academy of Management. Professor Phillips teaches courses in strategy, organisation behaviour, innovation, and leadership at the undergraduate and graduate level.

Events hosted by OFEL

ACADEMY OF MANAGEMENT ORGANIZATION AND MANAGEMENT THEORY DIVISION

ACADEMIC WORKSHOP

Together with the OFEL 2020 Conference, an academic writing workshop was held by the Organization and Management Theory (OMT) division of the Academy of Management.

The main objectives of the workshop was to strengthen participants' capacity for designing a high quality research paper, get feedback on their work, and to transfer the essential know-how on publishing in top journals.

Throughout the workshop senior editors from leading academic journals helped the participants transform their existing research results toward articles publishable in such outlets. We believe that the workshop has been an incredibly useful contribution for the participants as it provided an opportunity to share and develop research ideas in a critical, but supportive environment.

OMT
ORGANIZATION AND MANAGEMENT THEORY

ACADEMY OF MANAGEMENT

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CORPORATE GOVERNANCE GUIDELINE RELEVANCE FOR FAMILY PUBLIC INTEREST COMPANIES: A SMALL-STATE PERSPECTIVE

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Abstract
The objectives of this paper are to investigate the relevance of guidelines on good corporate governance (CG) to family public interest companies (PICs) within the small state of Malta and to recommend how existing guidelines may be improved and tailored for such companies. An explanatory mixed-methods empirical approach is adopted with a structured questionnaire being first administered to 17 respondents in 12 PICs owned by different families. This was then followed by semi-structured interviews with the representatives of 11 of these PICs. Findings indicate that there is a need for the existing guidelines to be improved for them to become more in line with the needs of PICs which are characterised by dominant family interests. In this respect, this paper recommends possible principles and guidelines that may be used by the relevant authorities either to improve the existing PIC guidelines or to issue a new set of guidelines aimed specifically for family PICs. Given the peculiarities of such companies, it is clear that the guidelines have to contain elements that address the CG structure, such as the need to formally document a family governance plan. Clearer guidance is needed on the appointment and composition of the Board of Directors, on the employment, conduct, compensation and performance evaluation of managers, as well as on the composition of the ownership of family PICs. Additionally, the paper concludes that a relevant factor for family PICs in carrying out improvements to their CG is that they continue to place more importance than other PICs to their continued existence.

Keywords: *Corporate Governance, Family, Guidelines, Malta, Public Interest*

Track: *Governance*

Word count: *9.165*

1. Introduction

Family businesses in Malta form the vast majority of the local business community (Farrugia, 2010; Zahra, 2017). Moreover, while studying family businesses may conjure up thoughts of "father and son" firms, some of the largest companies in Malta are family-run businesses (Farrugia, 2010).

The objectives of this paper are to investigate the relevance of the guidelines on good corporate governance (CG) to family public interest companies (PICs) in Malta and to recommend how existing guidelines may be improved and tailored to such family PICs. The study is conducted in Malta, a small island state in the European Union.

1.1 Definition of 'corporate governance'

The Cadbury Committee (1992) defined CG as the "*the system by which companies are directed and controlled*" (Para. 2.5). According to Muscat (2007) and Farrugia (2010), this definition was later adopted by the Maltese Working Group on CG which was set up by the Malta Stock Exchange (MSE) in 2001. The definition was adopted because it was deemed to be concise and sufficiently wide in scope (Working Group on CG, 2001). In the same year, the Malta Financial Services Authority (MFSA) issued The Code of Principles of Good CG for Listed Entities ("the Code").

1.2 The corporate governance framework in Malta

There are four authoritative sources that crystallise the concept of CG in Malta. The root source is the law. According to Muscat (2007), recommendations for good CG often stem from existing principles of law. Moreover, the concept of CG tends to find its way in every aspect of company law (ibid.).

The other three sources that encapsulate CG were issued by the MFSA. These are the Manual for Directors of Investment Companies and Collective Investment Schemes (CISs) ("the Manual"), the Guidelines for Public Interest Companies (PIC) ("the Guidelines"), and the Code of Principles for Listed Entities. Each one targets specific types of companies. The Manual targets investment companies and CISs, the Guidelines target public interest companies, and the Code targets listed entities. Figure 1 illustrates the four sources of CG in Malta.

The three documents issued by MFSA constitute a framework for the promulgation of good governance practices in companies where the public interest is especially at stake. The documents issued for each category indicate the regulator's cognisance of the different CG needs of each entity, depending largely on whether entities have securities issued to the public or whether they are regulated.

1.3 A focus on corporate governance guidelines

The Manual and the Code are two very specific documents that target particular types of public interest entities. The Manual is geared towards addressing the technical setup of investment companies (MFSA, 2014) whilst the Code targets listed entities (MFSA, 2001).

On the other hand, the Guidelines take a wider view. While steering away from the "comply or explain" principle in the Code (MFSA, 2001), the Guidelines target entities that are not necessarily listed. These include insurance companies, banks and other companies having publicly issued debt securities.

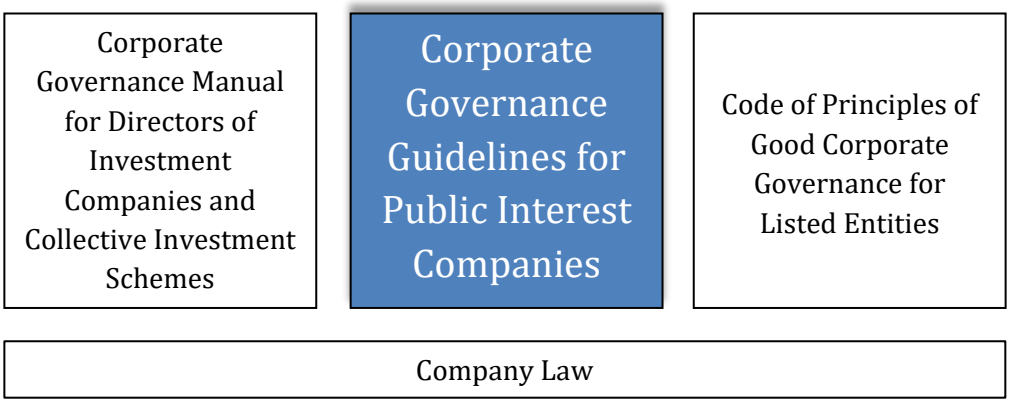

Figure 1: The Corporate Governance Sources for Maltese PICs

This study focuses on the relevance of CG guidelines to family public interest companies in Malta.

1.4 Definition of 'family company'

One of the difficulties is to define a family business, especially in the Maltese context. In the absence of an internationally recognised, legally binding definition of what constitutes a 'family

business' (Kraiczy, 2013; Zahra, 2017), defining what constitutes a family company for the purposes of the study is important because it will impact the interpretation of the results.

Family involvement in a company is the first condition necessary for a firm to be a family business (Chrisman, J. J. & Holt, D. T., 2016, cited in Chrisman J. J. et al, 2018). In fact, Hnilica and Maechek (2015) argue that there are three elements that constitute the making of a family business: ownership representation which refers to the percentage of ownership held by one family, management representation which refers to the degree to which family members occupy senior management positions, and board representation which refers to the degree to which family members occupy the Board.

All three elements measure the degree to which an interconnected group of individuals can influence the decision-making process of a business. Ownership of the majority voting rights gives effect to the full power of influence, that is, control. On the other hand, where the family holds a minority share of the ownership and the remaining portion is dispersed, influence can manifest itself to a lesser degree through board and management representation. In larger firms, it is possible for family members to own less than a majority of the shares and elect a board of directors that supports their interests (Tagiuri & Davis, 1996).

For the purposes of this study, a family-controlled company is defined as one having more than 25% of the share capital held by the founding family or next generation families, with two or more family directors. A family-influenced company is defined as having less than 25% of the share capital held by the family and two or more family directors (Baldacchino et al, 2019).

1.5 Definition of 'public interest company'

The Guidelines define a PIC as: (i) a regulated company excluding investment companies and CISs, or (ii) a company that has issued debt securities to the public and whose securities are not admitted to listing on a recognised investment exchange, or (iii) a government-owned entity established as a limited liability company. Whilst the definition in the Guidelines includes government-owned companies, it excludes companies whose securities are listed, ostensibly because listed companies are expected to adhere to the Code on good CG. Considering that listed entities form an integral part of the definition of a PIC whilst government-owned companies are not family-owned, a working definition of a PIC shall include any of the following three types of companies:

> (i) Companies whose transferable debt or equity securities are listed on a regulated stock exchange;
>
> (ii) Credit institutions, whether listed or not;
>
> (iii) Insurance undertakings, whether listed or not.

1.6 Need for the study

If family businesses form the majority of the local business community (ibid.) and the governance of a family company is more complex than the governance of a company with no family involvement (Cadbury, 2000), the Guidelines currently in place may be taking a one-size-fits-all approach that does not recognise the peculiar needs of family companies. There may be a gap which the current CG framework is not addressing.

A preliminary review of foreign literature pointed towards the codification of a set of principles of CG that are specific to family businesses. For example, one of the first initiatives was taken jointly by a group of German organisations - INTES Family Business Academy by PwC, the Family Business Network, and Die Familien Unternehmer. These entities co-jointly issued a Governance Code for Family Businesses in 2004 which is still being updated periodically. (INTES, FBN & Die Familienunternehmer - ASU, 2004).

A similar initiative was undertaken by the European Confederation of Directors' Associations which issued a set of CG Guidance and Principles for unlisted companies in Europe (ecoDa, 2010). Similarly, in 2011, the International Finance Corporation (IFC) published a Governance Handbook meant specifically for family businesses. In 2015, Riinvest Institute continued this trend and published a Governance Guide for Family-Owned Businesses.

Some of the principles in these guides address issues in family-controlled entities such as the relationship between family shareholders and minority shareholders, unfair prejudice, controlling interests versus the achievement of performance, barriers to entry, and family governance initiatives (Cadbury, 2000; Farrugia, 2010; IFC, 2011). These issues are expected to feature in the CG reality of family PICs in Malta.

2. The distinctive attributes of family companies

Cadbury (2000) claimed that it is necessary to recognise that the governance of family companies is more complex than the governance of companies with dispersed ownership. This is because of the distinctive features of family companies.

2.1 Concentration of power

Tagiuri and Davis (1996) identified various attributes of the family company. One of the most distinctive features is that individuals in a family organisation can take on simultaneous roles in three spheres of interest: as family members they take an interest in the welfare of the family; as owners they are primarily interested in a return on investment; as managers they are focused on the day-to-day running of the business.

This characteristic often results in individuals taking on multiple, overlapping roles in a family business (Hirsch, n.d.). The upside is rapid and effective business decision-taking because the overlapping roles tend to centralise decision-making (Tagiuri & Davis, 1996). A dominant leader may also instil healthy growth and business continuity which may be beneficial both to family interests and the public at large. In this context, evidence from Norway also suggested that ownership concentration positively affects a company's growth and profitability (Mishra, Randoy, & Jenssen, 2001). This was later confirmed by Chen (2012).

Nonetheless, the concentration of power may also result in conflicts of interest when family members pursue family interests rather than business interests (Daspit, et al. 2017; Tagiuri and Davis, 1996). Baldacchino et al (2019) argued that measures should be established to promote beneficial motives and eliminate detrimental, non-financial drivers that result in conflicts of interest. Concentration of power and overlapping roles often result in permanence of office (ibid.). There is also a tendency for family members to stick to their chair or executive role for an extended period (ibid.). For example, a characteristic of founding family owners is precisely the reluctance to accept professional managers capable of addressing new challenges (Mishra, Randoy, & Jenssen, 2001).

2.2 Emotional ties

Emotions often surface more easily between family members than between non-related individuals. This is because family members share a common history and the perceptions or impressions between them are unconscious and well ingrained (Tagiuri & Davis, 1996). This leaves more possibility for stronger emotions to be displayed among family members. These complex, deep-rooted ties may facilitate or complicate working relationships between family members (ibid.).

2.3 Covert communication lines

Due to the emotional ties and shared experiences, family members can exchange information more efficiently and with greater privacy (ibid.). The interaction in the family system does not typically follow an overt protocol and needs to be understood from the behaviour and attitudes of the family members (Hirsch, 2013). Family members may use special phrases, expressions and non-verbal language (Kepner (1983) cited in Hirsch (2013); Tagiuri & Davis, 1996). Covert lines of communication may lead to quicker decisions and may also act as an efficient dispute resolution tool (Taguri & Davis, 1996).

2.4 Illiquidity of shares

Mustakallio (2002) noted that the shares in a family business are generally illiquid. Similarly, Baldacchino et al (2019) explained that founding families are unlikely to dispose of their ownership. Share transfers in a family business setting are not the norm and tend to be triggered by exceptional events such as an injection of capital, inheritance, and family disputes (Mustakallio, 2002).

2.5 Propensity to distribute dividends

Thomas (2001) as cited by Mustakallio (2002) noted that in large, publicly-traded companies, the shareholders' return on investment comes from a combination of share price gains and dividends. Notwithstanding, in the case of family companies where there is no active market for shares, the financial return to the owners comes largely from dividends. In the absence of an active market, different interests may place pressures on scarce financial resources through dividend distributions that may not always be appropriate in the circumstances.

For instance, family shareholders may have different objectives depending on the type of position they hold. A family shareholder who also holds a managerial position with a regular salary would naturally be inclined to resist the distribution of dividends to the detriment of other minority shareholders (Riinvest Institute, 2015). On the other hand, family and non-family shareholders not involved in the management of the company will naturally push for the distribution of dividends (ibid.).

2.6 Weaknesses in family companies

The inherent characteristics of family companies give rise to certain defects that are only apparent in family companies. These weaknesses include suppressed corporate growth, agency problems between shareholders, disparities between family and non-family members and conflict.

Suppressed Growth

The overlap of executive and non-executive roles and the permanence of family members indicate a predisposition towards family interests as opposed to value creation (Le-Breton-Miller & Miller, 2009). This is because the retention of family control may take precedence over corporate growth. The consequential effects of the overlapping roles were also echoed by Baldacchino et al (2019) who identified the pursuit of control and non-economic goals as a characteristic of Maltese family companies.

Similarly, the illiquidity of family shares, the absence of a share transfer mechanism, and the family's reluctance to release its equity harms business operations and growth prospects when additional capital is required (Baldacchino et al, 2019). Mustakallio (2002) similarly explained that there is a trade-off between the need for the company to increase its capital in pursuance of a healthy growth strategy and the family's interest to retain control. The latter comes at the expense of the former (Jain & Shao, 2015).

The Principal-Principal Agency Problem

Several researchers argued that the most important agency problem in large companies is not the Berle and Means (1932) agency conflict between outside investors and managers, but the conflict between non-controlling investors and controlling family shareholders that can dominate managers (Cacciotti & Ucbasaran, 2017; Morck & Yeung, 2003; Shleifer & Vishny, 1997; Yeh, Lee, & Woidtke, 2001). This is likely to result in the family taking advantage of the company's resources for its personal interest at the expense of non-controlling interests.

Disparity among Family and non-Family Members

Family companies have a reputation for exhibiting favouritism toward family members (IFC, 2011; Lee, 2006 cited in Daspit et al, 2018). In a setting where the family company seeks to recruit human resources for its expansion, family members may be primarily interested in securing jobs for their relatives rather than attracting talent on a meritocratic basis (Debicki, 2017). This creates a disparity between the corporate needs of the company and the family interest.

The unequal treatment of family and non-family members may also be displayed post-recruitment. Daspit et al. (2018) noted that as the family company grows and hires non-family members, there is often a clear and pronounced distinction between family and non-family members in the organisation. This may lead to the unequal treatment of the two groups (IFC, 2011; OECD, 2015), also conceptually known as bifurcation bias (Verbeke & Kano, 2012). The desired outcome is to lock in family control (Morck & Yeung, 2004).

In this respect, Baldacchino et al. (2019) explained that, for the sake of good governance, family members seeking to occupy roles within a family company should not be given an unfair advantage over non-family individuals. By the same token, there should be no prejudice against family members owing to their family interest (ibid.).

Disputes and Family Conflict

Several researchers have claimed that there is fertile ground for disputes in family companies. Family relations and emotional ties may lead to disputes at some point in time (Baldacchino et al., 2019; Morck & Yeung, 2004; Sarbah & Xiao, 2015). A situation where non-family employees, managers, and directors are not privy to the communication lines of family members is likely to

result in uninformed decisions that undermine accountability and good governance (Tagiuri & Davis, 1996).

Moreover, different factions within the family may also be present. In this context, Cacciotti and Ucbasaran (2017) noted that the participation of an increased number of family members in the company's ownership results in greater diversity and reduces the ability of the family to exert a unified drive. The increased complexity in family ownership is most notably attributed to the decomposition of the founder family across subsequent generations over time (Zellweger & Kammerlander, 2015).

There is also a greater risk of conflict between family shareholders and minority shareholders (KPMG, 2010). Conflicts over investment, capital, pay-out decisions, and share transfers are also common in family businesses (Mustakallio, 2002). Therefore, there is a high probability that conflict, in some form or another, will dent good CG in family companies.

2.7 Governance in family companies

Composition of the Board

Baldacchino et al. (2019) claimed that a suitable proportion of non-family independent directors is likely to contribute towards transparency and accountability in Maltese family businesses. Participants in their study mostly agreed that there is a positive correlation between the Board's independence and financial performance. The contribution of independent directors is also highlighted in the Principles of CG published by the Organisation for Economic Cooperation and Development (OECD, 2015). Similarly, the Governance Guide for Family-Owned Businesses published by Riinvest Institute (2015) recommends that "for a company to be successful in the long run, it should establish a strong and independent board" (p.14). Excessive family involvement at board level restricts the Board's ability to function effectively (Baldacchino et al, 2019; Goh, Rasli & Khan, 2014).

Despite these observations, Baldacchino et al. (2019) also noted that in the Maltese context, blood is thicker than water. Family companies in Malta are not likely to appoint anyone who is resistant to family influence. This may lead to favouritism towards family members (Debicki et al, 2017; Lee, 2006 cited in Daspit et al, 2018) and a principal-principal agency problem (Cacciotti & Ucbasaran, 2017; Morck & Yeung, 2003; Shleifer & Vishny, 1997; Yeh, Lee, & Woidtke, 2001) where family interests run counter to the company's and other stakeholders' interests.

The importance of non-family directors is perhaps clearer in a family dispute, where independent directors may act as mediators. This is, however, not always possible, and conflicts may have to be resolved at other junctures (Baldacchino et al, 2018).

The Chief Executive Officer

When a family company is run by the first generation of family members, it is most likely that the post of CEO will be occupied by the most senior family member. In this circumstance, there tends to be a concentration of power in one family member (Farrugia, 2010). In the case of family companies who are no longer led by a dominant figure but are instead being directed by the second

or third generation of family members, Farrugia (2010) also noted that bringing in a non-family CEO would help to professionalise the company's senior management.

In much the same vein, Baldacchino et al. (2019) found that in the Maltese context the post of CEO needs to be independent from the family, especially if a chairperson is a family member. The main argument is that conflicting interests are more likely to arise when the two roles overlap, echoing the arguments of Daspit et al. (2017) and Tagiuri and Davis (1996). Baldacchino et al (2019) also points out that it is common to have a chairperson's role occupied by a family member since the role is non-executive.

Baldacchino et al. (2019) highlighted that having a family CEO is likely to put the Board in an uncomfortable position if performance is not satisfactory, especially if the CEO has a direct relationship with the members of the Board. Moreover, the CEO is likely to display a lenient attitude towards family-related management team members (Baldacchino et al, 2018).

It is acknowledged that certain senior management positions require skills which the controlling family might not have. Professional education and qualifications are necessary to ensure that competent individuals are appointed in senior management roles (ibid.).

This might not be easily recognised by the family members who will most likely try to fill in such posts as a means of entitlement towards the business. There is a trade-off between the family's entitlement to the business and the creation of value for the company (Farrugia, 2010) because conflicts may arise between the family's interest and the business' interest (Lansberg, 1983). There is also a trade-off between the family's interest and the public interest (Baldacchino et al, 2019).

Notwithstanding these observations, evidence provided by Braun and Sharma (2007) shows that the duality of the chair and CEO positions does not affect a company's performance. More specifically, it is noted that the relationship between duality and performance is contingent on the family's degree of ownership in the company. The lower the family's ownership stake, the more benefits are derived from separating the two roles (ibid.).

Whether or not the chair or CEO positions are occupied by family members, the values that these members can bring to the business cannot be ignored. The loyalty, enthusiasm (Donnelley, 1988), and firm-specific knowledge (Farrugia, 2010) of family members are unlikely to be matched by independent individuals.

The Family Constitution

The family constitution, also known as the 'family charter' or 'protocol', is a collective agreement which contains the rights and duties of those interested in the family's wealth. The family constitution lays down the company's family mission and outlines how the family goes about adhering to its mission and values in its business operations (IFC, 2011). The family constitution defines the roles, responsibilities, relationships, composition, and powers of decision-making bodies (Taylor Wessing, 2014). The constitution would typically contain the following elements: mission statement, values and vision; family-constituted bodies; board of directors; senior management; relationships between the family bodies, the Board and senior management; and

policies regarding family issues including employment, share transfers, and succession planning (Nixha et al, 2015).

The objective of the family constitution is to document how to maintain a good relationship between the family members and the family-constituted bodies around the company (Taylor Wessing, 2014). It might be opportune to ratify the family constitution at a time when there is stability within the company, probably when the founding family is still at the helm (KPMG, 2010).

Even though small companies may find it more convenient to work with an unwritten set of procedures, formally documenting the family constitution might become essential to the performance of the company as it grows larger (IFC, 2011). There is no blueprint for properly designing a family constitution that is applicable to all family companies (ibid.). Regardless, a properly formulated family constitution is expected to deal with subjects such as the family's vision for the future, the family's mission statement, the functioning of family bodies, family members' employment policies, and share transfers, amongst others (Taylor Wessing, 2014).

Family-Constituted Bodies

Members of the family can meet and discuss family matters in a structured way. Family members often express themselves in family meetings (Weiste, 2013). The need for family members to meet and discuss depends on the size of the company. Meetings may take place informally when there are a limited number of family members. As the family members increase, the need to formalise meetings might arise. In this context, Mustakallio, Autio and Zahra (2002) noted that family meetings tend to be more effective in large family companies. There are different types of bodies that families can establish to formalise family meetings, including the Family Assembly, the Family Council, and the Family Office.

Family Assembly

A family assembly is a meeting where family members discuss matters which concern them as owners (Neubauer & Lank, 1998). Family assemblies deal with issues such as approving the vision and values of the family, family employment, compensation and the election of family members to participate in other governance bodies (Farrugia, 2010).

A family assembly is established when the family business becomes more complex and should be composed of both managing and non-managing family members (ibid.). The meetings are usually chaired by the most senior person in the family (IFC, 2011). Family assemblies are deemed to be very important to prevent and remediate conflicts between family members, especially during an inter-generational change of hands (Farrugia, 2010). In this context, family assemblies can also enable the process of 'transgenerational entrepreneurship' which a family undertakes to develop entrepreneurial mindsets across subsequent generations (Habbershon et al., 2010 cited in Zellweger, Nason, & Nordqvist, 2011).

Family Council

A family council is a governing body that links the family with the company's governance organs and senior management (IFC, 2011). The members of a family council are elected from the family assembly (ibid.). The functions of a family council include nominating members for representation

in the Board, maintaining the family constitution and documenting the vision and values of the family (ibid.). Following an election process, the council should be composed of the most senior family representatives with the relevant qualifications and experience, whether or not they are directly linked to the family company (Farrugia, 2010).

A family council should be chaired by an individual with the necessary experience. A record of the council's meetings should also be kept (ibid.). Similarly to family assemblies, family councils can serve to prevent and resolve family conflicts (Brenes, Madrigal & Requena, 2011). It can also serve as an ideal venue for training the next generation of family directors and senior managers (Weiste, 2013).

Family Office

A family office is a separate body which is distinct from the family and the business. A family office is usually composed of independent professional managers who are tasked to provide advice on technical issues such as financial planning, wealth management and compliance (IFC, 2011). A family office is usually overseen by the family council (ibid.). Several wealthy families are likely to request the services of a family office: in this respect, family offices are mostly applicable to very wealthy families and therefore not necessarily relevant in the Maltese context. (Baldacchino et al, 2019)

3. Methodology

3.1 Research tool

A mixed methodology was selected for the study because it is a means to achieve the benefits of two different methodologies. Creswell and Piano Clark (2011) highlight that in a mixed research methodology, both quantitative and qualitative data are collected, analysed separately, and then integrated, either concurrently or sequentially, to address the research questions. This aims to address the deficiencies in both quantitative and qualitative methodologies (Creswell, 2015).

A structured questionnaire was used that contained close-ended questions in the form of a Likert scale ranging from 1 to 5. The close-ended questionnaire was designed on CG principles for family companies emanating from the literature review. A semi-structured interview schedule that contained open-ended questions was also used. The open-ended questions in the interview schedule were designed on the Guidelines issued by the MFSA.

3.2 Sample population

A purposive sampling technique was used to reach the research objectives. This technique requires a researcher to apply judgement to select the appropriate research participants. In this respect, experts in the field of CG ('Experts') and company secretaries ('Cosec's) of family PICs were selected as the target population for this study. Twenty-six potential Experts and Cosecs were identified.

Experts consisted of representatives from regulatory authorities, government bodies, academics, lawyers, and ex-company secretaries. Relevant contacts were sourced from publicly available information.

Cosecs consisted of company secretaries acting for family PICs. A list of companies was extracted from the MSE publicly traded list, including MSE Prospects. A list of insurance undertakings and credit institutions was also extracted from the MFSA-authorised list of service providers.

Cosecs were identified through a search performed on the database of the Malta Business Registry. Relevant details were also available on the MSE's website, the Maltese Council of Notaries' website, and corporate websites.

3.3 Data analyses

Quantitative data generated from the Likert scale questions of the questionnaire were analysed using IBM SPSS Statistics. The rating scores ranged from 1 to 5, where 1 corresponded to 'Strongly Disagree' and 5 corresponded to 'Strongly Agree'. Therefore, higher rating scores indicated a higher level of agreement with a particular statement. The mean score, median score, and standard deviation were calculated for each statement of the two groups of respondents. The ratings of the two groups were analysed in descending order of average Expert agreement.

Qualitative data was primarily collected through open-ended questions in the interview schedule. Additionally, qualitative data was collected through a 'comments' section inserted in the Likert scale questionnaire. Additional feedback on the Likert scale questions was also requested during the face-to-face interviews. The data was analysed by evaluating the transcribed data and identifying key themes and concepts.

3.4 Research limitations

Seventeen participants responded to the questionnaire, of which six were unwilling to be interviewed or did not respond to the invitation. Obtaining the contact details of some respondents proved to be difficult and some company representatives cited the General Data Protection Regulation as restricting them from providing the necessary details.

Cosecs were sub-categorised into three groups for the purpose of explaining the limitations of the research. The following are the sub-categories:

(i) Lawyers working as sole practitioners;

(ii) Lawyers employed with law firms; and

(iii) Company secretaries employed with family companies (most of whom were also lawyers).

Sole practitioners and professionals employed with a law firm gave more candid replies and therefore seemed less biased than family-employed Cosecs. In this respect, some family-employed Cosecs were very defensive in their replies. The replies given by family-employed Cosecs were, in some instances, a recital of the company's CG formula and a reflection of the company's system.

4. Findings and discussion

4.1 The family governance plan

Documenting the family's vision, mission, future share transfer plans, and working relationships vis-à-vis the continued growth of the family's wealth through a family governance plan would

serve to improve the stability and continuity of the company (KPMG, 2010). It is also seen as a positive measure to enhance the CG of a PIC owned by family interests because having a documented plan of action is a source of stability.

In fact, the second measure most agreed-to related to documenting the family's principles, vision, and mission in a formal and transparent manner. Experts and Cosecs agreed that formally documenting the family's vision and mission with respect to the business would enhance CG.

The time at which the document is formulated is crucial. The document needs to be formulated at the time when the family and the company are most stable. This is likely to be the case when the company is still being run by the first generation (ibid.) because conflicts and disagreements start to arise from the second generation onwards. In this respect, it is also a tool that might prevent family company weaknesses from developing at a later stage.

In particular, interviewees noted that CG guidelines should require a 'continuity plan', or a 'governance plan' in terms of where the family wishes to position itself in the medium to long-term. One Expert recalled a case when a family director introduced a family governance code to remediate the disputes that were taking place among the second and third generation family members. The 'code of family business' dealt with subjects such as the composition of the Board, education, and family share transfers, amongst others. Although the other family members resisted the implementation of the code by the family director, the Expert noted that "looking back, everyone acknowledged its beneficial effect".

4.2 Family fora

Documents including a family constitution are usually maintained by the family council (IFC, 2011). Nonetheless, since family assemblies are also responsible for formulating the mission and vision of the family (Farrugia, 2010), the family governance plan could also be maintained by the family assembly in the absence of a family council. Dialogue could therefore take place in a family assembly or a family council, where family members meet and discuss important family documents and information in relation to the business. This would contribute positively to good CG in family PICs.

In fact, the measure most agreed-to related to the establishment of a forum where family members can meet to provide and receive information in relation to the business. Both Experts and Cosecs agreed that establishing a governance body specifically for family members to meet and discuss would contribute to good CG. In this context, interviewees confirmed that the measure made sense in principle, although to their knowledge this was not being practised in Malta.

4.3 The chief executive officer

Experts generally agreed that allowing family members to form part of the senior management team would amount to good CG although Cosecs displayed a relatively neutral stance on this measure.

Respondents were generally neutral as to whether a family member should be allowed to act as CEO. In this context, interviewees noted that in principle "being a family member should not inherently disqualify anyone from being involved on the board or in senior management - the real issue is achieving the right balance." The question on whether the role of CEO should be occupied

by a family member remains a contentious one. Although Baldacchino et al (2019) noted that a family CEO might put the Board in an uncomfortable position, one cannot preclude a family member from occupying this position simply because of an affiliation with the family.

The possibility for family members to occupy the role of CEO should therefore remain. As a counterbalance to the appointment of a family CEO, the Board should ensure that its assessment of the CEO is not influenced by the affiliation with the family. One could perhaps propose a system where a family CEO is counterbalanced by an independent, non-family chairperson leading the Board.

Leaving the possibility of combining the roles of a chairperson and CEO was not perceived as ideal in the context of a family PIC. In this respect, findings indicated that the two roles should be divided in a clear manner. Nevertheless, this also depends on the company's ownership structure. As evidenced by Braun & Sharma (2007), the separation of the two roles tends to lose its desired effect on CG with a higher concentration of family ownership. This may suggest that separating the two roles in a founder family-owned company may not necessarily be beneficial. This argument gains even more weight when considering the positive association between founding family control and firm value (Mishra, Randoy, & Jenssen, 2001).

4.4 Composition of the board

The Boards of family PICs should not be composed of a majority of family members. As argued by Baldacchino et al. (2019), a suitable proportion of non-family independent directors is likely to contribute towards more transparency and accountability. Independence would be lost if the Board was composed of a majority of family members.

Findings indicate that there is a mixed feeling amongst participants on whether a family member should act as chairperson of the Board. Several interviewees were close to the territory favouring the appointment of an independent, non-family chairperson. The main reason given was that, because the chairperson is usually a strong founder member, there may be a higher risk of appointing 'yes' men with the aim of accommodating that dominant figure. This is also likely to happen because, as noted by Baldacchino et al (2019), family members tend to pursue the family's interest first. It is therefore acknowledged that a strong, dominant figure needs to be counterbalanced with independent individuals of sufficient calibre. On the other hand, it is acknowledged that the family cannot simply be side-lined, as noted by one Cosec:

"Having independent minded, non-executive directors that think outside the box and challenge the status quo is very important. But you cannot expect the one who gave birth to the 'baby' to just step aside."

This is totally understandable when considering that the family is the major shareholder and the driving force of the business. Therefore, a balance needs to be found on how the Board should be composed to ensure good governance.

Another consideration worth noting is the inter-generational effect on the CG system of a company. The CG system of a family PIC which is still being directed by the founding family does not have the same governance needs of a company being led by the second or third generations.

Therefore, there may be a case for distinguishing between companies directed by a single family, most likely being the founder family, and companies directed by more than one inter-related families.

CG guidelines should recognise that a family PIC directed by the founding family is more likely to be in a stable position because the founder usually holds a firm grip on the direction of the company, as noted by Daspit et al. (2017) and Tagiuri and Davis (1996). In this respect, it was also noted that a concentration of power tends to positively affect a company's performance (Chen, 2012; Mishra, Randoy, & Jenssen, 2001). Therefore, undermining a dominant figure by separating the roles of CEO and chairman may lose the desired effect the higher the concentration of family ownership (Braun & Sharma, 2007). In this context, CG guidelines should expect a counterbalance to a dominant person that does not undermine their effectiveness.

On the other hand, a family company which is being taken over by the second or third generations is in a much more vulnerable position. The vulnerability can be attributed to several reasons. It may stem from a vacuum caused by the departure of a dominant figure. It may be the cause of emotional ties (ibid.) and the different backgrounds of family members that may be hard to reconcile in the board room. Thus, it was noted that the independent, non-family directors become extremely important when "the second or third generations take over from the first generation". This is because in a family setting, "the emotions and egos are so strong that every business consideration becomes secondary", to the detriment of the company. In this respect, CG guidelines should expect a counterbalance which may only be achieved through the involvement of a non-family individual who takes on a leading and reconciliatory capacity.

This could be implemented by appointing an independent, non-family chairperson who may re-instil order and authority. By virtue of the chairperson's independence and his or her appointment by consensus, it would be hard for a family member or a family-appointed director to argue that a chairperson is acting in favour of one particular party. An independent chairperson would help to nullify any blinding emotions and prevent or help to resolve family disputes. This role would also introduce a sense of organisation and professionalism when the Board is mired with family clashes.

4.5 Tenure of family appointments

Research participants generally agreed with prescribing the retirement age of family directors to enhance CG in family PICs. In this context, three Experts explained that this was very important because "there comes a time when you have to go" and give way to the next generations, especially when the first generation of family directors reach a certain age.

There might be several negative connotations associated with permanence of office. For instance, as noted by Baldacchino et al (2019), having top positions occupied indefinitely might lead to a culture that resists innovation. This mentality could be eradicated by defining the number of years a family CEO ought to remain in office.

Defining the retirement age of directors could also contribute to a more balanced composition of the Board. In this respect, although family directors are more likely to stay on beyond a certain age, distinguishing between family and non-family members might create more problems. This is also true for the post of CEO. Therefore, a system that inhibits long tenures and that is equally applicable to family and non-family members should be consistently applied across the board.

4.6 Family competencies

Research participants agreed to formally requiring a minimum level of education and work experience for family members intending to take on a directorship role. Indeed, it may be hard to reconcile the views of family directors having different educational backgrounds. The probability of disagreements owing to the different backgrounds was highlighted:

"Some family directors have a professional educational background, while others have been working in the family company since they were teenagers. The clash is inevitable."

The different educational backgrounds of directors and managers breeds conflict, which is a distinctive weakness of family companies (KPMG, 2010; Mustakallio, 2002; Sarbah & Xiao, 2015). This is due to the fact that directors with a different level of education may find themselves speaking two completely different languages. Sometimes, there is also a sense of superiority which two sorts of family directors seem to be entitled to: one for the academic and professional experience achieved and the other for the hands-on work experience gained on home ground – the family business. That is the extent to which "family ties blind any form of logic and professionalism".

Prescribing a minimum level of competencies required from directors is beneficial to CG. As pointed out by Baldacchino et al (2019), professional education and qualifications are necessary to ensure that competent individuals are appointed. This requirement would also help to identify any training needs. Nonetheless, it is extremely difficult to find a balance in a family company setting. For instance, it would be hard to prove that a family member is not fit for purpose unless there are formal procedures for assessing competence. On the other hand, it would be counterproductive to over-regulate the appointment of directors because ultimately the appointees must be trusted by the family.

Therefore, although most participants agreed with prescribing a minimum level of education and experience for family directors, a more moderate approach could be to require a mentoring or training programme for all appointed directors (whether family or non-family) who do not have a minimum level of competency. This would give an opportunity for young family members to expand their business experience and qualifications without compromising the competence of the Board. Training programmes are likely to be effective from an early stage before directors are appointed to the Board. For instance, family-constituted bodies such as a family council provide an ideal place to mandate a training programme for potential board members as noted by Weiste (2013). The training programmes should be adequately documented to ensure transparency and accountability.

4.7 Conduct

Instilling a culture that requires some form of continuous professional education for family directors is seen as a favourable measure contributing towards better CG. In this respect, the Guidelines should widen the scope to include specific adequate training for directors and not only for managers and employees. This measure is likely to be effective because it may help less experienced directors whilst bridging the gap with other directors having a professional background. This may also go some way to addressing the conflicts arising from this gap.

Although laying down grounds for termination for family management and family directors was supported by most respondents, it is to be noted that a system that distinguishes between the conduct of family and non-family members across all levels of the organisation will tend to create more challenges. In much the same vein, defining penalties for non-compliance should be equally applicable to family and non-family members. Moreover, the system should be consistently applied consistent and enforced across the board by independent directors.

4.8 Family remuneration

The validation of remuneration levels in line with market benchmarks by external consultants would contribute to more transparency and better CG of family PICs that are not expected to have a remuneration committee. This would also help to prevent the unequal treatment of family and non-family members, which is a recurring feature in family-owned companies (Daspit et al, 2018; Debicki, 2017; Verbeke & Kano, 2012). Documenting these processes would also improve transparency and accountability towards all relevant stakeholders.

4.9 Performance evaluation

In a family setting, it is acknowledged that the principle that all directors should regularly review the performance of senior management might not be happening in reality. This is also very much related to the reality that the Board might work around the requirement to appoint 'independent' directors. The counterbalance provided by an independent, non-family chairperson heading the Board is equally relevant to counterbalance other senior executives and not only the CEO. This would also help to counter the disparate performance evaluation of family and non-family members, a weakness which was highlighted by various researchers. Performance reviews should also extend to all board directors irrespective of whether they are affiliated with the family.

4.10 The neutral sanctity of the family PIC

The portrayal of a company's interest as seemingly distinct from, or misaligned to, the interests of its shareholders may be somewhat hard to imagine. This is because the company is a creation of its shareholders aimed, first and foremost, for their benefit.

It is therefore ironic (and equally curious) that a significant number of participants have distinguished between the protection afforded to the interest of the 'company' and its 'shareholders' as though these could be ranked in order of priority, hence allowing for a clearer distinction of the two interests. More specifically, some respondents believed that the long-term interests of the company should be placed before the short-term interests of a dominant group of shareholders such as a family.

Considering the fundamental and most basic tenet that a company is supposed to act in the interest of its shareholders, why did interviewees distinguish between the interest of a company and its shareholders? In the context of a dominant group of family shareholders a plausible reason for this distinction could be that, for the purposes of this study, a company is not simply a family company, but also a public interest company. In other words, the public dimension of a family company may render the distinction between the interests of a company and its shareholders more apparent.

This is not to say that the interest of shareholders should not be paramount, but that in the context of the peculiarities displayed by family companies, the going concern of a family company with a

public interest dimension places foremost in formulating CG guidelines. The distinctive attributes of family companies, such as concentration of power (Daspit, et al. 2017; Tagiuri & Davis, 1996), weaknesses such as suppressed growth (Baldacchino et al, 2019; Le-Breton-Miller & Miller, 2009;), and a high probability of conflict (KPMG, 2010; Mustakallio, 2002; Sarbah & Xiao, 2015) render the family PIC a more fragile creature compared to its non-family peers. Using Grech's frame of thought (2014) in the context of the research findings, one can argue that the inherent characteristics of a family firm in a public dimension sanctify the company. In other words, the company's interests in terms of its business continuity should be given more weight in view of the family and public interest dynamics.

While recognising this concept would protect the interests of family shareholders because they stand to gain most from business continuity, it would also protect the public interest from short-termism, bad management, and conflicts of interest. Therefore, at some point, the interests of the family and the public converge for the proper continuation of the company. Figure 2 illustrates the intersection of these interests.

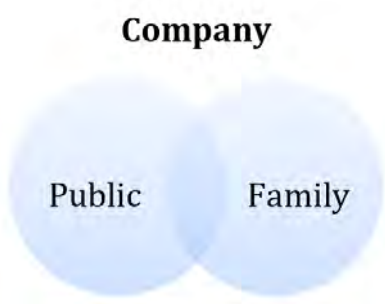

Figure 2: The Neutral Sanctity of the Family PIC

Several interviewees believed that CG guidelines should place the interests of outside stakeholders before the interests of shareholders especially in the case of family PICs. A guiding principle needs to spell out the importance of other stakeholders' interests, especially in the case of companies dominated by families. The argument may be relevant when considering that controlling shareholders can defend their interests in the board room, whilst other stakeholders cannot.

4.11 Share transfers

As highlighted by Mustakallio (2002), most interviewees noted that shares in a family business are generally illiquid. The ownership of family businesses does not change hand very frequently and is most likely triggered by extraordinary events such as the demise of a family member or family disputes. A share transfer plan that is triggered immediately after the occurrence of extraordinary events ensures certainty and business continuity. Moreover, a share transfer plan that does not necessarily target family members is a very important element in order to preserve the continuity of the company.

In this respect, pre-emption rights that are reserved exclusively to family members might bring a 'deadlock' situation. This is because family members not interested in the company and seeking

to liquidate their share might not want to cede their portion to the other family simply because emotions override any other consideration. A more efficient system can only be achieved if there is an all-encompassing strategy of where the family wants to position itself vis-à-vis the business. This could be achieved by formally documenting the family's plan. A family forum where members can discuss these plans would also be ideal.

If a family wants to remain in control, a share transfer plan intended to expedite share transfers among family members in extraordinary times would ensure continuity of business. In the case where the family wants to exit the business, a share transfer plan that ropes in other minority shareholders or third parties would be relevant for the continued existence of the company. Respondents were generally in agreement with principles such as establishing a pre-determined process for buying out family shareholders and giving the right of first refusal to the minority owners of the company. It was therefore acknowledged that these could have a positive impact on the company's continuity.

4.12 The conservation of capital

The conservation of capital reserves in a family PIC is of utmost importance to ensure the continued financial viability of the company and to avoid short-termism. Guidelines ought to highlight this aspect specifically by introducing the concept of a minimum maintenance level which would be determined on a company-by-company basis. This measure could help to reconcile the different family interests by creating a balance between those seeking a dividend return and other families whose primary source of income is the family business. Moreover, this would help to preserve the continuation of the company

5. Conclusions

The authors conclude that the Guidelines for PICs adopt a one-size-fits-all approach which in most cases is not relevant to the needs of family PICs in Malta. Guidelines should reflect the family companies' need to formally institute family meetings to improve the communication among members of the same family, between different families, and most importantly between the family and the company's structures. There is a need for family members to formally document a family governance plan including a family constitution. Moreover, there needs to be clearer guidance on the composition of the Board given the peculiarities of family PICs and the changeover from one generation to the next.

Clearer guidance should be provided on the process of appointing independent directors and engaging senior managers in the context of dominant family interests. In particular, the required competencies of directors should be highlighted. Guidance should be provided on how to determine compensation levels and monitor conduct and performance in a more transparent way. Family PICs should properly document the selection criteria and the Board's assessment for appointing independent directors and CEOs. A family PIC should document the basis for concluding that a director or a CEO is an independent, non-family person. This should increase accountability and make the processes more transparent.

This study also concludes that the Board should endeavour to appoint an independent, non-family chairperson when the power is distributed amongst multiple families. This may be the case when the Board is represented by second and third generation family directors. The Board should

establish and set out in writing a clear division of roles and responsibilities between the running of the Board and the executive responsibility for the running of the company particularly in the case of dispersed family shareholding structures (second and third generations).

The competencies required from directors to be appointed on the Board may vary from one company to another. Nonetheless, this study concludes that determining a minimum level based on company-specific criteria such as experience and qualifications would serve to identify any gaps required for the positions. The Board should address any gaps identified. For example, it could require a hand-holding period for prospective directors especially in the case of junior family directors. Examples of good practices include mandatory training or assistance from external consultants during the transition period. This should start from an early stage, possibly at the level of the family assembly or family council. Furthermore, the Board should ensure that there is adequate ongoing training for directors and not just for management and employees.

The authors also conclude that the continued existence of a family company is more important in the context of public interest companies. Because of the family and public dimensions, the company per se takes on a more distinct autonomy (and sanctity) that transcends its existence as a mere legal identity. Guidelines should also help family PICs to balance the duties owed to shareholders and the public in an equitable manner such that the dominant influence of family interests does not unfairly step on those of other stakeholders.

It is recognised that the concentrated shareholding patterns in family companies allow more control and oversight over management. But this cannot happen at the expense of other interests. Most importantly, it cannot happen at the expense of the communal interest in the case of family public interest companies.

This study focuses exclusively on Maltese family public interest companies. Although every effort has been made to conduct a comprehensive study on the subject matter, it remains that the study is subject to a number of limitations. All participants in the study were Maltese and the findings of the study are therefore limited to Malta. It is inevitable that the views expressed are influenced by the culture, regulations and systems within the country, particularly in a small state such as Malta. The study is also subject to the limitations that are inherently associated with the research methods that were adopted for the purpose of this study.

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CHARACTERISTICS OF THE HIDDEN ECONOMY IN HUNGARY BEFORE AND AFTER THE REGIME CHANGE

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Abstract
Lately, economists and policymakers have been paying even closer attention to the hidden economy. Indeed, it makes a difference to the economy how much money goes into the state coffers. In order to uncover the hidden economy however, it is necessary to be familiar with its nature and manifestations.
In this paper, with the aid of previous research and literature we attempt to illustrate the characteristics of the hidden economy in Hungary before and after the regime change and to map out the steps that have been taken to uncover it.
This publication was preceded by a systematic literature review on the definition, causes, and effects of the hidden economy, consisting of the collection of both data and literature related to the domestic hidden economy.
The following summarize the results from the synthesis of literature:

1. *The Hungarian hidden economy existed even before the regime change and took a variety of different forms. These include tips, bribes, informal payments, unauthorized work and patchwork, moonlighting, unauthorized rental of real estate, use of social property for personal gain, gains from the infringement of customs and exchange law, tax fraud by craftsmen and retailers, theft of public property, and corruption.*
2. *Since 1990, not only have the dynamics of the hidden economy strengthened, but its types of activities have changed significantly as well. These include, but are not limited to: omitting a portion of revenue from the register; recognizing non-incurred material production costs among expenditures; including an excessive portion of personal household maintenance costs among production costs; organizing business and study trips abroad; finder's fee; end-of-year depreciation or 'transfer' of inventories; wages of registered employees paid out of pocket; employment of unreported employees; parallel company formation; economic activity of unincorporated individuals and the income generated thereby.*
3. *The following are among the concrete steps taken in recent years to uncover the Hungarian hidden economy: the temporary employment booklet; the simplified entrepreneurial tax; the Electronic Trade and Transport Control System; online cash registers; the connection of vending machines to the tax office.*

Keywords: *Economic policy, Hidden economy, Tax*

Track: *Governance*

Word count: *4.525*

1. Introduction

Hassan and Schneider (Hassan & Schneider, 2016) studied 157 countries around the world and gave a very diverse picture regarding the development of the hidden economy. There are examples for each case, some of which we have highlighted here (Figure 1). We find countries where the hidden economy has significantly declined, some countries where it remains stagnant, and others where it has greatly increased between 1999 and 2013. There are countries where the hidden economy barely reaches 10%, such as Switzerland, Austria and the United States. There are others where it surpasses 70%, such as Bolivia, Honduras and Guatemala.

The author's twofold objective is to fill a very large gap in determining the "true" size of the hidden economy, since so far both static and dynamic comparisons have had multiple sources of error. For example, just consider the ever-changing definitions of hidden economy or the various measurement methods applied in different countries.

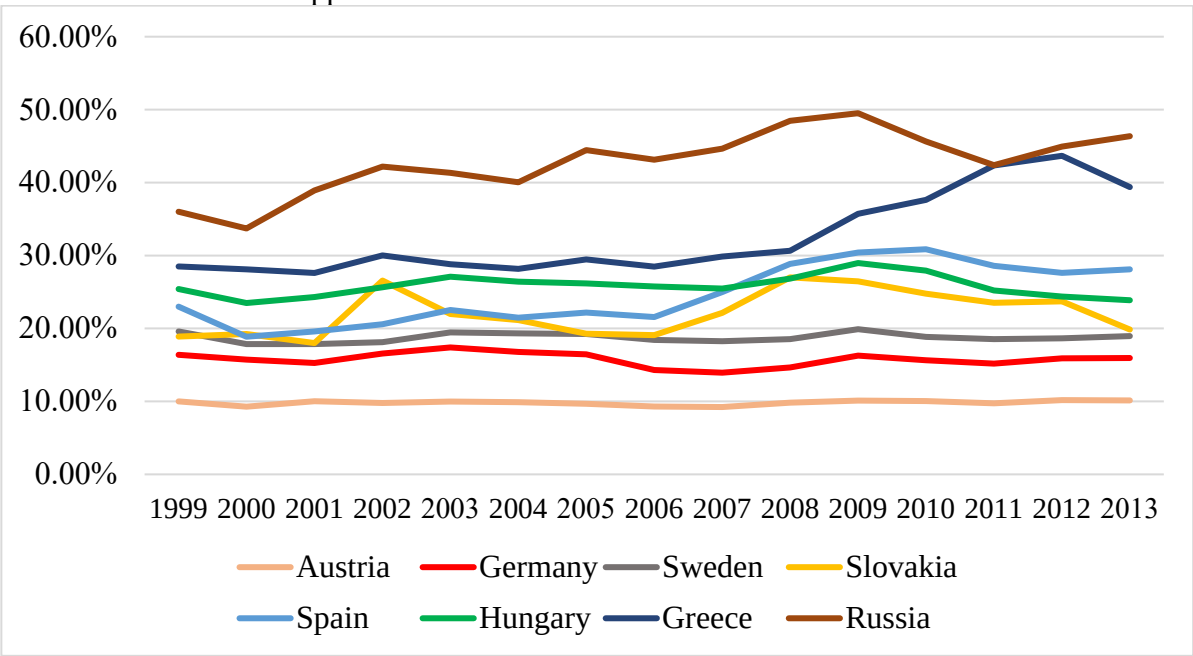

Figure 1: The size of the hidden economy as a percentage of the GDP (1999-2013)
Source: Edited by authors based on Hassan & Schneider (2016)

This topic first came up in the 20th century and has inspired many researchers to this day. Even during the initial phase, many people were interested in mapping out the hidden economy. For example, we can find observations of the underground economy in Helfferich's 1914 work. However, research on the subject increased significantly during the 1980s. First, the academic sphere began addressing this issue in the late 1970s. Feige (1979) blamed inaccurate statistical information for the fact that macroeconomics was unable to make adequate economic policy proposals. A decade later, measuring the hidden economy began to occupy the statistical offices of many countries. At this point, clarifying various concepts became a truly central objective.

2. Methodology

Literature reviews are needed in most of disciplines as volume of scientific publication has been increasing significantly.
Due to the mass of publication, researchers could not have always opportunity to examine in detail the literature of a given topic.
There are several advantages of processing literature:

- They could be useful for those who are researching the topics, as they can find the information, which are emphasized in different studies, in one place without spending a lot of time for quest of relevant literatures.
- They provide unbiased information about studies in a given discipline for the readers.
- Beyond that, they can help to determine the scope of further studies.

This publication was preceded by a systematic literature review on the definition, causes, and effects of the hidden economy, consisting of the collection of both data and literature related to the domestic hidden economy. While exploring the relevant literature verifiable scientific value and thus the restriction of place of publication of the selected works played a primary role. The following databases were utilized during our searches: Web of Science, MATARKA, Google Scholar and the ARCANUM database.

3. Definition of hidden economy

There are many difficulties facing conceptual clarification. Among other things, publishers on the subject refer to the hidden economy using numerous expressions (unofficial, underground, unregistered, second, irregular, etc) (Table 1).

Table 1: Most of the terminology available in the literature

Black	Cash-in-hand	Peripheral	Concealed
Hidden	Everyday	Submerged	Marginal
Second	Off-the-books	Irregular	Occult
Grey	Non-observed	Unobserved	Clandestine
Shadow	Subterranean	Parallel	Untaxed
Dual	Non-official	Unrecorded	Precarious
Ghetto	Unregulated	Underground	Twilight
Moonlight	Unofficial	Unorganised	Invisible
Other	Unexposed	Underwater	

Source: Edited by authors based on Williams (2004)

There are different names that cover more or less the same content, but there are also cases when multiple definitions are all headed by a single name. For example, there are authors who believe that hidden economy includes only informal activities (households and their production, unregistered companies) and underground activities (such as tax evasion, not respecting minimum wages, failing to meet health and safety standards). (Sík & Tóth, 1998; Dell'Anno, 2003; Belyó, 2008; Lackó et al., 2009) Others believe that in addition to these, the hidden economy also includes illegal activities, meaning the production, sale or possession of goods and services prohibited by law. (Schneider & Enste, 2004; Balogh, 2014; Csomós & Kreiszné, 2015; Bejaković, 2015) To give an example of different names referring to similar content, we would point out 'unobserved economy' as defined by Lackó et al. (2009) and 'irregular economy' of Feige (1979). These names further include barter transactions, activities performed under the guise of cooperative volunteer work, and services performed within households.

A uniform definition of hidden economy has other limitations as well. According to Belyó (2012, p. 28), "The difficulty of defining is due, among other things, to the dynamic nature of the licit economy and, as a result, to the dynamic nature of definitions related to the licit economy. The economy evolves over time, adapting to "de facto" changes in national economies (eg government regulation, general social attitudes and changes in the SNA)."

Due to the issues mentioned above, most of the concepts remain in the form of a general description. One of the early definitions comes from Feige (1979), according to which the hidden economy includes economic activities that are unreported or cannot be measured using current measurement techniques. Another broad definition is that the hidden economy consists of all unregistered economic activities that contribute to the officially calculated GDP. (Schneider & Enste, 2004)

There are authors who try to describe the hidden economy from various aspects. For example, Fekete and co-authors (Fekete et al., 2008) have approached the definition of hidden economy from several aspects (legal, ethical, statistical, political economy, or taxation).

From legal aspect the hidden economy means wrongdoer economical activities or pursue legal economical activities in illegal way.

From ethical (public perception) aspect the black can turn into grey, or moreover into white in some case based on the social justice, fairness or usefulness, contrarily, the activities of wanglers, who follow the words of law but act against public interest, can be ranged to black.

From statistical aspect it is hidden part of national economy production which can be only estimated with indirect methods in most cases.

Political economy evaluates it based on its hurtful effects to economy. Accordingly, all elements of statistically unobserved economy, such as food production of households for their own

consumption, are not included, on the other hand certain economical activities – like avoiding tax and customs payment – which are not considered as production are included.
According to taxation approach, the hidden economy means economical activities with tax evasion. Such activities could be include into this which are not productions and so they do not make added value but tax should be paid after it. On the other hand, illegal activities, like illegal drug trafficking which are seemed production in statistics, are not included.

4. The hidden economy in Hungary

The hidden economy can only be examined in its dynamics, as its components are constantly changing. This is especially true of the former socialist countries, since their components changed significantly before and after the regime change.
According to Kereszty (1996), there are 3 main stages in the development of the hidden, as he denotes it, "black economy."

1. The first stage is the period of formation, which dates back to the 1970s. It was characterized as being of a local nature, varying by region and by industry, and not of a significant size. The participants were motivated by the need to obtain a private benefit from state-owned companies and cooperatives, which served to meet their personal needs.
2. From the 1980s to the regime change. The methods remained unchanged, but the liberalization of the economy made it possible to accumulate significant wealth, mainly cash and currency, to build flats, homes, and resorts, and to purchase high-value Western brand cars. This period is considered the beginning of the initial capital accumulation.
3. From the early 1990s, holders of various illicit funds sought to take maximum advantage of the opportunities offered by the transformation of the economic system. In addition, the adventure capital arriving from beyond our borders and the often irresponsible lending practices of domestic financial institutions put billions into private hands without collateral or remuneration.

In the following, we divide the description of the hidden economy's characteristics into just two groups: before and after the regime change.

5. The hidden economy before the regime change in Hungary

The second economy (the hidden economy) derives from the structural deficiencies of the socialist planned system and from the cultural and historical development of certain Eastern European countries. Ironically, the second economies of these countries correspond with the counterparts the primary economies of capitalist countries. (Sampson, 1987)
There was no personal income tax in the countries of Central and Eastern Europe before the regime change, and salaries were determined in such a way that they did not have to cover various taxes or social benefits. At that time, the basic needs of the majority of society could be met from full-time earnings, and the main purpose of second-economy activities was "merely" to provide additional income. (Enyedi & Tamási, 1995)
Thus, socialist countries, where the hidden economy was intrinsically linked to the shortage economy, began to address this issue at a time when the problems of the state-owned economic system were becoming more prominent. (Lackó, 1995)
In the early 1980s, Hungary was the first country in the then European Socialist region to begin researching the hidden economy. The aim was primarily to estimate the size of the income generated by the hidden economy, as there was a contradiction between statistically reported income and level of well-being experienced. (Ékes, 1995)
For the study of the 1980s, the Economic Research Institute drew a line between transactions which do and do not involve the transfer of a sum of money. This includes economic crimes (fraud, embezzlement, corruption) and business theft, estimates of which were also attempted. The types of income recognized as invisible income at that time were tips, bribes, gratuities related to health and legal services, unauthorized work and patchwork, unauthorized rental of real estate, use of social property for personal gain (i.e., unauthorized work making use of company equipment),

gains from the infringement of customs and exchange law, tax fraud by craftsmen and retailers, gains from consumer harm, real estate speculation, theft of public property, corruption, fraud, and embezzlement. Research at the time left out activities that are commonly referred to as "moonlighting" today. As there was no extensive income tax, no tax was paid on these special forms of income. Their untaxed sums were not illegal and their extent, in turn, was unknown. In addition, underground trading and the interest on lending between households was left out of estimates. This was later estimated for the first time in the Consumer Price Index. (Ékes, 1995)

6. The hidden economy after the regime change in Hungary

In post-socialist countries, where the shortage economy gradually became a market economy, analysing and quantifying the hidden economy became an important task on the one hand because of the growing budget deficit and on the other hand because official statistics revealed large-scale production declines that were difficult to accept without estimates of the hidden economy's size. (Lackó, 1995)

The growth of the hidden economy during this period is essentially attributable to the following. (Ékes, 1995)

1. Transitioning a country's economy from one type of regulatory system to another is a formidable task. To do so, a new legal environment must be established that conflicts with the policies, regulations, and laws of the past. As a result, the entire period of transition is fraught with conflicting legislation and filled with situations that are not legally covered, meaning the existence of many loopholes.
2. Another circumstance that contributed to the expansion of the hidden economy was the spread of the private sphere. One of the fundamental conditions for the growth of the hidden economy is the possibility to conceal income. The more direct the buyer-seller or employer-employee relationships are, the easier this is. The proliferation of small organizations helps this process. In an organization consisting of a few individuals, all forms of income concealment are much simpler than in a large one; where the owner is the manager and the chief accountant as well as the cashier, the necessary controls are not in place.
3. Finally, there is a strange duality that prevails in the income distribution system, which also contributes to the spread of the hidden economy. With the exception of certain sectors - banking, some businesses, etc - wages based on the consensus of socialism are still common in the economy to this day. Meanwhile, other forms of distribution are seeking to become market-economy conforming (taxation, elimination of consumer price supports, introduction of principles regarding Social Security benefits, etc). The end result is widespread poverty, which contributes to hidden economic activity.

Semjén and Tóth (Semjén & Tóth, 2004) explained the growing importance of the hidden economy in the first phase of the economic transition at a time of transformation crisis as follows: a major economic downturn, limited resources for tax auditing and the initially low effectiveness of the auditing, the underdevelopment of market institutions, and the breakdown of contractual relationships.

After the regime change, the most typical forms, methods, and techniques used by economic agents in order to maximize their entrepreneurial income and employee compensation while at the same time minimizing tax, social security, and other obligations incumbent on them include: omitting a portion of revenue from the register; recognizing non-incurred material production costs among expenditures; including an excessive portion of personal household maintenance costs among production costs; the use or purchase of vehicles; organizing business and study trips abroad; allowances charged to representation and advertising expenses; finder's fee; purchase discounts; extra benefits for foreign businesses; end-of-year depreciation or 'transfer' of inventories; wages of registered employees paid out of pocket; employment of unreported employees; barter transactions for products or services that are not of equal value; parallel company formation; economic activity of unincorporated individuals and the income generated thereby. (Belyó, 1995)

In the years following the transformational downturn of the economic transition however, economic recovery fundamentally changed the behaviour of economic agents (government, businesses, households). Former incentives to participate in the hidden economy weakened and became obsolete, and at the same time, the tax audits became more effective as well. Accordingly, the behaviour of entrepreneurs and households in relation to the hidden economy changed, the importance of the hidden economy began to decline, and breaches of contractual obligations and violations of tax and financial discipline reduced in the Hungarian corporate sector (Semjén & Tóth, 2004).

In the years following the crisis of 2008, the problem of the shadow economy became once again more acute, especially for countries in transition, which still to this day face many structural imbalances inherited from the period of the planned economy. After all, the shadow economy reduces the amount of budgetary resources available to implement anti-crisis measures. (Fedajev & Arsić, 2017)

Most sources estimate the size of the Hungarian hidden economy at 20-25%. According to the study mentioned in the introduction, the hidden economy amounted to between 22% and 25% of Hungary's GDP between 2003 and 2013. (Schneider, 2016) It is not entirely comparable with the above, but it is important from a statistical economics point of view that the HCSO also uses estimates in its GDP calculations for activities and incomes that are declared below their true value or not registered at all. According to the estimation of the HCSO, they amounted to 15.3 percent of GDP in 2002 and 14.9 percent of GDP in 2005. (Balogh, 2014)

Belyó's 2016 research also fits in with the data below (Table 2). According to this, in Hungary, the proportion of the hidden economy in relation to the GDP did not change between 2010 and 2016. However, this does not mean that the size of the hidden economy is stagnant. While official GDP continued to grow between 2010 and 2019, the size of the hidden economy declined in the first years of 2010 and then started to grow strongly from 2014 onwards. This also means that the hidden economy is a decisive component of GDP growth during this period.

Table 2: The size of the official GDP and the hidden economy (2017 estimate)

Year	Official GDP (millions HUF)	Estimated value of hidden economic activities (millions HUF)	Growth of the hidden economy (2010 = 100%)	Proportion of the hidden economy in relation to the official GDP (%)
2010	27 051 695	4 057 754		15
2011	28 133 826	3 938 736	-2.93	14
2012	28 627 889	4 007 904	-1.23	14
2013	30 065 005	3 908 451	-3.68	13
2014	32 179 666	4 183 357	3.10	13
2015	33 712 000	4 382 560	8.00	13
2016	35 194 000	4 575 220	12.75	13
2017	37 299 000	4 848 870	19.50	13

Source: Edited by authors based on Belyó, 2016

7. Actions taken to uncover the hidden economy in Hungary

The legalization of the hidden economy requires the implementation of complex instruments of economic policy. However, a successful package of measures cannot be conceived without a clear political will since for each measure infringing upon the interests of a particular group, the lobbyists of said group are able to repeatedly prevent the technically justified actions. It is important that only enforceable rules are introduced. Restrictive measures alone cannot succeed unless at the same time measures that shape the economic environment are taken and are clearly welcomed by honest businesses. (Belyó, 1995)

The changes proposed by Belyó (1995) prior to the turn of the millennium have been implemented almost one after another ever since: the system of the average tax institution; regulation of

entrepreneurial cash flow; legalization of the declaration of assets; auditing of certain international financial operations; introduction of a company register; modification of the tax burden; adjusting the amount of the Social Security contribution; limiting the scope for black market trade.
According to the research of Eco-Vista (2016), several measures and initiatives have taken place in Hungary to promote the legal economy. This includes, for example, the establishment of the Hungarian Unified Labour Database (EMMA) after the country's accession to the EU. Labor inspections, which have already had quantifiable results, especially in the construction industry, have significantly increased. As of January 2008, illegal use of Social Security services is being sifted out. The Hungarian tax authority (today known as NAV in Hungarian) launched a campaign against VAT fraud, which is widespread in a variety of forms. A similar campaign had previously been launched against so-called bogus contracts as well. The modernization of administrative regulations has also begun, e.g. only legitimate companies can participate in public tenders.
Government actions combating the hidden economy can be divided into three groups. (Eco-Vista, 2016)

1. Measures that indirectly influence economic agents' decisions in relation to the hidden economy. These are steps to improve the security of business relationships. They include: predictable taxation, striving for tax rule transparency; establishing and operating efficient, verifiable, inexpensive, and easily accessible company information systems.
2. Another group of measures includes those taken directly to suppress the hidden economy. These include increasing the frequency of tax audits and the budget of audit apparatuses. Further, this includes increasing the effectiveness of audits but also rendering penalties more severe and determining optimal tax rates.
3. The third group may be formed from the measures that strengthen tax compliance and increase the moral costs related to tax evasion. Auditing, or the possibility thereof, and penalties are strong deterrents helping to reduce participation in the hidden economy. This is the reason why it is worth creating and maintaining a tax collection and auditing system with a modern infrastructure that is predictable and transparent. However, the maintenance of the control apparatus, the imposition of sanctions and their related penalties related to sanctions entails significant costs for taxpayers. These costs cannot be increased arbitrarily: after reaching a certain level within the hidden economy, it is no longer worth pumping more money into the auditing and sanctioning apparatus because the marginal yield of increasing activity will be negative.

8. The actions introduced in Hungary in recent years and their effect on uncovering the hidden economy

- *The temporary employment booklet (AM booklet)*
  A 2008 study looked at the impact of introducing the temporary employment booklet to uncover and suppress certain forms of unreported employment and the impact of introducing the simplified entrepreneurial tax (EVA) to improve the tax discipline of small businesses. According to the results of the research, the vast majority of AM booklet users (79%) committed fraud to some extent in their use of the booklet. The most typical way to do this is not to register part of one's working day and affix a smaller denomination stamp (generally the smallest, 400 HUF). Hidden employment through such fraudulence was most characteristic of the construction industry, with a slightly better result in the hospitality and trade sectors. However, it was generally found that in all sectors the AM booklet was working towards promoting the legal economy; typically, entirely illegal employment became semi-legal. (Fazekas & Semjén, 2008)
- *The simplified entrepreneurial tax (EVA)*
  With the introduction of the simplified entrepreneurial tax (EVA) on January 1, 2003, the government was aiming to reduce the administrative and tax burden on micro and small businesses, thereby increasing their economic activity and reducing their competitive disadvantage compared to larger enterprises. On the fiscal side, the aim was to improve tax

compliance, increase revenues and make tax policy more transparent. According to one study, the clear effect of EVA is that it has reduced the amount of tax evasion among those who converted to it and the so-called "exaggerated expense deduction" and "invoice production / purchase" have been practically eliminated among entrepreneurs who have switched to EVA. (Fazekas & Semjén, 2008)

- *Online cash registers*
  The introduction of online cash registers also served to promote the legal economy. Research in this area found that the retail sector saw a 20-25 percent increase in revenue for the smallest companies as a result of connecting to online cash registers and a 4-6 percent increase for medium-sized companies. Within this, the largest growth was in the consolidated accommodation and hospitality sector, with reported sales having increased by about 32-37 percent. (Lovics, et al., 2019)
- *Electronic Trade and Transport Control System (EKÁER)*
  EKÁER is a technical system for monitoring, controlling and registering the movement of goods, created and operated by the Hungarian National Tax and Customs Board. Its primary objective is to reduce the amount of abuses related to the transport of goods as well as VAT fraud. The system covers transactions between Member States as well as movements of goods for sale to the first domestic, non-final user. It also includes prior electronic filing with tax authorities of these statutory data and the reporting of delivery. This can indirectly lead to the elimination of the hidden economy, since by knowing the actual movement of the goods, the legal fate of the products supplied can also be verified by the combined use of NAV and HU-GO (a traffic monitoring camera system installed on the Hungarian road system, which tracks the movement of road toll vehicles and compiles a database of the information obtained since 2013). These two digital systems make it possible to significantly reduce the volume of goods traded without being taxed, as the only goods that can legally reach the market by road transport are those which have been duly reported in advance. This instrument indirectly protects honest market players and customers acting in good faith, improves equality of public burden sharing, and helps to substantiate government statistics and ensure sound economic policy planning. (Szilovics, 2019)
- *The connection of vending machines to the tax office*
  By the end of August 2019, all vending machines had to be connected to the tax office. The Ministry of Finance estimates that the current registration requirement may have a positive impact on tax compliance. In fact, NAV risk analysts can even compare this year's entrepreneurial income data with the traffic data that will arrive online at the tax office, and in the event of a large discrepancy, risk analysts pass the data collected to the auditors for further investigation.

9. Conclusion

Examining the hidden economy is a complex task from several aspects. The precise definition of the concept of the hidden economy also created a general specialized literature. The characteristics of the hidden economy in Hungary are worth examining before and after the change of regime. The scale of the tax system was not particularly prominent in the earlier period. Later, in the second section several factors influenced the processes. Privatization, liberalization, trans nationalization and the EU-accession also affected the state of the hidden economy. Today, uncovering (whitening) the economy is the dominant trend of the economic policy. The general attitude of society towards economic issues and economic development is also decisive factor to deal with in the future. At this point, the problem is also linked to the field of new institutional economics.

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THE COMPLIANCE OF THE ROMANIAN LISTED COMPANIES WITH THE PRINCIPLES AND PROVISIONS OF THE CORPORATE GOVERNANCE CODE

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Abstract
Starting from the research assumption that the Corporate Governance Code issued by Bucharest Stock Exchange (BSE) aims at building an internationally attractive capital market in Romania, based on best practices, transparency and trust that encourages companies to build a strong relationship with their shareholders and other stakeholders, communicate effectively and transparently and show openness towards all potential investors, in this paper we would like to present the degree of compliance of the companies listed on the Bucharest Stock Exchange with the principles and provisions of the Corporate Governance Code. The aim of this paper is achieved by presenting and commenting on the principles issued by the BSE regarding the corporate governance and by analysing the Corporate Governance Reports of the companies, presenting at the same time the compliance of the listed companies with these principles and provisions, by using the data issued in 2018 by the entities included in our study, namely the listed companies on the main market of the Bucharest Stock Exchange. Our analysis reflects that, although the provisions and principles of the Corporate Governance Code are not mandatory for the listed companies, they are largely implemented in the activity of companies because an efficient corporate governance system can represent a competitive advantage for any economic entity in the context of globalisation.

Keywords: *comply, corporate, disclosure, explain, governance*

Track: *corporate governance*

Word count: *4.825*

1. Introduction

Corporate governance is defined in the international literature (OECD, 2015) as the set of relationships between a company's management and its stakeholders. The first definition of the concept dates back to 1992 and presents corporate governance as the set of rules by which companies are directed and controlled. (Cadbury Report, 1992).

The Organisation for Economic Cooperation and Development (OECD) is one of the organisations that have been particularly involved in the implementation of certain provisions, structures and mechanisms of corporate governance, the developed principles being guidelines, rules of good practice for the organisation of companies and their way of reporting relationships with third parties (O. Jula, 2017). An essential feature of the Corporate Governance Codes is that they are implemented on the basis of the "Comply or Explain" principle which discloses to the market clear, accurate and up-to-date information regarding the compliance of the listed companies with the corporate governance rules.

In other words, a good corporate governance can be translated through efficient rules, policies and procedures of business management, administration and control. It is essential for companies that want to reduce operational and financial risks, increase performance, open towards new markets

and add more value to the relationship with their current and potential investors (Fulop. M, *et al*.2015).

In Romania, the concept of corporate governance appeared at the beginning of the 2000s, being initially governed by the Code of Management and Administration of the Bucharest Stock Exchange. (Apostol C.,2015).

According to BSE (2015), the purpose of the Corporate Governance Code is to create in Romania an internationally attractive capital market, based on best practices, transparency and trust. To achieve these goals, listed entities must comply to a great extent with the principles and provisions elaborated by the Bucharest Stock Exchange.

Researchers such as Vintilă G. and Moscu R. (2014) studied the level of compliance for 55 entities listed on the BSE in 2013 and found that the degree of compliance with the Code of Corporate Governance of BSE is achieved at a rate of 70.6%, the lowest score is based on a result of 21.1% and the highest is 92.3%. Rose C. (2016) investigates the degree of Danish firm adherence to the Danish Code of Corporate Governance and analyzes whether a higher degree of comply or explain disclosure is related to firm performance. His analysis shows that there is a positive link between Return on Equity / Return on Assets and Danish firm total corporate governance comply or explain disclosure scores. In their study Madanoglua M *et al*. (2018) defends the view that the adoption of corporate governance provisions should not be seen as a detriment to firms' financial performance. Using a set-theoretic method, such as the Qualitative Comparative Analysis (QCA), his findings revealed that there are three configurations of governance provisions that lead to superior financial performance.

The purpose of this study is to present the results of an analysis carried out on the companies listed on the main market of the Bucharest Stock Exchange in order to measure their degree of compliance with the principles and provisions of the Corporate Governance Code developed by the BSE in relation to the aspects regarding the responsibilities of the Board of Directors in the case of the individually managed companies or of the Supervisory Board / Directorate in the dualistic system, the risk management system and the internal control, the fair reward and motivation of the members of these boards and the value added through the relationship with the current and potential investors.

2. Methodology

In this paper we aim to measure the degree to which the companies listed on the Bucharest Stock Exchange (BSE) comply with the provisions and principles of the Corporate Governance Code developed by the BSE with regard to the responsibilities of the management, the risk management system and the internal control, the fair reward and motivation of the members of the Board of Directors or the Supervisory Board and the added value created through the relationship with the current and potential investors.

By means of the corporate governance statement, included in the Annual Report in a separate section, the listed companies perform a self-assessment of how “the provisions to be observed” are met and outline the measures taken to comply with the aspects that are not fully met. The research methodology used, the observation, was based mainly on *the analysis of the Annual Reports* and of the *Comply or Explain* Statement published by the entities analysed in 2018. Out of the 87 companies included in the Monthly Bulletin drawn up by the BSE in December 2018, a document presenting the main stock market indicators of the listed companies, we excluded from our analysis the companies that incurred losses in 2018 and those that did not draw up the Comply or explain statement (the main source of our data), thus keeping a number of 61 companies.

According to the Corporate Governance Code (BSE, 2015), the provisions and principles to be observed by the listed companies are structured in four sections, as follows:

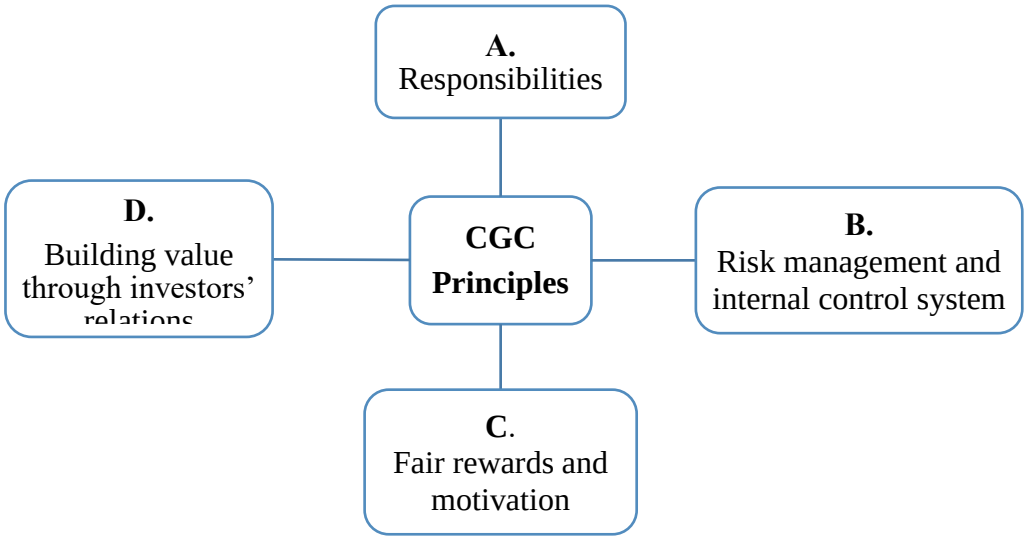

Figure 1: Sections of Corporate Governance Code
Source: own projection after BSE

Table 1: Corporate Governance principles and provisions	
Section A – Responsibilities	
A.1.	All companies should have internal regulation of the Board which includes terms of reference/responsibilities for Board and key management functions of the company, applying, among others, the General Principles of Section A.
A.2.	Provisions for the management of conflict of interest should be included in Board regulation.
A.3.	The Board of Directors or the Supervisory Board should have at least five members.
A.4.	The majority of the members of the Board of Directors should be non-executive. At least one member of the Board of Directors or Supervisory Board should be independent, in the case of Standard Tier companies. Not less than two non-executive members of the Board of Directors or Supervisory Board should be independent, in the case of Premium Tier Companies.
A.5.	A Board member's other relatively permanent professional commitments and engagements, including executive and non-executive Board positions in companies and not-for-profit institutions, should be disclosed to shareholders and to potential investors before appointment and during his/her mandate.
A.6.	Any member of the Board should submit to the Board, information on any relationship with a shareholder who holds directly or indirectly, shares representing more than 5% of all voting rights. This obligation concerns any kind of relationship which may affect the position of the member on issues decided by the Board.
A.7.	The company should appoint a Board secretary responsible for supporting the work of the Board.
A.8.	The corporate governance statement should inform on whether an evaluation of the Board has taken place under the leadership of the chairman or the nomination committee and, if it has, summarize key action points and changes resulting from it. The company should have a policy/guidance regarding the evaluation of the Board containing the purpose, criteria and frequency of the evaluation process.
A.9.	The corporate governance statement should contain information on the number of meetings of the Board and the committees during the past year, attendance by

Table 1: Corporate Governance principles and provisions	
	directors (in person and in absentia) and a report of the Board and committees on their activities.
A.10.	The corporate governance statement should contain information on the precise number of the independent members of the Board of Directors or of the Supervisory Board.
Section B - Risk management and internal control system	
B.1.	The Board should set up an audit committee, and at least one member should be an independent non-executive. The majority of members, including the chairman, should have proven an adequate qualification relevant to the functions and responsibilities of the committee. At least one member of the audit committee should have proven and adequate auditing or accounting experience. In the case of Premium Tier companies, the audit committee should be composed of at least three members and the majority of the audit committee should be independent.
B.2.	The audit committee should be chaired by an independent non-executive member.
B.3.	Among its responsibilities, the audit committee should undertake an annual assessment of the system of internal control.
B.4.	The assessment should consider the effectiveness and scope of the internal audit function, the adequacy of risk management and internal control reports to the audit committee of the Board, management's responsiveness and effectiveness in dealing with identified internal control failings or weaknesses and their submission of relevant reports to the Board.
B.5.	The audit committee should review conflicts of interests in transactions of the company and its subsidiaries with related parties.
B.6.	The audit committee should evaluate the efficiency of the internal control system and risk management system.
B.7.	The audit committee should monitor the application of statutory and generally accepted standards of internal auditing. The audit committee should receive and evaluate the reports of the internal audit team.
B.8.	Whenever the Code mentions reviews or analysis to be exercised by the Audit Committee, these should be followed by cyclical (at least annual), or ad-hoc reports to be submitted to the Board afterwards.
B.9.	No shareholder may be given undue preference over other shareholders with regard to transactions and agreements made by the company with shareholders and their related parties.
B.10.	The Board should adopt a policy ensuring that any transaction of the company with any of the companies with which it has close relations, that is equal to or more than 5% of the net assets of the company (as stated in the latest financial report), should be approved by the Board following an obligatory opinion of the Board's audit committee, and fairly disclosed to the shareholders and potential investors, to the extent that such transactions fall under the category of events subject to disclosure requirements.
B.11.	The internal audits should be carried out by a separate structural division (internal audit department) within the company or by retaining an independent third-party entity.
B.12.	To ensure the fulfillment of the core functions of the internal audit department, it should report functionally to the Board via the audit committee. For administrative purposes and in the scope related to the obligations of the management to monitor and mitigate risks, it should report directly to the chief executive officer.

Table 1: Corporate Governance principles and provisions	
Section C - Fair rewards and motivation	
C.1	The company should publish a remuneration policy on its website and include in its annual report a remuneration statement on the implementation of this policy during the annual period under review.
Section D - Building value through investors' relations	
D.1.	The company should have an Investor Relations function - indicated, by person (s) responsible or an organizational unit, to the general public. In addition to information required by legal provisions, the company should include on its corporate website a dedicated Investor Relations section, both in Romanian and English, with all relevant information of interest for investors
D.2.	A company should have an annual cash distribution or dividend policy, proposed by the CEO or the Management Board and adopted by the Board, as a set of directions the company intends to follow regarding the distribution of net profit. The annual cash distribution or dividend policy principles should be published on the corporate website.
D.3.	A company should have adopted a policy with respect to forecasts, whether they are distributed or not. Forecasts means the quantified conclusions of studies aimed at determining the total impact of a list of factors related to a future period (so called assumptions): by nature such a task is based upon a high level of uncertainty, with results sometimes significantly differing from forecasts initially presented. The policy should provide for the frequency, period envisaged, and content of forecasts. Forecasts, if published, may only be part of annual, semi-annual or quarterly reports. The forecast policy should be published on the corporate website
D.4.	The rules of general meetings of shareholders should not restrict the participation of shareholders in general meetings and the exercising of their rights. Amendments of the rules should take effect, at the earliest, as of the next general meeting of shareholders.
D.5.	The external auditors should attend the shareholders' meetings when their reports are presented there.
D.6.	The Board should present to the annual general meeting of shareholders a brief assessment of the internal controls and significant risk management system, as well as opinions on issues subject to resolution at the general meeting.
D.7.	Any professional, consultant, expert or financial analyst may participate in the shareholders' meeting upon prior invitation from the Chairman of the Board. Accredited journalists may also participate in the general meeting of shareholders, unless the Chairman of the Board decides otherwise
D.8.	The quarterly and semi-annual financial reports should include information in both Romanian and English regarding the key drivers influencing the change in sales, operating profit, net profit and other relevant financial indicators, both on quarter-on-quarter and year-on-year terms.
D.9.	A company should organize at least two meetings/conference calls with analysts and investors each year. The information presented on these occasions should be published in the IR section of the company website at the time of the meetings/ conference calls.
D.10.	If a company supports various forms of artistic and cultural expression, sport activities, educational or scientific activities, and considers the resulting impact on the innovativeness and competitiveness of the company part of its business mission and development strategy, it should publish the policy guiding its activity in this area.

Source: BSE Corporate Governance Code

For the entities included in our study we used a scoring system that reflects the extent to which they comply with the provisions and principles presented above, thus transforming the enunciative data into numerical, quantitative data. Taking into account the fact that in the Comply or explain statement the companies have three options through a self-assessment that reflects the full compliance, partial compliance or non-compliance, the following table reflects the scoring system used according to the response published by the studied companies:

Table 2: Conformity marks

Conformity mark	Significance
3	Full compliance with the principles and provisions
1	Partial compliance
0	Non-compliance

Source: author's own projection

Considering the 4 sections of the Code and the proposed scoring system, for section A a company can obtain a maximum of 30 points, for section B a maximum of 36 points, for section C, 3 points and for section D a maximum of 30 points. In total, a company can sum up 99 points, which reflects total compliance in all sections of the Corporate Governance Code. For the studied companies, the maximum score that can be reached is 6,039 points.

3. Results and discussions

The analysis of the Comply or explain statement made for each of the 61 entities studied in accordance with the scoring system, highlights the following level of conformity with the Code's provisions and principles:

Tabel 3: Level of conformity with the Code s provisions

Category	Maximum score	Obtain results	Comply assessment (%*maximum score)
Total CGC score	6.039	4.706	78%
Section A score	1.830	1.487	81%
Section B score	2.196	1.690	77%
Section C score	183	100	55%
Section D score	1.830	1.429	78%

Source: author's own projection

From the analysis carried out we can see that the studied entities comply to a great extent with the provisions of the Corporate Governance Code. The lowest result was obtained in section C, which refers to the remuneration policy which must be based on the fair reward and motivation for the members of the Council and for the CEO or the members of the Directorate. 45% of the studied entities do not publish the remuneration policy on the companies website and do not include information on its implementation in the Annual report.
The section analysis of the level of compliance with the provisions and principles of the Code reflects the following:

Table 4: Descriptive statistics for section A

Section A – conformity score	
Mean	24.3770
Standard Error	0.8772
Median	27
Mode	30

Table 4: Descriptive statistics for section A	
Standard Deviation	6.8511
Sample Variance	46.9387
Kurtosis	1.2300
Skewness	-1.4614
Range	27
Minimum	3
Maximum	30
Sum	1487
Count	61

Source: own projection

The mean of the scores obtained in section A is 24.38, with the median 27 and the mode 30. The lowest score obtained is 3, which reveals that out of the 61 companies under study some do not comply with the provisions of the Governance Code in terms of the existence of an internal operating regulation for the specialised committees or the composition, the independence and the quality of non-executive members of the Board of Directors is not compliant with the requirements of the Code, there being no clear distinction between executive and non-executive members of the Board of Directors. The highest score and the maximum of the section, the value 30, is obtained by companies that fully comply with the provisions of the code in terms of the responsibilities of the Board. Within this section, the model's amplitude is 27 and it reflects the difference between the maximum and the minimum score obtained by the companies under study.

Graphically, the results obtained by the studied entities regarding the level of compliance with the provisions of section A are reflected as follows:

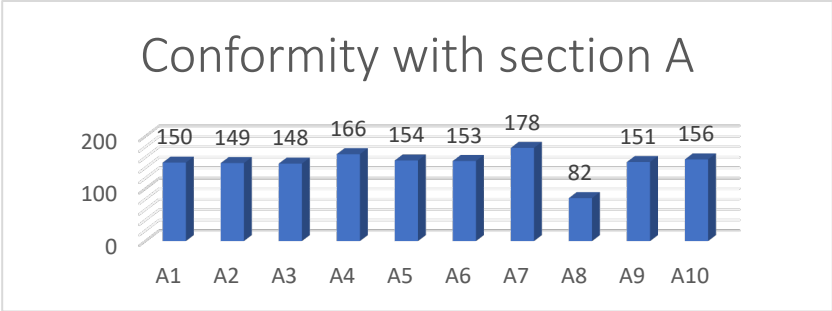

Figure 2: Conformity with section A
Source: own projection

From the previous figure we can see that out of the total of 183 points per section (full compliance of all the entities/section), the studied companies are approaching to this value, which means a satisfactory level of compliance with the provisions of the code. In a single section, A8, the results are below average, because most of the companies do not have a policy to evaluate the Council that reflects the purpose, the criteria and the frequency of the evaluation process.

Table 5: Descriptive statistics for section B	
Section B – conformity score	
Mean	27.7049
Standard Error	1.4597

Table 5: Descriptive statistics for section B	
Median	33
Mode	36
Standard Deviation	11.4007
Sample Variance	129.9781
Kurtosis	-0.0523
Skewness	-1.2091
Range	36
Minimum	0
Maximum	36
Sum	1690
Count	61

Source: own projection

The mean of the scores obtained in section B is 27.70, with the median 33 and the mode 36. The lowest score obtained is 0 which reveals that out of the 61 companies under study some do not comply with the provisions of the Governance Code in terms of establishing the Audit Committee to periodically examine the efficiency of the financial reporting, of the internal control and of the risk management system. Moreover, the companies neither comply with the principles of governance in terms of the independence and the non-executive independent member status for at least one person within the structure. The highest score and the maximum of the section, the value 36, is obtained by companies that fully comply with the provisions of the code. Within this section, the model's amplitude is 36 and it reflects the difference between the maximum and the minimum score obtained by the companies under study.

Graphically, the results obtained by the studied entities regarding the level of compliance with the provisions of section B are reflected as follows:

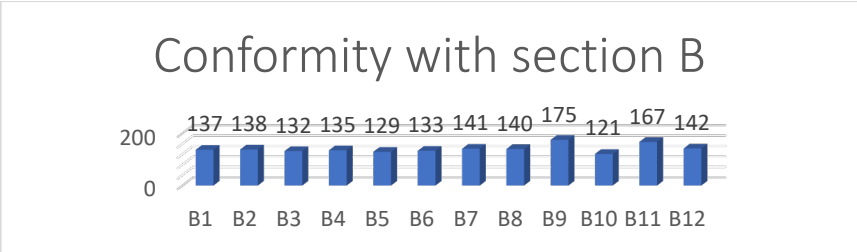

Figure 3: Conformity with section B
Source: own projection

From the previous figure we can see that out of the total of 183 points per section (full compliance of all the entities/section), most entities obtain a score above average, which means a satisfactory level of compliance with the provisions of the code.

Table 6: Descriptive statistics for section C	
Section C – conformity score	
Mean	1.6393
Standard Error	0.1734
Median	1

Table 6: Descriptive statistics for section C	
Mode	3
Standard Deviation	1.3544
Sample Variance	1.8344
Kurtosis	-1.8489
Skewness	-0.0974
Range	3
Minimum	0
Maximum	3
Sum	100
Count	61

Source: own projection

The mean of the scores obtained in section C is 1.63, with the median 1 and the mode 3. The lowest score obtained is 0 which reveals that out of the 61 companies under study some do not comply with the provisions of the Governance Code regarding the publication of the principles and arguments underlying the remuneration policy of the members of the Board of Directors or of the members of the Directorate. The highest score and the maximum of the section, the value 3, is obtained by companies that fully comply with the provisions of the code. Within this section, the model's amplitude is 3 and it reflects the difference between the maximum and the minimum score obtained by the companies under study.

Graphically, the results obtained by the studied entities regarding the level of compliance with the provisions of section C are reflected as follows:

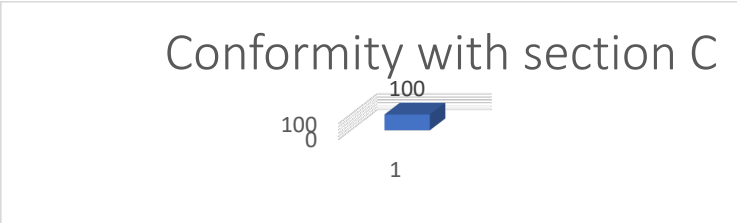

Figure 4: Conformity with section C
Source: own projection

In section C there is only one provision that must be respected by the listed entities which refers to the fair reward and motivation regarding the remuneration policy of the members of the Council and of the CEO, as well as of the members of the Directorate in the dualistic system. The results obtained reflect the above average compliance of the entities with the provisions of the code.

Table 7: Descriptive statistics for section D	
Section D – conformity score	
Mean	23.4262
Standard Error	0.7601
Median	24
Mode	30
Standard Deviation	5.9370

Table 7: Descriptive statistics for section D	
Sample Variance	35.2486
Kurtosis	0.9501
Skewness	-0.9955
Range	25
Minimum	5
Maximum	30
Sum	1429
Count	61

Source: own projection

The mean of the scores obtained in section D is 23.43, with the median 24 and the mode 30. The lowest score obtained is 5 which reveals that out of the 61 companies under study some do not comply with the provisions of the Governance Code regarding the organization of the investor relations service, the annual dividend distribution policy, forecasts, the participation of external auditors at the General Shareholders' Meetings when their reports appear on the agenda of the meetings, key factors influencing the development as well as publishing on the company's website the information presented during the annual meetings with analysts and investors. The highest score and the maximum of the section, the value 30, is obtained by companies that fully comply with the provisions of the code. Within this section, the model's amplitude is 25 and it reflects the difference between the maximum and the minimum score obtained by the companies under study.

Graphically, the results obtained by the studied entities regarding the level of compliance with the provisions of section D are reflected as follows:

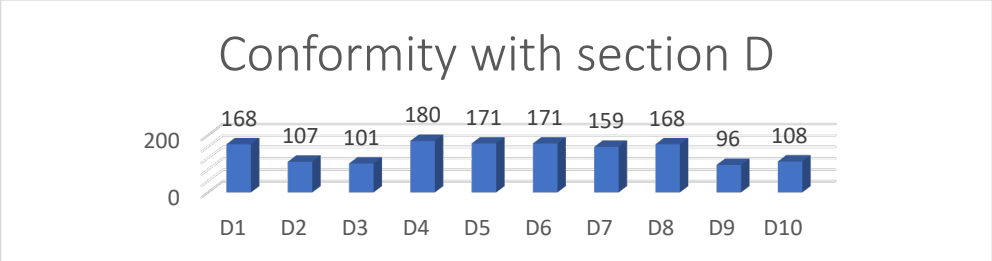

Figure 5: Conformity with section D
Source: own projection

From the previous figure we can see that out of the total of 183 points per section (full compliance of all the entities/section), most entities score above average, which means a satisfactory level of compliance with the provisions of the code. Only one provision, D9, records a lower score, respectively the one that states that a company should organize at least two meetings/conference calls with analysts and investors each year and the information presented on these occasions should be published in the IR section of the company website.

From a global perspective, the level of compliance with the provisions and principles of the code of the 61 studied entities is presented as follows:

Table 8: Descriptive statistics for total Corporate Governance score	
Total CGC score	
Mean	77.1475
Standard Error	2.9027

Median	86
Mode	93
Standard Deviation	22.6714
Sample Variance	513.9945
Kurtosis	0.5692
Skewness	-1.2484
Range	87
Minimum	12
Maximum	99
Sum	4706
Count	61

Source: own projection

The total mean of the scores obtained is 77.14 points out of a total of 99 points / entity with the median 86 and the mode 93. The lowest score obtained is 12 which reveals that out of the 61 companies under study there are entities that comply to a very low extent with the provisions of the Governance Code on the 4 sections, respectively regarding the responsibilities of the management, the risk management system and the internal control, the just reward and motivation of the members of the Board of Directors or Supervision and the added value created through the relationship with current and potential investors. The highest score, the maximum, the value 99, is obtained by companies that fully comply with the provisions of the code. Within this section, the model's amplitude is 87 and it reflects the difference between the maximum and the minimum score obtained by the companies under study.

In a general approach, we can state that the scores obtained by the companies included in the research reflect a high degree of compliance with the principles of corporate governance.

4. Conclusions

This study has focused on the compliance of the listed entities on Main Market of the Bucharest Stock Exchange with the Corporate Governance Code principles and provisions.

After processing and analysing the data collected from the Comply or Explain Statement published by the listed entities included in the study, we can outline the following aspects regarding the degree of compliance with the principles of corporate governance:

- The Comply or Explain statement reflects the extent to which the corporate governance rules are observed by the listed entities through a self-assessment that reflects the full compliance, partial compliance or non-compliance with the provisions of the Code. The statement can be included in the Annual Report or can be presented separately;
- The implementation of the provisions and principles of the governance code ensures transparency, trust for both current and potential investors, as well as the fair treatment of shareholders in relation to the access to information because the statement describes the aspects regarding the administration and the control of the company;
- We may notice the companies' favourable perception on the need to adopt the principles of corporate governance;
- As a consequence, we consider that the companies under study show a high degree of compliance with the principles of corporate governance developed by the BSE, thus understanding that good corporate governance can ensure the sustainable development of the company.

The contribution of the current study is to provide information regarding Corporate governance in Romania and the degree of compliance with the principles and provisions of the listed entities. Our

main research tool, the corporate governance index, calculated after a framework proposed by the authors for 61 listed entities in Romania reflects a high degree of compliance. We believe that the ease of access to additional funds, the increase of transparency in reporting, the sustainable development in the context of globalisation and the increase of the market value of the company are the benefits of an efficient corporate governance system that can represent a competitive advantage to any economic entity.

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THE DETERMINANTS OF CORPORATE GOVERNANCE DISCLOSURE LEVEL IN THE INTEGRATED REPORTING CONTEXT

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Abstract
In recent years, the analysis of corporate governance aspects is becoming a central element for understanding corporate dynamics and represents a clear indicator of investor confidence in the decisions taken by the management and board of listed firms. For this reason, corporate governance disclosure is receiving more and more attention from both a professional and academic point of view. The advent of integrated reporting represents a new tool for disclosing information relating to corporate governance. The goal of this study is to investigate the factors that can influence the level of corporate governance disclosure within the integrated reports. The analysis, conducted on a sample of 73 international firms, shows a positive effect of the firm size, firm profitability and audit quality. To our knowledge, this is the first study that analyses corporate governance disclosure level in the integrated reporting context.

Keywords: *corporate governance; disclosure; integrated reporting; information quality*

Track: *Governance*

Word Count: *3.623*

1. Introduction
In recent years, the analysis of corporate governance aspects is becoming a central element for understanding corporate dynamics and represents a clear indicator of investor confidence in the decisions taken by the management and board of listed firms. Since the early 1990s, the number of codes of corporate good governance has grown considerably to become an important criterion for assessing the level of transparency of companies and business compliance practices (Gandia, 2008).
The recent financial scandals that have hit European and US companies have clearly shown the need for firms to adopt recommendations (Ben-Amar & Boujenoui, 2006). In this regard, the regulatory agencies of various countries have set up special task forces in order to devise these recommendations and publish codes for best practices for corporate governance of listed firms (Aguilera & Cuervo-Cazurra, 2004; Broshko & Li, 2006; Collett & Hrasky, 2005; Cuervo-Cazurra & Aguilera, 2004; Li & Broshko, 2006). Therefore, as underlined in the Global Investor Opinion Survey, corporate governance represents an important criterion in investment decisions (McKinsey & Company, 2002). In fact, in their investment decisions, investors place greater trust in companies with good corporate governance (Gandia, 2008). In fact, the information relating to corporate governance allows investors to better determine the future performance of companies (Bhat et al., 2006). Therefore, in this perspective, the attention that capital markets devote to governance aspects should push companies to provide high quality information in order to increase their level of transparency (Ben-Amar & Boujenoui, 2006; Gandia, 2008).
The greater attention to information related to corporate governance is visible not only by the recent rules and regulations of world stock exchanges (Gandia, 2008), but also by the requirements of the entities that define international disclosure standards. In this regard, the International Integrated Reporting Council (IIRC) in the development of integrated reporting (IR) has provided an important focus on aspects related to corporate governance (Vitolla et al., 2019a; 2019b; 2019c; Raimo et al., 2019). It represents the last frontier of corporate disclosure and combines financial

and non-financial information in a single report (Vitolla et al., 2018; Vitolla & Raimo, 2018). Integrated reporting has also gained considerable importance from a professional point of view (IFAC, 2016; 2017; KPMG, 2016). With reference to corporate governance, integrated reporting aims to clearly show how it supports the company's ability to create value over time (IIRC, 2013). The corporate governance disclosure literature focused mainly on identifying the information that companies should provide and on the effects of this information (Gandia, 2008). An aspect not yet explored is represented by the analysis of factors capable of influencing the quality of corporate governance disclosure of companies. In this regard, the few studies in the literature have analysed the determinants of corporate governance information through a content analysis of annual reports and websites (Collett & Hrasky, 2005; Samaha et al., 2012; Gandia, 2008) or in alternative through the use of ratings (Ben-Amar & Boujenoui, 2006; Vander Bauwhede & Willekens, 2008). However, the absence of contributions aimed at analysing the corporate governance disclosure in the integrated reporting context is evident. This study aims to fill this important gap by investigating the factors that can influence the level of corporate governance disclosure contained in the integrated reports..

The remainder of this article is organized as follows: Section 2 analyses the background, Section 3 shows the study's hypotheses. Section 4 presents the methodology while Section 5 shows and discusses the results. The last section draws conclusions.

2. Background

The growing importance of corporate governance is demonstrated by the number of related contributions present in the literature in the field of accounting, management and finance (Bhagat & Black, 2002; Shleifer & Vishny, 1997). Corporate governance can be understood as a set of principles relating to the governance of firms and the way in which these principles are communicated externally (Gandia, 2008). Corporate governance disclosure studies focused primarily on the information that companies should disclose and on the effects of this information (López-Arceiz et al., 2019). Another part of the literature focused on the analysis of the media through which companies should disclose information related to corporate governance (Gandia, 2008; 2011). In fact, according to Bushman et al. (2004) corporate transparency depends on the channels and communication tools chosen by companies, which can hinder or facilitate the flow of information and therefore influence the availability of information from stakeholders. In relation to the different communication channels, past studies have focused on the information contained in the annual reports and websites (Collett & Hrasky, 2005; Samaha et al., 2012; Gandia, 2008). In this regard, Gandia (2008), making a comparison between the two channels, highlighted how companies that use internet as a communication tool present a higher quality corporate governance disclosure. In addition, the author added that the quality of corporate governance disclosure is influenced by the listing age, the presence of analysts, belonging to the communications sector and the visibility of companies.

The advent of integrated reporting provides companies with a new channel for communicating information related to corporate governance. It represents the last frontier of corporate disclosure and shows the interconnections between financial and non-financial information (Vitolla et al., 2019d). In this regard, the IIRC refers to six different types of capital: financial capital, manufactured capital, intellectual capital, human capital, social and relationship capital, and natural capital (Vitolla et al., 2019e). Among non-financial information, integrated reporting presents an important focus on intellectual capital (Vitolla et al., 2019f) and corporate governance, which in fact represents one of the eight content elements identified by the IIRC. The objective of an integrated report is, in fact, to show how an organization's corporate governance favours the creation of value in the short, medium and long term (IIRC, 2013). Therefore, for this purpose, an integrated report should show information relating to the structure of leadership, the components of corporate governance, the specific processes used to make decisions and the measures taken to influence and monitor corporate strategies (IIRC, 2013). In addition, an integrated report should represent the way in which ethics, culture and corporate values are reflected on the use of capital,

and the initiatives undertaken by governance to allow innovation (IIRC, 2013). Finally, it should provide information about the implementation of governance practices that go beyond legal obligations and about the link between remuneration and incentives (IIRC, 2013).
Despite the importance that the IIRC dedicates to aspects relating to corporate governance, in the literature there are no contributions aimed at analysing corporate governance information within the integrated reports. Therefore, this study aims to fill this gap by investigating the level of corporate governance disclosure contained in the integrated reports and by analysing some possible antecedents of this level.

3. Hypotheses development

Firm size: The empirical contributions in the literature show how the firm size represents a variable capable of explaining the political choices of disclosure, and specifically the quality and level of information provided voluntarily (Abdullah et al., 2015; Andrikopoulos et al., 2014; Bhasin et al., 2015; Bujaki & McConomy, 2002; Chow & Wong-Boren, 1987; Cooke, 1991; Depoers, 2000; Eng & Mak, 2003; Frías-Aceituno et al., 2014; Gul & Leung, 2004; Khan, 2010; Meek et al., 1995; Raffournier, 1995; Sharif & Rashid, 2014; Sierra-García et al., 2015). Larger companies are more likely to produce information and also incur lower costs due to economies of scale (Ben-Amar & Boujenoui, 2006; Gandia, 2008). Corporate governance disclosure is fundamental for this type of firms due to the complexity of corporate relationships (Gandia, 2008). A high level of information relating to corporate governance can reduce the monitoring costs of outside shareholders and information asymmetry that is higher in large companies (Eng & Mak, 2003). Furthermore, larger companies are subject to greater public pressure and therefore must provide more information (Marrone & Oliva, 2019; 2020; Vitolla et al., 2019c). The past contributions in the literature, in relation to corporate governance disclosure, have found a positive effect of the firm size on the amount of information provided by companies (Bujaki & McConomy, 2002). Therefore, in light of this, we introduce the following hypothesis:

H1: There is a positive association between the size of the firm and the corporate governance disclosure level.

Firm profitability: Past contributions in the literature have found a positive relationship between firm profitability and voluntary disclosure (Gandia, 2008). In this regard, Haniffa and Cooke (2005) showed that companies that generate high profit levels are very interested in providing information to highlight their performance to stakeholders (Malone et al. 1993; Siregar & Bachtiar, 2010; Udayasankar, 2008; Wallace et al., 1994). Furthermore, according to Singhvi and Desai (1971), greater levels of profitability persuade managers to provide more information in order to demonstrate the capacity of the firm to maximize shareholder value. Profitable firms will be more interested in disseminating information in order to promote a positive image of their performance (Sharif & Rashid, 2014). Finally, profitable firms may choose to publish higher-quality information in order to distinguish themselves from less-successful companies (Frías-Aceituno et al., 2014). In relation to corporate governance disclosure, companies characterized by high profitability levels could be incentivized to provide information in order to show the governance system to the audience (Ben-Amar & Boujenoui, 2006). Therefore, in light of this, we introduce the following hypothesis:

H2: There is a positive association between the profitability of the firm and the corporate governance disclosure level.

Audit quality: According to Jensen and Meckling (1976), external auditors represent an important corporate governance mechanism as they are in charge of providing a fair judgment on the quality of the information provided by the company (Al-Janadi et al., 2013; Barros et al, 2013; Francis et al., 1999). DeAngelo (1981) highlighted how auditor size represents a proxy for audit quality.

Larger audit firms are more likely to provide high quality services to preserve their reputation and avoid losing customers in case of misreporting (Barros et al, 2013). The direct consequence is that large audit firms do not accept pressures related to the disclosure of less accurate and detailed or incomplete information. In this regard, Titman and Trueman (1986) highlighted how the assumption of a large auditing firm signals to stakeholders the quality of the information provided. The contributions in the literature highlighted a positive impact of the size of the auditing firm on the level of voluntary disclosure (Craswell & Taylor, 1992; Debreceny et al., 2002; Inchausti, 1997; Kelton & Yang, 2008; Xiao et al., 2004). Therefore, in light of this, we introduce the following hypothesis:

H3: There is a positive association between the audit quality of the firm and the corporate governance disclosure level.

4. Research methodology

4.1 Sample

The sample of this study is composed of 73 international companies that publish an integrated report. To download these documents, we used the IIRC website. Specifically, we used two different sections of the website: "Leading Practices" and "<IR> Reporters". The presence of the reports on the IIRC website ensures that they have been drawn up in compliance with the <IR> framework. In addition, the alternation of these two sources ensures an adequate level of balance for the sample. In fact, the "Leading Practices" section contains higher quality reports while the "<IR> Reporters" section presents a list of reports of presumed lower quality. The integrated reports analysed are all related to 2017. The selected companies belong to different countries and operate in different sectors. Normal tests were conducted which demonstrated normal data distribution.

4.2 Variables and model specification

The dependent variable of this study is represented by the corporate governance disclosure level (CGDL) contained in the integrated reports. In order to measure the level of information this study uses a visual content analysis. Through this technique, in fact, we have sought specific information related to corporate governance within the integrated reports. To this end, we first identified a series of items related to corporate governance. For the identification of these items we started with those identified by Gandia (2008). Based on this study, we classified the items into three categories: board of directors, ownership structure and good governance. In relation to the board of directors, we have identified 14 different items. With reference to the ownership structure, we identified 4 items. Finally, with reference to good governance we identified 6 items. Therefore, the total of the identified items is equal to 24. Through a visual content analysis, we verified the presence of these items in each integrated report. We assigned a score of 1 in case of presence of the single item and a score of 0 in case of absence. Therefore, in light of this, the corporate governance disclosure level can assume a maximum score of 24. Table 1 shows the corporate governance disclosure scoring model.

The independent variables of this study are represented by firm size (SIZE), firm profitability (ROE) and audit quality (AUDQ). To measure the firm size (SIZE), we used the natural logarithm of the total assets. Firm profitability (ROE) was measured through return on equity. Finally, audit quality was measured through a dummy variable that equals to 1 if firm's report is certified by at least one "Big Four" accounting firm, and 0 otherwise.

We have also included some control variables. Specifically, we included: financial leverage (LEV), board size (BSIZE), environmental sensitivity (ESEN) and firm age (AGE). Financial leverage (LEV) was calculated as the ratio of the book value of debt over the book value of equity. Board size (BSIZE) was measured as the number of directors on the board. Environmental sensitivity (ESEN) is a dummy variable that assumes a score of 1 if the company operates in a highly polluting sector and 0 otherwise. Firm age (AGE) was measured as the number of years

from the establishment of the firm until the end of 2019.
To test the research hypotheses, this study uses a linear regression model. The following equation summarizes the analysis model:

$$CGDL = \beta_0 + \beta_1 SIZE + \beta_2 ROE + \beta_3 AUDQ + \beta_4 LEV + \beta_5 BSIZE + \beta_6 ESEN + \beta_7 AGE + \varepsilon$$

Table 1: – Corporate governance disclosure scoring model

Area	Total Score of the area
BOARD OF DIRECTORS 1) Board members 2) Board structure 3) Internal rules for organization and functioning 4) Functions and office of each director 5) Selection, de-selection and re-election procedures 6) Conduct rules for directors 7) Board's responsibility for the information disclosed to the markets 8) Relations between directors and major shareholders 9) Interests held by directors in share capital 10) Executive status and independence of directors 11) Independence conditions 12) Professional qualifications of independent directors 13) Offices held by any independent director in other companies 14) Directors' emoluments	14
OWNERSHIP STRUCTURE 1) Breakdown of percentage interests in the firm owned by major shareholders 2) Agreements entered into by the company with its directors and senior executives 3) Operations between the company and major shareholders 4) Treasury stock held by the company and significant variations	4
GOOD GOVERNANCE 1) Good governance criteria 2) Audit fees 3) Fees paid for non-audit services provided by audit firms 4) Disclosure of reports containing ethical principles (e.g. code of ethics or code of conduct) 5) Content of by-laws 6) Opinion of analysts and rating agencies	6
CORPORATE GOVERNANCE DISCLOSURE LEVEL	**24**

5. Results

5.1 Descriptive statistics and correlation analysis

Table 2 shows the descriptive statistics and the correlation analysis. As far as the descriptive statistics are concerned, an interested datum is represented by the average value of the dependent variable represented by the corporate governance disclosure level (CGDL). It has a value of 10.21 which indicates, on average, a low level of corporate governance disclosure level within the integrated reports. As for the correlation matrix, the results show the absence of multicollinearity. In fact, the highest correlation coefficient is 0.437 for AUDQ and CGDL. However, harmful levels of multicollinearity should not exist until the correlation coefficient reaches ± 0.8 or ± 0.9 (Farrar & Glauber, 1967; Gujarati, 1995; Kennedy, 1999). Multicollinearity was also tested through variance inflator factor (VIF) analysis. The highest value is equal to 1.17. The effect of multicollinearity is not significant when the values are less than 10 (Myers, 1990). Therefore, in light of this, it is possible to say that multicollinearity does not represent a problem in the interpretation of the results.

Table 2: Means, standard deviations, VIFs and correlations

Variables	Mean	S.D.	VIF	CGDL	SIZE	ROE	AUDQ	LEV	BSIZE	ESEN	AGE
CGDL	10.21	4.21		1							
SIZE	16.20	2.37	1.11	0.331***	1						
ROE	12.80	6.87	1.08	0.213**	-0.126	1					
AUDQ	0.87	0.33	1.10	0.437***	0.156	0.168	1				
LEV	6.25	6.12	1.17	-0.139	0.027	-0.123	0.041	1			
BSIZE	10.82	3.58	1.13	-0.051	0.144	0.032	-0.042	0.084	1		
ESEN	0.43	0.49	1.16	0.092	0.047	0.059	-0.004	-0.350**	0.028*	1	
AGE	52.79	49.92	1.12	0.084	-0.084	0.025	0.111	0.016	0.247**	0.081	1

Note: *n* = 73. S.D. = Standard Deviation. *** = significant at the 1% level; ** = significant at the 5% level; * = significant at the 10% level.

5.2 Linear multiple regression results

We tested the hypotheses of this study through a linear regression model. The results support hypothesis 1 (H1). In fact, there is a positive relationship between firm size (SIZE) and corporate governance disclosure level (CGDL) at p = 0.003. This result shows how larger companies provide a greater level of information relating to corporate governance within the integrated reports. In

addition, the results support hypothesis 2 (H2). In fact, they highlight a positive association between firm profitability (ROE) and corporate governance disclosure level (CGDL) at p = 0.092. This result underlines how the most profitable companies provide a greater level of information relating to corporate governance within the integrated reports. Finally, the results also support hypothesis 3 (H3). In fact, they highlight a positive association between audit quality (AUDQ) and corporate governance disclosure level (CGDL) at p = 0.002. This result underlines how the companies that have their report certified by at least one "Big Four" accounting firm provide a higher level of information relating to corporate governance.

Table 3: – Linear multiple regression results

Variables	Coefficient	Standard error	p-value
Cons	3.027	3.375	0.373
SIZE	0.575	0.189	0.003***
ROE	0.110	0.064	0.092*
AUDQ	4.416	1.355	0.002***
LEV	-0.087	0.755	0.252
BSIZE	-0.121	0.126	0.343
ESEN	0.154	0.920	0.867
AGE	0.008	0.009	0.379
N	73		
Adj. R^2	0.258		

*** = significant at the 1% level; ** = significant at the 5% level; * = significant at the 10% level

6. Conclusions

This study investigated the determinants of the corporate governance disclosure level contained in the integrated reports. The results first showed an average low level of corporate governance disclosure level within the integrated reports. Second, the results demonstrated a positive impact of firm size, firm profitability and audit quality. Large companies are more likely to produce information and also incur lower costs due to economies of scale. Furthermore, these companies are subject to greater pressure. These circumstances explain the positive impact of the firm size on the corporate governance disclosure level. As for profitable firms, they will be more interested in disseminating information in order to promote a positive image of their performance. Furthermore, profitable firms may choose to publish higher-quality information in order to distinguish themselves from less-successful companies. These circumstances explain the positive impact of firm profitability on corporate governance disclosure level. Finally, as regards audit quality, the reputation of the large accounting firms guarantees the quality of the information contained within the integrated reports. This circumstance explains the positive impact of audit quality on corporate governance disclosure level.

The results have important managerial implications. The managers of the largest and most profitable companies must increase the level of corporate governance disclosure in order to mitigate the pressures and show a good corporate image. In relation to audit quality, instead, managers should increase the quality of the audit in order to improve the level of information relating to corporate governance provided within the integrated reports.

This study is subject to a limitation related to the sample size. In fact, this study is based on a sample of only 73 companies. However, this limitation may represent a basis for future studies. In fact, future research will test the hypotheses of this study on a larger sample. In addition, future studies will be able to test the impact of other variables both at company level and at country level.

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COMPARING GOVERNANCE ARRANGEMENTS IN SOCIAL ENTERPRISING: THE INTERPLAY BETWEEN FOUNDER(S) AND THE "OTHERS"

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Abstract
Social entrepreneurs differ from other entrepreneurs to the extent that they privilege social value over the generation of economic rents. Literature on such social entrepreneurs questions mainly how they adapt to new institutional contexts to obtain material and immaterial resources and become sustainable. The aim of this article is to understand how central social enterprises embedded in the same emerging field and tackling the same social issue can develop different governance arrangements. In this article, we analyse two social enterprises born at the same time in an original socio-political context: the emerging field of "equal opportunities" in France, where state agencies, ministries, NGOs and corporations strive each to legitimate their vision. Our results show that even evolving within the same field, with comparable objectives, SEs can develop different governance arrangements following different models. For the two social SEs, endorsing a democratic governance system can largely hinder their capacity to gain the dominant field position they want to achieve. The two founders, with different approaches, utilise their management and directors, so, their governance mechanisms, in this ambitious positioning.

Keywords: *equal opportunity field, founder, France, governance arrangements, NGOs*

Track: *Governance*

Word count: *9.969*

1. Introduction

The governance of social enterprises and non-profit organizations (NPOs) has become an increasingly important topic in third-sector research. Due to the growing marketization and professionalism of the social sector (Hwang & Powell, 2009) in many countries, tensions in governance appear between the legal heritage of NPOs and their new business practices. This sector experiences a growing shift toward the hiring of professional managers, and the adoption of business-like formalized "best" practices. The aim of this article is to understand how central entrepreneurs of social enterprises (SEs) embedded in the same institutional field and driven by the same aims can develop different governance arrangements.

We build on Cornforth's (2004) definition of governance in the third sector as the systems and processes concerned with ensuring the overall direction, control and accountability of an organization. Governing implies the definition of the organization's mission and goals and outlines simultaneously the best possible actions to achieve organizational survival and growth within an evolving and demanding society. So, governance is not only about the role and composition of the board, it also encompasses the impact of other actors and stakeholders who contribute to the governance arrangements.

In this article, we analyse two social enterprises born at the same time in an original socio-political context: the emerging field of "equal opportunities" in France, where state agencies, ministries, NGOs and corporations strive each to legitimate their vision. The core mission of the two studied

SEs is to encourage, through mentoring, young people from deprived urban areas to engage in higher education studies. Within this emerging institutional field, both SEs bridge particular high school students' educational path and the corporate world.

We undertook a longitudinal case study (2005-2017) with a chronological perspective. We collected data from the two organizations and conducted interviews with key actors (founders, board members, managers). Our results show that even evolving within the same field, with comparable objectives, SEs can develop different governance arrangements. Both cases reveal the central position of the SEs' founders. Their singular professional trajectories and their different backgrounds and networks have deeply influenced the earliest governance arrangements. In one case, the business governance model was adopted; in the other case, the philanthropic governance model dominated. These two models converged in the way boards were formalised supporting organizational growth's needs. However, decision-making processes are actually reflecting complex governance structures influenced by the founders. Moreover, the appointment of professional managers did not convolute the governance arrangements which still reflect the central positioning of the two founders in their SEs.

This research contributes to the understanding of social entrepreneurship governance arrangements facing multiple stakeholders.

We structure our arguments as follows. First, we review the literature on social entrepreneurs and their governance structures. Second, we introduce the two case studies within their context and explain our methodology. Third, we present the findings, focusing on the different governance arrangements, from business-like to philanthropic-like in the complex field of equal opportunities in France. Finally, we conclude with a short discussion and conclusion.

2. Theoretical framework

There has been little research on the governance challenges and support needs of social enterprises (Spear *et al.*, 2009; Huybrechts *et al.,* 2014). The main questions are: what are the governance arrangements of social enterprises? How distinctive are they from the governance systems of new ventures or corporations?

Cornforth (2004) defines the governance in the third sector as the systems and processes concerned with ensuring the overall direction, control and accountability of an organization. Governing implies the definition of the mission and goals of the organization and outlines simultaneously the best possible actions to achieve organizational survival and growth within an evolving and demanding society. Governance arrangements shall then address the specificities of social enterprises, facing expectations of multiple public and private stakeholders and led by individual social entrepreneurs (SEs).

2.1 Social entrepreneurs : institutional entrepreneurs in a social field

Various definitions and approaches of social entrepreneurship have appeared since the emergence of the term in the 1980s (Short et *al.,* 2009; Dacin et *al.,* 2010). Some would put forward the commercial vision, some others emphasize the social value rather than income generation, and even can be focused on employment creation for the low-qualified unemployed or the disabled, who are normally excluded from the labour market. These definitions focus on either the characteristics of the individual social entrepreneur (Light, 2009), the social problem addressed and the targeted outcomes, or the processes and resources used to reach the social entrepreneur's goals.

In this paper, we consider the social entrepreneurs as institutional entrepreneurs within a social field. Social entrepreneurs differ from other entrepreneurs to the extent that they privilege social value over the generation of economic rents (Dacin et *al.,* 2010). Battilana *et al.* (2009) propose two key categories of enabling conditions for institutional entrepreneurship: field characteristics, and actor's social position. In emerging fields, the lack of institutionalized practices and clearly

identifiable norms makes it easier for actors to bring about institutional change and affords them considerable advantages as they shape the field (Maguire *et al.,* 2004). In such fields, actors' social position might affect their perception of opportunities and gives them differential access to resources (Bourdieu, 1988). Their ability to build or frame a new field relies simultaneously on a cognitive dimension – inventing alternative modes of getting things done (Beckert, 1999) – and on a social position conferring power (Hardy & Maguire, 2017). This social position refers both to their formal position in their organization and in the field, and to their socially constructed identity. Institutional entrepreneurs' unique political and social skills (Maguire *et al.,* 2004) provide them with the ability to induce cooperation among others, using or establishing relational networks for example. Institutional uncertainty offers then wide ground to social entrepreneurs to be strategic and opportunistic (DiMaggio, 1988). Consequently, institutional entrepreneurs have to be reactive in taking dominant positions when opportunities appear. Their position in the field is both an initial enabling condition and a result of the institutionalization of the field. In this context, accessing to critical resources becomes strategic, and organizations tend to implicate stakeholders in their governance structures to secure it (Campi *et al.,* 2012; Middleton 1987; Miller-Millesen, 2003).

Lastly, scholars studying individual social entrepreneurs identify their ability, motivation and behaviours to enact change with various degrees of altruism (Drayton, 2002; Zahra *et al.,* 2009). Furthermore, literature associates social entrepreneurship with "systemic change" (Alvord *et al.*, 2004) and social activities related to networking with a plurality of social actors. SEs are social not only because of their ends, but also by the way "they carry out their activities, share their knowledge, and celebrate their work" (Dacin *et al.*, 2011: 1207). Dees (1998) argues that this definition highlights the sustainable solutions developed by the SEs within a broader context and embedded in a process of continued learning and community participation. He states that SEs are: "playing the role of change agents in the social sector by adopting a mission to create and sustain social value, recognizing and relentlessly pursuing new opportunities to serve that mission, engaging in a process of continuous innovation, adaptation and learning, acting boldly without being limited by resources currently in hand" (Dees, 2001).

2.2. Social enterprises facing expectations of multiple stakeholders

Social enterprises created by social entrepreneurs are thus framed by the twofold concept of social value and entrepreneurship. Several researchers (Battilana & Lee, 2014; Battilana & Dorado, 2010; Kraatz & Block, 2008) define these social enterprises as hybrid organizations in which coexist and sometime compete a social logic and a business logic. Logics shape acceptable goals and principles within a field, thus influencing organizations' priorities (Pache & Santos, 2013), and the coexistence of competing logics might thus create tensions. Social enterprises that combine business and charity at their core face unique governance challenges, related to joint accountability to both social and economic objectives (Battilana & Lee, 2014).

Among these tensions, the commitment of social entrepreneurs to achieve specific social objectives challenges the concepts of authority and leadership of the founders of social enterprises, because of the particular organizational structures that these ventures may adopt (Shaw & Carter, 2007) and the multiplicity of stakeholders they face. In these enterprises, the configuration of stakeholders' involvement contrasts with that of for-profit businesses where shareholder's hegemony disappears as non-for-profit organizations are assimilated to firms without owners (Hansmann, 1980).

Consequently, social enterprises usually use legal forms that allow and enhance socio-economic democracy by acknowledging stakeholders, other than investors, the right to participate formally in the governance bodies (Huybrechts et *al.,* 2014). Social entrepreneurs can indeed decide for various legal forms for their social enterprises including incorporated forms or associations and charities, especially when they serve charitable purposes (Spear *et al.*, 2009). For all these forms,

the legislator has provided the basic governance requirements to ensure the good use of resources and the survival of the organization while growing. In France for example, the prevailing non-for-profit form in the social sectors is the association, for which the legal status has been set by the "1901 law". Under this law, associations are built around democratic principles: gathered in a general assembly, members who demonstrate their commitment to the mission, democratically elect, among themselves, a volunteer board of directors leading the association (Pache & Santos, 2013).

However, practice can fill with different contents governance systems within similar SEs depending on their varying stakeholders' influence. In this regard, Ebrahim *et al.* (2014) argue that: "In terms of organizational governance, social enterprises offer a rich subject of study as they combine … potentially divergent stakeholder interests", as the shareholders' primacy dissolves. Thus, deciding for an association as a legal form, social enterprises will have to challenge complex governance arrangements as divergent interests and democratic decision-making processes must live together.

2.3. Governing social enterprises: the centrality of the social entrepreneur

In this regard, governance arrangements of SEs help in defining the organization's mission, goals and actions to achieve their growth, taking into account the legal requirements as well as the cultural and institutional environments of their multiple stakeholders. Governance arrangements are therefore supposed to be democratic and invite participation not only to those who have been financially involved, but also to very different stakeholders brought together around the same project: employees, volunteers, beneficiaries, users, supporters, government, etc.

There is a large literature on (corporate) governance that looks at how organizations involve their stakeholders at different decision-making levels (Clarkson, 1995; de Graaf & Herkströter, 2007; Freeman & Reed, 1983). This involvement can be rather passive (information) or more active (representation) (Huybrechts *et al.,* 2014). Inviting stakeholders to join the governance structures, such as the general assembly and the board of directors, represents a long-term relationship between the organization and a particular stakeholder category (Mitchell *et al.,* 1997).

Resource dependency theory explains the power position of some stakeholders from the moment they play a critical role in ensuring organizational survival by reducing uncertainty, managing important environmental dependencies and mobilizing resources at the benefit of the organization (Cornforth, 2004; Labie, 2005; Pfeffer & Salancik, 1978). Institutional demands are conveyed by key external actors, in regulatory bodies or funding organizations for example, who diffuse them across the field and exercise pressures for compliance (DiMaggio & Powell, 1983). However, Huybrechts *et al.* (2014) argue that "stakeholder involvement may result from unconscious and 'irrational' processes of legitimization and dominance. These processes may explain why in some cases stakeholders with little strategic interest are given primacy, or why potentially strategic stakeholders are ignored". They underline the symbolic role of stakeholders' involvement and governance structures. Structures and practices such as board composition "can become invested with socially shared meanings, and thus, in addition to their 'objective' functions, […] serve to communicate information about the organization to both internal and external audiences" (Tolbert & Zucker, 1996: 171).

Among the key stakeholders providing financial resources, private funders may favour governance structures that reproduce business-like governance structures, which they view as legitimate and efficient. In the American context, Hwang & Powell (2009) showed that foundations are influential because the funds they provide bring particular mind-sets and practices with them. Grants contain requirements for evaluations, hiring consultants, and management training sessions for board members. In that regard, Foundations can play a critical role in homogenising organizations in the non-profit field as they promote "modernity" in management. In the French context, Eynaud (2019) underlines that public funders may also foster the professionalization of governing practices and the managerialism of associations. He argues that association develop managerial costing tools

and performance indicators to meet the requirements of the funders.

SEs face then pressures towards a business-like governance model, that is not necessarily consistent neither with their social mission nor with the involvement of other key stakeholders, such as the beneficiaries, the volunteers and the employees, in the decision-making processes. A wider accountability to multiple stakeholders, and a formal involvement of other stakeholders than the main funders would then foster a more democratic governance model. This later is more aligned with a philanthropic governance model. In such a view, the strong actors' collaboration within the same governance bodies limits the fuzzy areas and increases the capacity for understanding and problems solving (Eynaud, 2019). The presence of several opinions at the same time highly contribute to the quality of management and to effective mission-based strategic planning (Valéau *et al.,* 2019), as information is shared, reciprocal actors' control is upheld and innovation is enhanced (Borzaga & Depedri, 2015).

However, gathering a large number of actors with different interests around the same project is not easy to manage (Valéau *et al.,* 2019; Abzug & Webb, 1999). Sharing democratically the decisions presupposes a certain number of procedures that may appear burdensome (or even counterproductive) for some actors and can hinder the agility of a social entrepreneur.

The main challenge resides though in the power balance between main stakeholders (Eynaud, 2019). Actually, SEs are located in the intersection of different sectors in society so they need to reconcile diverse viewpoints (Martin & Thompson, 2010). The participation of different stakeholders might undermine the core mission of the organization (Dees & Elias, 1998). Particularly in social enterprises, the relevant stakeholder will be more closely related to the impact an enterprise has on society rather than to its financial activities. In that matter, Pache and Santos (2013) highlight the importance of a strong identity in order to combine the social and business logics and keep or gain legitimacy from the stakeholders. Therefore, it is the social entrepreneur's responsibility to achieve an alignment between the components of the social entrepreneurship framework (Wei-Skillern *et al.,* 2007). In that sense, the identity of the founder/entrepreneur, the person who owns the idea, the inspiration or will is the balancing aspect in the social enterprise's core mission. Thus, the founder/entrepreneur can play a central role in modelling the governance arrangements of the social enterprise.

3. RESEARCH CONTEXT AND METHOD

To understand how two different social entrepreneurs tackling the same issue at the same time can build different governance arrangements, it is important to appreciate the socio-political context in which the organizational forms emerged and evolved. Accordingly, we specify the *equal opportunities* field in the French context and identify the major actors within this emerging field. Then, we present *Promise and Teli,* the two social enterprises and their boards, following the main chronological landmarks: beginning, growth and effort to become a legitimate and visible organization within the field. Finally, we draw our data and method.

3.1. Equal opportunities: an emerging field

Equality is one of the three core values of the French *Republican Pact*. In this context, *equality* refers first to equal rights for citizens (to vote, to benefit from public services…) and to regulation against potential discriminations. *Equality* is also related to a minimum economic well-being for all, guaranteed by the French state through its social policy and the redistribution system. These legal and economic dimensions induce public policies for equality. Over the past decades, the republican French egalitarian ideal is gradually substituted by the concept of "equal opportunities", presented as the ultimate expression of social cohesion (Barles, 2001). Hence, the French public education shall ensure equal opportunities for all children and young people, and spread values and knowledge required for all citizens (Dubet, 2014). However, since the 1960s, the public education has been regularly denounced for its deficiencies. By disputing objectives of social equality on one side and selection of elites on the other, it would produce and re-produce social

inequalities (Bourdieu & Passeron, 1964). From this period, *equal opportunities* are regularly stated as an objective of Ministries of education.

Moreover, from an educating social issue, *equal opportunities* have progressively gained influence in other spheres of society, becoming an employment and an urban life issue. Namely, over the last decades, economic crisis and unemployment, as well as dramatic socio-political events such as riots in the suburbs in 2005 have led *equal opportunities* policies back to the forefront. Those events deeply question the education system and its failures in promoting equality and fraternity, as core values of the French nation. Finally, whereas the state and local or national associations traditionally promoted equal opportunities, new social entrepreneurs appeared, and the field gained in importance. Several organizations sprang at the same period on the principle of mentoring young people from deprived area by companies' staff members.

3.2. Data sources and analysis

We conducted a longitudinal (2005-2018) in-depth case study of two non-profit organizations named *Promise and Teli*, within the field of equal opportunities in France. The cases provide rich data on how the governance mechanisms develop and interact over time. Documents and interviews constitute the major data sources for our study. Documents comprise archival data, press accounts, web publications and internal publications detailing the structure, missions and actions of *Promise and Teli*. Table 1 summarizes the main data sources.

Table 1: Steps in the transformation of SEs/governance

	Main events and steps in social enterprises	
Timeframe	*Promise*	*Teli*
2004-2007	Hiring first professional manager	Hiring first professional manager
	Bureau constitution (4 members)	Bureau constitution (3 members)
	Social entrepreneur (general representing) payment plan	Effective management committee (all volunteers)- No board
2007-2013	Professional appointment of new board members (13 members)	Social entrepreneur (chairman) payment plan
		Board structuring (12 members)
2010- 2017	Growing and legitimizing	Growing and legitimizing
	Accountability and social impact performance indicators	Accountability and social impact performance indicators
	Extending field influence vs struggling	Extending field influence vs struggling

Semi-structured interviews were conducted with 31 key informants, selected and interviewed according to their position and involvement in the processes of decision making and growth (Eisenhardt, 1989). All of them were involved, connected to, or knowledgeable about the development of the two SEs: representatives, former mentees still involved as "ambassadors", students currently mentored, representatives of public organizations and corporate partners, board members, founders. The interviews were organised in three rounds: firstly, in March 2017 - with a phase of collecting archival data; secondly from February to June 2018, and thirdly from October 2018 to May 2019. The 31 interviews were all recorded and transcribed, with a total duration of 50 hours.

In addition, we extracted data from the organizations' websites at different dates throughout our

analysis, to build a data base, independently from the various changes occurred, in order to triangulate facts (Eisenhardt, 1989). We also collected archival data dating back to 2005 at the field level, including 140 media articles on *Promise and Teli*, and numerous publications and official reports on equal opportunities policies. Finally, we also used web-based accounts of organizational identities and missions. This provided distinctive access to elements that organizations use to present themselves to specific audiences (Sillince & Brown, 2009). The archival data gave an understanding of the context in which *Promise* and *Teli* operate, and how they act as social entrepreneurs and interact with their stakeholders within the field.

3.3. Promise and Teli: the cases

Promise and Teli have emerged in a very particular socio-political context. In the 2000s, France faced several and deep turbulences: political changes and new laws concerning education and suburbs, social (2005 riots) and economic crisis (2008), and violent terrorist attacks (2015). Hence the principle of equality was confronted with the question of relations to the others and of individual and collective identity. France was the arena of harsh debates and intense emotions about the French identity and the core value of equality. The reality of the Republican pact which guarantees "Liberty, Equality and Fraternity" to each citizen was put into question. Doubts on the real social integration of young people with "immigrant backgrounds" (even though most of them were French) and political discourses on the broken "social ladder" in France became more frequent.

In this complex environment, the two SEs grown and consolidated to become legitimate and visible organizations within the field of equal opportunities. Table 2 displays the organizations' several states of development in chronological order.

Table 2: Data sources

Data source	Type of actor/ organization	Number
Semi-structured interviews: 31 (between 30 minutes and 2 hours long; 28 face-to-face/3 by phone)	Representatives of public organizations	4
	Representatives of corporations, partners of *Promise and Teli*	3
	Promise and Teli managers	18
	Board members	4
	The founders	2
Newspapers	National press articles on *Promise and Teli* (2012-2018)	140
External documents	Legal Reports (Cour des comptes, Borloo report, Haut Conseil Vie Associative...)	12
	Reports and documents from consulting firms and think tanks on impact and equal opportunities	23
Internal documents	Documents from *Promise and Teli* websites (reports, detailed programs)	40
Illustrative websites consulted	Official websites of the ministry of education, urban policy, social cohesion (summaries of laws and public programs)	5
Other archival data	Data on *Promise and Teli* board members and	-

	partners Videos of interviews of Stéphane and Sasha promoting and explaining their visions and programs	20

Between 2004 and 2007, *Promise and Teli* emerged around a very similar contribution to *equal opportunities* relied mainly on mentoring young people from deprived areas and training them to foster academic ambitions. Both social enterprises structured about eight years after their starting point. This was possible with the appointment of managers who, for both, actively took the lead on the coordination and implementation of projects but not on the decision-making process, still between the hand of the founders. During this phase, under the leadership of their respective social entrepreneurs, *Promise and Teli* diffused actively their vision of what equal opportunities programs should be. During this period also, the executive committees found a way to attribute a payment plan for each of the founders, without having to leave the leading position (the French "1901 law" permits chairman remuneration for associations under very restrictive conditions).

For both organizations, the founders' consciousness of inequalities was the sparkling factor. Each one of them, for different reasons, engaged in willing to find a solution to what the first (Stéphane) called the "*lack of equal freedom of choice*" and the second (Sasha) the "*lack of real freedom*". For both of them, France has failed in its political choices to offer to youth the same opportunity to enrolling in the adequate curriculum and reaching high ambitioned career. Consequently, the system is seen as playing a central role in perpetuating social and economic inequalities, and both wish to participate in eroding it away.

Between 2011 and 2018, new partners joined *Promise and Teli*, particularly large consulting firms and financial institutions, playing key roles in supporting their growth.

4. Findings

The two SEs emerge as one solution to promote equal opportunities in a new way, supported by the government, companies, and *Grandes Ecoles*. *Promise*, initiated as a public-private partnership, reflects a shared interest for a new type of actions dedicated to equal opportunities. *Teli* was rather an association of friends' willingness (based on personnel challenges) to participate in the social struggle against inequalities.

Our programs reflect the ambition of giving to all young people a chance for success whatever their socio-cultural background or economic situation. (Promise founder).

To create unexpected encounters between these young people, who limits their ambition despite their talent, and you, companies, volunteer employees who have an experience to share and a desire to act. (Promise website, consulted 2015).

We work to compensate for the so-called social handicap of our godchildren, so that they professionally integrate in more quickly and with a 10% higher salary. (Teli founder).

Teli works for a society where success does not depend on social, economic and cultural origins, for a society where success depends on social ties and civic commitment… On our planet there is a positive community determined to forge links across worlds that ignore each other. They inspire, succeed and engage... (Teli website, consulted 2015).

Even though the creation path of the two enterprises is different, both have the strong ambition to become one of the French leaders in 'accompanying young people from modest backgrounds towards their success'. While both are involved in acting in the field of equal opportunities, *Promise* is more concerned with diffusing business codes, instead, *Teli*'s actions aim at creating a "positive community", implicitly imbued with meritocratic values.

Promise and *Teli* were considered by several *Grandes Ecoles*, historically embedded in a meritocratic culture, as a bridge between different worlds, in line with the Republican pact promoting "equal opportunities". These institutions of higher education are often criticised for their elitism, so they were keen to participate to these projects. Thus, they were represented as a socio-political project, to which companies may contribute, without contesting the central place of professors.

> *By this common will, clearly expressed, the social opening of Grandes Ecoles is not a myth but a reality, inscribing equal opportunities at the heart of the republican project. (...) It is desirable that the companies' involvement towards higher education and research continues and strengthens. (…) All pupils in high schools should have information about this Promise project, thanks to their professors. (P. Pouvil, Head of ENSEA, Engeneering Grande Ecole, Press conference April 2005)*

The two social enterprises decided for a legal form of an association under the 1901 French law. In general, the law gives the members of the association complete freedom to define their operating bodies, their attributions and the body empowered to represent them vis-à-vis third parties. Generally, the members gather in a general assembly and vote for a board who votes for a bureau (these two bodies can be merged in one). The latter legally should be composed of a president, a secretary general, a treasurer and eventually a vice-president. The bureau is a central governance body in an association and its members cannot be remunerated unless the association's funds exceed 1,000,000 euros. Still the association can decide to compensate the president if the gathered funds are superior to 200,000 euros.

The president is the agent of the association and not its legal representative. She/he may act in the name and on behalf of the association while having effective and constant control over it. In that regard, the board/bureau can decide for another representative who would hold the legal responsibility.

4.1. *Promise*: The central founder and the board

Stéphane has a university degree in law and a professional education in HR management. He spent all his career in management in big companies and his last corporate job was Corporate Responsibility & Social Innovation VP in a big French corporation. He defines himself as an expert in diversity issues and equal opportunities.

> *"I was in a company and I wanted to recruit young executives who reflected the image of France, in all its diversity, but I couldn't find the engineers I needed". (Stéphane).*

As Stéphane lived in an overseas department, the question of diversity seems for him "natural". He declares to have been shocked when he first moved to the "metropole" and noticed that "depending on the territories you come from, you experience spatial segregation. The different strata of the population don't necessarily mix". This trajectory activates his sense of equality and he starts engaging and creating associations in that regard. He wants to make the corporate recruitment of diverse people possible in the future by actively sponsoring deprived but gifted young pupils accessing the best engineering schools in France.

> *"In the end, what makes the difference between young people are the points of access with people who are able to decode higher education and therefore able to advise them. » (Stéphane.)*

Hence, he participates in building a public-private partnership in response to both a public need and a stake of his company who was looking for diversity for recruitments. The first development stages of *Promise* include building an organizational structure, growing (in numbers of beneficiaries, partners, resources, programs, etc.), and gaining a central position in the field. The SE promotes equal opportunities for young people from deprived suburbs, by connecting partners around beneficiaries, as shown in figure 1. In few years, *Promise* acquired the reputation of active

social enterprise promoting equal opportunities through original mission, goals, governance structure and organizational design.

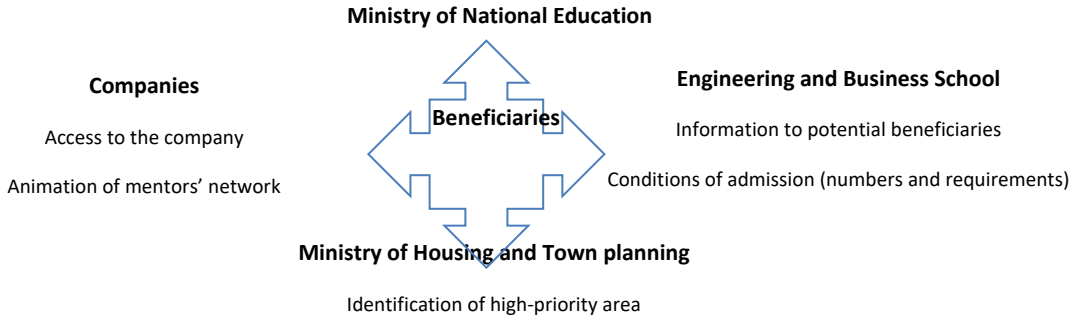

Figure 1: Actors roles (*Promise* communication 2010)

From the public-private partnership, *Promise* shifted into an association legal form under the French law 1901. Stéphane had no trouble to convince his former large Telecom company's CEO to join. The latter was very sensitive to the idea of participating in balancing the inequalities of opportunities as himself was not the result of the French elitist educational system. Then Stéphane briskly impelled important company's providers to follow and get on board. The request was clear; the companies engaged in providing with both funds and mentors.

At the beginning *Promise's* bureau/board was created around Stéphane and three CEOs of big public French corporations. The bureau decided to appoint Stéphane as the "general representative", accumulating the autonomy of a CEO and the diplomacy of an association leader. With this decision, he represents legally the association and more broadly signs contracts or grant applications on behalf of the association.

Promise decided also to control any new membership making it almost impossible to be a member without being sponsored[1]. About thirty new members have been appointed over 15 years and from very close professional backgrounds. After the 5 first years, Stéphane decided to constitute a board of directors inviting 10 main big public companies, whom the CEO was sensitive to the association's cause (financial donations and mentors) and two highly publicised women to join (one representing the figure of success as she is a worker's daughter with a Parisian engineering *Grandes ecoles* diploma and one academic with a political position). Finally, he asked a hunter to look for a high ethics-financial profile woman to complete the board.

> *… he needed women, I think that's why I was recruited because the board was only made by bosses of the CAC 40 so it's a little bit "claptrap" (Board member).*

In 2017, the board was composed of two visible categories of profiles: the big companies' (donors) CEOs (all men) and the personalities/woman. Figure 2 illustrates the governance mechanisms and their interactions in *Promise*.

[1] We asked to attend to one of the general assembly but we couldn't access. The manager did not say no, however, he never answered to our request.

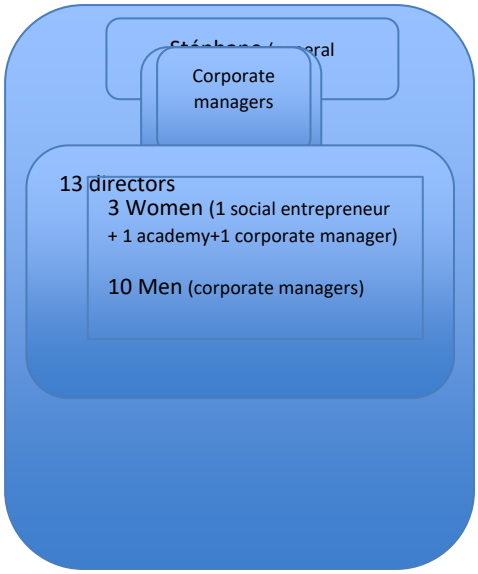

Figure 2: The three governance mechanisms of *Promise* in 2017

Promise's board is dominated by representatives of big companies (mostly telecom sector and financial institutions) invited to take a seat in the board whereas public partners are absent, despite their significant support with recognition (public-interest organization), tax advantages for funding, and public subsidies. All members have a personal relationship with Stéphane and if needed he asks them directly to do a specific activity (opening a network, developing a MOOC, etc.).

> *Yes as soon as he asks me something… I always ask how I can help you… here are my skills and Stéphane didn't hesitate... I put him in touch with other associations... so I'm someone who makes a lot of connections... (board member).*

The board of directors officially meets once a year. Stéphane exposes the activities of the year, the projects and the big spending accounts. The board was clearly "used" to serve the ambition and activities of the association, however, it was not a team. It was rather an aggregation of very important business men ready to support.

> *It's an association that was rich by its board of directors. And if a boss asks his corporate team to do something for Promise, it was perfectly done. (board member).*

With their network and influence, the board members serve as a symbolic pressure for success and a social leverage to obtain resources (databases, meetings, funding, etc.). Stéphane also plays with that to make the association visible and respected.

> *It's bound to work especially when you put in the board of directors bosses of the CAC 40 … it's bound to work because it's too much of a shame for the bosses if it doesn't work... everybody better make it work. (board member).*

4.2. *Teli*: The central founder, the friends and the board

Sasha has a very different social and educational background from Stéphane. He descents from a rich industrial family with a large experience in foundations and associations. He started by a Bachelor in philosophy and then ended with a Phd in strategic management. In the meanwhile, he gained a master's degree from a prestigious Business School and another one from ENA, a private and a public *Grandes écoles* in Paris. He trained in public policy at the *Cour des Comptes* and in the ministerial cabinet at *Bercy* (Ministry of Finance). He has been a strategy consultant for more than 10 years, first in one of the leading international consulting firms, then by founding his own

consultancy firm.

In 2004, he decided to create with three close friends an association which supports the success of high-potential students from modest backgrounds, thanks to the mentoring of young professionals. His first partners where socially gifted friends sensitive to the same urgency to balance inequalities. Their vision of equal opportunities is partly different from the one of Stéphane:

> *"I remember, before creating Teli, we were discussing together in a bar, and in the suburbs it was practically an insurrection at that time… and we realised looking at our professional environment that it was not about racism, because a lot of people talked then about the lack of integration and racism, but we realised it was more about social racism, racism between social classes" (co-founding friend)*

For them, the notion of equal opportunities was less connected to corporate codes and more to cultural codes with the republican ideal of fraternity. From the beginning, the association was closely related to the founders, who are also the members of the bureau/board and the general assembly. All men, friends from the same schools (*grandes ecoles*) and with large professional networks.

> *'At the very beginning we were more mentors than mentees.. we didn't know how to access this deprived young pupils" (co-founding friend)*

Sasha has invited those friends to create the association with regard to their motivations and availability, but also to their symbolic contribution:

> *I was part of the group around Sasha... I was the youngest and the most emblematic because I benefited from the social lift… I have succeeded well… and I was attracting the most mentors..." (co-founding friend).*

> *"We started with the "Tupperware method": we were 8 and each member brought 8 mentors, so we started with 64 mentors" (co-founding friend)*

The Bureau was at the heart of the decision-making process (budget, resources, programmes, etc.) and Sasha seems also to be the "initiator" of a plenty of projects. He wanted to solve all problems related to the educational process; accessing to the best schools, orientation, financing, student residency, etc. The bureau acted as a moderator to keep on the innovation part within the realistic time and means of the association.

> *He brought an entrepreneurial vision, a very attractive vision, I was the numbers man, so I was more like: if we make commitments, how are we going to finance them? The reality is that we have always managed to finance them. He had a lot of projects all over the places... we tried to frame him, channel him. (bureau member).*

Sasha was dedicating much time to the association in comparison with his friends whom were very involved but only committing few hours a week. His needs of growth were obviously in line with his fertile creativity and big ambition and he convinced his friends in a first step to appoint a manager and to gain size. In a second step, he decided to be fully engaged himself and convinced his friends to overcome a certain size to become visible and professionalise the association.

> *"The lab was also an idea of Sasha, who was doing his PhD himself and thought it was interesting, and I think he was absolutely right, to create a separate structure to develop new services, new products. There were still some fiscal, legal and other problems that were a bit complex to solve, but they were solved. At that time we had developed in many different directions, and we had a strategic committee and we said to ourselves, "How can we accelerate even more and change scale?*

> *What needs to be done to improve the society... he always had a political vision... the association became his main activity and it became TOO SMALL for him... if we want to have an impact, we have to grow up, he kept repeating !" (bureau member).*

While growing, *Teli* appointed more managers for each one of the many projects Sasha was thinking about. The SE stated to structure and formalise its functioning. It was important to evolve toward professionalisation since the association reflects the professionalism of its directors serving (in their perspective) professional aims.

> *"It was one of the subjects: helping associations to raise their level of professionalism, vis-à-vis the associates and especially vis-à-vis donors, is very important and increasingly so. Very early on, we were really managed like an SME with chartered accountants and auditors, we also did impact assessments to measure the impact we had, the return on investment, etc... a very corporate approach that we wanted to have from the beginning." (bureau member).*

In 2010/2011, governance started to be structured by enlarging the bureau and creating the board. The appointment of directors was made by affinity and co-optation of the central core of friends. Over 6 years, twelve new members/directors have been appointed from very different professional backgrounds. Sasha came with a list declaring: "*it is time to grow*" and the board was very quickly built up. All members are benevolent with a very clear objective: supporting Sasha to develop the association. The majority of them were Sasha's friends or acquittances, so that he could lean on their voice.

> *The members are chosen for that... probably... that was the unconscious deal: help me to develop Teli... but don't feel to drift the core mission !... (board member)*

The full board was composed of three visible categories of profiles: companies' (donors) representatives, state-access network persons and impactful social entrepreneurs. With a fine-grained analysis, the board was the extension of the bureau with 3 more involved people (the core board), the rest of the members had a seat to complete a diverse-looking board. Some members declared never attended a board meeting (full board). Once a year, two mentees are invited to the board as to make them participate to the debates without having a formal voice. Lastly, the board does not have all stakeholders' representatives (for example, employees or the state agencies/ministries, mentors, etc.). Figure 3 illustrates the three governance mechanisms.

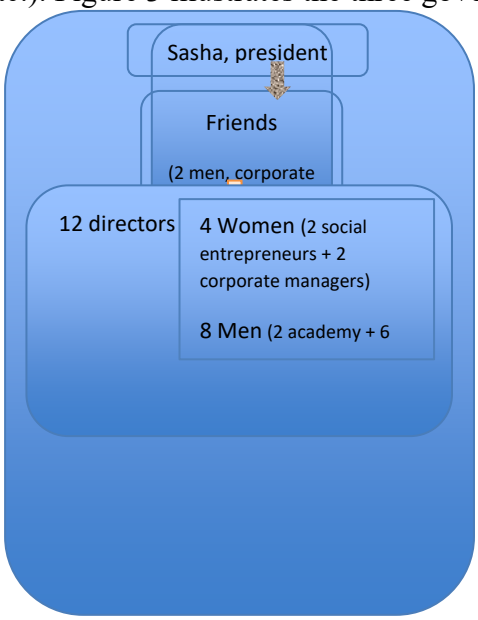

Figure 3: The three governance mechanisms of *Teli* in 2017

The core board was the main management and governance body. Generally, strategy and finance are the central elements of discussions, for example the payment plans or the development of new programmes. However, the full board is used to display the professionalisation of the association, which means, efficiency and performance. It helps also maintaining some donors aware of the actions increasing though their commitment to the association. Moreover, the board is activated to

secure the survival of the association.

> *It's an advisory body, serving to keep the link and then also reporting to them, because they commit themselves, they commit their managers, they put money in. So we have to tell them what we are doing with it. (board member).*

> *We are still an entrepreneurial association, so the board of directors is obviously important. The board of directors is here to make sure we don't do anything stupid (the founder).*

The board was a formal structure with a minute drafted for each meeting. Once a year, the general assembly ratified the financial and the activities reports. The board also served to keep away traditional political games into associations. The full board was seen as a professional body, gatekeeper of the survival of the association, and more aligned with a business-like model. This was also possible with the controlled membership, which will prevent from the board turmoil.

> *...It's this kind of political game within the associations... we absolutely didn't want that... we wanted efficiency, we wanted to move forward, we wanted to have a clear, precise approach. and professional approach towards our donors... and young people... and also towards the academic world. (bureau member).*

> *… what inspired us was the governance of a company... so clear shareholders, a clear boss... and shareholders who don't change every 4 mornings... so if I REPLY that in the associative world... a stable board of directors and FAST decision-making circuits... (bureau member).*

5. Discussion and conclusion

Social entrepreneurs differ from other entrepreneurs to the extent that they privilege social value over the generation of economic rents (Dacin *et al*., 2010). Literature on such social entrepreneurs questions mainly how they adapt to new institutional contexts to obtain material and immaterial resources and become sustainable (Greenwood *et al*., 2011; Battilana & Lee, 2014). The aim of this article is to understand how central social enterprises embedded in the same emerging field and tackling the same social issue can develop different governance arrangements. We show how a governance arrangement can be inspired either by a business-like functioning or by a philanthropic-like one and can contribute to better understand corporate governance.

In the complex field of equal opportunities, *Promise and Teli* managed strategically to increase their legitimacy, acquiring more financial and symbolic supports from various stakeholders. Both gained influence in the field of equal opportunities, moving their boundaries and extending their territories, from central (Paris) to national settlement. *Promise* also won the tender for social impact bonds to promote equal opportunities program. While growing, the two studied social enterprises actively professionalised their functioning and structured their governance bodies. Professionalisation includes formalised governance and managerial functions, as well as internal information, financial and control systems (Dekker *et al*., 2013, 2015; Flamholtz & Randle, 2007). There is greater role differentiation within the two SEs' structure however the same concentration of power base (the founder in one case and the core board in the second). Table 3 summarises the main findings from which we build our discussion.

Table 3: *Promise* and *Teli* governance bodies

	Promise	*Teli*
Association's philosophy	Companies can change the society	People's will can change the society
	facilitate access to the business world, make people see the	Restore the social lift

	challenges beyond the classroom and create success stories based on social diversity.	
Governance mechanism	3	3
Bureau composition	The founder his higher up and 2 other CEOs (4)	The founder and his friends (3)
Bureau role	Legal paper work	Moderator, supporter, gatekeeper
Bureau functioning	Informal, few meeting	Informal, very frequent meetings
Board composition	Majority CEOs- Appointed, identified as cause-sensitive	Friends, family, personalities and CEOs – Co-optation
Board role	Atomised resource leverage, Budget endorsement	Professionalisation, Management and challenge
Board formation	Business opportunism-Professional, network approach	Personal approach
Board functioning	Formal, once a year	Formalised, 3 to 4 a year
Board member number (without the bureau)	13	12
Woman on board	3	4
Board member turnover	2 to 3 year shift	Almost stable over the period
Decision making	The founder	The bureau
Board representation	Business-like model: if you do your work, we agree	Friend-like model: we are doing the work with you
Board structure	Founder: central core, no team	Founder: central core, no team
General assembly	Closed membership : board members and some other companies	Closed membership: board members and some beneficiaries
Size (in number of managers) in 2017	Around 30	Around 30

The socio-professional analysis of the members appears as the preliminary step to understanding their motivations. The two founders wanted to tackle the social inequalities generated by social reproduction even though they have very different personal trajectories. The first one considers himself a "*transclasse*" (Jaquet, 2014) a "class-passing", coming from a modest family background with university level and professional career in the private sector. For him, these elements give him the experience and the legitimacy in understanding the complex question of equal opportunities. He builds his rhetoric on saving deprived young people from their deterministic socio-cultural framework. The second one is descendent of a philanthropic rich family, he gained multiple diplomas from different Parisian *grandes ecoles*. He did almost all his professional career in the public sector which, for him, gave him the experience and the legitimacy of the good republican man who wants to remedy social injustice. He builds his rhetoric on acting to change politically the society.

The two founders are central to the creation and development of the associations and they represent their DNA. They gathered around them their natural networks: CEOs for the first one and friends (working mainly in finance institutions) for the second one. This first circle has conditioned the future governance arrangements of the two associations. Even though the two SEs have formally the two level of the legal associations' governance bodies: the general assembly and the board/bureau, they have not developed similar functioning modes.

Results show several points of convergence. The first is the high and similar educational background of the majority of board members and managers. Almost all of them have at least a master degree at one of the (Parisian) *Grandes Ecoles,* such as business and engineering schools, IEP Paris, ENS, or ENA. The second similarity is the core mission and actions of the association which are remarkably alike. Despite the very different trajectories of the two founders, their analysis of the problem of the educational inequalities and its solution have "striking parallelism" and their visions of why to do it (educational success should not depend on social backgrounds) and what to do (mentoring) is extremely aligned.

The third point is the absence of expertise of the boards regarding the core activity of the association. This reinforces the centrality of the founders whom the directors trust in the strategic choices they make. The forth element of convergence is that the boards do not assemble all the associations' stakeholders (especially the state, the employees, the mentees and the beneficiaries). In both cases, the actual boards' configurations are strengthening and legitimising the power of the founders who act as every "good businessman", putting the board in their hands, organizing and driving it. Lastly, the fifth convergent element reflects the non-democratic model of the two SEs governance models. The membership is tightly controlled in both cases to maintain the power centrality of the founder/bureau.

Results show also different variances in the governance arrangements of the two social enterprises. The first one is the relationship that has each founder with the bureau and board members. In one case, the relationship is business-like and this has impacted the role and functioning of the governance bodies. In this case, the bureau is a legal fiction and the board is basically a legitimising artefact, used to confirm the professionalisation of the social enterprise. The founder maintains a one to one relationship with all members and this can keep them from organising in a team structure.

In the second case, the relationship of the founder with the majority of the members is friendship. This gave the core board more presence and weight in the decision-making process and in the financial control of the activities. The core board challenges the founder asking the "good" questions about the feasibility or the timing of some programmes or strategic directions. The core board also plays a controlling role on the use of the financial resources as the association raises private and public funds. Finally, the core board acts also as a brake on the founder's overwhelming need for innovation. Even though this board covers several roles, the founder still is in the heart of the social enterprise. As for the first case, the full board is used to display the professionalisation of the association.

The second difference resides in the members' turnover, which is higher in one case than in the other one. This confirms the role content for each one of the two boards of the social enterprises. The "stable" core board participates more in the governance of the association and in the decision-making process. The third dissimilarity is the governance models of the two social enterprises. The first one roots in the business-like model, centred around a powerful leader. The second one shows more philanthropic oriented model with a shared decision-making process in a group of friends which resembles a "privileged club", even though the leader is also influential.

Results show also that the two founders embody the social enterprises' governance and that the governance arrangements are only conducive of fairness and balance which might contribute to build trust and increase the legitimacy of the social enterprises within the field of equal opportunity. In the two cases, institutional uncertainty widely supported the two social

entrepreneurs to be strategic and opportunistic (DiMaggio, 1988; Fligstein, 1997). Consequently, both were reactive in taking dominant positions when opportunities appear.

In the emerging field of equal opportunities, the two social entrepreneurs acquire multiple resources gaining multiple supports from actors of various interests (Fligstein, 2001; Maguire et al., 2004). In this regard, they use the board of directors as to comfort different actors (especially the state agencies and other social investors) in their capacity to trust the organizations. Even though they have multiple stakeholders, the two social enterprises are not democratic organizations as they only invite few to participate in the decision-making process. For the two social SEs, endorsing a democratic governance system can largely hinder their capacity to gain the dominant field position they want to achieve. The two founders, with different approaches, utilise their management and directors, so, their governance mechanisms, in this ambitious positioning.

Taking a step back, it is also useful to deepen our understanding of the task of creating and maintaining effective governance mechanisms (Nordqvist *et al.*, 2014). Three of these mechanisms exist and seem to participate to the survival and performance of the studied social enterprises : founder, directorship, and management. For coherent governance it is important for SEs to define and clarify the roles and contributions of these three mechanisms. We have shown that the dynamics of the three mechanisms at the strategic apex of the SEs may vary in actions and interactions.

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GOOD AND TRANSPARENT MANAGEMENT OF STATE-OWNED COMPANIES - REALITY OR UTOPIA?

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Abstract
Certain tasks in the Republic of Slovenia are in the domain of the state or local community. In order to carry out these tasks, state-owned or public companies have been established. The management of such companies is not always good and transparent, and as a result it often leads to considerable damage to public property. Such situations are mostly caused by poor management by the management boards, and rarely by poor and inadequate control by the supervisory boards. They are also the result of poor and inadequate communication between the management and supervisory boards. Unfortunately, poor governance does not occur in isolated cases and the mismanagement of such companies is often only introduced to the public through affairs that are presented in the media. There are, however, also some positive exceptions with good and transparent corporate governance that bring profits to the shareholders and, consequently, lower the prices of individual services for citizens.

Keywords: *corporate governance, good practice, public companies*

Track: *Governance*

Word count: *5.558*

1. Introduction

Based on the Act on Physical Assets of the State, Regions and Municipalities (Official Gazette of the Republic of Slovenia, No. 14/2007, ZSPDPO) different legal entities governed by public law are recognized in the Republic of Slovenia, i.e., the state, self-governing local communities, public-law institutions, economic public-law institutions, public agencies, public funds and public enterprises. In the following we will focus on the last of these, i.e., public enterprises, hereinafter referred to as JPs.

A JP is a public enterprise that performs one or more different public services on a larger scale and has a monopolistic character (Ivanjko, Š., Kocbek M., Ljubljana, 2003), which can be considered as profitable. It provides public goods, for example, energy and water supply, transport, environmental protection. It is financed either by the payment of public goods or from the state and municipal budgets, and differently from the interpreters of the Association of Accountants, Financiers and Auditors of Slovenia. JPs primarily run (local) public services for environmental protection. A JP is established as a status form in one of the legally organizational forms of companies in accordance with the Companies Act (ZGD-1) (Official Gazette of the RS, No. 42/2006 (60/2006), 26/2007-ZSDUB , 33/2007-ZSReg-B, 67/2007-ZTFI (100/2007), 10/2008, 68/2008, 23/2009 Odl.US: U-I268 / 06-35, 42/2009 and the Services of General Economic Interest Act (ZGJS) (Official Gazette of the RS, No. 32/1993, 30/1998-ZZLPPO, 127/2006-ZJZP) on the basis of an ordinance adopted by the municipal council of individual municipalities.

There is also the possibility of the privatized performance of economic public services on the basis of concessions, which are not possible for public enterprises.
From this it can be concluded that JPs are generally not stimulated to achieve good business results due to their status form and the fact that the free disposal of profits is no longer in the domain of the JP, but of the owner. In the case of a loss there are more options: the JP usually receives funds

from the budget, is recapitalized, the price of the service is subsidized or the owners simply raise the price for the service provided by the JP.

All JPs are considered to be:
- public purchaser
- supervised by the Court of Auditors.

New legislation, which will regulate the position of public enterprises, has been in preparation for several years, but it has not yet come into force, despite the unambiguous findings by the state of the RS itself (State-Owned Corporate Governance Policy, No. 47600-13/2009/5, Ljubljana, 23rd of July 2009). Most JPs, therefore, operate without a desire for good business results, and it is often the case that individual JPs are a source of the non-transparent spending of money and sometimes even criminal acts of management structures. The public tends to be informed when public money has already been spent. In most cases the responsible authorities do not have to bear any consequences for their actions, the complaints on the courts are poorly prepared, it takes too long, and there are mostly no clear convictions of the accused. But nevertheless, there are also examples of good practices where JPs generate good business results, which I will try to show below.

2. Presentation of the JP CČN Domžale – Kamnik d.o.o.

The public enterprise Central Wastewater Treatment Plant Domžale–Kamnik (hereinafter JP CČN DK) is the fourth-largest wastewater treatment plant in Slovenia and has been operating since 1980.

It was established as a part of the Domžale water-supply enterprise and it received its wastewater from the municipalities of Domžale and Kamnik. JP CČN DK was established as an independent business entity in 1990 and covered several municipalities with their own water-supply enterprises. The former municipalities of Domžale and Kamnik were later divided into several municipalities, so that the CČN DK covered the following municipalities: Domžale, Kamnik, Mengeš, Komenda, Trzin. The municipality of Cerklje na Gorenjskem joined the ownership of JP CČN in 2015. Since November 2015, the following municipalities are the owner of the enterprise: Domžale (39 %), Kamnik (33 %), Mengeš (14 %), Komenda (6 %), Trzin (4 %) and Cerklje na Gorenjskem (2 %). These municipalities are also the owner of the infrastructure facilities of the CČN (Stražar, M., Portorož, 2019).

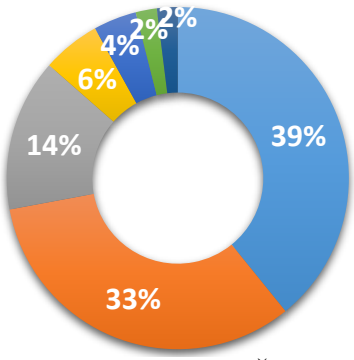

Figure 1: Equity shares of the JP CČN DK

3. Description of the company's activities

The key activity and a priority task of the enterprise JP CČN is "sewerage" (classification number 37,000). The enterprise performs a wastewater-treatment service for the above mentioned six municipalities, which are the owners of the enterprise.

The enterprise was established to support the CČN infrastructure and thus provide a quality wastewater-treatment service in the region. Until today, JP CČN maintains the notion of its basic mission, which is to ensure the quality of urban wastewater treatments at an affordable price. The priority task of the enterprise is economic and efficient urban wastewater and storm-water treatment within the mandatory public utility service (OGJS), which is the responsibility of the municipalities. CČN DK provides services on the basis of the Cleaning Ordinance, the Company Agreement and the Contract for the Lease of Infrastructure Facilities.

In addition to OGJS, JP CČN also performs industrial wastewater treatments, liquid waste treatments as well as intellectual services in these fields in accordance with the business strategy. These additional activities are carried out within the framework of special and market services with the aim of reducing the price of wastewater treatment for citizens as well as increasing the added value of the enterprise based on the surplus revenues achieved by marketing activities in accordance with the MEDO Regulation.

JP CČN performs wastewater treatment at the infrastructure installation (facilities), owned by municipalities. The role of the infrastructural facilities is to enable basic urban wastewater and stormwater treatments within the OGJS. In order to achieve the objectives, it is very important to provide a high-quality infrastructure, which must be fit for purpose and has to be properly maintained and modernized. For the next few decades, this goal was achieved by a successful upgrade in 2017. The reconciliation and dependence of the enterprise and the infrastructure enables an efficient and high-quality cleaning service, which is reflected in the satisfaction of users and owners and, most importantly, in responsible environmental management. In addition, the scope and function of the existing infrastructure also enables the performance of special services on a commercial basis for the external clients, in accordance with the owners' instructions.

A well-maintained infrastructure means the performance of basic and additional activities.
The high level of knowledge, experienced employees, and the use of all available methods, analyses and process parameters calculations enable optimal management of the cleaning processes at all levels. Pursuant to the terms of the lease agreement, which regulates business and operational relations between the owners and the tenant, JP CČN performs additional business activities for managing the infrastructure records and prepares reports for the owners. JP CČN pays the owners rent in the amount of infrastructure depreciation and at the same time represents a key process support to the CČN infrastructure and provides an efficient wastewater-treatment service through professional process management.

In addition to OGJS services and special services performed on public infrastructure, the JP CČN experts group also provides marketing services, which are considered as intellectual services and provide additional revenue to the enterprise. These services include, in particular, expert consultancy in the field of wastewater treatment, pilot experiments on the operation of special technological processes, experiments on the decomposition of different substrates, more complex analyses and expert opinions on the efficiency of the processes. The education of wastewater treatment personnel from the whole of Slovenia is one of the activities that brings a high professional reputation with the public as well as financial revenues for the enterprise. The training is provided by the professionally trained staff of JP CČN and partly by foreign lecturers.

4. Sustainable Development Strategy

In order to achieve the set goals in terms of sustainable development, a working environment has been created where the employees with their engagements and competences are the driving force for the success, growth and development of the enterprise. With diligent work and the personal commitment of the each individual, the group overcomes a narrow mindset and follows a clearly defined path of responsibility towards nature and people at every step. They are committed to high

ethical, environmental and work standards, and therefore build partnerships and mutual trust through open peer relationships. In its sustainability program, JP CČN has defined responsible behaviour towards employees, owners, users and the social and natural environment by integrating ecological, economic and social aspects, which are valued as performance indicators. From the sustainable-development point of view, JP systematically undertakes activities for recognized and socially important factors. Through the sustainable development guidelines, activities are undertaken to raise the enterprise recognition and evaluate investments in ecological and economic indicators. Due to the sensitivity of the CČN system in terms of coexistence with the local environment, its activities are carefully monitored and communicated with the interested public following the principle of a correct relationship with the environment.

The most important goal of the enterprise's activities is to follow sustainable development in all aspects and to act on the principle of social responsibility at all levels of operation. The enterprise is socially responsible to the natural and social environment with the priority goal of maintaining clean water, which is one of the most important basic assets. JP CČN manages the treatment plant, which became, after a successful upgrade, again the leading plant in Slovenia. It follows the important goal of continuous development, complemented by the implementation of basic research tasks for gaining a broad knowledge of the field of wastewater treatment. In addition, they trained operators at all professional levels for wastewater-treatment plants and provide expertises in the field of wastewater treatment. Crucial for maintaining the business success is the risk management, which is achieved by considering and addressing all the critical factors and high-quality process management. The best-possible success in the given circumstances is achieved by a high level of knowledge. Upgrading the CČN infrastructure created conditions for quality process control and ensuring the mission, vision and high goals at the process and business levels. The sustainably oriented and reliable performance of high-quality effluent treatment and the implementation of support processes contributes significantly to ensuring the conditions for healthy living in the natural environment. Thus, they supply users with high-quality services at an affordable price and develop professional solutions to reduce environmental impacts.

The sustainable development guideline incorporates important goals that are pursued on a daily basis. Firstly, the activities are aimed to reducing the environmental impact. The emphasis is on ensuring the quality of the treated water for reducing the impact on the Kamniška Bistrica river and the groundwater. This is achieved through continuous education and increased interdisciplinary skills. Therefore, efforts and resources are being invested in research and development as well as the introduction of modern technologies for the removal of various pollutants from the wastewater. This objective is also pursued through activities that include education, counselling and raising awareness of the local population and legal entities about the importance of reducing water use, treating wastewater and preserving our environment.

The goal of sustainable development is foremost followed by responsibility to employees. In this way we build trust and encourage them to acquire knowledge, which is very important for managing a demanding system, such as a wastewater-treatment plant. Through a transparent and reciprocal collaboration with the owners a common path is built. The performance of special services means an exception among Slovenian public enterprises, therefore conscientious work in this area also shows responsibility to the users. Due to the high depreciation and higher-quality cleaning services, our residents still pay an acceptable price for the service, which is partially covered by specific activities.

5. Upgrade in the year 2017

In 2017, the upgrade of the infrastructure for tertiary treatment, necessary for the effective implementation of wastewater treatment to the applicable standards, was completed. The treatment

plant provided the required level of cleaning over the years and as a part of the upgrade also implemented stricter environmental standards.

The investment in the upgrade amounted to about €15.5 million, where 80 % of the eligible funds came from the EU through the Cohesion Fund. An increased value of fixed assets and depreciation, which represent the rent paid by the enterprise to the infrastructure owners (in this case the six municipalities), is significantly greater than it was before the upgrade. The rental cost is distributed by water gauges to all users and represents the network charge, paid monthly by the users. The network charge is also included in the calculation of the treatment costs for industrial taxpayers. Such a treatment is carried out according to a special methodology where the cost depends on the load and degradability of the individual waste water. Equally, the cost of the network charge is taken into account when calculating the price for receiving liquid waste. The treatment of industrial wastewater and liquid waste does not fall under the category of OGJS, but represents special services, whose revenues reduce the price for their users.

The cost of the service includes the materials and services necessary to achieve the proper quality of the treated water that the CČN discharges into the Kamniška Bistrica river. The cost of wastewater treatment is charged separately and represents the equal amount (in m^3) of drinking water consumed in each household. After the upgrade, the cost of the service increased due to receiving more wastewater for cleaning and providing a greater cleaning effect, the increased consumption of chemicals and energy, increased maintenance and spare parts, and more dehydrated sludge.

Through the implementation of special services and a market approach, CČN DK managed to keep the network charges and the OGJS services below the average of comparable cleaning facilities in Slovenia, despite the upgrading of the infrastructure, which requires higher rent and costs in order to provide an improved cleaning effect. The total cost of the wastewater treatment for the average household thus increased from about €4 per month to about €7 per month, which is below the Slovenian average.

6. Market analysis with risk management

The company pursues the goal of providing a high-quality service at an affordable price, which is achieved through the additional performance of special and market services that are outside the scope of the OGJS. Due to the fact that JP CČN does not exclusively carry out activities within the framework of the OGJS, it is exposed to potential business risks that must be taken into account when planning its operations. Revenue and expense risks affecting business stability are managed through an advanced, process and business professional approach, supported by experience and professional knowledge. Effective risk management can crucially contribute to better results and safer performance of the enterprise's primary and supportive activities to ensure a sustainable, business-oriented management with a positive business result at the end of the financial year. Risks are assessed in the management as well as in the operational performance of our activities. High-quality is ensured by the implementation of the ISO 14001 standard, which is constantly upgraded to achieve the desired goals, in accordance with the nature of the enterprise's activities.
In the area of risk, the enterprise has been paying a lot of attention to following new technological approaches and, in recent times, to tightening the legal conditions, which are based on a tendency of increasing environmental protection from all possible aspects. The CČN system operates in accordance with the Environmental Protection Authorization (OVD), which incorporates the Industrial Emission Directive (IED) guidelines and defines the entire JP CČN activity, requiring the system to have an integrated approach and quality management of all environmental risks. In particular, more and more requirements and conditions for investing are emerging from the legislation, which is connected with the introduction of new technologies, more and more mandatory monitoring with an increased set of analyses and measurements and upcoming

obligations for the extraction of raw materials from individual fractions of the wastewater treatment processes. More importantly, in terms of risks to society, it is worrying that legislation or state authorities are placing more and more restrictions and tightening conditions for the reception of liquid waste by treatment plants. This fact may have a significant impact on the cleaning cost for citizens in the future, which at this time is still low and acceptable only because the company is treating liquid waste.

All identified aspects of the risk are interrelated. Quality assurance is thus crucial, as reflected by the adequacy of the prescribed parameters across all emission sources. Only in the case of quality assurance at all sources and levels we will be able to create the conditions for the intended range of services, which in turn is also linked to market demand. It is only at this stage that any demand can be considered as a business opportunity, which, if successful, is reflected financially. In case of a reduction of the volume of special services, which is the most risky in terms of process and financial planning, it will be necessary to start a timely approach to the price of the wastewater-treatment service for the category of OGJS. Regular monitoring of all aspects related to the operation of processes, business fluctuations and changes in the legislation enables the timely identification of threats to the stability of the enterprise's operations.

The enterprise will continue to manage its resources economically with a sustainable and holistic approach to performing its activities and successful operations. An important concern is cost management and economical use, which is done through regular and careful procurement procedures and a thorough review of each contract. On the cost side, there is the risk of potential unforeseen events and technological problems in processes that are usually difficult to influence. These risks have been adequately managed in the past and will be expected in the future due to years of experience and good expertise.

In the area of risk, two of the most critical indicators are identified that could have a significant impact on the scope of the operations of the enterprise in the future, i.e., the achievement of environmental requirements and the scope of special services.

Environmental requirements

The successfully completed upgrade of the system has significantly reduced the risk of financial and misdemeanour liability due to the potential non-achievability of legal requirements. In the event of exceeding the parameters at the outflow or outflow of the sub processes, significant risk would arise because the CČN would have a restriction on the acceptance of liquid waste, which would consequently significantly reduce the JP CČN revenues. According to the MEDO Regulation, revenues from special services are taken into account in such a way as to reduce the cost of a particular public service. Due to the interconnectedness and impact of special services revenues on the price of OGJS, there is a risk of uncertainty in the volume of market revenues, which poses a potential risk to the enterprise's operations.

The CČN system operates in accordance with the prescribed values or within the requirements of the environmental permit, which is expected in the future. All process assemblies within the system function properly and the basic wastewater treatment activity is carried out to the intended extent and quality. Due to the complexity and variability of external process conditions, the existing process sets are subject to certain risks, so in the future our main objective will be operationally aimed at managing risks by effectively managing the processes in all conditions and reaching the statutory limit values on all the emission sources.

The wastewater-treatment service, as the main activity and the liquid-waste-treatment service as the support activity, must be provided in a quality and demonstrable manner at all times, which is achieved through regular monitoring and appropriate measuring devices and analyses. Risks in this segment are usually of a technological or technical nature and are managed by a team of

experts through a critical appraisal approach and an immediately effective response. Only in this way can the risks of quality assurance, which could seriously jeopardize the business future and consequently have an impact on environmental pollution through increased emissions, be reduced.

Extent of specific services

JP CČN has been engaged in the disposal of liquid waste as a special activity for many years, which is a rarity in wastewater-treatment plants in Slovenia. This advantage has been gained and maintained by being classified as an IED member and obtaining an IED environmental permit. The enterprise has recognized the business potential related to the ecological aspect, which is reflected in the professional approach to solving the problem. This activity, related to the revenues and the cost of cleaning for the OGJS category, is permitted on the basis of a professional skilled research team and years of experience in managing the processes of wastewater treatment and the disposal of liquid waste. Analytical and experimental procedures have been developed to verify substrates for suitability of reception. Thus, the reception of liquid waste is limited to only certain waste classification numbers that the CČN can accept in accordance with the OVD, with the amount depending on the capacity of the disposal facilities and the possibility of treating these substrates in a process sense. Risks associated with the reception of liquid waste require a timely and effective response to changes in the process conditions and the adaptation of market activities. For this reason, they have developed a base of acceptable substrates and a plan for the scope of services for the future. The specific services segment assesses the scope and type of services, taking into account the potential risks posed by intense competition, the consequent need for price reductions and, in particular, procedural constraints.

The treatment of industrial wastewater and liquid waste falls under the scope of special services, and at individual emission sources, in accordance with the OVD, we are obliged to ensure that the processes ensure adequate quality on the discharge from the installations. Since the limit values for discharges from individual processes (EK and BRO) are very low, there is a certain risk of exceeding the values and, consequently, the prohibition of the acceptance of this wastewater into the CČN system.

Therefore, special attention will be paid to the management of these processes and, with the professional knowledge and the necessary resources, we will ensure that, in the light of new environmental and technological requirements, this waste is enabled. The quantity of services is also very important in the industrial wastewater segment as any failure of an industrial plant means a significant reduction in wastewater volume or the cost of a service would have a significant impact on the price of public services, so there are also some risks in this part. The trend in the scope of industrial wastewater treatment services is difficult to plan with greater certainty, as industrial pollutants cannot be estimated in the long term due to fluctuations in production processes. However, it is important that the upgraded CČN offers the reception of greater volumes and greater loads of wastewater from industrial sources, which is an important fact for industrial users. The planning of the volume of industrial wastewater poses a certain risk in terms of forecasting the quantities and also the cost of the service, which depends on the load of each source of pollution. All major industrial users are contracted and the cost covers the cost of cleaning this category at a profit.

7. Revenue analysis

Considering the fact that the company does not work as a classic sewage treatment plant with limited activity solely within the framework of OGJS, but derives a significant part of its revenues from special services, the realization of revenues is more unpredictable and depends on the processing capacity and success of acquiring business in the market.

According to the MEDO Regulation, revenues from users of the cleaning service are divided on the network charge and the cost of running the cleaning service. The network charge is charged to the amount of infrastructure depreciation and the revenue from the treatment service represents the cost of running the wastewater treatment. The amount of revenue from the basic wastewater treatment depends on the volume of quantities accepted for treatment. Revenue is generated only on the basis of a charged amount that is much lower than the amount actually received.

In 2018, revenues from the OGJS category involving households and the municipal wastewater were € 2,137,319, which is an 88 % of increase compared to the previous year. Increased revenues are primarily the result of an increase in the price of the network charge and also of the service, and partly also a consequence of additional connections to the sewer network. Revenues from the category of sewage sludge and sludge cleaning, accounted by the amount of consumed drinking water, were € 121,243, meaning 135 % higher than last year, due to the increase of network charges and services from 1.1.2018.

Revenues from the treatment of industrial wastewater received by the CČN through the sewer network, which represents the category of special activities, were € 1,285,808, which is 4 % less than in the previous year. Revenues of this category under the invoiced price fully cover their own price, including the network charge. Revenues from special driveway activities totalled € 695,005 in 2018, an increase of 29 % over the previous year. The increased revenues are mainly due to the increased cost for the provision of these services by JP CČN. The volume of quantities accepted that do not represent the activities of the OGJS is crucial to ensuring sufficient revenue to fully cover the cleaning service. According to the MEDO Regulation, revenues from special activities, if carried out on infrastructure, must cover the loss of revenue due to the failure to reach its own price at the OGJS. This means that in the case of reduced volumes and revenues from specific activities, the cleaning price of the OGJS category will have to be increased to the level of its own price.

Total revenue from all the above categories and from marketing services amounted to € 4,379,555, which is 32 % more than in the previous year. The increase in revenues can be seen primarily in the category of OGJS, where, despite the increase in the beginning of 2018, the sales price of the service and network charges is still much lower than its own price, since the loss of revenue is covered by revenues from special services.

The following is a graphically presented share of wastewater by source in 2018, which shows a clear difference between the percentages of received wastewater and the revenue from these quantities, which is significantly higher for special services compared to the category of OGJS. The following is a table of financial output by category and municipality for 2018, compared to 2017. Further, a table of revenue from the network charge by municipality for 2018 is presented.

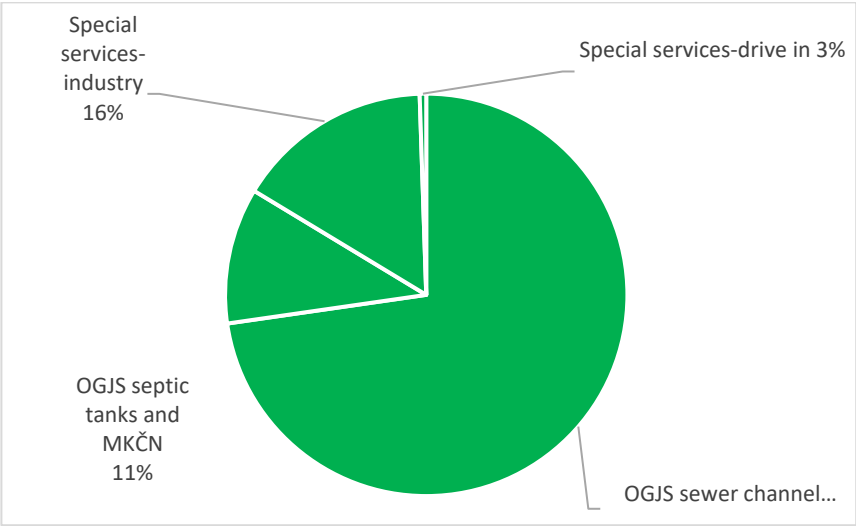

Figure 2: Percentage of calculated wastewater quantity by sources in m^3

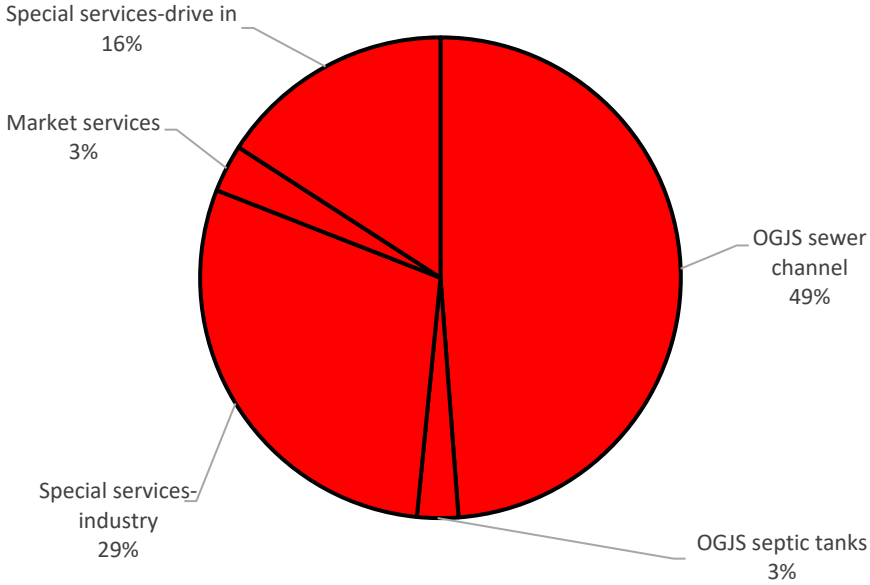

Figure 3: Share of operating income by source in EUR

8. Performance appraisal and performance indicators of the company

Table 1: (Stražar, M. 2019) presents a comparison of business results for 2017 and 2018. The increase of operating income and net profit is clearly evident. The latter represents almost 9.5 % of the value of revenue for 2018, which is an extraordinary result for a public enterprise.

TABLE 1 (EUR)	Achieved 2018	Share (%)	Planned 2018	Comparison achieved/ planned 18	Achieved2017	Share (%)	Comparison 18/17
Overall operating income	4.387.817	99,69	4.126.171	106,34	3.329.662	98,89	131,78
Overall Turnover	4.401.673	100,00	4.127.171	106,65	3.366.874	100,00	130,73

TABLE 1 (EUR)	Achieved 2018	Share (%)	Planned 2018	Comparison achieved/ planned 18	Achieved2017	Share (%)	Comparison 18/17
Total expenses	3.889.549	100,00	3.996.873	97,31	3.036.276	100,00	128,10
Net profit	417.601	100,00	105.541	395,68	271.979	100,00	153,54

Business and financial performance indicators of the company

Below is a comparison of JP CČN's business results and the average of the industry sector using indicators of accelerated coverage of short-term liabilities, operating efficiency and average monthly salary per employee, published by the Agency of the Republic of Slovenia for Public Legal Records and Related Services. Industry sector E 37 - sewage treatment is considered for the comparison.

Comparison of JP CČN's operations with industry average E 37 - sewage treatment

TABLE 2: INDICATOR	2018 JP CČN	2017 JP CČN	2017 E 37 average
Quick ratio	5.31	8.49	1.60
Overall efficiency	1.13	1.11	1.00
Monthly wage per employee (EUR)	2.204	2.307	1.521
Labour cost per employee (EUR)	36.101	36.732	25.971
Value added per employee (EUR)	76.026	64.709	33.814
Labour cost in added value (%)	47.48	56.76	76.80

A comparison of the JP CČN business with the industry average E 37 - sewage treatment has certain limitations, as industry data include the operations of all wastewater-treatment and wastewater-service providers, both public and purely commercial, without including service providers that are dominantly engaged in another activity. The methodological appropriateness of the selected indicators for assessing business performance is also limited. The ratio of accelerated coverage of short-term liabilities should be analysed together with other liquidity indicators as a static indicator. The company has no financial debt leased and fully finances capital operations, so the maturity of financing sources is much better than in the industry. The indicators are higher than the industry and comparable to previous years, while being significantly better than the average of the utility sector, E 37 - sewage treatment. The amount of the average monthly salary depends very much on the educational structure of the employees, which is generally high in companies that perform wastewater treatment only, because this is dictated by the requirements of technological processes.

9. Satisfaction of service users and the role of the Supervisory Board

Satisfaction of service users

In December 2018, the enterprise received a Survey of Customer Satisfaction with JP CČN Domžale—Kamnik d.o.o. Services, ordered earlier that year. The survey raised some key questions for service users about their knowledge of the company, their reputation, their satisfaction with the services, the relevance of the price/quality ratio, and any complaints about the work of the company.

In the research source (Cerkvenik, S., 2018) the two most important issues are found: satisfaction with the services provided and the relevance of the price/quality ratio by the respondents are given a very high rating. Satisfaction with the services provided was rated on a scale of 1–5 with a rating of 3.9, and 70 % of the respondents rated the price/quality ratio as adequate.

Role of the Supervisory Board

The Supervisory Board was constituted only in 2012. At present, the SB has three representatives of shareholders who have certain supervisory tasks in accordance with the applicable social contract. The impact and the work of the Supervisory Board on the management of the enterprise are not measurable so far, but they are also reflected in the enterprise's exceptional business results and the impeccably executed €15 million investment in upgrades, which did not result in any affair, complaint or damage to the enterprise's reputation. In 2018, the Supervisory Board also carried out a self-assessment of its work in accordance with the source (Kovač, B., et al.) and informed the Management Board about its findings.

10. Conclusion

In the modern world, the success of the enterprise is mostly highlighted by economic indicators. The responsibility for protecting the nature and the environment is often forgotten.

An example of the organization and activity of a public service enterprise CČN shows that much more can be achieved on a treatment plant than required by the public service provider and the owners. Successful performance of specific and market-based services will reduce the cost of wastewater treatment for the user by providing acceptable household costs, contributing a permitted share of profits to municipal budgets, and facilitating the enterprise's advanced and development-oriented business strategy. This makes the enterprise more than just a public service enterprise.

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KNOWLEDGE CREATION PROCESS IN INTERNAL AUDIT FUNCTION – PERFORMANCE IMPROVEMENT BETWEEN EXPLORATION AND UTILIZATION OF KNOWLEDGE

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Abstract
In the context of current business environment, where circumstances and conditions of doing business jointly with technology change very rapidly, organizations have to adapt themselves adequately in order to survive. Facing such dynamic environment organizations that actively approach to changes tend to identify and utilize assets they possess or resources they could exploit, create information and knowledge (Lopez et al., 2005), process and transfer them. Skills and knowledge of employees are often treated as a comprehensive potential for improvement of organizations (Gupta and Sharma, 2016), but their adequate utilization, which lead to learning in organization, demand primarily organizational context and strategic orientation, on one hand, and defined process of organizational learning on the other. According to Song et al. (2014) performance of an organizational unit might be identified as an appropriate indicator of the success of organization in balancing between behavioral factors and engagement of employees and organizational context. The role of internal audit has not been fully recognized in the context of learning and knowledge creation as there are significant areas that allow for further improvement through systematic learning and knowledge management. The necessity of identification of possible roles of internal audit is especially important in relation to lessons learned and acquired knowledge from auditing exercises and their successful application within the system at a later stage. Looking at internal audit through this lens there appears a completely new perspective of its role, added value and performance. The paper explores the knowledge creation process in internal audit function, covering explicit and tacit knowledge, as well as relations between knowledge creation process and internal audit performance improvement based on self-reports of internal auditors. The analysis was performed on the responses of 95 internal auditors, comparing results between two regions, Scandinavia and Balkan, not limited to particular industry. The questionnaire was carried out in second semester of 2018.

***Keywords**: Internal Audit Performance Improvement, Knowledge Creation Process, Organizational Learning, Dynamic Theory of Knowledge Creation*

Track: *Management & Leadership*

Word Count: *6.548*

1. Introduction

In knowledge-based organizations the ability of creating knowledge is considered one out of two leading goals, together with application of knowledge (Spender, 1996). Knowledge creation observed as a process, the output of processes, or as a value-adding outcome (Mitchell and Boyle, 2010) represents a value chain in which each phase commits additional value in improvement of organizational performance and competitive advantage (Carlucci et al.,2004; Cooke, 2005; Holsapple and Singh, 2004; Lee and Yang, 2000).

The position of internal audit has recently received increasing importance within corporate governance, particularly due to its changing character and links to the risk-based internal control approach. Internal auditors have utilized this position by altering internal audit functions and mode of engagements broadening their scope and areas of involvement to risk management, control and

governance processes, in order to increase the value added to organizations. Nevertheless, this change also entails broader exploration and redefinition of internal audit processes, competencies and roles (Arena and Azzone, 2009), as well as transformation of self-images of internal auditors (Sarens et al., 2016). On the other hand, in rapid changes of business environment and businesses themselves, which require an increasing necessity and high expectations of internal audit function support, internal auditors are enforced to keep the pace, to develop and to improve knowledge of the organization's processes, risk management and control systems (Deloitte, 2012). Regardless, the role of internal audit has not been fully recognized in the context of learning and knowledge creation as there are significant areas that allow for further improvement through systematic learning and knowledge management. The necessity of identification of possible roles of internal audit as knowledge creator is especially important in relation to lessons learned and knowledge acquired from auditing exercises and their successful application within the system at a later stage. In such complex business environment and framework of increasing attention to the role, added value and performance of internal audit, it would not be incoherent additionally to explore different aspects of internal audit in an organization.

2. Research Interest

The aim of the paper is to observe knowledge creation by internal audit function, as a sub process of organizational learning, and to analyze relations and perspectives for successful application of this knowledge within the organization at a later stage, for internal audit function, audited but also other organizational units. The paper explores the dynamic aspects of knowledge creation processes, interaction and conversion between explicit and tacit knowledge among internal auditors, impacts and relationships among spiral knowledge phases and internal audit performance improvement.

The study with 1 key question and 1 hypothesis covers self-report of internal auditors in context of organizations they work for and internal audit function they belong to, in terms of creating knowledge, potential of internal audit for knowledge creation, and identification of and description of corresponding interrelations.

The key research question of the paper is:
Q1: What are the relationships among the phases in knowledge creation processes in internal auditing and internal audit performance improvement?

H1: The knowledge creation process in internal audit function will positively influence the internal audit performance improvement.

2.1 Theoretical framework

Internal audit role in organizational learning entails a proactive approach to challenging current organizational processes at the individual level, at the organizational unit level and at the organizational level (Becket and Murray, 2000). The audit process, as stressed by Becket and Murray (2000), is an example of productive learning that emphasize learning and knowledge creation making both the explicit and implicit more noticeable. Internal auditors deliver independent, objective evaluation of organization's governance and its effectiveness, but also act as catalysts for change (Swanson, 2010), providing outcomes aimed to add value and to improve the organization. In order to success in dynamically changing environment contemporary internal auditors must provide a high level of knowledge and contribution to learning equally or more than level of changes is (Pickett, 2000).
The complete overview of internal audit function within an organization is a complex overlap among the roles internal audit has taken over, or expected to take over, and providing value to the organization through managing performance of internal audit. Perspectives of observations among stakeholders are multisided and due to the predefined basic role and characteristics of internal audit

not always complementary. However, a deeper exploration of roles, added value, and performance, including relevant tools and measures and interrelations among them, are still underdeveloped.

The role of knowledge creator by internal audit function, within specific organizational context (Lenz, 2013), is complementary to the role of farmer (Sarens et al., 2016), internal auditors who learn and improve organization without formal authority in knowledge creation but by inspiring others and utilization of their outcomes and capabilities in becoming party who drives changes.
As follows each audit is a part of learning, an ongoing and progressive process without no predefined outcomes and clear end (Pickett, 2000). Moreover Picket (2000) in seeking knowledge creation directly correlates learning to development and progress of organization.
Finally, according to Eden and Moriah (1996) effective internal audit can improve learning process in the organization, as well as positively influence motivation, deterrence and process improvements.

Organizational learning is associated with the creation of the major source of competitive advantage for organizations in the future (Senge, 1990; Stata, 1989), and additionally to the sustainable competitive advantage of an organization (De Geus, 1998). Organizational learning is a process that aims to help the organization to acquire and continuously to utilize the knowledge (Cummings and Worley, 1997), in order to understand and to manage their experiences (Glynn et al., 1992). The role of organizational learning is to reduce uncertainty and change resistance (Geertz, 1964), to improve the organization's efficiency and performance (Cummings and Worley, 1997; Collis, 1996), to create the major source of competitive advantage (Senge, 1990; Stata, 1989) for the survival of today's organizations (Lähteenmäki et al., 2001), and for reaching the leading role in future (Ortenblad, 2004).

Organizational learning on unit level comprises the processes through which organizational units (departments or divisions) change as a result of experience (Argote and Opfir, 2005), acquired directly by focal organizational unit, or indirectly from other units (Levitt and March, 1988). In addition, description of characteristics of organizational units and their roles is also important for further research on learning within organizations as it affects learning among them (Argote and Ophir, 2005). The main sub-processes through which organizational learning on unit level appears are creating, retaining, and transferring knowledge; new or evolving knowledge within the organization (Argote et al., 2001).

The existence and development of organizational learning is directly related to capabilities of an organization to recognize the potential usefulness of knowledge, especially in terms of development of homogeneous understanding of the various interpretations by organizational units (Huber, 1991). In order to understand organizational learning it is important to realize that organizational learning takes place in a context (Glynn et al. 1994), within milieu of internal and external forces in which the organization perform its tasks, affecting not only work and processes but also performance of the organization.

Moreover, learning should not be observed merely as a pure obtainment of knowledge but essentially as its utilization aiming application of changes (Cameron and Green, 2004). The model of change through learning, with origin in organizational development and later applied to learning organization and knowledge management, as stated in Green (2007), stress importance of organization maturity for changes by ensuring adequate capacities for changes, definition of appropriate processes for feedback and learning, knowledge creation as well as knowledge transfer.

Knowledge creation, as a sub-process, appears at the beginning of the learning processes. The terminology used in description of knowledge creation is diverse; knowledge creation and

retention (Argote et al., 2001), knowledge acquisition (Huber, 1991), knowledge discovery and invention (Cummings and Worley, 1997), and as such the terms would be covered in the paper by term of knowledge creation. Knowledge creation refers to creation of new knowledge and utilization of the organization's memory; i.e. exploration of a new and exploitation of existing knowledge (March, 1994). Knowledge is defined (Nonaka, 1994) as *dynamic human process of justifying personal beliefs as part of an aspiration for the "truth.*" Moreover, knowledge of organizational units has a pivotal position in learning within organizations due to its role in the growth of unique potential and competitive advantage in firms (Argote and Ingram, 2000).

2.2 Research Framework

Knowledge creation process

The exploration of knowledge creation by internal audit we basically developed on the dynamic theory of knowledge creation by Nonaka (1994), defined as process of transformation and amplification manifested in the determination of systemic organizational learning, and exhibited in interaction between tacit knowledge and explicit knowledge in spiral process. The whole theory is designed on three main pillars: 1) the SECI model of knowledge creation (Nonaka and Takeuchi 1995); 2) the Japanese Ba concept of shared context which corresponds to the SECI model modes (Nonaka et.al, 1998); and 3) the knowledge assets basis.

For the study purpose we were focused on SECI model of knowledge creation which articulates the connections between the epistemological and ontological dimensions of knowledge creation process, and illustrates 4 modes of continual interrelations between tacit and explicit knowledge (Nonaka, 1995):

1) **S**ocialization – conversion from tacit knowledge to tacit knowledge through shared experience between individuals
2) **E**xternalization – individual process of conversion tacit knowledge to explicit knowledge
3) **C**ombination – conversion of combination of explicit knowledge from different organizational context to a more usable "new" explicit knowledge
4) **I**nternalization – conversion from explicit knowledge to tacit knowledge i.e. learning by doing.

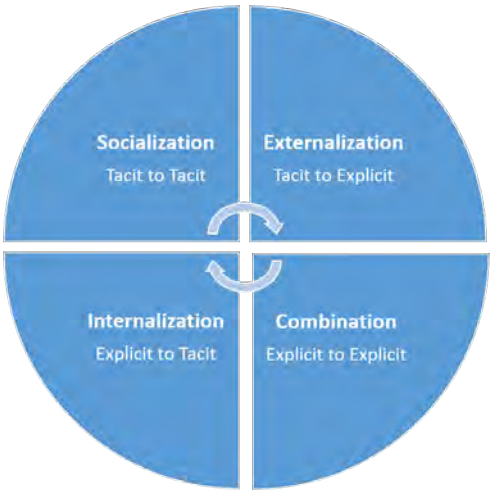

Figure 1: Spiral process of knowledge creation – SECI model

The epistemological dimension defines transformation and interaction between tacit knowledge and explicit knowledge and results in creation of new ideas and concepts. The ontological dimension is oriented to relations among individual, inter/intra-organizational and organizational knowledge, and more precisely conversion of individual knowledge into group/organizational unit knowledge, and further conversion of the group/organizational unit knowledge into organizational knowledge, including possible reverse actions.

Model of observation of knowledge creation process in internal audit function includes: setup of internal audit function and enlarging of knowledge of internal auditors within an internal audit function, sharing experience among internal auditors, conceptualization and crystallization of experience shared among internal auditors, justification of quality of created knowledge and knowledge network.

2.3 Internal Audit Performance Improvement

Definition of an effective performance management system as a results oriented system that establish harmonization of individual with organizational goals and strategy is tendency in modern organizations (Pulakos, 2009). Three main challenges that appear from its establishment are: what kind of activities should be measured, which performances are of interest for measurement, how can/should performance indicators be measured. These challenges are at least equally if not sometimes even more important in measuring performance of internal audit and its improvement due to position and roles internal audit plays within organization. As spectrum of perspectives and attitudes of stakeholders towards internal audit are broad so measures that should be used for assess and evaluation of internal audit performance are similarly diverse and stratified as well. Exploration and analysis of relevance of measures are presented by internal audit associations (IIA, national chapters and professionals), big external audit and consulting firms and academics. For the ground of identification of relevant internal audit performance improvement measures for our research we basically started with CBOK (2015) the Internal Audit Value Proposition, characterized by assurance, insight, and objectivity, jointly with Performance Measurement Triangle, that provides alignment of performance expectations between internal audit and stakeholders, continued with IPPF practice guide of measuring internal audit effectiveness and efficiency (IIA, 2010), and ended with measuring value and performance that were further decomposed and developed by Ernst & Young (2016).

Internal audit performance improvement indicators of relevance for the study purpose we constructed on review of existent relevant literature and analyzed by 22 items, divided into 3 sets, related to performance, value and capacity of internal audit function.

3. Methodology

3.1 Data collection

The data collection was based on the quantitative methodology established on relevant literature, modification of existing and development of new instruments. In order to collect the data we developed an online questionnaire in English, using LimeSurvey platform, consisted out of 4 main sections, 11 subsections and 86 items.
For the measures of three out of four main sections; dimensions of learning organization, organizational knowledge process creation and internal audit performance improvement; we used five-point Likert scale, ranging from 1 (completely agree/significantly increasing) to 5 (completely disagree/significantly decreasing). Fourth section was consisted out of demographic related multiple choice, one choice and text questions. Since the relationship between internal auditing and knowledge creation has not exploited in academic writing or in internal audit practice, and therefore due to certain degree of novelty of the topic, the paper covers broader context of internal audit profession, not limited to a particular industry.

In the final stage of development the draft of the questionnaire was discussed with three internal audit practitioners and academics from three countries, South Africa, Germany and Macedonia/FJRM. Based on comments the draft of the questionnaire was slightly redefined and restructured.

Our intention initially was to cover internal auditors from the Europe reaching them over national internal audit associations. We contacted, with included proposal for cooperation, 42 associations in 40 countries over their official e-mail addresses in period July-October; 20 of them responded to the proposal, 13 out of 20 accepted the proposal for mediation and sent the link of the questionnaire over e-mail with the invitation for participation to their members, 2 out of 20 accepted the proposal for mediation and provided the link of the questionnaire with the invitation for participation to their members over associations' websites and the rest were not interested or not in position to get involved.

The total of 184 completed and 595 partially completed questionnaires were collected in period from August 2018 to January 2019, from 18 countries. Upon initial analysis, taking into account that number of collected questionnaires from 11 countries was insignificant, we decided to focus our research on two regions and comparison between them, Scandinavia (Norway and Denmark) and Balkan (Bosnia and Herzegovina, Serbia, Croatia), with 95 completed questionnaires and response rate 3,18% and 3.21 % in average.

Table 1: Population

Variable	Value	Scandinavia		Balkan	
		Size	Percentage	Size	Percentage
Population		43		52	
Industry	Financial Services	21	48.84%	23	44.23%
	Government	9	20.93%	9	17.31%
	IT and Telecommunications	0	0.00%	4	7.69%
	Manufacturing	9	20.93%	11	21.15%
	Services	2	4.65%	4	7.69%
	Education	2	4.65%	1	1.92%
Number of employees	Under 9	0	0.00%	0	0.00%
	10-49	0	0.00%	3	5.77%
	50-249	0	0.00%	12	23.08%
	250-999	3	6.98%	15	28.85%
	1000-4999	13	30.23%	16	30.77%
	5000-50000	26	60.47%	6	11.54%
	Above 50000	1	2.33%	0	0.00%
	Average	16,309.50		2,776.20	
Number of internal auditors	Under 3	4	9.30%	20	38.46%
	4-10	17	39.53%	17	32.69%
	11-30	11	25.58%	12	23.08%
	31-80	3	6.98%	0	0.00%
	81-150	7	16.28%	1	1.92%
	Above 150	1	2.33%	2	3.85%
	Average	35.0		24.0	
Primary responsibility	Head of Internal Audit/CAE	15	34.88%	18	34.62%
	Senior Internal Auditor	25	58.14%	27	51.92%
	Junior Internal Auditor	3	6.98%	7	13.46%
Education Background	PhD/DBA	4	9.30%	1	1.92%
	Master	34	79.07%	34	65.38%
	Bachelor	5	11.63%	17	32.69%
Certification	Acquired at least 1 international audit certificate (CIA/CFSA/CRMA/CGAP/CCSA/QIAL/CISA)	23	53.49%	10	19.23%
	Acquired at least 1 international finance/accounting certificate (ACCA/CFA/CPA)	3	6.98%	1	1.92%
	Acquired at least 1 local country audit certificate	8	18.60%	36	69.23%
	Acquired at least 1 local country finance/accounting certificate certificate	10	23.26%	7	13.46%
	Still did not acquire any certificate	9	20.93%	8	15.38%
Gender	Male	29	67.44%	21	40.38%
	Female	14	32.56%	31	59.62%
Age	Under 30	1	2.38%	5	9.62%
	31-40	12	28.57%	18	34.62%
	41-50	13	30.95%	16	30.77%
	51-60	15	35.71%	11	21.15%
	Above 60	1	2.38%	2	3.85%
	Average	46,8		42.8	
Experience in internal auditing	Under 3	6	13.95%	11	21.15%
	4-6	8	18.60%	7	13.46%
	7-9	4	9.30%	11	21.15%
	10-12	5	11.63%	16	30.77%
	13-15	3	6.98%	6	11.54%
	Above 15	17	39.53%	1	1.92%
	Average	13.0		8.1	

These two regions were chosen on the basis of cultural (Hofstede et al., 2010) and heritage similarities of countries within the regions, on one hand, but also similar business related indicators of countries within the regions expressed in corporate governance index values (Kaufmann, 2004), on the other hand. In the European context these two regions are on the opposite sides and values in both observed aspects, so we consider them relevant for the study purpose.

3.2 Data analysis

For the analysis of data several techniques were conducted. As a starting step we conducted general descriptive and scale reliability analysis as basic ones. In next phases, in order to answer the research questions of relationship among defined variables and relevant correlations, canonical correlation was conducted.

Canonical correlation analysis was conducted for the assessment and measurement of the relations among variable sets, sets of the phases of knowledge creation process, and sets of the internal audit performance improvement. Underlying principle of canonical correlation analysis is to provide correlation between the set of dependent variables and the set of independent variables (Hair, et.al, 2006).

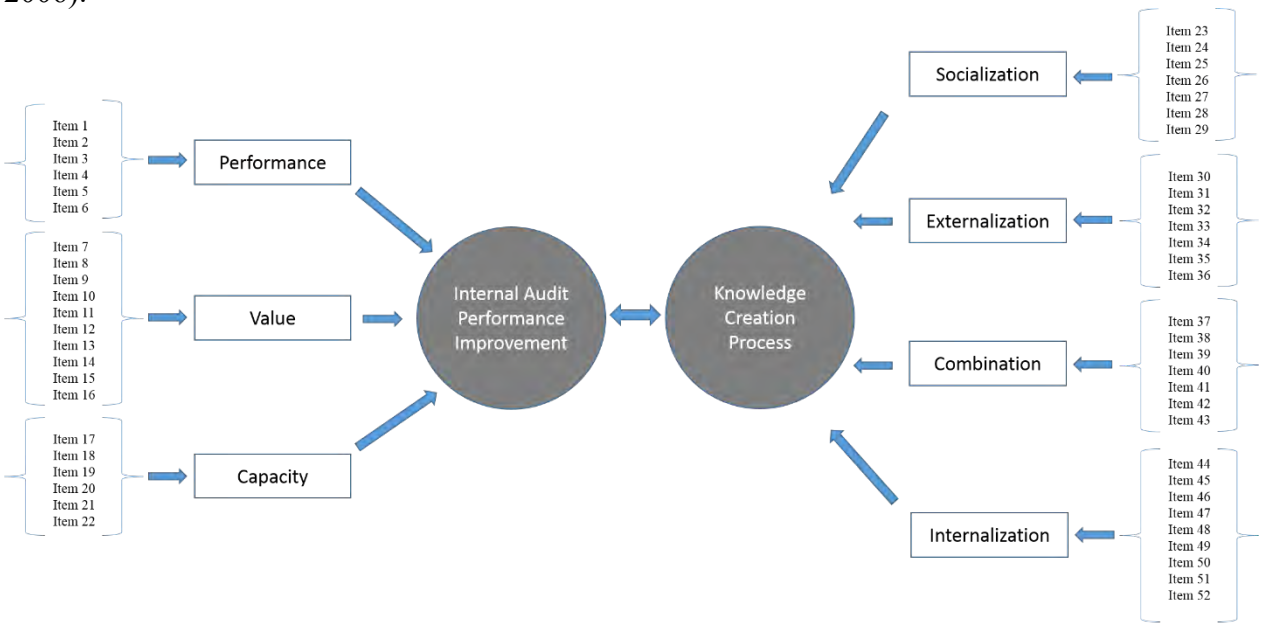

Figure 2: Canonical correlation model

The main advantages of canonical correlation as a multivariate technique (Sherry and Henson, 2005) are: minimization of experiment wise error/test wise error/Type I error (Thompson, 1991), adequacy of investigation of variables that have multiple causes and multiple effects, such as application in behavior research, usage instead of other parametric tests (ANOVA, MANOVA, multiple regression, Pearson correlation, t-test, point-biserial correlation, discriminant analysis, etc.) in many cases and under specific circumstances (Sherry and Henson, 2005).
The canonical correlation analysis was performed by the MANOVA multivariate analysis of variance using the SPSS 25 statistical software.
The theories were applied in internal audit process and examined within the context of the study. The paper is in a certain extent methodologically connected to the work of Song (2008), with a significant modification in terms of structure and research concept.

4. Discussion of results

Item Reliability Analysis

For the purpose of analysis of internal consistency level and reliability of multiple item measurements we used Cronbach's alpha analysis (Schmitt, 1996). The results indicated the satisfactory level of internal consistency of items within separate construct variables with scores between .799 and .914 and thus of the substantial reliability for further research, except for Performance whose score was significantly below .700 in one of observed models.

Table 2: Overview of item reliability statistics

	Cronbach's Alpha		N of Items
	Scandinavia	Balkan	
Socialization	0,855	0,899	7
Externalization	0,904	0,914	7
Combination	0,867	0,898	7
Internalization	0,799	0,892	9
Performance	0,325	0,691	6
Value	0,800	0,895	10
Capacity	0,799	0,885	6

According to Cronbach (1951) even though a high score of alpha was desirable the key point should be interpretation of obtained scores which was often possible without reaching high values of alpha. Schmitt (1996) claimed that there is no boundary of general acceptance of alpha stressing that instruments with quite low score of alpha can be used and be useful in some circumstances. Bearing in mind previously said, research concept and purpose of study we decided to keep Performance as a variable for the exploration of relevant correlations

Canonical Correlation Analysis

We conducted a canonical correlation analysis using four independent variables - predictors and three dependent variables - criterions evaluating relationship between two related variable sets, knowledge creation process and internal audit performance improvement department separately on two populations (Balkan and Scandinavia). Relevant test statistics described the full canonical correlation model meaning evaluation of shared variance between the independent and dependent variables across all canonical functions.

The full canonical correlation models were statistically significant, with score of Wilks's Λ=.336, $F(12, 119.35) = 5.073$, $p < .001$ for Balkan (Bmodel) and Λ=.500, $F(12, 95.54) = 2.383$, $p < .001$ for Scandinavia (Smodel). Accordingly, the overall score of R_c^2 for the full Bmodel 1- Λ=.664, and .500 for the full Smodel, showing proportion of variances shared between all variable sets across functions, could be interpreted as statistically significant.
The performed analysis resulted in three functions with R_c^2 of .605, .131, and .022 for each function in Bmodel, with the sum for the set of all three functions of .757 comparing to the indicator of the full model that showed explanation of .664, of the variance shared between all variable sets across functions. On the other hand the analysis showed significantly lower scores of R_c^2 in Smodel of .356, .172, and .061 for each function, and of .590 for the set of all three functions comparing to the indicator of the full model that showed explanation of .500.

Also we made analysis of reduction of dimensions in order to test hierarchal arrangement of functions for statistical significance, F1(12, 119.35)=5.073, $p < .001$, F2(6, 92.00)=1.294, p =.268, F3(2, 47.00)=0.521, p=.597 for Bmodel, noting that the full model (Functions 1 to 3) was statistically significant, and Functions 2 to 3 and Function 3 were not statistically significant. According to effect of R_c^2 for each function, the first two functions were considered significant for the further analysis in the study context (60.5% and 13.1% of shared variance). On the other hand functions for statistical significance for Smodel F1(12, 95.54)=2.383, p=0.010, F2(6, 74.00)=1.656, p =0.144, F3(2, 38.00)=1.228, p =.304 noting that the full model (Functions 1 to 3) was statistically significant and Functions 2 to 3 and Function 3 considered as not statistically

significant. According to effect of R_c^2 for each function, the first two functions were considered significant for the further analysis in the study context (35.65% and 17.25% of shared variance).

The Function 1 explained canonical correlation between two variables with residual variance left over unless the correlation between those variables is 1.00. The Function 2 explained canonical correlation of residual variance between variables that were not observed by Function 1.

Table 3: Overview of canonical correlation analysis

	Function 1 - Balkan			Function 2 - Balkan			
Variable	Coef	r_s	r_s^2 (%)	Coef	r_s	r_s^2 (%)	h^2 (%)
Performance	-0,013	-0,745	55,50	1,381	0,358	12,82	68,32
Value	-0,480	-0,758	57,46	-1,398	-0,356	12,67	70,13
Capacity	-0,702	-0,893	79,74	0,035	0,237	5,62	85,36
R_c^2			60,48			13,08	73,56
Socialization	0,064	-0,735	54,02	-1,386	-0,620	38,44	92,46
Externalization	-0,594	-0,945	89,30	0,136	-0,132	1,74	91,04
Combination	-0,196	-0,861	74,13	0,812	0,195	3,80	77,93
Internalization	-0,348	-0,910	82,81	0,210	0,001	0,00	82,81
	Function 1 - Scandinavia			**Function 2 - Scandinavia**			
Variable	Coef	r_s	r_s^2 (%)	Coef	r_s	r_s^2 (%)	h^2 (%)
Performance	0,636	0,829	68,72	-0,395	-0,366	13,40	82,12
Value	0,443	0,71	50,41	-0,125	-0,187	3,50	53,91
Capacity	0,354	0,445	19,80	0,934	0,891	79,39	99,19
R_c^2			35,65			17,24	52,89
Socialization	-0,492	0,329	10,82	1,208	0,876	76,74	87,56
Externalization	1,524	0,86	73,96	-0,337	0,390	15,21	89,17
Combination	-0,151	0,361	13,03	-0,41	-0,001	0,00	13,03
Internalization	-0,329	0,29	8,41	0,141	0,501	25,10	33,51

The analysis summarized in table 3 and additionally presented in Appendix in tables 5 and 6 included relevant standardized canonical function coefficients and structure canonical coefficients of Functions 1 and 2, squared structure coefficients and canonical communality coefficient for both functions for each variable.

1) <u>Bmodel</u>

The coefficients at the Function 1 for Bmodel showed primary contribution of Capacity and secondary contribution of Value to synthetic dependent variable, with a non-significant contribution of Performance. The previous conclusion was confirmed by distribution of scores of structure coefficients and squared structure coefficients of Capacity and Value, and was not confirmed by score of structure coefficients and squared structure coefficients of Performance, whose structure coefficients showed the score very close to that of Value and a modest function coefficient. The score differences of coefficients as previously described were based on multicollinear nature (Deegan, 1978) of relations between Performance and other dependent variables. For all of dependent variables coefficients had the same sign, indicating positive relations among them.

On the other side, among independent variables at the Function 1 Externalization showed primary contribution followed by Internalization and Combination, and a non-significant contribution of Socialization. The scores and distribution of structure coefficients and squared structure coefficients confirmed previous conclusion. For all of independent variables structure coefficients had the same sign indicating positive relations among them. Since structural coefficients for both sets of variables had same sign they were positively related.

Looking at the Function 2 for Bmodel the coefficients showed primary contribution of Performance and Value on almost same level but different sign with multicollinear natures of both

variables and a non-significant contribution of Capacity. The scores and distribution of structure coefficients and squared structure coefficients confirmed previous conclusion.
The coefficients of independent variables at the Function 2 showed primary contribution of Socialization followed by Combination but with different sign, and with non-significant contributions of rest two variables. The scores and distribution of structure coefficients and squared structure coefficients showed high significance of Socialization and no significant scores of the rest. Regarding the sign of relations Value, Socialization and Externalization on one hand and Performance, Capacity, Combination and Externalization had same sign. It is interesting that in all cases scores of squared structure coefficients had opposite distribution of scores comparing the Function 1 and the Function 2.

Finally, canonical communality coefficient (h^2), the percentage of variance in each variable interpreted by the canonical correlation analysis, explained level of usefulness of the observed variable for the entire model and was calculated as the sum of squared structure coefficients in each function. Distribution of scores of canonical communality coefficients between 68.32% and 85.36% for dependent variables and between 77.93% and 92.46% showed high level of usefulness in the model. The hypothesis is confirmed.

2) Smodel

The coefficients at the Function 1 for Smodel showed primary contribution of Performance, secondary contribution of Value and tertiary of Capacity to synthetic dependent variable confirmed also by distribution of scores of structure coefficients and squared structure coefficients. For all of dependent variables coefficients had the same sign, indicating positive relations among them.
Among independent variables at the Function 1 Externalization showed primary contribution with multicollinear nature followed by Socialization and Internalization and Combination at the end. The scores and distribution of structure coefficients and squared structure coefficients confirmed previous conclusion of significance of Externalization, the rest three variables showed very similar scores. For all of independent variables structure coefficients had the same sign indicating positive relations among them. Since structural coefficients for both sets of variables had same sign they were positively related. These results supported theoretical background and expectations of relationships between variables.

Looking at the Function 2 for Smodel the coefficients showed primary contribution of Capacity and significantly lower scores of Performance and Value. The scores and distribution of structure coefficients and squared structure coefficients confirmed previous conclusion.
The coefficients of independent variables at the Function 2 showed primary contribution of Socialization with multicollinear nature, followed by Internalization and Externalization, and with non-significant contribution of Combination. The scores and distribution of structure coefficients and squared structure coefficients confirmed previous conclusions. Regarding the sign of relations Performance, Value and Combination on one hand and Capacity, Socialization, Externalization and Internalization had same sign.

Regarding canonical communality coefficient (h2), distribution of scores showed very high level of usefulness in the model of Capacity 99.19% and Performance 82.12% for dependent variables; Externalization 89.17% and Socialization 87.56 for independent variables; high level of usefulness of Value 53.91%; low usefulness of Internalization 33.51% and very low usefulness of Combination 13.03%. The hypothesis is confirmed.

4.1. Discussion

Comparison of results of analysis of both regions, presented as Bmodel and Smodel, showed the overall scores of R_c^2 higher than 50% showing statistically significant proportion of variances shared between all variable relations across functions. In both regions analysis of internal audit

performance improvement and knowledge creation process variables coefficients had the same sign indicating positive relations among them in the Function 1 which was created to maximize the canonical correlation between two sets of variables. These results supported theoretical background and expectations of relationships between variables. In most cases in both regions, scores of squared structure coefficients had complementary, opposite distribution of scores in the Function 2 comparing to those in the Function, except for Combination and partially for Internalization in Scandinavia. For several variables the coefficients showed multicollinear nature and necessity for a deeper exploration of correlations among those variables that should be observed as disaggregated. The canonical communality coefficient (h^2) reviewed that in both regions observed variables for the entire model possessed high level of usefulness in explanation of variances, above 50%, except for Combination and Internalization in Scandinavia.

4.2 Limitations

Our research is also subject to few limitations. First, broader coverage of European/worldwide internal auditors might provide more stratified or different results in terms of relevance or interrelations among variables. Second, the research under state boundaries i.e. culture might result in a more aggregate population and exclude a potential influence of cultural characteristics. Third, focus on an industry or comparison of results among industries might have similar differentiations among variables. Fourth, collecting data from respondents using questionnaires on their native language might provide them a bit deeper understanding and avoidance of potential misunderstandings and doubts but also increase the number of complete responses. Finally, method of collecting data by self-reporting may cause tendency of respondents to provide insincere answers and their personal attitudes not fully based on relevant real results, situations and conditions of organization.

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Appendix

Table 4: Summary Item Statistics

		Mean		Minimum		Maximum		Range		Maximum / Minimum		Variance		Nr of Items
		a	Balkan	a	Balkan	a	Balkan	a	Balkan	a	Balkan	a	Balkan	
Socialization	Item Means	1,824	1,964	1,372	1,635	2,233	2,346	0,860	0,712	1,627	1,435	0,082	0,070	7
	Item Variances	0,675	0,932	0,287	0,589	0,998	1,250	0,711	0,661	3,479	2,122	0,059	0,040	
Externalization	Item Means	1,970	2,082	1,512	1,923	2,465	2,269	0,953	0,346	1,631	1,180	0,093	0,018	7
	Item Variances	0,792	0,941	0,494	0,750	1,092	1,210	0,598	0,460	2,211	1,614	0,036	0,022	
Combination	Item Means	2,239	2,305	1,884	2,000	2,651	2,519	0,767	0,519	1,407	1,260	0,088	0,040	7
	Item Variances	0,810	1,291	0,534	1,187	1,059	1,470	0,525	0,284	1,983	1,239	0,035	0,010	
Internalization	Item Means	2,212	2,246	1,744	1,654	2,814	2,808	1,070	1,154	1,613	1,698	0,113	0,126	9
	Item Variances	0,888	1,164	0,372	0,778	1,539	1,614	1,167	0,836	4,137	2,074	0,217	0,095	
Performance	Item Means	2,457	2,436	2,116	1,942	3,186	2,962	1,070	1,019	1,505	1,525	0,150	0,155	6
	Item Variances	0,689	0,740	0,443	0,484	0,957	1,057	0,514	0,574	2,160	2,186	0,033	0,046	
Value	Item Means	2,242	2,419	2,000	2,250	2,628	2,654	0,628	0,404	1,314	1,179	0,042	0,023	10
	Item Variances	0,558	0,757	0,351	0,593	0,719	1,065	0,368	0,472	2,047	1,796	0,016	0,025	
Capacity	Item Means	2,004	2,426	1,791	1,904	2,558	2,731	0,767	0,827	1,429	1,434	0,083	0,089	6
	Item Variances	0,600	1,363	0,456	0,755	0,872	1,691	0,415	0,936	1,910	2,239	0,022	0,113	

Table 5: Reliability statistics

	Cronbach's Alpha		Cronbach's Alpha Based on Standardized Items		Cronbach's Alpha if 1 Item Deleted - min		Cronbach's Alpha if 1 Item Deleted - max		N of Items
	Scandinavia	Balkan	Scandinavia	Balkan	Scandinavia	Balkan	Scandinavia	Balkan	
Socialization	0,855	0,899	0,856	0,901	0,823	0,870	0,853	0,903	7
Externalization	0,904	0,914	0,905	0,914	0,879	0,890	0,902	0,918	7
Combination	0,867	0,898	0,865	0,898	0,826	0,869	0,872	0,891	7
Internalization	0,799	0,892	0,811	0,898	0,761	0,873	0,807	0,894	9
Performance	0,325	0,691	0,307	0,710	0,133	0,563	0,464	0,770	6
Value	0,800	0,895	0,804	0,897	0,761	0,875	0,807	0,896	10
Capacity	0,799	0,885	0,809	0,886	0,716	0,850	0,832	0,882	6

Table 6: Test of significance – Bmodel (Balkan)

Multivariate Tests of Significance (S = 3, M = 0, N = 21 1/2)

Test Name	Value	Approx. F	Hypoth. DF	Error DF	Sig. of F
Pillais	,75729	3,96760	12,00	141,00	,000
Hotellings	1,70308	6,10732	12,00	131,00	,000
Wilks	,33605	5,07325	12,00	119,35	,000
Roys	,60401				

Eigenvalues and Canonical Correlations

Root No.	Eigenvalue	Pct.	Cum. Pct.	Canon Cor.	Sq. Cor
1	1,53044	89,86286	89,86286	,77770	,60481
2	,15049	8,83609	98,69895	,36167	,13080
3	,02216	1,30105	100,00000	,14723	,02168

Dimension Reduction Analysis

Roots	Wilks L.	F	Hypoth. DF	Error DF	Sig. of F
1 TO 3	,33605	5,07325	12,00	119,35	,000
2 TO 3	,85036	1,29452	6,00	92,00	,268
3 TO 3	,97832	,52071	2,00	47,00	,597

Table 7: Test of significance – Smodel (Scandinavia)

Multivariate Tests of Significance (S = 3, M = 0, N = 17)

Test Name	Value	Approx. F	Hypoth. DF	Error DF	Sig. of F
Pillais	,58967	2,32409	12,00	114,00	,011
Hotellings	,82701	2,38914	12,00	104,00	,009
Wilks	,50020	2,38298	12,00	95,54	,010
Roys	,35649				

Eigenvalues and Canonical Correlations

Root No.	Eigenvalue	Pct.	Cum. Pct.	Canon Cor.	Sq. Cor
1	,55397	66,98438	66,98438	,59706	,35649
2	,20839	25,19754	92,18192	,41527	,17245
3	,06466	7,81808	100,00000	,24643	,06073

Dimension Reduction Analysis

Roots	Wilks L.	F	Hypoth. DF	Error DF	Sig. of F
1 TO 3	,50020	2,38298	12,00	95,54	,010
2 TO 3	,77729	1,65571	6,00	74,00	,144
3 TO 3	,93927	1,22847	2,00	38,00	,304

THE NEW AND EMERGING ROLES OF CHIEF AUDIT EXECUTIVES IN THE ERA OF DISRUPTIVE CHANGES

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Abstract
Today's constantly changing external and internal environment of companies requires excellent leaders who will anticipate these changes, be proactive and make right decisions at the right time by adjusting its mission, vision and strategy, innovating business methodologies, implementing and applying new digital technologies and investing in talent. In other words, extraordinary leaders need to transform overall business operations to achieve greater long-term success in the era of disruptive changes. In that process, the internal audit function has prominent role in large, diversified and decentralized companies, as well as in the public interest entities, to provide holistic assurance, advice, insight and foresight. As part of a company, the internal audit function is on several ways impacted by modern, uncertain business conditions and changes in company's business. To achieve mission of internal audit and add value to their stakeholders, chief audit executives have central leading role. Considering that, chief audit executives need to be courageous, agile and innovative leaders of the internal audit functions, competent and objective assurance providers and strategic business partners.

Keywords: *Chief Audit Executive, Competencies, Disruptive and Technological Changes, Internal Audit Function, Roles and Responsibilities*

Track: *Management & Leadership*

Word count: *8.525*

1. Introduction

"Change in the business world is accelerating as the effects of globalization, advances in technology, and revolutions in geopolitical landscapes reach deeper into societies around the globe" (Harrington, Piper, 2015, 4). In other words, changes in external and internal business environment are driven by "macroeconomic pressures; a procession of corporate crises, regulatory responses, ensuing compliance efforts; and the changing nature of both organizational technology and the operational workforce that relies on these systems to support their business processes" (Galvanize, 2019, 3). These new and emerging trends, on the one side, bring opportunities for achieving competitive advantage and greater business success, but on the other side, create new, atipical and dynamic risk landscapes which can negatively impact companies' business. To achieve business success in today's constantly changing and evolving business environment by transforming risks into opportunities, these new and emerging trends or events need to be proactively foreseen and continuously monitored in the companies. "Internal audit is in a race to define its place in a rapidly changing world" (The IIA's Audit Executive Center, 2019, 29). Competent and proactive leaders "who can master these world-changing developments will guide their organizations to success. However, success will come only to those who can balance the opportunities and risks created by these technological advances, and internal audit must play a central role in helping them find that balance" (The IIA's Audit Executive Center, 2019, 29).

In order for internal audit functions to fulfill their new, emerging and increasingly demanding tasks, key role play their leaders, chief audit executives. Their roles, responsibilities, and tasks are

becoming more and more complex, demanding and responsible, while struggling with scarce resources and 'doing more with less', pressures from various stakeholders, continuously changing environment, required competencies, and so on. In order to fulfill internal audit function's mission, vision, strategies, objectives, and to participate in the achieving company's success, chief audit executives have several key roles and responsibilities, which are constantly multiplying. Firstly, chief audit executives need to have adequate attributes, characteristics, and competencies for leading and managing the internal audit functions. This means that they "need to have strong management skills – and the ability to efficiently use resources – to achieve the internal audit function's objectives" (The IIA's Audit Executive Center, 2017, 22). Secondly, in order to deal with increasingly complex and constantly changing internal audits' and companies' environment, chief audit executives need to develop and upgrade their own and team members' competencies with the necessary and contemporary knowledge, skills, and abilities to provide independent assurance, relevant consulting activities, proactive insights, and meaningful foresights on increasingly complex risk issues (The IIA's Audit Executive Center, 2019, 29), related contemporary technological trends and disruptive events. Thus, chief audit executives "need to do more to educate their teams about the organizations in which they operate. Individual auditors can act to acquire industry specific certifications to enhance their understanding of the business and to help build personal credibility with management" (Harrington, Piper, 2015, 14). Thirdly, chief audit executives should act as a strategic business partners to their stakeholders and make "their voices heard in boardrooms and C-suites" (The IIA's Audit Executive Center, 2019, 29). "To play a leading role in the success of their organizations, internal auditors need to anticipate the requirements of their stakeholders. In today's dynamic risk landscape, that is no easy task. The board, management, control functions, and internal and external assurance providers have a broad range of constantly shifting, often competing, and sometimes poorly communicated needs that internal auditors should fundamentally understand and serve. Internal auditors must improve communication channels to better anticipate stakeholder expectations, particularly during the audit planning and approval processes. They must demonstrate how and why their audit plans meet the key risks the business faces in pursuing its strategy. Failure to do so often leads to a dangerous expectations gap between internal auditors and stakeholders" (Harrington, Piper, 2015, 5).

Therefore, the main research question of this paper is: whether and how chief audit executives have adapted to contemporary business conditions? According to the research question, research objectives are: 1) to investigate which roles and responsibilities have chief audit executives and how they are changing, 2) to analyze and show characteristics and competencies of modern chief audit executives, and 3) to show and give a critical review of the most important results of previously conducted research on global level about chief audit executives' roles, responsibilities, and competencies. To achieve research objectives, theoretical review of secondary data will be made and methods of analysis, synthesis, description and comparison will be applied. Research results will indicate current state of roles and competencies of chief audit executives, and main challenges that they are facing with. In the paper will also be given recommendations for acquiring new competencies and advices on how chief audit executives should deal with their new roles and responsibilities to achieve better results that add value.

2. Chief audit executives' roles and responsibilities in the era of disruptive changes

Chief audit executive represents a person responsible for leading and managing the internal audit function. Internal audit "is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes" (The Institute of Internal Auditors Global, 2019b). Related to the *Definition of Internal Auditing*, very important in understanding the importance and roles of the internal audit is its *Mission* which "articulates what internal audit aspires to accomplish within an organization" (The Institute of Internal Auditors Global, 2019a).

The *Mission of Internal Audit* is "to enhance and protect organizational value by providing risk-based and objective assurance, advice, and insight" (The Institute of Internal Auditors Global, 2019a). Therefore, chief audit executives need to act according to the *Definition* and *Mission of Internal Audit*, and all other related and relevant guidance, in order to add value, improve business operations, and help companies accomplish its objectives.

For accomplishing its roles and responsibilities within and outside the internal audit function, chief audit executive needs to have adequate attributes, characteristics, and competencies. "Internal audit's success depends on the direction provided by its chief audit executive and the organization's management team. Therefore, finding a chief audit executive with the requisite characteristics is critical for all organizations" (Venkataraman, 2016, 5). Because of its specific position in the company, chief audit executive has "a high degree of interaction with senior management and the board and thus needs to demonstrate the right attributes and skills for the position" (The Institute of Internal Auditors Global, 2010, 1). Considering that, chief audit executive's "unique role in the organization requires independence and objectivity while also demonstrating an ability to partner within the organization to add value to its operations. Independence and objectivity are fundamental to the chief audit executive's role because the individual must be willing to raise difficult issues with both senior management and the board, even if that proves unpopular" (The Institute of Internal Auditors Global, 2010, 1).

Organizational independence means that "the chief audit executive must report to a level within the organization that allows the internal audit activity to fulfill its responsibilities" (The Institute of Internal Auditors Global, 2019c, 33). Chief audit executives typically have a dual reporting lines. So, in order "to ensure effective organizational independence, the chief audit executive has a direct functional reporting line to the board. Generally, the chief audit executive also has an administrative, or "dotted", reporting line to a member of senior management" (The Institute of Internal Auditors Global, 2019c, 34). In other words, in practice, chief audit executives generally functionally report to the board or to the audit committee of the board, and administratively to the chief executive officer, chief financial officer or similar. „Examples of functional reporting to the board involve the board:

- approving the internal audit charter
- approving the risk-based internal audit plan
- approving the internal audit budget and resource plan
- receiving communications from the chief audit executive on the internal audit activity's performance relative to its plan and other matters
- approving decisions regarding the appointment and removal of the chief audit executive
- approving the remuneration of the chief audit executive
- making appropriate inquiries of management and the chief audit executive to determine whether there are inappropriate scope or resource limitations" (The Institute of Internal Auditors Global, 2019c, 33).

On the other side, administrative reporting to the chief executive officer or similar enables regular, day-to-day internal audit operations. Administrative responsibilities, for example include, "supporting information flow within the organization or approving the internal audit activity's human resource administration and budgets" (The Institute of Internal Auditors Global, 2019c, 25).

Today's modern and constantly changing business conditions raise a question "of whether traditional reporting lines are sufficient to ensure that internal audit findings and recommendations are being heard" (The IIA's Audit Executive Center, 2019, 25). Differences and variances in the audit committees' structures and responsibilities "create the real possibility that in some organizations internal audit is not involved with committees that handle critical issues, such as cybersecurity and overall risk governance. For example, in many organizations, risk and IT

committees, not audit committees, are tasked with overseeing cybersecurity and cyber preparedness. Such conditions could handicap internal audit's ability to deliver perspectives about those vital risk domains. Additionally, the administrative reporting line in many organizations could further limit internal audit's ability to communicate with the chief executive officer" (The IIA's Audit Executive Center, 2019, 25).

Individual objectivity means that "internal auditors must have an impartial, unbiased attitude and avoid any conflict of interest" (The Institute of Internal Auditors Global, 2019c, 42). Furthermore, "internal auditors exhibit the highest level of professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined. Internal auditors make a balanced assessment of all the relevant circumstances and are not unduly influenced by their own interests or by others in forming judgments" (The Institute of Internal Auditors Global, 2019c, 7). In general, individual internal auditors and especially chief audit executives need to be ethical what means that they all need to conform with the overall *Institute of Internal Auditors Global Code of Ethics* principles and rules of conduct. Besides objectivity, *Code of Ethics* also includes principles and rules of conduct of integrity, confidentiality, and competency. "While individual internal auditors are responsible for their personal conformance with the *Code of Ethics*, it is perhaps especially vital for the chief audit executive (CAE), as the leader of the internal audit activity, to uphold the *Code of Ethics* principles and rules of conduct, thereby setting the tone for the value of ethics among the team" (The Institute of Internal Auditors Global, 2019c, 8). "To maintain credibility, chief audit executives must demonstrate the ability to escalate difficult issues to an appropriate level to ensure they are adequately addressed. In addition, a chief audit executive exhibits the attributes of integrity, intellectual curiosity, and a focus on audit quality" (The Institute of Internal Auditors Global, 2010, 1).

Chief audit executives have very important roles and responsibilities that are constantly changing, revolutionizing and upgrading. Modern digital economy era, or era of disruptive changes, characterized by macroeconomic pressures, regulatory changes, and disruptive technological advances, fosters changes in the traditional chief audit executives' roles, responsibilities, and jobs, while simultaneously introducing new roles, responsibilities, and tasks for them. In order to effectively and efficiently accomplish their roles, responsibilities, and tasks in modern times, chief audit executives need to have appropriate attributes and characteristics, which include (The Institute of Internal Auditors Global, 2010; The IIA's Audit Executive Center, 2017; The IIA's Audit Executive Center, 2018; The Institute of Internal Auditors Global, 2018a; The Institute of Internal Auditors Global, 2018b; Tušek, Ježovita, Halar, 2018; Galvanize, 2019): independency, integrity, objectivity, confidentiality, competency, intellectual curiosity, intelligence, inquisitiveness, quality, tech-savvy and data-savvy, courage, empathy, strategically-oriented, people-oriented, communicability, agility, flexibility and innovation.

First and foremost, chief audit executive needs to be competent, effective and courage leader of the internal audit function. In order to effectively fulfill this accountable role and accompanying responsibilities and tasks, chief audit executive "must be able to think strategically about the internal audit function, its mission, and its strategic resources, including attracting highly qualified staff" (Galvanize, 2019, 5). "Chief audit executives should set clear expectations for the internal audit activity. Therefore, to successfully manage internal audit, the chief audit executive must be able to develop and execute a strategic plan to ensure the completeness of the audit universe, including determining the general competencies and behavioral skills of the auditors, using the appropriate tools, sharing information, monitoring the reporting process, and interacting with the activities of third-party providers" (The Institute of Internal Auditors Global, 2018a, 3). The chief audit executive "is the leader of internal audit and should set the tone at the top, leading by example" (Venkataraman, 2016, 15). Moreover, "it takes courageous leadership to enhance and protect organizational value. Chief audit executives must have the courage to look both outward

at the organization, and inward at the internal audit function" (The IIA's Audit Executive Center, 2017, 21). This means that chief audit executives, as proactive leaders of changes, need to be at the forefront of internal audit functions' changes and, by doing so, at the forefront of changes and innovation of overall companies' business operations (Tušek, Ježovita, Halar, 2018, 284). For changing and innovating traditional internal audit functions' ways of doing business, chief audit executives need to be first in the line for accepting and implementing innovative practices, technologies, and methodologies that lead to reengineered internal audit operations, its success and, in the end, adding greater value to companies. Today, chief audit executives are dealing "with the challenges of doing more with less, continuing to tame unruly internal controls and data environments, and working with increasingly technology-savvy business partners. Successfully addressing these demands requires a combination of leadership, processes, and tools like automation, analytics and continuous auditing to deliver greater efficiencies and effectiveness" (Galvanize, 2019, 3). Considering all that, "chief audit executives need to lead the response to disruption with innovative strategies and an agile approach supported by the right talent. The tendency for some chief audit executives might be to wait for others to act first. This is a recipe for irrelevance. Chief audit executives need to position internal audit to be an internal disruptor, relentlessly challenging the status quo, identifying and focusing on emerging risks. It is not the first time internal audit has needed to transform itself, and it likely will not be the last. But vulnerability, driven by disruption, requires transformation *now*" (The IIA's Audit Executive Center, 2018, 5). Regarding that, chief audit executive should, in the end, "have a strong focus on the quality of the internal audit activity achieving the highest level of professionalism. This includes adhering to the *International Professional Practices Framework*, which requires establishing a quality assurance and improvement program and undergoing internal and external quality assessments" (The Institute of Internal Auditors Global, 2010, 2). "Professionalism refers to the knowledgeable use of significant skills, and performing work at the highest of levels. (…) Professionalism, in the context of internal audit, refers to a function whose very foundation is immersed in ethics" (The Institute of Internal Auditors Global, 2018a, 2).

Besides of its key role as a leader of the internal audit function, chief audit executive is also, at the same time, a competent and objective assurance provider and strategic business partner. For that reason, chief audit executive (Galvanize, 2019, 5):

- must demonstrate a solid understanding of the company's business, core strategies, risk appetite, and risk tolerance
- must be willing to raise difficult issues with senior management and the audit committee, even if such actions prove unpopular
- must partner with senior management and the audit committee to help them fulfill their broad responsibilities for effective governance, and
- must be seen as business partner rather than 'corporate cop'.

As previously stated, chief audit executive "should be both a partner to senior management in monitoring the organization's ethical and operational environment and an independent and objective professional in assessing the results of management's work on behalf of the board" (The Institute of Internal Auditors Global, 2010, 2). Considering these two confronting roles, it is necessary for chief audit executive to balance responsibilities that come out from these roles "and deliver an unbiased and equitable assessment under all circumstances. Uncompromising ethics, the ability to listen with an open mind, and the strength and integrity to be firm under pressure will enable the chief audit executive to report to the board and senior management evidence-based, objective findings of the internal audit work performed" (The Institute of Internal Auditors Global, 2010, 2). Chief audit executives "intent on establishing their function's value as a strategic business partner can leverage a unique opportunity to provide additional risk insights, given their visibility into, and understanding of, their enterprise's holistic risk management activities" (Galvanize, 2019, 5). This can be easily achieved because chief audit executive should also "be a curious explorer, investigative reporter, and avid analyst whose role it is to discover, interpret,

question, and challenge“ (The Institute of Internal Auditors Global, 2010, 2). By doing so, overall internal audit will be seen as a valuable resource and function that adds value and provides independent and objective assurance, consulting services, insights, and foresights to all levels of the company's organization (The Institute of Internal Auditors Global, 2010, 2). Chief audit executives “must not only communicate clear expectations to internal auditors about an organization’s goals and strategies, but also advocate for the expected value internal audit brings. This is accomplished by understanding what stakeholders want, agreeing on objectives and priorities, planning activities and strategies, establishing resources, and monitoring performance” (The Institute of Internal Auditors Global, 2018a, 4). “Just as internal audit’s role in the organization is evolving from providing reactive and passive hindsight assurance to one of delivering proactive insight and foresight, so too must its view of alignment reflect the changing needs of the board” (The IIA’s Audit Executive Center, 2019, 4). “Alignment with board and executive management views on risk is essential for internal audit to successfully provide outstanding service and be viewed as a value-added and essential resource. Not only must internal audit be thoroughly and continuously aligned with the board and executive management, it is imperative for practitioners to be cognizant of whether and how these stakeholders view and understand risks and opportunities. This begins and ends with assuring that boards have complete and accurate information on which to base their decisions” (The IIA’s Audit Executive Center, 2019, 2). Therefore, when chief audit executives are taking a leadership roles as a business-aware auditors, they are, on the one hand, helping to the rest of their organizations to become more audit-aware, and on the another hand, freeing up their own internal audit resources to focus on other priorities and areas of high strategic risks (Galvanize, 2019, 6). Besides of its methodological and technical nature of work, chief audit executives also need to give special attention to the interpersonal aspects of their work. “Internal audit engagements by their nature are interpersonal, and the quality of interpersonal dynamics – how internal auditors communicate and establish relationships with others in the organization – is likely to have an effect on audit outcomes. Understanding interpersonal dynamics is essential to effective auditing” (The IIA’s Audit Executive Center, 2017, 16). Connected with that, “empathy can improve the tone of an interaction. Bringing empathy into the audit means understanding the audit process from management’s perspective. For example, auditors should reiterate that they want to help management improve processes and provide assurance to key stakeholders. This collaborative approach can encourage management to take ownership of audit results and help the audit to be more successful” (The IIA’s Audit Executive Center, 2017, 18).

In the end, in today’s digital economy era and constantly changing business environment, for developing competent, valuable, insightful, and proactive internal audit functions that add value and contribute to the overall companies’ success, chief audit executives need to strategically play a leading role, beat the expectations gap and invest in excellence (Harrington, Piper, 2015, 26). Chief audit executives, as devoted leaders of their internal audit functions, are playing the leading role by anticipating the needs of stakeholders, developing forward-looking risk management practices, continually advising the board and audit committee, and being courageous (Harrington, Piper, 2015, 26). Furthermore, chief audit executives, as committed representatives of their internal audit functions, are beating the expectations gap by supporting the business’s objectives, identifying, monitoring, and dealing with emerging technology risks, enhancing audit findings through greater use of data analytics, and going beyond *The International Standards for the Professional Practice of Internal Auditing*. Finally, chief audit executives, as motivating and encouraging managers, are investing in excellence by investing in talent, in themselves and in other internal audit functions’ members, and recruiting, motivating, and retaining great team members (Harrington, Piper, 2015, 26). These “imperatives for internal audit can help practitioners at every level challenge themselves to grow professionally and increase their value in the business market“ (Harrington, Piper, 2015, 26). Chief audit executives “today need to make a tough choice: remain as traditional auditors focused on executing the audit plan, or elevate their role, particularly

in the area of risk management, to that of a strategic business partner to the C-suite. Those who choose to reside on the more tactical side of their job description may enjoy less financially rewarding career opportunities; however their services will still remain in high demand for the foreseeable future. Those who take advantage of innovation, enhanced board committee relationships, and other strategic priorities, will help lead their companies to greater success" (Galvanize, 2019, 3).

3. Chief audit executives' competencies in the era of disruptive changes

In order for chief audit executives to successfully perform their various roles, responsibilities, and tasks, they need to have the right knowledge, skills and abilities, or in one word, competencies. The Institute of Internal Auditors Global in 2013 developed and published a revised *Global Internal Audit Competency Framework* (The Institute of Internal Auditors Global, 2013). *The IIA Global Internal Audit Competency Framework* "is a tool that defines the competencies needed to meet the requirements of the *International Professional Practices Framework* (*IPPF*) for the success of the internal audit profession" (The Institute of Internal Auditors Global, 2013, 1). A competency can be defined as "the ability of an individual to perform a job or task properly, being a set of defined knowledge, skills and behavior" (The Institute of Internal Auditors Global, 2013, 1). In other words, "a competency describes the knowledge, skills, abilities, and other characteristics needed for effective performance in a given role" (Rose, 2015, 5). Chief audit executives can their competencies acquire through formal academic education and continual professional development. In today's era of disruptive changes, these competencies need to be constantly updated and upgraded. Thus, for internal audit profession the key for success is ongoing training and education, or in other words, lifelong learning. Continual professional development can be formal and informal. Formal continual professional development refers to attaining professional certifications in or outside the internal audit profession, while informal professional development refers to all other forms of trainings that update and upgrade chief audit executives' competencies. "Internal audit certification improves one's internal audit skills and knowledge and provides credibility and respect in the profession" (Venkataraman, 2016, 9). The Institute of Internal Auditors Global strongly encourages that all chief audit executives attain the *Certified Internal Auditor* (*CIA*) designation in order to "demonstrate a strong understanding of the roles and responsibilities of internal audit, the *International Professional Practices Framework*, and audit technical skills" (The Institute of Internal Auditors Global, 2010, 1).

The IIA Global Internal Audit Competency Framework, which can be seen on Figure 1, "outlines the ten core competencies recommended for each broad job level, namely internal audit staff, internal audit management and the chief audit executive. Each core competency is supported by a list of more detailed competencies that further define the core competency statement. While the core competencies have been defined individually it should be understood that there are connections and interdependencies between all of the competencies" (The Institute of Internal Auditors Global, 2013, 1). As outlined in Figure 1, the ten core competencies that internal auditors should posses are: professional ethics, internal audit management, the *International Professional Practices Framework*, governance, risk and control, business acumen, communication, persuasion and collaboration, critical thinking, internal audit delivery, and improvement and innovation (The Institute of Internal Auditors Global, 2013).

Figure 1: *The IIA Global Internal Audit Competency Framework*
Source: (The Institute of Internal Auditors Global, 2013, 2).

„*The IIA Global Internal Audit Competency Framework* is best understood by reading from the bottom to the top" (Rose, 2015, 6). The first two set of competencies in *The IIA Global Internal Audit Competency Framework*, professional ethics and internal audit management, "provide a firm foundation for the delivery of internal audit. In order to be able to provide an effective service, internal auditors need to operate according to high ethical standards and coordinate the resources and activities of the internal audit function" (The Institute of Internal Auditors Global, 2013, 2). Furthermore, "the principal points of focus of an internal auditor's expertise are the *International Professional Practices Framework*, governance, risk and control, and business acumen. The *International Professional Practices Framework* is the primary source of professional standards for internal audit that the Institute of Internal Auditors Global provides to all internal auditors around the world. Additionally, internal auditors require technical expertise in governance, risk and control to inform their work and help organizations accomplish their objectives. Business acumen in the form of understanding the client organization, its culture, the way it works, the sector it operates in and the local and global factors that act upon it is another essential prerequisite that enables internal auditors to provide effective assurance and advisory services and so add value to the organization" (The Institute of Internal Auditors Global, 2013, 2). In the end, "internal auditors need to be competent in communication, persuasion and collaboration, and critical thinking in order to deliver internal audit engagements, and drive improvement and innovation in an organization" (The Institute of Internal Auditors Global, 2013, 2).

Therefore, the key skill categories for modern chief audit executive include business, technical, and process skills, communication and listening skills, and people management skills (The Institute of Internal Auditors Global, 2010, 1-2). The „expanded sphere of responsibility requires the chief audit executive to acquire and augment certain soft skills in addition to the technical audit skills that are needed to perform the traditional chief audit executive role" (Venkataraman, 2016, 4). These once acquired competencies need to be constantly updated and upgraded in order to reflect modern business conditions that characterize organization where internal auditors operate. "To effectively evaluate risk, assess sufficiency of controls, identify process improvement opportunities, and effectively communicate with senior management and the board, the chief audit executive must have a good understanding of the organization's business processes and the

structures used in the delivery of these processes. Additionally, in today's environment where IT drives key business processes, the chief audit executive needs to understand the organization's IT environment to identify and assess the magnitude of the IT-related issues facing the organization" (The Institute of Internal Auditors Global, 2010, 2). Additionally, "the chief audit executive must communicate in a concise, professional manner to be effective in articulating risks and opportunities to a broad spectrum of stakeholders, including the board, senior management, external auditors, and regulatory agencies. The chief audit executive also must demonstrate excellent listening skills during all exchanges with the various stakeholders" (The Institute of Internal Auditors Global, 2010, 2). Also, it is crucial that chief audit executive has excellent people management skills. "To build and sustain a successful internal audit team, which may include or consist of cosourced professionals from an external service provider, the chief audit executive must be an effective leader and exhibit expert management skills. The chief audit executive must be able to bring out the best in people, while balancing differing needs of professional growth, travel, and personal life" (The Institute of Internal Auditors Global, 2010, 2).

4. Review of the results of conducted empirical surveys about chief audit executives' roles, responsibilities, and competencies

In this paper, the results of very important global surveys, in the profession of internal audit, about chief audit executives' roles, responsibilities, and competencies are presented, and results compared and critically reviewed. First surveys whose results are presented are annual *North American Pulse of Internal Audit* surveys, and second is *The Global Internal Audit Common Body of Knowledge* (further in text: *CBOK*) survey. The IIA's Audit Executive Center from 2011 gathers insights from leaders in the internal audit profession through the annual *Pulse of Internal Audit* surveys (The IIA's Audit Executive Center, 2019, 2). "Each survey collects information about both established and emerging issues that are important to the profession as well as information about internal audit management" (The IIA's Audit Executive Center, 2019, 2). On the other side, "*CBOK* is the world's largest ongoing study of the internal audit profession, consisting of two phases: the *Practitioner Survey* and the *Stakeholder Survey*. The first phase is led by the *Internal Audit Foundation* and supported by IIA Institutes and chapters around the world to include comprehensive studies of practitioners at all levels. The second phase is a global study consisting of audit stakeholder perspectives (senior management, audit committees, and boards) and will complement the findings of the practitioner study. The results of this combined research will provide a rich overview of how the profession is currently being practiced and changes that are anticipated in the future" (The Institute of Internal Auditors Global, 2019d). In the Table 1 are presented general information about annual *North American Pulse of Internal Audit* surveys conducted from 2015 to 2018.

Table 1: General information about *North American Pulse of Internal Audit* surveys

Type of *Pulse* survey	**Year**	**Time period**	**Number of responses**		
			Total	CAE	Director/senior managers
North American	2016	-	**486**	433	53
North American	2017	online survey 20th October to 11th November 2016	**538**	460	78
North American	2018	-	**636**	552	84
North American	2019	online survey 5th September to 4th October 2018	**512**	447	65

Source: Authors' preparation according to: (The IIA's Audit Executive Center, 2016, 42; The IIA's Audit Executive Center, 2017, 2; The IIA's Audit Executive Center, 2018, 2; The IIA's Audit Executive Center, 2019, 2).

As it can be seen from the Table 1, in the *North American Pulse of Internal Audit* surveys conducted from 2015 until 2018, the majority of participants were chief audit executives, with directors or senior managers in the internal audit functions as a minority of participants. Online survey for the *North American Pulse of Internal Audit* 2019 report was conducted from 5th September to 4th October 2018 (The IIA's Audit Executive Center, 2019, 2). As it can be seen from the Table 1, total number of respondents was 512, of which 87% were chief audit executives, and 13% were directors or senior managers. "Respondents primarily come from the United States (85%) and Canada (10%) with the remainder coming from a variety of other countries" (The IIA's Audit Executive Center, 2019, 2). Results of the survey shown in the Figure 2, from the *North American Pulse of Internal Audit* 2019, about chief audit executives' administrative reporting line, reveal that 40% of respondents say that they report administratively to the chief financial officer or similar, while 31% of respondents report to the chief executive officer, with the remainder reporting elsewhere within the organization (The IIA's Audit Executive Center, 2019, 40). "A breakdown by type of organization shows that chief audit executives in publicly traded and privately held organizations are much more likely to report to the chief financial officer – about 7 in 10" (The IIA's Audit Executive Center, 2019, 25). This results can be also seen on Figure 2. The Institute of Internal Auditors Global "recommends that the chief audit executive reports administratively to the chief executive officer (CEO), both so that the chief audit executive is clearly a senior position and so that internal audit is not positioned within an operation that is subject to audit" (The Institute of Internal Auditors Global, 2019c, 31). The results shown are relatively unfavorable, because the chief audit executive' administrative reporting line to the chief financial officer "in many organizations could further limit internal audit's ability to communicate with the chief executive officer" (The IIA's Audit Executive Center, 2019, 25). This situation "creates an additional reporting layer between the chief audit executive and the chief executive officer" (The IIA's Audit Executive Center, 2019, 25).

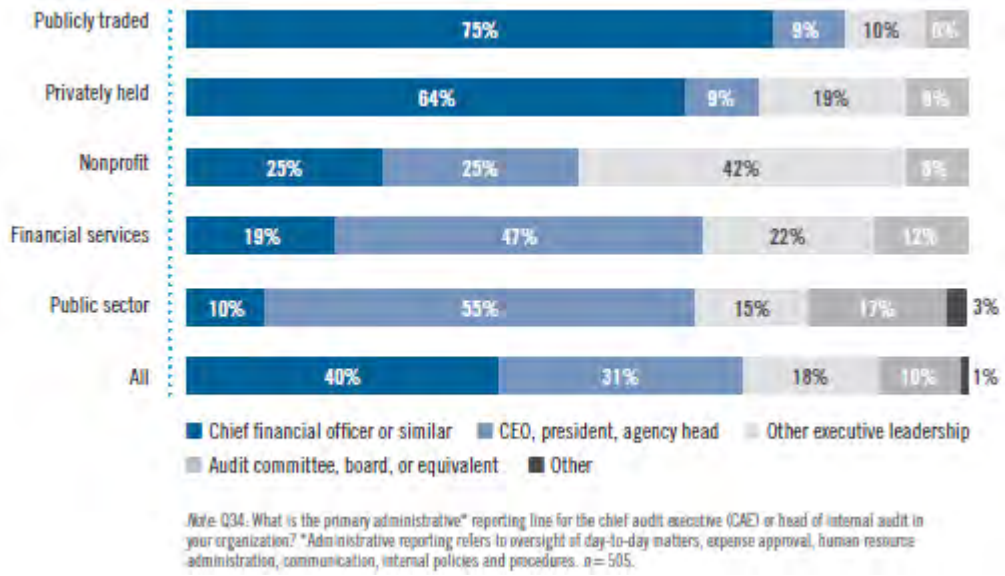


Figure 2: Chief audit executives' administrative reporting lines – results of the *North American Pulse of Internal Audit* 2019
Source: (The IIA's Audit Executive Center, 2019, 25).

Regarding the administrative reporting lines of chief audit executives, similar results to the *North American Pulse of Internal Audit* 2019 survey can be seen across *North American Pulse of Internal Audit* 2016, 2017, and 2018 surveys (Table 2).

Table 2: Chief audit executives' administrative reporting lines

Primary administrative reporting line of CAE	2016	2017	2018	2019
Chief financial officer or similar	35%	39%	42%	40%
Chief executive officer, president, agency head	35%	33%	32%	31%
Other executive leadership	5%	18%	12%	18%
Audit committee, board, or equivalent	9%	6%	7%	10%
Other or N/A	16%	4%	7%	1%
Number of respondents	486	520	625	505
Type of conducted survey	*North American*	*North American*	*North American*	*North American*

Source: Authors' preparation according to: (The IIA's Audit Executive Center, 2016, 43; The IIA's Audit Executive Center, 2017, 24; The IIA's Audit Executive Center, 2018, 28; The IIA's Audit Executive Center, 2019, 40).

In the Figure 3, results of the *North American Pulse of Internal Audit* 2019, about chief audit executives' functional reporting line, reveal that the majority, 82%, of respondents functionally report to the audit committee, board, or equivalent.

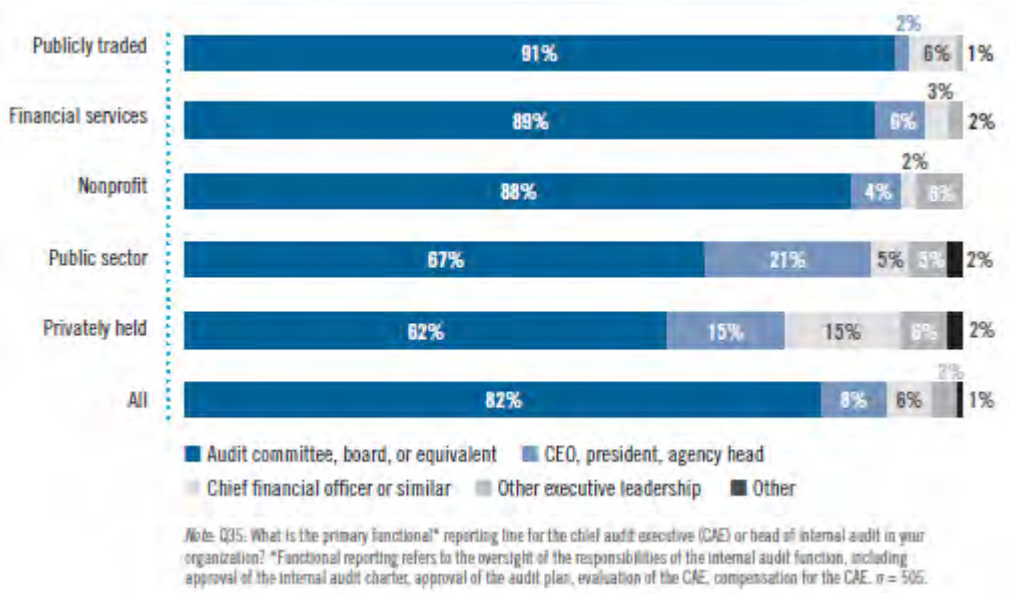


Figure 3: Chief audit executives' functional reporting lines – results of the *North American Pulse of Internal Audit* 2019
Source: (The IIA's Audit Executive Center, 2019, 40).

Regarding the functional reporting lines of chief audit executives, similar results to the *North American Pulse of Internal Audit* 2019 survey can be seen across *North American Pulse of Internal Audit* 2016, 2017, and 2018 surveys (Table 3). This results are also compared to the global *CBOK* 2015 survey results, and relatively similar results can be seen. Even though the results seem satisfying, in today's era of disruptive changes it should be questioned whether these traditional reporting lines are sufficient, and should chief audit executive functionally report, maybe, to other types of committees in order to handle critical issues, such as cybersecurity or overall risk governance.

Table 3: Chief audit executives' functional reporting lines

Primary functional reporting line of CAE	2015	2016	2017	2018	2019
Audit committee, board, or equivalent	72%	83%	88%	86%	82%
Chief executive officer, president, agency head	19%	9%	5%	6%	8%
Chief financial officer or similar	4%	5%	3%	5%	6%
Other executive leadership	0%	1%	3%	3%	3%
Other or N/A	5%	2%	1%	0%	1%
Number of respondents	2599	486	520	625	505
Type of conducted survey	*Global CBOK*	*North American*	*North American*	*North American*	*North American*

Source: Authors' preparation according to: (The IIA's Audit Executive Center, 2015, 17; The IIA's Audit Executive Center, 2016, 43; The IIA's Audit Executive Center, 2017, 24; The IIA's Audit Executive Center, 2018, 28; The IIA's Audit Executive Center, 2019, 40).

The *CBOK* 2015 *Practitioner Survey* was conducted from 2nd February to 1st April 2015 (Harrington, Piper, 2015, 2). In the survey participated 14.518 respondents from 166 countries all around the world (Harrington, Piper, 2015, 2). Out of the total number of respondents, if the results are structured by the employee levels in the internal audit functions, 26% of the respondents were chief audit executives, 13% directors, 17% managers, and 44% internal audit function' staff (Harrington, Piper, 2015, 2). Figure 4 shows percentage of *CBOK* 2015 *Practitioner Survey* participants across global regions. The majority of respondents were from East Asia & Pacific region (25%), Europe & Central Asia region (23%), while the minority of respondents were from Sub-Saharan Africa region (6%), and South Asia region (5%) (Figure 4).

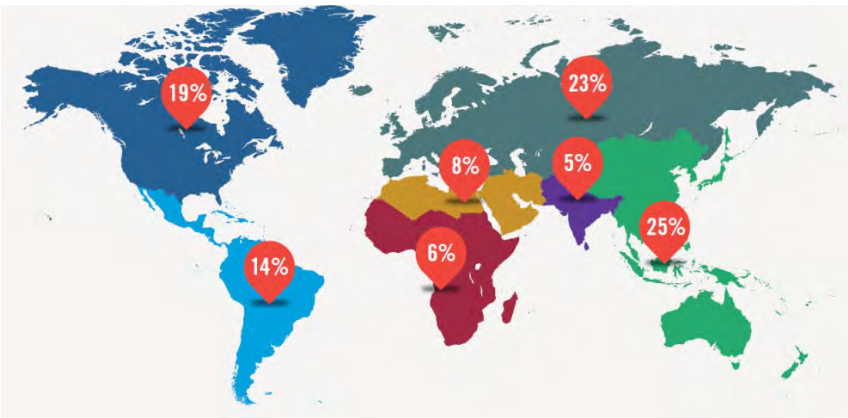


Figure 4: *CBOK* 2015 *Practitioner Survey*: Participation from global regions
Source: (The IIA's Research Foundation, 2015, 3).

Chief audit executive „is not an entry-level position. Years of experience and training are necessary to equip the individual to assume the broad array of responsibilities expected of the role" (Venkataraman, 2016, 6) that have previously been described. Overview of the most important results of the *CBOK* 2015 *Practitioner Survey* reveals that (Venkataraman, 2016, 6-17):

- the majority of chief audit executives are 40 years old or older (77%) with median age between 40 and 49
- chief audit executives have been in the workforce for approximately 15 years, and they have on average 6,8 years in the chief audit executive role
- still chief audit executive is a male-dominated position, but the proportion of female chief audit executives worldwide is growing

- the percentage of female chief audit executives is significantly higher in public sector and not-for-profit organizations (37%), than in other types of organizations
- the majority of chief audit executives are holding at least a bachelor's degree (94%)
- accounting continues to be the preferred major or the most significant field of study for majority of the chief audit executives (64%)
- more than half of the chief audit executives have a certification (53%)
- chief audit executives report an advanced level of competency in their self-assessment against ten core competencies from *The IIA Global Internal Audit Competency Framework*
- chief audit executives appear to be committed to their profession and their position, because 72% of chief audit executives are planning to stay in the internal audit profession, 9% plan to retire, while 19% are not sure about their plans or are planning to leave the internal audit profession.

As it can be seen from the Figure 5, overall results show that accounting still continues to be the preferred major or the most significant field of study for the majority of chief audit executives (64%), following by the internal auditing (44%) and business management and business (44%) (Venkataraman, 2016, 7). Regarding regional differences, in Europe the majority of chief audit executives are majoring business management and business (50%), following by accounting (45%), and economics (45%).

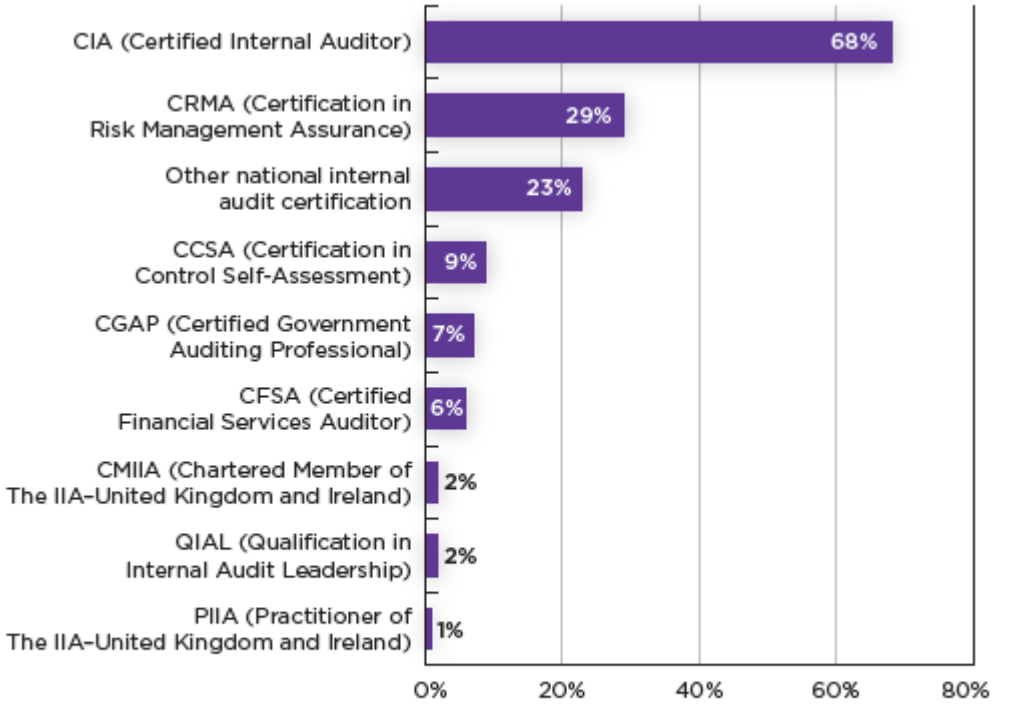
Major or Significant Field of Study	Latin America & Caribbean	East Asia & Pacific	Middle East & North Africa	Europe	Sub-Saharan Africa	South Asia	North America	Net
Accounting	72%	57%	71%	45%	87%	84%	80%	64%
Arts or humanities	4%	4%	1%	4%	0%	2%	7%	4%
Auditing (external)	49%	20%	39%	26%	40%	60%	16%	29%
Auditing (internal)	74%	58%	52%	33%	54%	74%	12%	44%
Business management and business	44%	38%	47%	50%	50%	46%	34%	44%
Computer science or information technology	16%	10%	15%	10%	15%	16%	8%	11%
Economics	15%	16%	33%	45%	26%	43%	10%	26%
Engineering	7%	5%	5%	7%	1%	3%	1%	5%
Finance	44%	22%	41%	39%	49%	59%	20%	34%
Law	10%	12%	13%	17%	20%	35%	2%	12%
Mathematics/ statistics	8%	4%	7%	9%	13%	18%	3%	7%

Note: Q5_ [5a] What were your academic major(s) or your most significant fields of study? (Choose all that apply.) by Q501: Global region. (From Q6a to Q6h, grouped into World Bank regions) In what region are you based or primarily work? Base *n* = 3,225; total *n* = 3,344; 119 missing; 77% filtered out.

Figure 5: Academic majors of chief audit executives – results of the *CBOK* 2015 *Practitioner Survey*
Source: (Venkataraman, 2016, 8).

„Organizations expect their chief audit executives to possess a diverse portfolio of skills – skills that are acquired and refined through years of experience. A strong background of internal audit and industry experience provides an advantage for those aspiring to become a chief audit executive" (Venkataraman, 2016, 7). Academic background is very important, but it is not enough. In order to up skill and improve its competencies, chief audit executive should attain certification in or outside the internal audit profession. As it can be seen from the Figure 6, the majority of chief audit executives have a certified internal auditor designation (68%), following by certification in

risk management assurance (29%), and other national internal audit certifications (23%). It is clear that for the chief audit executive position, technical competencies are required, but they are not sufficient. According to the results of the *CBOK* 2015 *Practitioner Survey*, several characteristics and skills are critical and needed in order to become a chief audit executive which include: understanding of business and risks, leadership and ethics, strategic thinking, critical thinking, breadth of knowledge, executive presence, and excellent communication (Venkataraman, 2016, 15-16).



Note: Q21: [Q12] Which professional certifications and/or qualifications do you have related to internal auditing? (Choose all that apply.)

Figure 6: Internal audit certifications of chief audit executives – results of the *CBOK* 2015 *Practitioner Survey*
Source: (Venkataraman, 2016,11).

5. Conclusion

Chief audit executive is a person who is responsible for effective and efficient leadership and management of the internal audit function. Regarding that, chief audit executives have different and very responsible roles that are constantly changing in today's era of disruptive changes. In order to successfully accomplish their roles, responsibilities, and tasks in modern times, chief audit executives need to have appropriate attributes, characteristics, and competencies, which need to be constantly updated and upgraded.

Therefore, internal audit functions together with their leaders, chief audit executives, are in the race to define its place in a rapidly changing world. Chief audit executives' main roles are competent and proactive leader of the internal function, professional assurance, consulting services and insights provider, and strategic business partner to their stakeholders. In order to achieve these roles and accompanying responsibilities, chief audit executives need to have appropriate academic backgrounds, continually educate themselves by attaining professional certifications and participating on other types of training, and on that way always be in the pace with disruptive changes that affect their work. Chief audit executives need to be ethical, or in other words, they need to comply with the principles and rules of conduct of *The Institute of Internal Auditors Global Code of Ethics*, that include: integrity, objectivity, confidentiality, and competency. Internal audit

function needs to be independent, what means that chief audit executive must report to a level within the organization that allows the internal audit function to fulfill its responsibilities. Chief audit executive also needs to be professional, intellectually curious, intelligent, focused on audit quality, tech-savvy and data-savvy, courageous, strategically-oriented, people-oriented, communicative, agile, flexible, change and innovation catalyst, and work with empathy. Furthermore, according to *The IIA Global Internal Audit Competency Framework*, the ten core competencies that chief audit executives should posses are: professional ethics, internal audit management, *International Professional Practices Framework*, governance, risk and control, business acumen, communication, persuasion and collaboration, critical thinking, internal audit delivery, and improvement and innovation. Today more than ever before, besides technical competencies, like the *International Professional Practices Framework* and IT knowledge, key competencies for chief audit executives are soft skills, or competencies, like communication and listening skills, people management and leadership skills, business acumen and professional skepticism, critical and strategic thinking.

Results of the conducted global *CBOK* 2015 *Practitioner Survey* reveal that the majority of chief audit executives are 40 years old or older, with median age between 40 and 49, what means that this position is not an entry level position, and years of experience and training are necessary to be equipped for this challenging role. This position is still a male-dominated position, but the proportion of female chief audit executives worldwide is growing. The majority of chief audit executives are holding at least a bachelor's degree, and their preferred majors are accounting and internal auditing. As previously stated, for chief audit executive is very important continual professional development. Regarding that, results show that more than half of the chief audit executives have some type of certifications, and they have advanced level of competencies. Regarding the organizational independence, questions were raised from the results of the *North American Pulse of Internal Audit* surveys conducted from 2015 to 2018 regarding the traditional reporting lines of chief audit executives. Results revealed that on average 40% of chief audit executives report administratively to the chief financial officer, 31% report to the chief executive officer, with the remainder reporting elsewhere within the organization. On the other side, around 82% of respondents functionally report to audit committee or board. In today's era of disruptive changes, these traditional reporting lines should be questioned in order to achieve appropriate organizational independence that will allow chief audit executives to better accomplish their roles, responsibilities, and tasks, and by doing so, add value to the companies they work in.

In the end, it can be concluded that chief audit executives have an important role in the organizations and companies where they work. As proactive leaders and catalysts of changes and innovations, chief audit executives need to be simultaneously at the forefront of internal audit functions' changes and changes of overall companies' business operations. To do that, chief audit executives need to constantly professionally develop themselves by updating and upgrading their competencies, and acquiring new ones for the era of disruptive changes.

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THE IMPACT OF USERS ACTIVITIES ON PURCHASE BEHAVIOR IN SOCIAL MEDIA ENVIRONMENT

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Abstract
This study analyzed how social media activities have an influence on users' behavior that could determine the purchase decision process. The aim of this paper is to determine the purchase intentions and attitude of social media users as well as repurchase attitudes and satisfaction with the purchase made via social media. Also, the aim of this paper is to define the influence of ads and notifications on their final purchase decision. The research instrument was an online questionnaire on a sample of 504 Facebook users. Confirmatory factors analysis (CFA) and Analysis of variance (ANOVA) were used. Two factors were extracted using factor analysis, named credibility and personalization factors. Results of variance have shown that there is a significant difference between these two factors and purchase attitude, purchase intention, repurchasing and purchase satisfaction of users in a social media environment. Further, significant differences have shown between credibility and personalization factors and the impact of ads and notifications on the user's purchase decision in the context of a social media environment. These findings have significant theoretical and managerial implications.

Keywords: *social media, online purchasing behavior, online repurchase intentions, online purchase satisfaction*

Track: *Management & Leadership*

Word count: *4.400*

1. Introduction

The interpersonal communication via a virtual environment has become a daily routine of every consumer and they are more inclined towards shopping experiences through the Internet and social media. Consumer behavior using social media websites for communication has become an important issue for markets. The increasing popularity of social media among consumer forced the company to make its business more oriented via social media. It can be noted that social media have become an unavoidable part of companies' business where they are trying to attract the potential and actual consumer in order to improve consumer engagement and therefore gain competitive advantages.

Social media includes a wide range of online information and sharing formats including social networking sites, creativity works-sharing sites, collaborative websites, and microblog sites. Also, social media contain word-of-mouth forums such as blogs, company sponsored discussion boards and chat rooms, consumer-to-consumer e-mail, consumer product or service ratings websites and forums, internet discussion boards and forums (Mangold and Faulds, 2009). Social media is providing relevant and updated information and content in order to make a strong relationship with consumers. Consumers are spending more and more time in the social media environment and therefore they have easier access to needed information and knowledge about their desire brand.

The popularity of social media among society and friends is another important reason for consumers to be on social media. The growing importance of social media like Facebook, YouTube and others in consumers' lives has an increasing influence on their consumer behavior (Hutter, et al., 2013). In social media, there are a lot of social networking tools that are available

for the businesses and individuals but Facebook, Twitter, YouTube, and Bloggers are the four popular social media tools used by people worldwide (Sin, et al, 2012). Social media such as Instagram or Facebook nowadays represents an ideal tool for eWOM (Jansen et al., 2009; Knoll, 2016).

The purpose of social media is to create an exchange with content by common users that may influence each other through existing social connections (Kaplan and Haenlein, 2010). Consequently, the complexity of the decision-making process is increasingly influenced by social media interaction but the outcomes of social media activities are still disputed among practitioners and managers (Hoffman and Fodor, 2010). Therefore, the impact of social media activities on consumers' decision-making purchasing process needs to be understood (Edelman, 2010). The aim of this paper is to determine the purchase intentions and attitude of social media users as well as repurchase attitudes and satisfaction with the purchase via social media. Also, the aim of this paper is to define the influence of ads and notifications on their final purchase decision. The purpose of this paper is to analyze how social media activities impact on the users' purchase behavior. By involving social media users i.e. Facebook user, the author has sought to explain the impact social media activities on their purchase behavior.

The paper is structured as follows. Next section presents literature review for the importance of social media tools in consumer behavior which follows the literature review of consumer activities in the social media environment and the influence of these activities on their purchase intentions and attitudes. Data and methodology are presented in section 4, while results and discussion of findings are reviewed in the following section. The paper finishes with concluding remarks, limitations, and recommendations for future research.

2. Literature review

The interactivity of social media has not only enhanced access to information but also allowed consumers to be part of a social community as creating content, sharing content or making social interactions. From a consumer's perspective, the use of information communication technologies i.e. social media provides a number of benefits, including functionality and convenience in accessing information, a wider selection and comparison of products, competitive pricing, cost reduction, and product diversity (Bayo-Moriones and Lera-Lopez, 2007). Social media has also influenced consumer purchase behavior from seeking the information to the post-purchase stage such as dissatisfaction or satisfaction with the purchased products (Mangold and Faulds, 2009).

Nardi, et al. (2004) investigated the user's individuals reasons to express themselves online and they reported five major motivations for blogging: documenting one's life, providing comments and opinions, expressing emotions, articulating ideas through writing, and forming and maintaining community forums. Social media communication mainly refers to the review and recommendation of families, friends, and others in their social network. Reviews are one of the key areas that have emerged from social media (Hajli, 2014) and consumer's reviews are generating great values for both consumers and companies.

Consumers reviews have grown quickly on the internet (Forman et al. 2008) and the company actively encouraged consumers to rate and give a review for bought products (Bronner and de Hoog, 2010). Previous research has indicated that product reviews have a positive effect on consumers' purchasing behaviors and intentions to buy (Maria and Finotto, 2008). Positive or negative reviews could significantly influence the consumer's attitudes (Lee, et al., 2008). Bailey (2005) showed that many consumers check product review websites where consumers post reviews of consumer products for the purpose of making a suitable purchasing decision. Users believe more than ever reviews on their social media site from previous consumers when making

purchase decisions (Hinz et al., 2011). Duan et al. (2008) in their study, point out that consumers trust opinions from people outside their social network, such as online reviews. The consumers have more confidence in the information and suggestions received from other consumers than through advertisements or ads of companies posted via social media. On the other hand, eWOM as a source of information is more effective in influencing consumers' decision-making than other marketing communication channels (Kozinets et al., 2010). Wang and Wei (2012) found that social media influence on consumers purchasing decisions in two ways: directly by conformity with peers and indirectly by reinforcing product involvement.

One of the forms that came from social media activities is word of mouth (eWOM) that are increasingly changing consumers' online purchase decision-making (Pan and Chiou, 2011; Cong and Zheng, 2017). Therefore, some studies have examined the impact of eWOM consumers' decision-making processes (De Bruyn and Lilien, 2008) and showed that consumer reviews have significant impacts on consumer purchase decisions (Chevalier and Mayzlin, 2006; Duan, et al., 2008; Forman, et al., 2008.). Goyette, et al. (2010) point out four eWOM dimensions of negative and positive eWOM, content and intensity eWOM. The consumer who is inclined toward eWOM is interested in reducing risk, securing lower prices, and having easy access to information before they make purchase decisions (Goldsmith and Horowitz 2006). The internet consumers are likely to be more inclined towards an individual approach especially in a social media environment where they can achieve better post-purchase satisfaction and individual engagement. Wang and Rodgers (2011) identified two major forms of eWOM, information-oriented and emotion-oriented. The first type consists of websites such as consumer review forums and product feedback pages. This content includes objective consumer-based experience such as product characteristics that provides reliable information's and give a sense of credibility. On the other hand, the second type of context is online communities and social networks where these consumer reviews tend to emphasize subjective product experiences, such as providing individual and personalized approach by a specific company.

EWOM plays a very important role on purchase intentions (Sher and Lee, 2009) and in many studies, the positive relation between purchase intentions and eWOM characteristics were found (Do-Hyung et al., 2007; Tseng, et. al. 2014; Bataineh, 2015). In the study, Erkan and Evans (2016) stated that the characteristics as quality, credibility, usefulness, and adoption of information, needs of information and attitude towards information are the key factors of eWOM in a social media and that they could influence on consumers' purchase intentions. Hutter et al. (2013) stated that a user's engagement with a Facebook fan page has a positive influence on users' brand awareness, eWOM activities, and purchase intention.

It can be concluded that staying competitive in today's challenging market involves creating unique and individual content on social media in order to capture user interest, increase their brand awareness and create strong consumer engagement.

3. Research methodology

In this paper, based on an online survey, the author tries to analyze the differences in online purchase behavior in the context of social media. Data was collected through a survey questionnaire using the sample of Facebook social media users . The users of Facebook users can provide a good foundation for marketers' activities in order to target social media users effectively.

The empirical survey was carried out in June 2018. The first part of the online questionnaire was related to the demographic characteristic of respondents such as gender, age, education level, and monthly income level. Also, the first part of an online questionnaire included questions such as

the most frequently used social network and frequency of use. The second part included statements that determine the activities of users and their purchase behavior in a social media environment. All statements in the second part of the online questionnaire were carried out by a five-point Likert-scale, ranging from strongly disagree (1) to strongly agree (5). For developing the measurement scale of social media user's activities, the author used current internet marketing literature. The statements of the measurement scale were associated with the activities that users take in the process of purchase decision in a social media environment. Table 1 shows the sample characteristics of respondents.

Table 1: Sample characteristics

Characteristics	***N***	***Percentage (%)***
Gender:		
Male	167	33,1
Female	337	66,9
Total	504	100,0
Age:		
18 and less	45	8,9
19-25	110	21,8
26-35	175	34,7
36-45	116	23,0
46-55	53	10,5
56 and more	5	1,0
Total	504	100,0
Education:		
Elementary school or less	43	8,5
Secondary school /qualified workers	389	77,2
College /Highly qualified workers	46	9,1
University degree	24	4,8
Master and doctoral studies	2	0,5
Total	504	100,0
Monthly income (HRK):		
-1999	61	12,1
2000-3999	161	31,9
4000-5999	118	23,4
6000-7999	38	7,5
8000-	17	3,4
Without income (unemployment, students)	109	21,6
Total	504	100,0
The most frequently used social media[2]		
Facebook	428	84,9
Instagram	59	11,7
LinkedIn	6	1,2

[2] It was offered an answer in the online questionnaire, none of the respondents use the social network, Twitter and it is not stated in Table 1. In the context of this question, 9 respondents did not provide an answer.

Snapchat	2	0,4
Total	495	98,2
Frequency of use social media		
Once a week	185	36,7
Daily	224	44,4
Several times a day	95	18,8
Total	504	100,0

Source: Research findings (N=504)

Collected data were analyzed using the software packages for processing qualitative and quantitative data of social research - SPSS 20.

4. Research results

Before using the factor analysis, the reliability of Cronbach's alpha coefficient of the measurement scale of social media user's activities was determined. Results show a high value of the Cronbach's alpha coefficient (0.924) indicating high reliability of the measurement scale. The value of the Kaiser-Meyer-Olkin test was very high (KMO=0.871) and the Bartlett test of sphericity was statistically significant ($\alpha \leq 0.05$). Therefore, the Bartlett test of sphericity indicated the statistical probability that the correlation matrix has significant correlations between at least some of the variables, while the Kaiser-Meyer-Olkin test measure of sampling adequacy showed acceptable sampling adequacy. The construct of the convergent and discriminant validity of the measurement scale was examined through confirmatory factor analysis with Varimax rotation. Two factors with eigenvalues above 1 were extracted (Table 2).

Table 2: Total variance explained for the measurement scale of social media user's activities

	Initial eigenvalues			Rotation Sums of Squared Loadings		
	Total	Variance %	Cumulative %	Total	Variance %	Cumulative %
1	6,39	53,28	53,28	6,39	53,28	53,28
2	1,25	10,45	63,74	1,25	10,45	63,74

Extraction Method: Method Principal Component Analysis
Source: Research findings (N=504)

The factor analysis was used in order to reduce a large number of variables to a smaller number of factors. Based on the results, it is evident that 53.28% of the total variance with an eigenvalue of 6.394 is explained by Factor 1, whilst 10.46% with an eigenvalue of 1.255 is explained by Factor 2. Together, these variables explain 63.74% of the total variance that indicates that the factor model is suitable for further analysis. The next table show factor loadings for the measurement scale of social media user's activities.

Table 3: Factor loadings for the measurement scale of social media user's activities

Variable	Factor 1	Factor 2
V.1	,815	
V.2	,800	
V.3	,745	
V.4	,692	
V.5	,682	
V.6	,676	

V.7	,641	
V.8	,600	
V.9		,811
V.10		,796
V.11		,788
V.12		,774

Extraction Method: Principal Component Analysis.
Rotation Method: Varimax with Kaiser Normalization.
Source: Research findings (N=504)

As can be seen from Table 3, factor loadings for all variables were greater than 0.60 which indicate good convergent and discriminant validity of measurement scale. Rotated factor structure matrix achieves the goal of data reduction and shows the best summary of linear relations. Based on grouped variables and their content it can be concluded that Factor 1 includes activities related to the credibility and trustworthiness of the reviews and comments and it is named the credibility factor, whilst Factor 2 was including statements related to activities of creating a personalized and customize interactions and is named the personalization factor. The purpose of factor analysis is achieved and the interpretation of factors is acceptable.

Further analysis of variance (ANOVA) is performed to determine whether there is a significant difference between the factor of credibility and personalization and features of online purchase behavior in a social media environment. The next table shows the analysis of variance between factors of credibility and personalization and attitude toward purchasing via social media.

Table 4: Analysis of variance between credibility and personalization and attitude toward purchasing via social media

	Sum of squares	**df**	**Mean square**	**F**	**Sig.**
Credibility	90,33	4	22,58	27,30	,000
Personalization	353,06	4	37,48	52,97	,000

Source: Research findings (N=504)

According to the results of variance, significant differences between a factor of credibility and attitude toward purchasing via social media can be observed. As it can be seen, there is a significant difference between credibility factor and attitude toward social media purchasing ($p<0.000$, $F=27,309$) that show that consumer who are following and trust reviews and comments have a positive attitude towards purchasing via social media. These types of users consider reviews and comments from previous consumers trustworthy and therefore believe that purchasing via social media is a safer and reliable process. Statistical analysis shows that there is a significant relation between personalization and attitude toward purchasing via social media ($p<0.000$, $F=52,979$). The result shows that these users who are looking to improve interactions on social media have positive purchase attitudes. In that way, they see social media as a suitable place where they can found required interactions and relation with personalized features. The next table show results of variance analysis between the factors of credibility and personalization and intention toward purchasing via social media.

Table 5: Analysis of variance between credibility and personalization and intention toward purchasing via social media

	Sum of squares	**df**	**Mean square**	**F**	**Sig.**

Credibility	95,87	4	23,96	29,37	,000
Personalization	96,85	4	24,21	29,74	,000

Source: Research findings (N=504)

The results from Table 5, indicate that there are significant differences between the credibility and consumer intention toward purchasing via social media ($p < 0.000$, $F = 29,379$). The result of the analysis reveals that these consumers are more inclined toward purchasing via social media due to the possibility of browsing the reviews and comments of previous consumers. The result reveals significant differences between the personalization factor and purchase intention in a social media environment ($p<0.000$, $F=29,749$). According to the results, it is evident that users who have a stronger need to create personalized interactions via social media will be more inclined to make a purchase. The results of the difference between variance analysis between credibility and personalization factors and satisfaction toward purchasing via social media are shown in Table 6.

Table 6: Analysis of variance between the factor of credibility and personalization and satisfaction toward purchasing via social media

	Sum of squares	**df**	**Mean square**	**F**	**Sig.**
Credibility	73,85	4	18,46	21,46	,000
Personalization	76,78	4	19,19	22,47	,000

Source: Research findings (N=504)

Based on research findings presented in Table 6, it is evident that differences between credibility factor and consumer satisfaction with purchasing via social media exist ($p<0.000$, $F=21,469$). Such differences indicate that these users who based their purchase only on reviews and comments will be more satisfied with the purchase via social media. It indicated that their satisfaction is the result of a review and comments on previous users of these products. A further result of the analysis, between the factor of personalization and consumer satisfaction toward purchasing via social media, show significant differences ($p<0.000$, $F=22,474$). It is pointed out that these users are generally satisfied with the purchase probably because they created an individual interaction and therefore achieved a unique and personalized approach via social media. Table 7 shows the results of variance between factors of credibility and personalization and repurchase via social media.

Table 7: Analysis of variance between credibility and personalization and repurchase via social media

	Sum of squares	**df**	**Mean square**	**F**	**Sig.**
Credibility	76,14	4	19,03	22,25	,000
Personalization	124,05	4	31,01	40,84	,000

Source: Research findings (N=504)

The results of the analysis indicate that the differences between the factor of credibility and consumer repurchase via social media are significant ($p<0.000$, $F=22,253$). It showed that these users will make purchases again based on the reviews and comments from the consumers who already have experience with a particular product. These result suggest that these users who have a high level of trust toward reviews and comments will likely make a purchase again in social media. Also, the significant difference has shown between the personalization factor and consumer repurchasing via social media ($p<0.000$, $F=40,840$). The result explained that users who are using social media for personal interactions, show the characteristics of satisfying users and they will be willing to repeat a purchase via social media in order to enhance a relationship with the preferred

company. The following table shows the results of one-way analysis computed for credibility and personalization factors and the influence of ads and notifications towards purchase attitudes of social media users.

Table 8: Analysis of variance between credibility and personalization and the impact of ads and notifications on the user's purchase decision

	Sum of squares	**df**	**Mean square**	**F**	**Sig.**
Credibility	203,64	4	50,91	84,86	,000
Personalization	73,9	4	18,48	21,50	,000

Source: Research findings (N=504)

Based on the results in Table 8, there is a significant difference between credibility factor and the impact of ads and notifications on the users purchase decision via social media ($p<0.000$, $F=84,866$) suggesting that purchase decisions of these users are significantly influenced by the ads and notifications in a social media environment. Also, the results reveal significant differences between the personalization factor and the impact of ads and notifications on the purchase decision via social media ($p<0.000$, $F=21,501$). The results indicate that consumers who search for a personal approach will be more under the influence of ads or notifications. These consumers regardless of whether they are following the reviews and comments or look for unique engagement via social media have stated that ads and notifications received through social networks significantly influence their purchasing decision. Finally, it indicated that their purchase behavior and final purchasing decisions will be determined by activities on a social media site.

Since the variation within groups is confirmed, we can assume that forms of purchase behavior in social media environments such as consumer attitudes, intention and satisfaction can significantly differ according to different user's activities via social media. Also, it can be concluded these users will be more inclined toward repurchasing in the context of a social media environment.

5. Conclusion

The social media could be considered as one of the main places where companies could improve interaction with their consumers in order to create their activities that could influence consumer purchase behavior. Social media is one of the major communication channels for consumer engagement in order to build a reputation and image of every company. Based on their activities, they have strength in building or destroying the reputation of a certain company.

The purpose of this study was the analysis of social media involvement in the user's purchase decision process. It is obvious that users have two main activities in social media environments such as user's analysis of comments and reviews of previous consumers as well as creating custom and personalized interactions in the context of social media. The first type of activities is related to the user's activity of reviewing the comments or recommendations from previous consumers or their friends in social media. The second type is associated with the user's activities of creating individual or custom connectivity via social media. In general, research results reveal that these two types of activities in the social media environment significantly impact users purchasing behavior, especially on their purchasing decision.

Further, the results of the analysis indicate that there are significant differences between credibility factor and user's attitude, purchase intention, repeated purchase and purchase satisfaction in the context of social media. Therefore, the users who search for comments and recommendations in

social media environment have a positive attitude toward purchasing via social media and the will probably have stronger purchase intentions and make a purchase again with the high level of post-purchase satisfaction. Also, users who are seeking for uniqueness approach via social media will have positive attitudes toward purchasing and have stronger intentions for purchasing in a social media environment. Further, these users who are looking for personal interactions have a high level of purchase satisfactions toward purchasing and therefore will purchase again via social media. It is interesting that both types of users stated that ads and notifications that appear in the social environment could strongly influence on their final purchase decision.

Determining the differences in activities in social media usage, this study contributes to the marketing literature. Hence, this study identifies that reviews and comments from previous consumers as main activities of eWOM have to be an important component of company's online social media strategy as well as the making the better interaction with the actual and potential users in the context of social media.

The main limitation of this study is a limited sample. This research has been conducted with Facebook users that limit the generalization of the results. Therefore, future research could expand the sample to give greater strength to the analysis. Also, further research could expand research by adding more variables or using the current one within different contexts or the country in order to determine the differences in social media usage that can bring valuable theoretical and managerial insights. Finally, future academic research should examine further and deeper in order to get a more complete image of the different usage activities and develop an effective instrument to measure their influence on users purchase behavior in a social media environment.

Based on the results, it can be concluded that companies have to be more effective in establishing quality communication with users i.e. potential consumers in a social media environment. Many companies need to be aware of the importance of providing assistance in the user's decision-making process in the context of social media. Through social media or through brand communities, the companies have to repeatedly reinforce the good image and brand awareness within their actual or potential consumers. If a company have a tendency to be approachable, people-friendly, then the companies need to create a brand community in order to get valuable information about their products and also to create a high-quality interaction with their loyal consumers. Within an online social community or brand community, the companies need to create content that provides users with a unique and enjoyable experience which will attract them to purchase and create positive eWOM among them. The companies that use social media as an integral part of the business, could outline the consumer interaction to a greater extent. This disregarding the impact of social media and the influence of eWOM, for companies have significant negative consequences for their businesses. Also, the companies necessary to include the strong influence of eWOM and design online marketing strategies specifically for the social media environment. Therefore, social media tools have to be incorporated as an integral part of every company's strategy.

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ENHANCING POST-TRANSITION ECONOMY COMPETITIVENESS BY DETERMINING ARTIFICIAL INTELLIGENCE INDUSTRIAL USE APPROPRIATENESS - A PROPOSED ASSESSMENT FRAMEWORK

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Abstract
The fourth industrial revolution has proliferated numerous technology platforms and key enabling technologies, including one of the most influential ones, artificial intelligence (AI). Although considered one of the most influential disruptive technology, usually described as a game-changer, it is still not entirely clear in which industry or sector the AI may produce stronger impacts than in the other. On the other side, it is very well known that the prime enabler of AI expansion in its intensity and usability is access to and availability of large data quantities. Consequently, according to their current data policies, the global frontrunners in AI development are nowadays USA and China. The question arises, how do firms in post-transition economies, specifically operating in restrictive and regulated data access and use environment, as EU is, can benefits from the AI use in their industries or the public sector. Almost all of them are preparing or having already in operation their national strategies of AI uptake and use. Nevertheless, it is still not entirely clear which particular industries or their niches are appropriate to be favoured and supported through tailored AI industrial expansion policy measures. Thus, the purpose of this paper is to conceptualise an analytical appropriateness assessing framework for the AI industrial or sectorial suitability use in a form of technique relevance heatmap, aiming to enhance the competitiveness of post-transition economies (such as this examined case of Croatia). It will be also complemented with recommendations for its translation and generalization on other similar global environments. Results produced by this paper will assist practitioners to conceptualise and operationalize focused national policies and funding instruments in supporting the development of the AI in their economies. It will furthermore assist scholars to construct and build-up their specific empirical research around the proposed model.

Keywords: *artificial intelligence, strategic positioning, post-transition economy*

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1. Introduction

Taking into consideration reigning global megatrends, where the climate changes, scarcity of limited planet resources and so far unimaginable exponential development of digital technologies are imposing a challenge that will almost certainly provoke a subsequent humanity transition. Here the author of this text envision an answer, and premierly introduces and articulates the plausible next stage in human evolution, the Geoeconomy (Vlacic, 2020), which represents the next stage of civilization development, the 5th industrial revolution. Such a novel Geoeconomy concept is essentially characterized by the use and combination of state-of-the-art technologies, particularly the artificial intelligence, in managing the scares and ultimately limited planet resources. The most robust global initiatives nowadays that are aiming to catalyse such ambitious humanity leaps are, The European Green Deal Investment Plan, which is mobilising at least €1 trillion EUR, and its key tool EU Just Transition Mechanism, that mobilises another 100 billion (European Commission, 2019) over the period 2021-2027 in the most affected regions[3]. When the diffusion

[3] https://ec.europa.eu/regional_policy/en/newsroom/news/2020/01/14-01-2020-financing-the-green-transition-the-european-green-deal-investment-plan-and-just-transition-mechanism

and the consequences of the AI are in question, these are furthermore complemented by the EU white paper on AI (EC AI whitepaper, 2020)[4] and the EU Data strategy (EU data strategy, 2020)[5]. In addition, the continuous evolution of smart cities, intelligent medical care, intelligent transportation, intelligent logistics, intelligent robots, self-driving vehicles, smart-phones, intelligent toys, smart communities, and smart economies, provides a broad market demand and driving force in terms of a new development of both AI technologies and applications (Li et al, 2017). Investments in AI solutions are prevalent in business areas such as customer service management, as well as among some other industries where the data are rich and voluminous and at the same time they are interlaced with human reactions. Among other industries, numerous greenfield use-cases in healthcare are identified, and some of these cases involve disease diagnosis and improved care, and rely on rich data sets incorporating image and video inputs, including those from MRIs (McKinsey GI, 2018). Investigation of AI technologies epistemology and the propensity of investments in it can often be vague in terms of resulting economic effects and nationwide economic impacts, both from the supply and demand side.

When the regional, national or even continental AI consideration levels are in question, there are numerous potentials of AI technologies translated in effects on overall national economic effects, niche impacts on national and regional industries, impacts on manufacturing effects, impacts on labour markets and other redistributive effects, and others (EU economic impacts of AI, 2019).

In that sense we are witnesses of incessant emergence of national AI policies, plans and strategies, which are attempting to optimize the impact on the rate of improvement in AI use; by the speed of diffusion, the nature of the technology, and by AI deriving consequences (Agrawal, Gans and Goldfarb, 2018). Most obviously, as with other technologies, policies that provide development support for AI are likely to accelerate technological progress as are policies that strike the appropriate balance with respect to intellectual property (Williams, 2016; Scott Morton and Shapiro, 2016). However, three other policy categories - privacy, trade, and liability - are likely to impact the diffusion of AI in ways that are different than other technological innovations. A quick analysis of some of these strategies reveals takes on AI that are subsumed to the overarching objective of advancing national interests. Therefore, what are these national plans on AI telling us about the return of great power competition?

In order to answer the mentioned challenges, this paper aims to produce the appropriate framework intended to examine the AI diffusion suitability for given national industry, aiming to contribute to the global knowledge body from scholars' perspective, but also at the same time to the national competitiveness from practitioners' perspective.

Thus, the purpose of this paper is to conceptualise an analytical appropriateness assessing framework for the AI industrial or sectorial suitability use in a form of technique relevance heatmap, aiming to enhance the competitiveness of post-transition economies (such as this examined case of Croatia), complemented with recommendations for its translation and generalization on a global scale.

Following this introduction, theoretical background and a literature review on the currently available theoretical background are presented. It includes the overview of the current AI trends in use, global AI reaches and impacts, AI paradigms and technology classification, latest trends in Croatian national environment AI development, including use cases in sectors and industries. The second part ends with articulation and articulation of the research challenge. The third part presents the ideation, construction process and operational results in the form of the empirical proposed model, specifically constructed to assess the economic effects of AI diffusion appropriateness heatmap. The proposed model ensures a structured contextual framework for next stage practical research work and its operationalization. Paper ends with resulting discussion on results, conclusions, and identified limitations.

[4] https://ec.europa.eu/info/sites/info/files/commission-white-paper-artificial-intelligence-feb2020_en.pdf

[5] https://ec.europa.eu/info/sites/info/files/communication-european-strategy-data-19feb2020_en.pdf

2. Theoretical background

In examining the available theoretical body of knowledge there is a scarcity of appropriate scholars' attempts to assess and operationalize the AI use (diffusion and consequences) suitability at the national levels. The author is assuming that it is a result of a rather novel, fluid and complex nature of the researched topic. In setting the appropriate model to evaluate the AI impact on the economies and society one has to take into consideration numerous elements. Starting first from the wide palette of available AI paradigms and technologies, the complexity of the industry where AI shell be diffused, the availability of data, and all other specifics of the assessed environment. Nevertheless, the thorough examination of scholar literature and other available relevant theoretical sources has resulted in the identification of a number of research papers and reports prepared by professionals (McKinsey, 2018; BCG, 2018, PWC 2018 and 2019, and similar) which are partially tackling the same issue.

AI impact on the economies and society

It is a globally accepted common global paradigm that artificial intelligence (AI) may transform the productivity and GDP potential of the global economy. Strategic investment in different types of AI technology is needed to make that happen. The majority of AI related studies emphasise that AI will have a significant economic impact. A study produced by Price Waterhouse Coopers (PWC, 2018) estimates that global GDP may increase by up to 14 % (the equivalent of US$15.7 trillion) by 2030 as a result of the accelerating development and AI diffusion ramping-up.

In their report, McKinsey GI (2018) argues that AI (and automation) may, on one hand, facilitate the rise of massively scaled organisations, and on the other will enable small players and even individuals to undertake project work that is now mostly performed by bigger companies. This could spawn the emergence of very small and very large firms, the end result being a barbell-shaped economy in which mid-sized companies lose out. Other likely effects are increased competition, firms entering new areas outside their previous core business, and a deepening divide between technology leaders and laggards in every sector. (European Union, 2019).

McKinsey GI (2018) furthermore argues that early adopters, that is, companies that fully absorb AI tools over the next five to seven years, will most probably benefit disproportionately. At the other end of the spectrum would be the slow adopters or non-adopters, which are likely to experience some economic decline. The market share is likely to shift from the laggards to the front-runners, which would be able to gradually attract more and more of the profit pool of their industry. This may lead to a 'winner takes all' phenomenon, similar to what is currently observed on technology related markets.

In their work (EU economic impacts of AI, 2019) authors are emphasising that advances in AI and technology could enable front-runners to make a decisive break from the pack and become 'superstars' enjoying the highest productivity levels. This can have significant consequences. OECD (Andrews, Criscuolo and Gal, 2015) has raised the question as to why apparently non-rival technologies are not diffused to all firms. It may well be that the widening productivity gap between firms can be attributed to the highly uneven process of technological diffusion, which favours global frontier firms over laggards. This may occur because global frontier firms can better protect their advantages; this could eventually even contribute to a slowdown in aggregate productivity growth in the economy. These widening productivity and innovation gaps are surely going to attract a lively policy debate on the unequal distribution of the benefits of AI.

In this context, it is useful to look at the industries that are moving to the forefront of AI deployment. McKinsey GI (2018) envisions AI as already having a significant impact and great commercial potential in sectors such as marketing and sales, supply chain management, logistics and manufacturing. A survey by the Boston Consulting Group (BCG, 2018) emphasises the automotive and technology, logistics, and transport sectors as already being at the forefront of AI diffusion. It also unveils that process industries (chemicals, mining, steelmaking, etc.) are fairly lagging behind. In their study Price Waterhouse Coopers (2018) expects that thanks to AI all sectors of the economy will see a gain of at least 10 % by 2030. The report says that the services

industry is to gain the most (21 %), with retail and wholesale trade as well as accommodation and food services also expected to see a large boost (15 %).

Industry and sector use cases

To understand the AI application in practice and its diffusion in the industry it is advisable to examine it through use cases. McKinsey GI (2018) evaluates that in more than two-thirds of examined use cases AI can improve performance beyond that provided by other analytics techniques. Similar analytics is provided also by others, PWC (2018), BCG (2018), BCG/MIT Sloan (2019) etc. Such analytics of use cases are offering valuable information about which are the industries or sectors where the AI diffusion may produce the highest possible impacts. Figure 1. Represents industry and sector-related use cases with AI implementation potential incremental values (McKinsey, 2018).

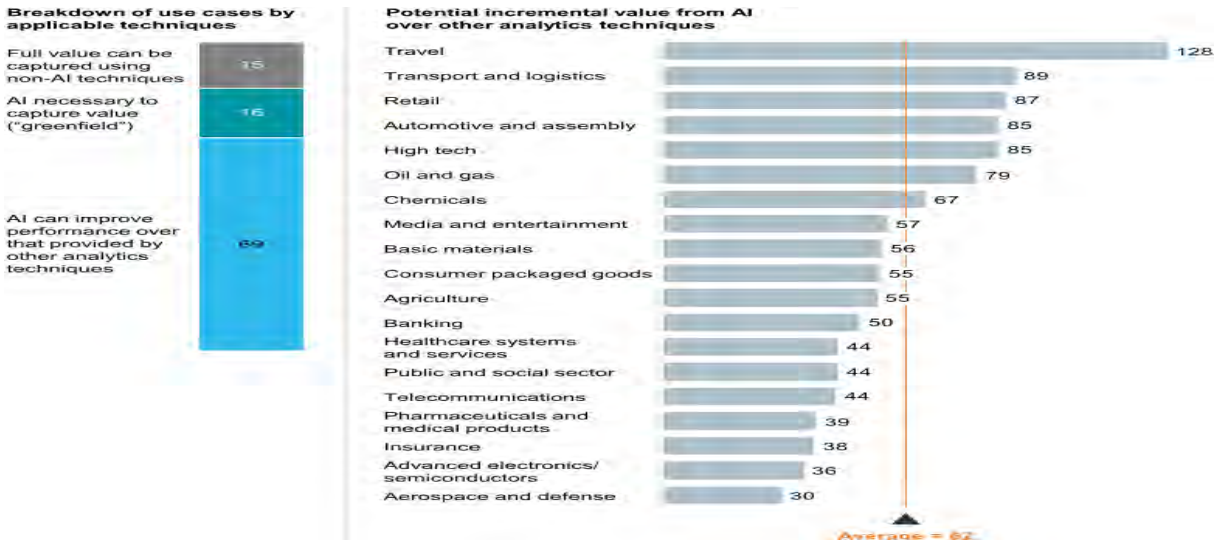

Figure 1: Use cases with AI implementation potential incremental values (McKinsey, 2018)

The global AI race

The race to become the global leader in artificial intelligence is on the roll. In the past two years, Canada, China, Denmark, the EU Commission, Finland, France, India, Italy, Japan, Mexico, the Nordic-Baltic region, Singapore, South Korea, Sweden, Taiwan, the UAE, and the UK have all released strategies to promote the use and development of AI[6]. No two strategies are alike, with each focusing on different aspects of AI policy: scientific research, talent development, skills and education, public and private sector adoption, ethics and inclusion, standards and regulations, and data and digital infrastructure.

In their work, Agrawal, Gans and Goldfarb (2018) are stressing that national policies are focused on and influencing impacts on two key AI dimensions: diffusion and consequences. First, in addition to subsidies and intellectual propriety policy that will influence the diffusion of AI in ways similar to their effect on other technologies, three policy categories - privacy, trade, and liability - may be uniquely salient in their influence on the diffusion patterns of AI. Second, labour and antitrust policies will influence the consequences of AI in terms of employment, inequality, and competition.

[6] https://medium.com/politics-ai/an-overview-of-national-ai-strategies-2a70ec6edfd
https://futureoflife.org/national-international-ai-strategies/?cn-reloaded=1, http://www.unicri.it/in_focus/files/Report_AI-An_Overview_of_State_Initiatives_FutureGrasp_7-23-19.pdf,
https://medium.com/politics-ai/an-overview-of-national-ai-strategies-2a70ec6edfd

As earlier mentioned, EU is pursuing a digital strategy that builds on its history of technology development, innovation and ingenuity, vested in European values. The White Paper on Artificial Intelligence (AI) and the European data strategy presented on the 19th of February 2020 was intended to demonstrate that Europe can act as a forerunner in global digital standards and technological development while putting people first. In addition, in 2019 25 European countries signed a Declaration of cooperation on Artificial Intelligence (AI). Whereas a number of Member States had already announced national initiatives on Artificial Intelligence, they declared a strong will to join forces and engage in a European approach to deal therewith. By teaming up, the opportunities of AI for Europe can be fully ensured, while the challenges can be dealt with collectively[7].

When national investments in AI level are examined, by states produced AI national plans and budgets are offering such insights Figure 2. (Campbell, 2019). How those funds are nationally allocated is extremely valuable for the analytical purposes.

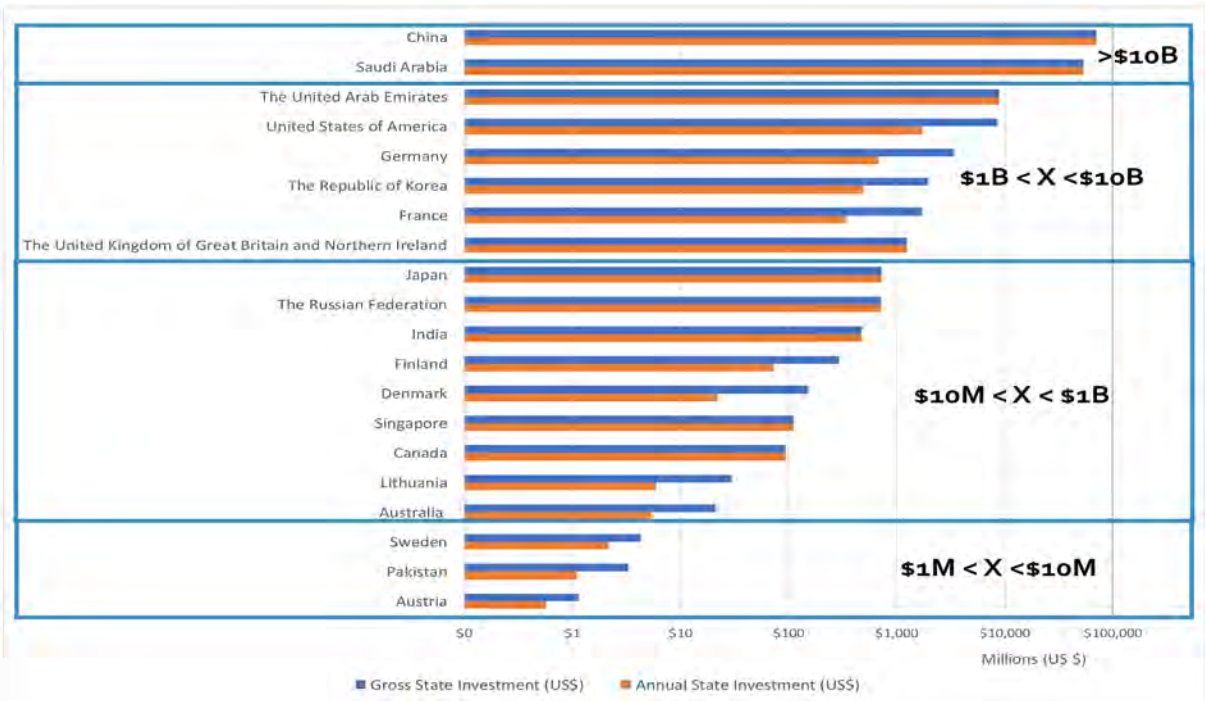

Figure 2: Government-sourced investments by nations (Campbell, 2019)

Artificial Intelligence as a General Purpose Technology

In their paper Agrawal, Gans and Goldfarb, 2018 first define AI, and then argue that AI is likely to be the next general purpose technology (GPT) characterized by pervasive use across a wide variety of sectors and technical dynamism (Bresnahan and Trajtenberg 1995). Along with other data presented in the paper, they view this as evidence that AI is a GPT in the method of invention. It will, therefore, have a widespread impact on the economy, accelerating growth. However, it is still far away from the 'fearsome' General AI. Ben Goertzel, president of the Artificial General Intelligence Society fairly optimistically expects the General AI appearance in just seven years. On the other side, Reinforcement learning pioneer Richard Sutton provided a median guess that artificial general intelligence will arrive by 2040. Gary Marcus, often seen as an AI sceptic, provided a confidence interval of 30 to 70 years. Many others say never. If artificial general intelligence is imminent, then a key policy challenge will be for the institutions to keep up with the abilities and needs of a world with machine intelligence.

[7] https://ec.europa.eu/digital-single-market/en/news/eu-member-states-sign-cooperate-artificial-intelligence

In general, AI technologies and paradigms can be classified in numerous ways, among others a comprehensive AI classification is presented as AI Knowledge map, developed by Corea (2018) and presented on figure 3.

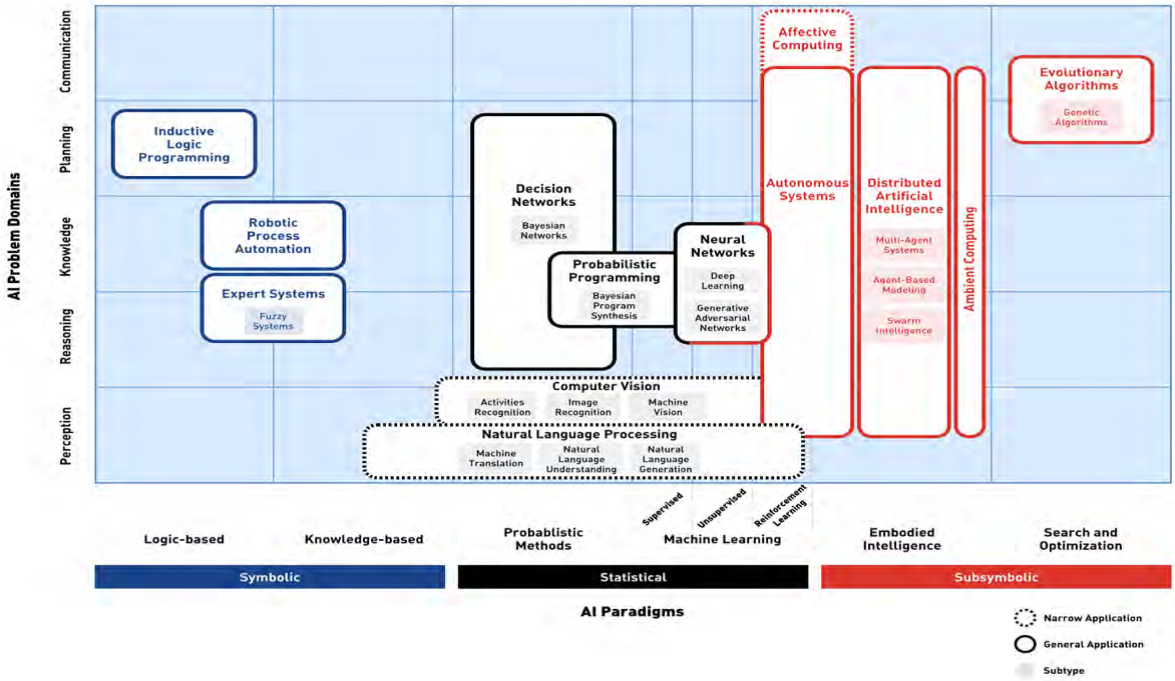

Figure 3: The AI Knowledge technology and map and developed by Corea (2018)[8]

National AI propelling intensity and initiatives

In attempts to analyse the AI diffusion in smaller countries, particularly these emerged from as transition economies, the right question is in which areas, sectors or industries AI can develop to be internationally important. The next emerging question related to the national competitiveness is, can AI act as an important and impactful growth driver? The proper example of post-transition economy in setting the appropriate national AI strategy is Estonia, which dedicated 50MEUR in stimulating and boosting selected economic sectors[9].

In relation to this paper examined post-transitional economy, in 2019 Croatia was not immediately ready to sign the EU Member States national initiative on Artificial Intelligence due to many issues. Finally, it was the last one to sign it a few months after. On the Government Artificial Intelligence Index (Miller, 2019) Croatia is placed at the 62nd place out of 194 ranked countries.

In order to motivate and rump-up the AI diffusion scene, several nongovernmental initiatives were triggered. One of the most influential ones is proposed by the Croatian Employers Association (CEA/HUP), the next is coming from the independent community AI2FUTURE[10] and the recently established CRO.AI[11].

From the practitioners' side, Croatia is witnessing a number of emerging start-ups that are engaged in specific vertical industries, Gideon Brothers, Robotiq.AI, AIRT, VINGD and similar. These are supporting logistics, SW robots, insurance business and financial industry with the new AI–based algorithms and predictive models, or on the other side driving their human-centric solutions toward the artificial intelligence, especially in the fields of healthcare.

[8] https://www.forbes.com/sites/cognitiveworld/2018/08/22/ai-knowledge-map-how-to-classify-ai-technologies/#190c2fd27773

[9] https://f98cc689-5814-47ec-86b3-db505a7c3978.filesusr.com/ugd/7df26f_27a618cb80a648c38be427194affa2f3.pdf

[10] http://ai2future.com/

[11] https://www.croai.org/

In 2020 the Croatian Ministry of Economy and Entrepreneurship finally decided to activate the creation of a National Plan for AI Implementation, a document (among several other National plans) where the national strategy, action plans, and key steps needed to defined in order to boost the national AI development and diffusion.

The research challenges and targets

In shaping up the National AI Plan the principle question is, which methodology will be used to establish the appropriate match between the available AI paradigms/technologies and the national industry topology and their potentials? What are the optimal matchmaking spots that will maximise the impacts and represent eligible technology development opportunities for intended governmental incentivised financing? Such spots could be established in a form of AI industrial labs, test beds or polygons. Last but not the least, in using that methodological approach can Croatia establish itself as a niche leader, innovator or supplier of technology based solution portfolios based on Artificial Intelligence?

As previously mentioned, the overarching research challenge and proposition of this paper are to contextualise an analytical suitability assessment conceptual framework that will serve as a practitioners' and researchers' vehicle in examining the genesis and economic feasibility of AI diffusion.

Additional value that the authors are seeking out of the proposed research model is pragmatic linkage to the national policy, whereby it could result in recommendations of tailored strategies aiming to redesign national incentivising instruments designed to catalyse and accelerate the development and expansion of AI technologies. While producing such outputs, one has to be segment specific, because there are two basic incentivising categories, the sole users of AI technologies for their operational functionality on one side, and the producers/suppliers of AI solutions and business models on the other. This paper will attempt to evaluate both sides in creating the unique matchmaking AI vs. industry appropriateness heatmap.

The next goal set by this research is the generation of a quasi-universal practical model that will be nearly applicable in other similar environments matching the Republic of Croatia one, precisely the post-transitional nations and their environments. In addition, the outputs will be complemented with recommendations for its translation and generalization wider on a global scale.

Last but not the least, the results of the subsequently conducted empirical research based on the proposed model, will contribute to the further expansion of the theoretical knowledge body in the examined fields of AI economics and managerial practices.

The author is furthermore looking forward, considering the synergic interactions and spillover effects of the proposed research, to use produced results in comparison with firms' technology innovation ability, intensity, and implications. Such findings will be used to bridge or eventually shorten the differences in perceiving the firms' AI technology innovation issues between firms themselves and the government, which was in case of the Croatian economy already recently examined by Vlacic, Dabic, Aralica (2018) and Vlacic et al, 2019.

3. The proposed model

When it comes to ideation, conceptualization, and operationalization of the model, the first step represents understanding the insights of the business environment on which the research shall be applied. In the context of this research, the Republic of Croatia is considered a post-transition economy (Bozic and Botric, 2017), part of the EU association, with the business environment conditions similar to other Eastern EU countries. The conceptualization and the proposed operationalization of the model focus on transnational universality and generalization in the sense that proposed model with minor modifications can be applied in other similar operating environments.

AHP methodology use

In order to determine the adequate matchmaking result the AHP method is selected. AHP has been extensively applied mainly in decision-making applications (Saaty, 1996). Through AHP, the importance of several attributes is obtained from a process of paired comparison, in which the relevance of the attributes or categories of drivers of intangible assets are matched two-on-two in a hierarchic structure. The AHP modelling process involves four phases, starting from structuring the problem, performing the measurement and data collection, determination of normalized weights and synthesis finding solution to the problem, also suggested by Tummala (1994). The AHP matrix may be complemented and combined with other decision matrix analysis methodologies such as Pugh Matrix Analysis or also known as Multi-Attribute Utility Theory.

Data collection and multistage process

Assuming that the problem is already articulated and structured, in setting the realistic research expectations one has to be aware of the current environmental circumstances and the available resource base, particularly in data availability. Therefore setting certain boundary conditions and leading criteria is necessary as a first step. Taking into consideration Croatian scarcity in data quantities and access, and industrial niche focus in conjunction with the human-centric approach is highly recommended as leading criteria in the targeted research scenario.

As specified in the AHP methodology conduction, the next in the research methodology is to perform relevant data collection. A relevant group of opinion makers and experts in the fields of AI use and industrial counterparts will be selected. It is assumed that the relevant satisfactory sample number will be between 50 and 60. They will be selected from various stakeholder groups, primarily the industry representatives, AI suppliers, and practitioners, but also the academia, industrial associations and civil society members.

The intended form of data collection is a semi-structured interview with a structured focus and concise questionnaire. In order to achieve a satisfactory response, sole members of the National AI Plan Working Group (about twenty of them) will be used as interviewees in the role of the opinion and decision makers, but at the same time as interviewers for the rest of the selected population sample.

The analytic process is designed as multi-stage one, for both, the AI paradigms and technologies and also for the matching industries. The first step in the evaluation of AI technologies will be the extraction and filtering of the appropriate already in use from the comprehensive available AI paradigms (Corea 2018). At the same time, techniques that may be suitable and/or show potentials, but at the moment are not available or not sufficiently diffused, will be identified and selected as well. Thus, one obtains a suitable data set represented by AI segments that may induce a significant economic impact, both in the near present but also in the medium term. As a preliminary taxonomic definition of the technology categories within the initial steps, the earlier presented AI technology map (Corea 2018) will be used, presented in table 1.

Table 1: AI knowledge map based on Corea (2018) and technology taxonomy structured

	AI paradigms					
AI problem domains	**Symbiotic**		**Statistical**		**Subsymbiotic**	
	Logic based	Knowledge based	Probabilistic methods	Machine learning	Embodied intelligence	Search and optimization
Perception			Natural language programming Computer vision	Natural language programming Computer vision	Autonomous systems Distributed artificial intelligence Ambient computing	
Reasoning	Expert systems (Fuzzy systems)	Expert systems (Fuzzy systems)	Decision networks (Bayesian)	Probabilistic programming Neural networks	Autonomous systems Distributed artificial intelligence Ambient computing	
Knowledge	Robotic process automation Expert systems (Fuzzy systems)	Robotic process automation Expert systems (Fuzzy systems)	Decision networks (Bayesian) Probabilistic programming	Probabilistic programming Neural networks Autonomous systems	Autonomous systems Distributed artificial intelligence Ambient computing	Evolutionary algorithms
Planning	Inductive logic programming		Decision networks (Bayesian)	Autonomous systems	Autonomous systems Distributed artificial intelligence	Evolutionary algorithms
Communication				Affective computing Autonomous systems	Affective computing Autonomous systems Distributed artificial intelligence	

					Ambient computing	

A similar two stage process will be applied to the industry sampling category. This raw set of unstructured data deriving from different sources will be extracted from nationally available classifications and statistic data and other available secondary data sources (McKinsey, PWC, BCG, others) particularly using the presented use cases. As with the AI technologies, the first step represents the creation of a shortlist in current industries where presumably the AI may produce higher impacts, particularly identifying those with low hanging fruits potential. At the same time, it has to project the industries that the Republic of Croatia is strategically focused on, and intent to grow in the future.

Figure 4. is representing a structure of the proposed model, including data sets on one side which are representing selected AI technologies, and selected matching industries on the other.

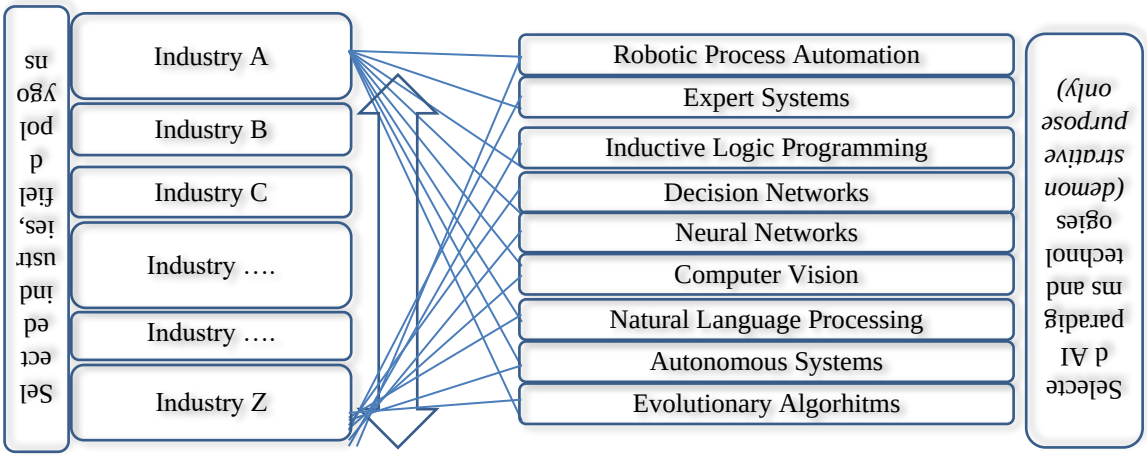

Figure 4: Proposed research concept, the appropriateness assessment framework

The next step represents application of the AHP method, which produces the required heatmap appropriatnes technology use matrix for given national industries. Obtained results are visualised in the for of the technology relevance heatmap (table 2.), whereby the fields with higher values (or color intensity) are representing the preferable matchmaking hotspots. Such extrapolated hot spots are representing ideal candidates for the further focus and attention, being ideal eligible combinations for the governmental incentivising measures provided by the industrial and/or innovations policies.

Table 2: Technology relevance heatmap, simulated and projected results

		Selected AI Paradigms and technologies *(demonstrative purpose only)*								
		Robotic Process Automation	Expert Systems	Inductive Logic Programming	Decision Networks	Neural Networks	Computer Vision	Natural Language Processing	Autonomous Systems	Evolutionary Algorithms
Industries, field polygons	Industry A	2,02	6,7	3,99	9,34	3,65	5,24	1,23	9,21	4,04
	Industry B	5,9	2,37	1,97	1,17	8,59	7,6	7,28	4,23	7,05
	Industry C	7,79	2,35	1,02	2,35	1,2	8,77	3,51	2,59	4,93
	Industry ...	7,33	7,36	5,31	2,92	5,89	2,3	1,78	3,13	5,44
	Industry…	5,5	3,51	2,27	3,56	3,37	7,9	8,61	7,83	7,27
	Industry Z	3,92	6,71	2,55	6,86	2,76	5,55	6,5	2,49	0,88

4. Conclusions and Limitations

AI has significant potential to boost economic growth and productivity, but at the same time, it may create equally serious risks of job market polarisation, rising inequality, structural unemployment and emergence of new undesirable industrial structures (European Union, 2019). It is expected that big players (USA, China) will dominate the global arena, nevertheless, there's a space for smaller players, including the post-transitional economies, including Croatia. In the case of the latest, the process has to be rather analytical on one side, but also niche oriented, innovative and risk taking on the other. There is no silver bullet for such an approach, but a well planned and executed national strategy that involves a number of stakeholders – government, organizations, academia, and individuals. All of them should have a clear understanding of what

needs to be the overarching goal as a common vision, but most importantly, we need to understand how deep and wide digital transformation based on AI paradigms may move the society forward.
In order to address such a challenge, this paper is offering a developed AI technology vs. industry assessment model in a form of technology heatmap that may correspond to smaller, especially post-accession economies, but it can be also applied to larger ones. Such heatmap shells allow scholars, practitioners, but also policy makers, to focus their efforts on developing national AI diffusion plans. Thus generated heatmap will significantly assist in selecting the appropriate national strategic directions and create appropriate incentivising measures within their policy mixes.
The output of this paper represents the concept of a tailored research model that is intended to get operationalized through the empirical second phase. The presented methodology will be furthermore optimised and bespoke in its operationalization to suit the conditions of post-transitional economies, but at the same time, it shall be also applicable and transferrable to other candidate economies.
Finally, empirical operationalized outputs shell assist the national innovation triple helix stakeholder; the business practitioners, the policymakers and the academic researchers, in better contextual articulating the AI diffusion efforts and strategies within National AI Plans as a constitutional part of National Development Strategy 2030 (NRS2030).

Identified limitations

Identified limitations in this paper are primarily related to the planned interviews and their questionnaire outputs, primarily in optics of responses quality and quantity, their segmentation and responses distribution, as well as the possible biased profile of questionees. From the operational point of view, due to the ballistic expansion of AI technologies, it is of crucial relevance to conduct the empirical research with no hesitation, whereby if postponed or delayed the produced results may be of significantly less or no relevance at all. A similar situation is recently noted in a field of widely examined Industry 4.0, which has rapidly transited from the propelling emerging platform few only years ago to nowadays almost mature one.
The next limitation may be noted in intentionally omitting the public sector use, which by many is considered as extremely important for the technology prototyping, particularly through applying the Public Procurement of Innovation principle, in this case for AI diffusion. Nevertheless, including the public sector in the scope of this proposed research may dilute operationalization efforts and expected findings. Considering that it is suggested for the public sector to be included in separate independent research.

In any moment of decision making, as this one is, the best thing you can do is the right thing, the next best thing is the wrong thing, and the worst thing you can do is nothing.

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ANTECEDENTS OF FIRM'S COMPETITIVE BEHAVIOUR AND PERFORMANCE INDICES

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Abstract
In the hypercompetitive environment firms constantly need to be aware of unexpected attacks, both from the big as well as small competitors, even from those firms that do not seem to be direct and serious competitors. Hypercompetition is not just something typical for the IT industry, it becomes commonly used term to describe competitive environment in many industries. Hypercompetitive environment is characterized by very aggressive and unpredictable competitive moves and countermoves done by competing firms in order to sustain or improve their performance. There is a general opinion 'the more aggressive you are, the better performance indicators you achieve'. By studying more deeply all available empirical results in competitive dynamics research, we can say that above mentioned thesis makes sense in general, but is not universally promising strategy. Positive impact is especially evident in a newly developed markets and markets with high growth potential. Very aggressive strategy can cause higher costs and destroy firm's performance indicators. Resource rich firms choose to be very aggressive on the market. Contrary, it does not mean that resource poor firms with specialized resources and capabilities cannot be aggressive and successful. Even firms with high performance indicators are not motivated to act aggressively. However, many other characteristics should be taken into account in order to consider why competitive aggressiveness diminishes or increases firm's performance. Above mentioned facts induce to include firm's internal factors (top management, team heterogeneity, firm size, firm age, resources and capabilities, complexity of organizational structure) and external factors (changes in the environment, institutional investors, newly or developed markets, market growth) that impact competitive behavior and consequently, performance indices.

Keywords: *competitive dynamics, performance and competitive antecedents, firm performance*

Track: *Management & Leadership*

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1. Introduction

Several theoretical concepts of the modern strategic management theory aim to discover the key factors that determine a firm's success. The industrial organization view posits that industry environment determines success or failure of the firm (Porter, 1980). The resource-based view finds the sources of a firm's success in specific resources that are heterogeneously distributed and imperfectly immobile across firms (Barney, 1991). According to the institutional based view, successful firms are those that constantly adjust their business activities based on defined formal and informal legitimate behavior (North, 1991). The upper echelon theory is focused on the analysis of decision makers' characteristics that are predictors of strategic competitive behavior and firm performance (Hambrick & Mason, 1984). Dynamic capabilities are interested in a firm's internal characteristics like integration, reconfiguration and the development process of the firm's competencies that may be the source of the firm's competitive advantage and performance (Teece, Pisano & Shuen, 1997). This concept is a certain extension of the resource-based theory.

Each and every above-mentioned theoretical concept of strategic thinking tries to explain the sources of a firm's performance and the achievement of competitive advantage in a different way. Some of them are focused on the analysis of external factors that determine the scope of their business, while the others rely on internal strengths, like the firm's resources and capabilities, processes, or characteristics of decision makers. The competitive dynamics view of strategical

thinking stresses that a firm's competitive behavior on the market can significantly influence the firm's performance (Ferrier, Smith & Grimm, 1999; Chen & Miller, 2012; Miller & Chen, 1994). This view is developed on the foundations of Schumpeter's theory of 'creative destruction'. By the term 'creative destruction', Schumpeter explained a firm's constant exposure to change, like the mutation process in biology (Schumpeter, 1950). The change is a consequence of a firm's internal and external factors. However, the main initiator of change is competition coming from new products, new markets, or new organizational forms.

Rapid technological development and globalization processes have significantly intensified competitive intensity in the market. Firms are doing their business in the environment of constant struggle to get ahead of others. D'Aveni (1994) stated that a hypercompetitive environment is a circumstance of short-lived competitive advantage. This is not the same as an environment of perfect competition, even if it mostly resembles it. In order to survive and to be successful, these circumstances require constant generation of competitive actions and a complex set of different competitive moves in comparison to the ones from their competitors.

The competitive dynamics view emphasizes that strategic competitive behavior of a firm on the market is extremely important for its success and the success of its competitors. Performance is driven by specific visible moves generated by a firm that are reflected in new products, new marketing campaigns, quality upgrades, changes in prices, new markets, etc. (Ferrier, Smith & Grimm, 1999; Baum & Korn, 1999, Chen & Miller, 1994).

Researchers have systematized the above-mentioned different competitive actions into different types. Grimm & Smith (1997) have identified four types of competitive moves: entrepreneurial, Ricardian, deterrent and co-optive. For example, entrepreneurial actions are related to new product introductions, Ricardian stand for price changes, and deterrent actions are related to aggressive advertising campaigns. Chen (2007) has divided firms' actions into: positioning (price changes), transformative (investment in R&D, new technologies) and power action (patents). Smith et al. (1991) divide them into strategic and tactical actions. Strategic actions are those that are difficult to implement by competitors and require more time to adequately respond to. Tactical actions, in principle, are simple competitive moves and market opponents will very quickly respond to them (Chen, Farh & MacMillan, 1993).

Within the competitive dynamics view, there have been developed several analytical directions that contribute to a better understanding of a firm's strategic behavior, from the analysis of the action-response relationship, to competitive analysis at business unit level, firm or multibusiness level, tending to connect micro and macro business research topics. These are as follows: competitive interaction (action-level studies), strategic competitive behavior and competitive repertoire, multimarket and multibusiness competition (corporate-level studies), integrative competitive analysis and competitive perception (Chen & Miller, 2012). The competitive interaction stream is focused on the study of competitive moves and countermoves at a micro level of competitive analysis, where researchers clearly distinguish commonalities and differences among market players. They are interested in how the complexity of a firm's organizational structure impacts the speed of a firm's countermoves to certain competitive actions initiated by competitors (MacMillan, McCaffrey & Van Wijk, 1985), how simple competitive moves induce fast response from competitors (Chen, Farh & MacMillan, 1993; Chen, Smith & Grimm, 1992), how the aggregated level of competitive moves, initiated by several firms on the market, influences the firm's competitive reactions (Zucchini & Kretschmer, 2011), or the analysis of the number of a firm's competitive moves that trigger the countermove by its competitors (Tsai, Su & Chen, 2011). The strategic competitive behavior and competitive repertoire stream studies the relationship between firm performance and the aggregated level of a firm's competitive moves, or the impact of their action complexity level on firm performance indices. Moreover, Ferrier, Smith & Grimm (1999) introduced the term 'action dissimilarity', aiming to find the link between different firm's action types compared to their main opponents, and their consequences on firm

performance. Multibusiness and multimarket competitive analysis introduced the concept of 'mutual forbearance' by which researchers explain the situation where firms cope with their competitors in more than one market and recognize mutual dependencies among each other. That notion motivates firms to carefully dose the intensity of their competitive aggressiveness strategy due to unwanted escalation in other commonly shared competing markets (Chen & Miller, 2012). In that situation firms usually conduct less aggressive competitive strategy because they are aware of the fact that every aggressive competitive move will adequately be countermoved (Gimeno & Woo, 1999). The integrative competitor analysis concept intends to integrate different firm characteristics in order to more precisely explain the impact of competitive aggressiveness on a firm's performance (the firm's resources or market commonalities). Competitive perception includes cognitive elements of decision makers presented in the awareness-motivation-capability framework that are predictors of actions and reactions of the firm.

2. Internal and external antecedents that frame a firm's competitive behavior

Competitive action repertoire covers the analysis of a firm's competitive intensity and the complexity of its competitive moves (Miller & Chen, 1994; Ndofor, Sirmon & He, 2011, 2015; Ferrier & Lyon, 2004; Connelly et al., 2016). Competitive aggressiveness (intensity) is one of the main constructs inside the competitive dynamics research. It explains the impact of the total number of competitive moves or a relative number of competitive moves of a firm (or a business level segment) in the market at a certain point in time (commonly used one year) on performance indices (Ferrier Smith & Grimm, 1999; Ferrier & Lyon, 2004; Miler & Chen, 1994). A firm's competitive behavior considers a firm's competitive moves and countermoves compared to its main opponents on the market. A competitive move by a firm influences competitive behavior of other firms on the market, where they are trying to defend or improve their performance, while negatively impacting a competitor's performance. Derfus et al. (2008) explained this phenomenon as *'red queen race'* effect. The second construct of the competitive action repertoire studies the relationship between a firm's performance and the range of different kinds of competitive moves a firm carries out, like price changes, product introductions, quality upgrades, marketing campaigns, entrance into new markets, new alliance, and so on.

The strategic competitive behavior and action repertoire stream are focused on the analysis of the competitive repertoire and a firm's performance and, in general, many empirical studies show their positive relationship. Ferrier, Smith & Grimm (1999), having analyzed competitive moves in 40 different industries, showed that more active firms on the market are more successful firms. The same results were presented by Young, Smith and Grimm (1996), who studied competitive moves and a firm's performance relationship in the IT industry. Connelly et al. (2016) also reported a positive relationship, while analyzing a firm's behavior in shorter and longer time periods. In the short-term period firms are supposed to, using agile and fast competitive moves, paralyze opponents, delay their countermove and ensure themselves temporarily competitive advantage (D'Aveni, 1994). The strategy of competitive aggressiveness gives firms the opportunity to add value to their customers by offering better price-quality ratio (Nadkarni, Chen & Chen, 2015). Moreover, an aggressive strategy opens up the constant process of learning-by-doing and, as a consequence, gives the opportunity to implement complex strategies that are difficult to implement by competitors (Nadkarni, Chen & Chen, 2015).

The above mentioned empirical and theoretical scientific papers have mainly found a positive relationship between a firm's competitive aggressiveness and performance. But there are empirical studies that have identified a negative or statistically insignificant relationship. Ferrier & Lee (2002) analyzed a firm's competitive activity and price stock changes and did not find a significant relationship between them, but they found a negative relationship between a firm's competitive intensity and stock price changes of their competitors. Andrevski & Ferrier (2016) showed, based on an empirical study of firms from three different industries, characterized by working in

hypercompetitive environment, that strategy of competitive aggressiveness is not always a promising strategy for firm performance. They found a 'U' curved relationship between a firm's aggressiveness and performance indicators - very aggressive strategy often induces costs and diminishes performance. Miller & Chen (1996) found a negative relationship between simple competitive moves and performance in a fast-growing market, as well as in the situation of market uncertainty. However, Miller & Chen (1994) and Miller (1993) found a positive relationship between simple competitive moves and a firm's performance in the short-term period, while in the long-term period simple competitive moves negatively affected performance indices because they are easily copied by competing firms.

What motivates organizations to aggressively perform on the market? Derfus et al. (2008) mentioned that contestability on the market and, as a consequence, performance indices depend on industry context and conditions on the market. Firm environment is getting more and more complex, which impacts firms' strategic directions. On the other hand, firms can also shape competitive dynamics on the market using their top management team characteristics, organizational characteristics and processes, resources and the intensity or speed of their competitive moves. Hence, market variations are a consequence of internal and external antecedents that are not easily perceived based on a firm's fragmented analysis (Scumpeter, 1950). Industry leaders and challengers use different competitive strategies on the market (Woo & Cooper, 1983; Basdeo et al. 2006). They use different strategies in new and already developed markets (Chen, Lin & Michel, 2010). In order to more deeply analyze the above-mentioned relationship, internal organizational antecedents and external factors that trigger a firm's competitive behavior and performance should be included (Chen & Miller, 2012). Commonly studied antecedents in the competitive dynamics view are:

- characteristics of the top management team,
- firm's resources,
- working in new or already established markets,
- size and age of the firm,
- results from the previous year,
- market diversification,
- institutional investors,
- industry velocity,
- market growth potential,
- industry concentration and entry barriers, etc.

Competitive dynamics research is grounded in the behavioral characteristics of **the top management team** (Chen Su & Tsai, 2007). Their heterogeneous structure positively affects the level of competitive intensity due to a better perception of different opportunities and threats on the market. Hambrick, Cho & Chen, (1996) found that the top management team's educational background and continuity of work have a positive relationship with the tendency to generate a competitive move, while their different educational backgrounds have a negative consequence on the speed of the competitive move. A heterogeneous top management team can increase the firm's performance using a simple repertoire of competitive moves (Ferrier & Lee, 2002). Ndofor, Sirmon & He (2015) empirically tested the relationship between the upper-echelon theory and firm competitive dynamics. They found that a heterogeneous top management team has a positive relationship between a firm's resources and its competitive intensity. However, they identified a negative relationship between competitive intensity and firm performance. Smith et al. (1991) found that working experience and education have a positive impact on the prediction of competitor's actions (Smith et al., 1991). The top management team's racial diversity and their sexual orientation at all organizational levels are predictors of growing firm performance (Andrevski et al., 2014). They perceive different customers' needs and express it in specific competitive actions on the market. The empirical results presented by Andrevski et al. (2014)

indicate that the top management team's racial diversity indirectly, through competitive intensity, positively influences firm performance. Additionally, they found that racial diversity and sexual orientation have a positive relationship with a firm's performance and this effect is more expressed in racial diversity – performance relationship in an environment of high growth potential. The number of Board members can also impact the level of competitive complexity. Connelly et al. (2016) found a negative relationship between firm performance and the number of Board members, because they are slower in the decision-making process. Small firms are therefore faster in that process, but their decisions can cause far-reaching unfavorable consequences, which is not the case for larger ones.

A firm's age and size are internal antecedents of the firm's competitive behavior and performance indices. Older firms accumulate more resources and have a richer working experience, but they are not always able to generate all required market competitive moves. Ndofor, Sirmon & He (2011) found a negative relationship between a firm's age and the complexity of their competitive actions. Firm size is determined according to the organizational structure, number of employees, turnover, or market position. This antecedent is very important for a firm's strategic behavior. Large and small firms develop different competitive strategies and start from different positions. Large firms use economies of scale, enjoy reputation, brand awareness and working experience; their activities are covered by media and strategic options are mainly triggered by the utilization of their resource base. However, those firms have complex organizational structures and are prone to inert behavior (MacMillan, McCaffrey & Wijk, 1985; Smith et al., 1991). The results of an empirical study conducted by Chen & Hambrick (1995) showed that: a) small firms are more active on the market and generate new competitive moves faster than their large counterparts; however, large firms possess more resources and capabilities and have a reputation on the market that gives them the opportunity to adequately respond to initiated actions, b) small firms react slowly to competitor moves, but they are faster in the implementation process of a certain competitive move due to their flexibility and flattened organizational structure, and c) competitive countermoves done by small firms are more perceived than countermoves by their large opponents.

Resources necessarily play an important role in a firm's competitive dynamics and performance measures. Those firms that possess more resources are more aggressive and more successful (Derfus et al., 2008). Using market commonality and resource similarity, Miller & Chen (1996) provided a basis for integrative competitive behavior. He showed that firms with similar resources are very careful in the intensity of their competitive moves because they are aware of the fast competitive reactions from their opponents. A firm's slack resources can be predictors of the firm's competitive behavior and performance. They represent a firm's resources that are easily activated into new competitive actions (Carnes et al., 2019; Ndofor, Sirmon and He, 2011) and enable a firm to quickly respond to competitor's moves (Smith, Ferrier & Ndofor, 2001; Young, Smith & Grimm, 1996). Carnes et al. (2019) studied the effect of different types of slack resources on competitive aggressiveness and performance indices. They found that available slack, potential slack and recoverable slack positively impact competitive intensity and a firm's performance. Moreover, they found that slack resources have a direct and indirect impact (through competitive aggressiveness) on a firm's performance, while the indirect impact partially mediates among analyzed variables. Ndofor, Sirmon & He (2011) stress the importance of specific resources of a firm that are responsible for market aggressiveness and competitive advantage achievement. Andrevski & Ferrier (2016) found that firms can be successful and aggressive on the market even with few and specialized resources - knowledge about narrowly specialized technology has a positive impact on a firm's competitive behavior on the market. Apart from internally developed resources, firms have access to external resources. Alliances with other firms can positively contribute to competitive aggressiveness on the market and help firms to achieve cost efficiencies via the process of splitting, combining and jointly developing certain resources (Andrevski & Ferrier, 2016).

Results from the previous periods may cause positive and negative effects on the competitive behavior of the firm. Chen, Lin & Michel (2010) found that previous results positively impact a firm's performance, regardless of the firm's size and market situation (new or developed market). The same empirical results were presented by Miller & Chen (1996), Nadkarni, Chen & Chen (2015) and Andrevski & Ferrier (2016). Favorable business results from previous periods may bring firms into the state of inertial behavior (Miller & Chen, 1994). Through time, their top management team becomes dormant and unmotivated to proactively act and look for new market opportunities. Miller & Chen (1996) found a positive relationship between business results from previous periods and the simplicity of their competitive moves in a stable business environment. However, in an uncertain environment they found a negative relationship.

With the **market diversification** antecedent, firms enter into the competitive arena with different customers and competitors. More diversified markets require different knowledge and give the opportunity to offer diversified competitive actions (Chen, Farh & MacMillan, 1993; Miller & Chen, 1994). This competitive environment holds firms awake and properly informed about markets and customers' needs, which is opposed to inert behavior (Miller & Chen, 1996).

Firms set up different competitive strategies in **new and already established markets**. New markets are characterized by high levels of uncertainty, weak knowledge about the customers' needs and a fuzzy market structure (Katila & Shane, 2005), while developed markets have clearly established market rules and well-known market players (Chen, Katila & Piezunka, 2012). Chen (2007) analyzed a firm's competitive intensity in new and already established markets and found stronger firm's competitive intensity in new market segments. However, in already developed markets empirical results show that firms use the strategy of less intensive competitive behavior accompanied with simple competitive moves and slower response time to competitor's attack. Chen, Lin & Michel (2010) analyzed competitive behavior in new and already established markets and found that very successful firms are not equally motivated to engage in aggressive behavior. They choose the strategy to maintain *the status quo* and to be prepared to adequately react to competitive moves initiated by competing firms. Opposed to market leaders and very successful firms, challengers are very active and tend to disturb current market settings and to take over a part of the market segment (Ferrier et al., 1999). In new markets, the above-mentioned firms choose different strategies. Successful firms are very aggressive on new markets and actively invest in R&D, while less successful firms are more careful in the generation of competitive moves (Chen, Lin & Michael, 2010). Chen, Katila and Piezunka (2012) analyzed competitive dynamics in a new and established market, in terms of strategies used by large and small firms on the market. Their empirical results indicate that large firms benefit from competitive moves that require investments in R&D of new products in already established markets, while in new markets they positively impact performance indicators by generating competitive actions that require R&D of existing and new products of the firm. Opposed to large ones, small firms conduct selective strategies and generate competitive moves that are not easily recognized by competitors. Their strategy is focused on R&D activities of existing products responsible for specific competitive moves that will ensure them to pass *below the radar* of their large counterparts (Chen, Katila & Piezunka, 2012). The results of an empirical study conducted by Chen, Katila and Piezunka (2012) found a stronger relationship between competitive activity and firm performance in growing markets than in an already established one.

The **market growth** antecedent signals that even simple competitive moves can generate very good business results. Firms are not preoccupied with the analysis of a competitor's entrance and exit from the market arena and market leaders are those that benefit the most due to their utilization of the accumulated resource base that is reflected in sales growth and market position (Derfus et al, 2008; Chen, Katila & Piezunka, 2012). However, market growth increases a manager's complacency with current business results and, through time, makes them enter into inertial competitive behavior. Through time, this competitive strategy has negative consequences, especially when a firm enters into a period of uncertainty and when overly simple competitive

moves are not sufficient for achieving competitive advantage and firm performance (Miller & Chen, 1996).

Industry velocity is an externally driven antecedent of a firm's competitive behavior which represents the rate of emergence and disappearance of market opportunities (Nadkarni, Chen & Chen, 2015). Firms conduct different competitive strategies in an environment susceptible to constant and unpredictable change and in a stable environment. Nadkarni, Chen & Chen (2015) found that the strategy of competitive aggressiveness has a positive impact on performance and that this relationship is stronger in a high velocity environment.

Institutional investors can dictate the type of strategic options brought by decision makers. Connelly et al. (2016) found that institutional investors have a negative impact on the level of a firm's action complexity, while dedicated investors have a positive impact. Hughes-Morgan, Ferrier & Morgan (2018) analyzed the relationship between long-buyer/short-seller investors and the change in a firm's stock prices. Empirical results indicate that long buyers have a positive impact on the intensity of competitive moves on the market, as well as short sellers. However, if a firm's strategy is overly aggressive, it can cause additional costs and have negative consequences on firm performance. In that situation short sellers will sell their stocks as soon as possible. Hughes-Morgan & Ferrier (2014) showed that a simple competitive repertoire has a positive impact on the level of stock risk because investors can easily, based on their mental maps, process the firm's competitive market moves.

3. Conclusion

Competitive dynamics research analyzes the relationship between the competitive action repertoire and firm performance. Empirical results and theoretical achievements found that firms can benefit from being aggressive and launching a complex set of competitive moves on the market, especially in a hypercompetitive environment where firm performance is short-lived. The above-mentioned relationship requires including internal firm's characteristics, as well as an external competitive environment in order to study more deeply the impact of aggressive and complex firm's competitive behavior on firm's performance. Commonly studied antecedents are top management team characteristics, firm's resources, size and age of the firm, results from the previous year, market diversification, working in a new or already established market, industry velocity, market growth potential, institutional investors, or industry concentration and entry barriers. Competitive action repertoire is seen as a medium between a firm's performance and internal and external antecedents.

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INSTITUTIONAL DISTANCE: CONSTRUCT OF ISOMORPHISM RELEVANT TO MULTINATIONAL COMPANIES

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Abstract
The institutional environment in which multinational companies act is unique and complex. It is unique in the sense that the subsidiaries of multinational companies are facing dual pressures from both the host country and the country of the parent company. Further, the complexity of the environment presumes the need for global integration and the need for the local adaptation. Although some countries are characterized by a more favorable institutional environment for establishing and expanding business, in other countries the institutional environment is a challenge for multinational companies. In this paper, the author will present the current theoretical knowledge and references in already conducted research regarding the institutional distance in the context of multinational companies and its subsidiaries.

Keywords: institutional distance, institutional environment, isomorphism, multinational companies

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1. Introduction

The institutional environment in which multinational companies act is unique and complex. It is unique in the sense that the subsidiaries of multinational companies are facing dual pressures from both the host country and the country of the parent company. The institutional environment from the perspective of multinational companies is complex because of the need for global integration and consistency, also because of the need for the local adaptation (Rosenzweig & Singh, 1991). Adaptation to the local environment of the host country is a necessary prerequisite for achieving legitimacy (Kostova, 1999). Often, these needs for adopting and adapting to the local environment and conditions are contradictory, which is further burdened by the imperative to use best practices in all subsidiary countries in order to easily manage and utilize competencies to achieve efficiency (Taylor, Beechler & Napier, 1996).

Although some countries are characterized by a more favorable institutional environment for establishing and expanding business practices, in other countries the institutional environment is a challenge. Institutional theory theorists suggest that challenges and difficulties from the institutional setting are related to institutional pressures to make companies isomorphic to local conditions and practices to make foreign businesses legitimate (Kostova & Roth, 2002) and on the other hand, the more institutional the distance, the more the transfer of the parent company's business practices to its subsidiaries is difficult.

This review paper will provide insight into the theoretical perspective of institutional distance as a construct inseparable from the operations of multinational enterprises in today's business environment. Additionally, the empirical findings of the conducted research so far in the relevant literature will be presented.

2. Institutional distance: theoretical background

Institutional distance is defined as the relative difference in the quality of institutions of the country of origin and the host country (Gaur & Lu, 2007), and in the conceptualisation of this matter the differences in market, political and social conditions that represent institutional quality are analyzed. The inefficiency or poorly established key institutions in the host country will negatively

affect the operations of the subsidiaries operating under such local conditions. The lack of appropriate market mechanisms for information distribution and the lack of transparency increases the cost of identifying and evaluating a multinational subsidiary as a credible business partner for other players in that market. Furthermore, poorly regulated political and legal institutions limits establishing quality business contracts, potentially leading to an inability to build stable and long-term relationships with local suppliers, which will impede the exchange and distribution of goods and services (Pattnaik, Choe & Singh, 2015).

Institutional distance can also be seen as the extent of institutional differences between the country of origin and the host country. Institutional distance is based on the institutional profile of the state, which consists of three dimensions: regulatory, cognitive and normative (Kostova, 1999). Institutional distance provides an explanation for the organizational behavior of multinational sunsidiaries and monitors the operations of subsidiaries in two key aspects: (1) establishing legitimacy in the host country and (2) transferring strategic orientations and organizational practices from the parent company to foreign subsidiary (Kostova & Zaheer, 1999). Edwards and Kuruvilla (2005) imply that the institutional environment of the host country is complex and idiosyncratic and may be an obstacle to the successful transfer of business practices. Hall and Soskice (2001) focused on identifying specific attributes of the institutional setting at the country level, and used the results to explain variations in inter-institutional organizational behaviors and the degree of differences between institutional environments across countries. Kostova (1999) finally systematized the institutional differences that multinational companies face as institutional distance; the greater the difference between the institutional environment of the host country and the country of origin, the more severe are the difficulties in transferring and establishing organizational business.

Institutional infrastructure is often subject to layering processes (Mahoney & Thelen, 2010), that is, new institutions are added to existing previous institutions and can be potentially revived or used for new purposes. This conclusion offered a perspective on how institutional environments are characterized by a multitude of different institutional logics and interpretations of the environment (Thornton & Ocasio, 2008). When these logics coincide or are ambiguous they can create multinational enterprises a strategic opportunity and a solution for overcoming distances, creating patterns of behavior that have hitherto deviated from the host country's standard business practices (Jackson, 2010).

The resources offered by the institutional context of the host country provide MNCs with the opportunity to use, reinterpret, or adapt behavior to overcome institutional distance and to shape behavior acceptable in the host country. However, over-availability of resources can adversely affect the overcoming of institutional distance precisely because of institutional complexity and the “pluralistic institutional environment” of which Micelotta and associates (2017) wrote, concluding that institutional plurality makes it difficult to assimilate and engage in institutional change.

The formal regulatory component of institutional distance influences the increase in the cost of learning the "rules of the game" in international business and the new environment. Multinational subsidiaries face a liability of foreigness that is likely to act as a source of competitive disadvantage for a multinational enterprise (Eden & Miller, 2006). Although the tendency in some industries is to standardize business practices to reduce the effect of institutional differences across countries (Larsen & Manning, 2015), institutional distance influences important strategic decisions such as business expansion locations (Schwens et al., 2011), ownership issues (Eden and Miller, 2004), and the analysis of business performance of foreign affiliates (Gaur & Lu, 2007).

Gaur and Lu (2007) argue that while there are potentially negative effects on a subsidiary operating in a country with different regulatory institutions, remote regulatory environments provide opportunities for institutional arbitrage. For example, in the United States, many multinational

companies with originally weak regulatory contexts in the country of origin set up R&D centers to benefit from well-placed intellectual property protection contracts. However, in cases of perceived high levels of institutional distance, Gaur and Lu (2007) argue that the scope of such arbitrage becomes narrower, resulting in a decrease in competitive advantage. As regulatory institutional distance increases, subsidiaries face an institutional distance where they cannot find an adequate solution and where relational dangers are too high and ultimately adversely affect the performance of the subsidiary.

Differences in formal institutions, such as laws and regulations, and the implementatin, as well as differences in informal institutions such as norms and cognitions that result from cultural differences (Peng et al., 2009) affect the organizational behavior of multinational subsidiaries. Institutional theory assumes that "regulatory" differences between countries will increase the "foreigner" characteristics of subsidiary and increase the cost of learning the "rules of the game" (North, 1991). Differences also arise from the different types and characteristics of business systems between countries that affect the way capital and labor are organized and controlled, managed by economic exchanges and competing interests, and state policies affect economic activities, the financial system and education systems.

3. Overview of the most significant research

Recent empirical research has conceptualized institutional distance as a multidimensional construct given the complexity of the institutional environment (Fortwenge, 2016). Researchers have shifted their interest towards defining the dimensions and attributes of the institutional environment that are critical to international business and the behavior of MNCs. Countries differ in the way companies coordinate business activities, and institutions vary in strength, so institutional pressures also appear at different intensities. Furthermore, institutions are different globally and internationally; even geographically close countries often have significantly different institutional environments. The latter is increasingly approached to understand the institutional environment as one that offers a particular source of resources for strategic opportunities and is no longer seen solely as a limiting factor (Dörrenbācher & Geppert, 2017).

The degree of institutional distance is usually calculated by summing the specific values of the cognitive, normative and regulatory dimensions that represent a particular institutional environment (Kostova, 1999): the greater the distance between the two countries, the greater and negative is the effect of the distance (Kostova & Roth, 2002). This perspective of institutional distance has proved significant as it explains the burning problems of international business such as why MNCs have difficulty transferring business practices to subsidiaries (Kostova & Roth, 2002), but does not provide explanation for how and why institutional distance between the two countries is so significant for transfer of practices.

Jackson and Deeg (2008) conclude that institutional distance also affects the difference in terms of coordinating business activities in a particular institutional setting. Ahmadjian (2016) points out that the specifics of countries are characterized by a certain societal logic. Institutional distance is often shown only as the difference between the institutional infrastructures of the two countries. What this perspective lacks is a reflection on how institutions can weaken or more severely restrict organizational behavior, and that institutionalization must necessarily be scaled; the varying degrees of power of institutions differently affect the behavior of international subsidiary, so context is very important to observe (Faulconbridge & Muzio, 2015).

The Shirodkar and Konara (2017) study comprehensively analyzes the impact of formal institutional distance on the performance of multinational subsidiaries, and is driven by the increasing development and increasing influence that primarily formal institutions have on the institutional distance and multinational affiliate performance. The subsidiary's performance, as the dependent variable, was measured by the return on equity (ROE). The latent variable, formal institutional distance between the host country of the subsidiary and the parent company, was

measured by the Dow index, the Kaufmann index, the Hoth index and the indices proposed by the International Country Risk Guide. Ownership was measured using dummy variables that take a value of 1 in case of wholly-owned subsidiary (i.e. 100% ownership) and 0 if the company is partially foreign-owned with at least a 10% interest. Experience in the host country was measured in years that subsidiary was present in the countries observed.

In the first hypothesis, they propose that greater formal institutional distance will negatively affect the performance of subsidiaries of MNCs in emerging markets. The hypothesis was accepted by results from 17 different countries showing that formal institutional distance was significantly negatively correlated with the performance of subsidiaries operating in Central and Eastern Europe. They conclude that new markets create an environment where differences between the regulatory framework of the host country and the country of origin sublimate the characteristics of the foreigner. The results also confirm that new markets represent a unique context in which potential opportunities are arising from differences in institutions, as some authors have argued, are not directly linked to achieving competitive advantage.

The second hypothesis assumes that the negative effect of the formal institutional distance on subsidiary performance may be partially mitigated by a partial subsidiary ownership. They conclude that the negative effect of formal institutional distance on subsidiary performance is stronger for wholly-owned subsidiaries, whereas for partially domestic-owned subsidiaries, this effect is not statistically significant, leading to diametrically opposite conclusions from those studies that use a (too) general context (exploring only one country of origin: Japan) and argued that the full ownership option improved the survival rate of subsidiaries in an institutionally distant context (Gaur & Lu, 2007).

Third hypothesis assumes that the negative effect of formal institutional distance can be mitigated with greater experience of the subsidiary in the host country, and the results supported the hypothesis. Institutional distance has a strong negative impact on the activity of new subsidiaries in the market, and this negative effect diminishes over time and with the longer presence of the subsidiary in the new environment. Although previous studies have theorized that experience decreases with liability of foreigness, these authors were the first to empirically prove it. This is confirmed and elaborated that with greater experience and knowledge acquired by the subsidiaries they would be perceived as legitimate and would incorporate into the social and political contexts of the host countries, which will ultimately have a positive impact on the affiliates' business performance.

Salomon and Wu (2012) argue that foreign companies from institutionally distant countries use experience to learn more about the institutional environment of the host country and, as a result, do not need to rely on imitation of the firm's domestic strategies in order to reduce foreigner characteristics; specifically they are interested in how two forms of experience, domestic competition and parent company experience, shape the impact of institutional distance on local isomorphism, and select U.S. bank branches from 1978 to 2006 as a sample.

The US banking industry is highly regulated and banks are facing strong pressures to adapt to the institutional environment (Miller & Eden, 2006). Banks are not only influenced by regulatory component of the environment, but they must also be keenly aware of the fact that legitimacy has been attained, so authors Salomon and Wu conclude that this industry offers an appropriate environment for studying isomorphic foreign enterprise strategies. In particular, they argue that foreign firms from institutionally distant countries are more likely to adopt a local isomorphism strategy in order to gain legitimacy and mitigate the liability of foreigness, and the authors apply a multidimensional approach since previous research has focused on looking at only one dimension and its impact on organizational behavior.

They use an isomorphic local strategy as a dependent variable which they measure as similarity between the asset portfolios of a foreign bank and a domestic US bank on an annual basis.

Measurements of banks' asset portfolios are categorized by Miller and Eden (2006) based on their distribution into eight categories: commercial loans, real estate loans, consumer credit, other loans and leases, cash, overnight loans, securities and fixed assets. They set the institutional distance as an independent variable and apply a multidimensional measurement approach. Institutional distance is measured through: cultural distance using Hofstede's dimensions of culture; they measured the economic distance by financial market orientation using the ratio of market capitalization to GDP divided by the ratio of bank loans to the private sector and GDP; regulatory distance is measured through bank regulations, banking regulations, competition rules and capital rules, and the authors set their own measure of regulatory distance; they measured political distance as the absolute value of the CHECKS index, which captures the total level of political volatility within the country and measures the number of veto participants, assuming that more veto players will mean more rigorous verifications and controls, which will also affect predictability political environment between the country of origin of the foreign bank and the United States. To measure the ability of foreign bank subsidiaries to gain experience by learning from their home country competitors, the authors create a measure that captures the experience of banks from the same homeland based on the time of competitors' presence in the observed statistical area; they defined competition experience as "the cumulative years of experience that banks from the same homeland have in the same statistical area at time t". Since a bank may open banking institutes before establishing a branch, it is possible that experience prior to establishing a branch may help in opening the first branch. In addition, as the measure of the firm's own business experience varies over time, it covers additional banking institutions established by the bank after opening a branch, since a bank with more institutes can use its understanding of the local market to change its business strategy.

The authors hypothesize that the difficulties of doing business in the host country are likely to increase with the institutional distance between the host and the country of origin, and as a result, are more likely to opt for local isomorphism as a mitigating strategy to gain legitimacy. In line with this hypothesis, they conclude that the foreign bank strategy adopted is similar to that of local US banks, as cultural, economic and regulatory distances between the country of origin and specifically the United States of America increase. But they cannot conclude the same for a measure of political distance, citing as a possible reason that foreign firms do not use local isomorphism to mitigate the influence of political distance. Nevertheless, the results generally support the assumption that institutional distance influences the chosen business strategy of foreign firms. They further hypothesize that applying the experience of foreign firms from institutionally distant countries (domestic competitors and their own enterprise operations) will benefit more than those firms of institutionally similar countries that enjoy the privilege of less reliance on isomorphic local strategies. Empirical results neither systematically supported these hypotheses, nor that the experience of institutionally distant countries would direct or influence local isomorphism.

This suggests that the strategies used by foreign companies are relatively sustainable and resilient; in the long run, institutional distance influences strategic commitment given that companies are faced with initial strategic commitments that must be fulfilled. However, it has been empirically confirmed that the experience of owning a business has an impact on cultural distance, implying that companies can blend in with the local cultural environment, as accumulating experience and increasing understanding of the local environment provides some breadth in strategy selection.

The research of Solomon and Wu (2012) is a multiple contributor to the institutional literature: the research proves that there is significant heterogeneity in isomorphic strategies, and the results suggest that local isomorphism strategies do not suit all firms equally; foreign companies from more remote institutional environments will find it useful to imitate local competitors. Furthermore, this research examines the impact of institutional distance on the specific operational decisions that companies make in the host country; research to date has examined the impact of institutional distance on site selection or market entry strategy, however, this is the first study to

directly contrast institutional distance and local institutional isomorphism. Finally, with this research, institutional distance was analyzed as a multidimensional construct, while the research to date has largely examined one dimension: the cultural, economic or political dimension separately.

Finally, the results of this research suggest that institutional distance influences the final choice of a foreign firms' strategy and that in the future, institutional distance should be viewed as a multidimensional construct. More precisely, research indicates that while a local isomorphism strategy may help firms (especially managers) from institutionally distant countries to quickly establish legitimacy, managers must be aware that such a commitment potentially imposes a specific strategic direction on future business, since adopting a local isomorphism strategy in the short term may limit the ability enterprises in further progress.

4. Conclusion

Looking at multinational companies from an organizational structure perspective, management is a complex task. Geographic distribution contributes to difficult coordination. Since multinational companies operate in at least two markets, they must comply with each of the regulatory requirements, legal frameworks, and each country's legal system is unique and specific. Geographical distribution implies a significant difference in legal systems and non-market institutions. The structures and practices of corporate governance can therefore vary considerably. The complexity of the international environment is also compounded by the fact that the international legal relationship is not clearly defined especially in the segments of jurisdiction, extraterritoriality, protection of intellectual property and in the segment of bribery and corruption.

Institutional distance is a key concept in international business and research since it can be argued that international management is indeed distance management. The interest in institutional distance does not diminish despite sensitization and a stronger interest in managing sociocultural differences, which undoubtedly means that distance will continue to be an important construct when managing and studying multinational affiliates.

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THE IMPORTANCE OF CONTEXT IN ORGANISATIONAL COMMUNICATION

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Abstract
Traditional models of communication comprise the well-known elements such as: sender, receiver, message, code, channel, feedback. However, the study of organisational communication shows that another element is of equal importance and that is the context. The communication context may be defined as the environment for communication interaction which includes not only the specific time and place of the interaction, but also the roles, relationships and status of the communication participants. Having as starting point Pamela.Shockley- Zalabak's research in the field of organisational communication, the purpose of this paper is to show the importance of context in organisational communication and the relationship between the organizational context and the communication context. Is the communication context always shaped by the organizational context in professional interaction? Is communication able to shape or alter the organizational context in any way? Where do mentalities and culture collide with the organizational context creating more difficult circumstances for professional communication? Answers to these questions are sought for in this paper which will comprise a theoretical approach followed by a more practical one in which we are going to analyse the context implications in the professional communication within a department from a public institution in our country.

Keywords: *communication, context, competency, experience, sensitivity, team*

Track: *Management & Leadership*

Word count: *5.126*

1. Introduction

The word communication originates in the Latin verb "communicare" which meant to share and the Latin nouns "munus" which meant public duty, task and "munis" which meant "the one who does his duty". This origin shows clearly that the term has always referred to the idea of sharing, being open, show goodwill towards the others. At the same time, it can also be seen as "a duty" because we communicate all the time in one form or another and we have an obligation to share information and to communicate well especially in the professional environment.

Communication has various definitions. It can be defined as the process through which information is exchanged and understood by two or more people, usually with the purpose of motivating or influencing behaviour. Communication does not mean only transmitting information, but also sharing it. It means to speak but also to listen and to provide feedback. Effective communication is, according to an expert in the field, "When two people interact, they put themselves in the other one's shoes, they try to perceive the world as the other one does, they try to predict how the other one will answer. This interaction means taking roles and using emphatic skills. The purpose of the interaction is a kind of merger between one's self and the other, a complete ability to anticipate, to predict and to behave according to the other's personal needs." (Daft, 2006: 489). This definition can also be applied to the field of managerial and organizational communication.

2. The communication process

In any communication situation there are two key elements: the sender and the receiver. The sender is the one who wishes to transmit an idea or a concept to the others, to look for information or express a feeling or a thought. This is done by sending a codified message to the receiver, which implies that the code should be common so that both parties should understand the message. The message is sent through a communication channel which can be face to face, by phone or in writing. The receiver decodes the message and he will send a feedback to the sender under the form of a reply message. Without a feedback, the communication process is incomplete and ineffective. The feedback ensures the effectiveness of communication because it allows the sender to realize whether the receiver has understood the message or not. Errors may occur because of faulty coding or decoding of the message or because of external factors such as noise, disturbing factors of various kinds or bad choice about the transmission channel.

Linguistically speaking, the effectiveness of communication is given by the correct understanding of the message and the existence of suitable feedback. The communication process also involves psychological and behavioural aspects. Communication implies openness to interaction and a genuine desire to communicate from all the parties involved. Refusal or aversion leads to the failure of the communication act.

Given the complexity of the process and its importance in a variety of fields, business included, there have been a lot of theories and models of communication since early times up to now. The history of communication is closely connected to human evolution and to the development of social and economic relations as well as of technology and science. All ages in history showed concern for communication since Adam Smith (1723-1790) first mentioned the idea that communication contributes to the organization of collective work in factories and to the structuring of economic spaces. In time, empirism and pragmatism, Laswell, Shannon and Weaver, Saussure, Jakobson elaborated famous models as a basis for more advanced approaches such as the systemic trend, the Palo Alto School, or the linguistic-pragmatic theories.

As our focus is organizational communication, we are going to refer next to the study of this field and the theories and models which have been elaborated in time by specialists in the area.

2.1 The study of organizational communication

A compilation of articles entitled *The Articulate Executive* (which appeared in Harvard Business Review) tried to comprehend exhaustively all the types and characteristics of communication at organizational level: formal and informal communication, internal communication practices (presentations, briefings, meetings, interviews etc.), public-oriented communication (external communication). They also considered in-house training, conflict management, intercultural issues, communication technologies.

Organizational communication has suffered (as process and characteristics) a lot of changes in time. Before 1920, communication in small organizations was mostly formal. As the size of companies increased, the main concern became downward communication. Nowadays, communication in organizations has become not only complex and varied, but also extremely important for the functioning and the success of the organization.

Historically speaking, we can say that communication has always been among the research interests of thinkers in the field of management or economics in general. For Taylor, hierarchical communication was very important whereas for Fayol horizontal communication played an essential part. For the representatives of the human resources and relations trends (Mayo, McGregor, Likert) the most important relations are those of communication inside the group. Modern theories have brought an integrative perspective in the study of communication which is extended at the level of the whole organization. Newer orientations suggest alternatives based on flexibility and self-management. The development of the theories and ideas about organizational communication is greatly influenced by the technological progress and by globalization. The new

information technologies have changed the way communication works at all organizational levels and research is clearly focussed on this area at the moment.

A comprehensive study considers that approaches to organizational communication can be divided into two major trends. The first one regards communication as an independent element in an organization and it was illustrated by Drenth (1998) who defined communication as sending and receiving messages through means and symbols and sees communication as a key element of the organizational climate. The second trend sees communication as the basis of an organization and it was reflected by Myers&Myers (1982: xv) who defined organizational communication as a unifying central force which allows coordination among people and leads to organized behaviour. The same opinion is shared by Rogers&Rogers (1976:3) who considered that "the individuals' behaviour in organizations is best understood from the point of view of communication."(quoted in Baker, 2002:3)

2.2 Theoretical perspectives

Specialists consider that there are three major theoretical perspectives in the study of communication: the technical perspective, the contextual perspective and the negotiated perspectives.

The technical perspective is associated with the information theory elaborated by Claude Shannon and Warren Weaver (1949). Their model shows that a message, elaborated by a source, is coded by a sender under the form of signals which follow a channel, where it may be subject to distortion, reaching the receiver who decodes the message and sends back a feedback.

The contextual perspective does not focus only on the content, but also on the broad context of communication. Words are seen as symbols interpreted in a context. Mead (1934) and Blumer (1972) see communication as symbolical interaction which creates meaning for itself and for the society. Discourse analysis is an extension of the contextual perspective. This theory is important for organizational communication because it shows how, through its own discourse, an organization marks its own limits. Discourse creates collective representations, as it is both interpersonal and collective, subjective and contextual.

The third approach (negotiated perspectives) belongs to Lazega (1992). He examines how the communication context is negotiated, how we build adequacy and knowledge standards for example. He elaborated a model based on the interactive feedback from the technical approach, showing that the feedback exchange can be seen as an interpersonal negotiation process.

In the 1980's there was a shift in the field of organizational communication research, as researchers began to study more and more the dynamics of the relations between the communication processes and the human organization systems. The study of communication tends to explore more the construction of the meaning between the participants to the organizational act who influence each other in the context of power relationships. Language is not only a representation of reality, it is part of reality. Deetz (2001, quoted in Hargie&Tourish, 2009) believes that organizations should be looked upon as complex discourse formations in which discourse practices exist in the organization, but they also "produce" organizations. In other words, communication reflects the relationships between the members of the organization, but it also creates them, forms them and explains them to those involved in a more or less successful way.

Communication is clearly the key to organizational excellence. But which is the key to communication? The most frequent answer is communication skills/competencies. They have been defined and explained in a variety of ways.

The majority of models and interpretations found full expression in the organizational communication model proposed in 2002 by Pamela Shockley-Zalabak. She keeps the basic elements of communication (sender, receiver, message, channel, noise), its processes (coding,

decoding, feedback) and adds interaction of the experience fields which are specific to the sender and the receiver, the organizational context of communication and the communication competencies. She considers four such competencies: the knowledge competency (the ability to understand the organizational communicational environment), the sensitivity competency (the ability to sense correctly the meanings and the feelings of the other members of the organization), the skills competency (the ability to analyse organizational situations correctly and to initiate the organizational messages correctly), the values competency (the ability to take responsibility for effective communication).

2.3 The communication competency and the importance of context

As early as 1938, Chester Barnard in his work *The Functions of the Executive,* described as a primary responsibility of executives the development and maintenance of a system of communication. Research, since then, "has linked organizational communication to managerial effectiveness, the integration of unit works across organizational levels, characteristics of effective supervision, job and communication satisfaction, innovation, adaptability, creativity, and overall organizational effectiveness and performance. " (Zalabak, 2015:5). According to the same author, we are in a postindustrial information society moving to a conceptual age and as Daniel Pink (2005, quoted in Zalabak, 2015) describes this shift: "the future belongs to a very different kind of person with a very different kind of mind –creators and empathizers, pattern recognizers, and meaning makers. These people –artists, inventors, designers, storytellers, caregivers, consolers, big picture thinkers- will now reap society's richest rewards and share its greatest joys". (p.1) This means that organizations will need competent communicators at all organizational levels.

It is widely recognized that in this complex and information-rich society the key to organizational excellence is communication excellence which, according to P. Shockely-Zalabak "stems from the dedicated commitment of people, people who are motivated to work together and who share similar values and visions about the results of their efforts." (Zalabak, 2015:5). So, how do we achieve communication excellence? How do we determine if we are competent organizational communicators?

The same researcher considers that communication competency is composed of knowledge, sensitivity, skills and values and it arises from interaction of theory, practice and analysis. Other researchers, such as Fred Jablin and Patricia Sias (2001) created an ecological model that revolves around four systems:

- "the microsystem, which contains the developing organizational member and other persons from the immediate work environment;
- the mesosystem, which represents the interrelations among various microsystems (for example, what individual learn in project teams may affect their competence in a functional work group)
- the macrosystem, which does not represent the immediate context in which an individual works, but does impinge on him or her
- the exosystem, which represents the overarching, cultural belief system, forms of knowledge, social, technological and political ideologies" (Jablin&Sias, 2001: 836-837)

Sherry Moreale (2009) suggests a linkage between communication competence and ethics. Stephen Littlejohn and David Jabusch (1982) consider that communication competency is "the ability and willingness of an individual to participate responsibly in a transaction in such a way as to maximize the outcomes of shared meanings" (quoted in Zalabak, 2015:6). This shows that when thinking about our communication competency, we form impressions of our own competency while making evaluations about the competency of others. Littlejohn and Jabusch's approach represents the basis for Pamela Shockely-Zalabak's model as they built communication competency on four basic components: process understanding, interpersonal sensitivity, communication skills and ethical responsibility. Hence from we return to the competency-based

approach to organizational communication mentioned before which is formed of: knowledge, sensitivity, skills and values.

Knowledge competency represents the ability to understand the organizational communication environment and it develops through the exploration of the interactive process nature of human communication. Sensitivity competency is the ability to sense organizational meanings and feelings accurately and it is related to our ability and willingness to understand what others feel and do. Skills competency is the ability to analyse organizational situations accurately and to initiate and consume organizational messages effectively and it develops through analysis and practice opportunities. Values competency represents the importance of taking responsibility for effective communication, thereby contributing to organizational excellence.

In addition to the communication competency, Pamela Shockely-Zalabak's model of organizational communication includes two more elements besides the traditional ones (sender, receiver, message, channel, code, noise): field of experience and context. The field of experience is "a set of specific experiences or background that all parties in communication bring to bear on the interaction. Generally, it is believed that the more common the field of experience among those communicating, the easier it is to share similar meanings or to construct shared realities." (Zalabak, 2015:13). What we do and what we say in a particular situation depends a lot on how much we know about it from our experience. When we are exposed to new things, we may react very differently compared to situations which we encountered in the past.

"Communication context is the environment for the communication interaction. Context includes not only the specific time and place of the interaction but also the roles, relationships and status of communication participants. As such, prior interactions between participants contribute to the construction of the current communication context. […] We can therefore say that context is both culturally and physically influenced and as with other elements in the communication process, perception of context can differ from one communication participant to another." (Zalabak, 2015:14).

3. Case study: fields of experience and context in the case of a particular department

The following analysis refers to department from a public institution which is formed of 18 people and which has been undergoing changes which led to the conclusion that they have serious communication issues.

Background: the department in question was led by an autocratic manager for more than 20 years. This manager did not cultivate teamwork or encouraged open communication between management and members. Whoever had a personal opinion the head did not like had to suffer consequences. Many people left the department and the others did their jobs fearing the manager all the time. Given the fact it was a public institution, almost nothing could be done given the fact that the head of department had very close connections with the top management of the institution. Although this situation might seem awkward, let us take into account that we are talking about a public institution and not a private company in a former communist country where democracy does not have a long tradition.

This management style has left its footprint on the actions and behaviours of all the members of this department, whether older or younger. Practically, this management style shaped their **field of experience** because the majority of them had never experienced something different. Although they had read about management practices, nobody could imagine a different situation at the time. Basically, in their overall communication competency, **the knowledge competency** about management and communication between members of a team was strictly limited to theoretical stuff whereas their field of experience was represented only by the autocratic management style, no teamwork, competition between colleagues and fake relationships dictated by the rules imposed by the head of department.

What do we mean by fake relationship? The other departments of that public institution had the impression that everybody was happy in that particular department because nobody heard of conflicts, complaints or other kinds of misunderstandings. However, the situation was totally opposite. The majority of the members of the department were unhappy or indifferent except a few who were the boss's "favourites" and had certain privileges. The latter ones were always the "good ones" who agreed with the boss and put her decisions in practice. There were no conflicts and no complaints because nobody dared complaining or even having a dispute with a colleague. The worst which could happen was one of the "favourites" complaining to the boss about another colleague and the boss taking measures against that person. In this way, we can notice that also **the sensitivity competency** was affected because starting with the head of department, nobody really cared about what others really felt, everything was filtered through the boss's attitude towards that person and what somebody felt in reality had to stay inside that person, otherwise their behaviour would have been considered inappropriate.

Let us look at an example about how the management style influenced the sensitivity competence of the members in the department in question. At some point, two new colleagues were hired, theoretically for a limited period of time (4 years) with the strong promise that it was just a formality and their contract would be extended. However, when the deadline came, the promise did not come true and the two colleagues were made redundant although they had had good results and there was enough work for everybody. One of them consulted again the employment documents and discovered that actually her work contract was for an unlimited period of time, so she sued the institution in order to get her job back. She won and returned to work. However, the head of department was angry and reprimanded other people in the department who were close to the colleague in question. She reproached them that they had recommended that person for the job and that they knew she would sue, but said nothing (although nobody knew about it). Consequently, when she returned to work she was accused by her colleagues of disloyalty and of harming them and the image of the department/institution. Thus a conflict appeared and has continued ever since. Nobody took into account the other person's position and motivation for fighting for her job. Their sensitivity competency became so limited by the boss's perception that they could not understand that a mother of 4 children in her 40's, with limited employment possibilities, would have the right to fight for her job and to find ways to get it back.

It is necessary to mention that all these examples and information were collected by direct observation and discussion with members of the department. It can be seen how the management style affected the employees' communication competency and their field of experience. What about the context?

Organizational context has been defined in different ways; mainly it is about the characteristics of the organization including the firm's size, degree of centralization, degree of formalization and managerial structure. We can say that communication in a company is mainly shaped by the organizational context as communication systems differ between large and small companies and so does the degree of formalization. If we consider the context in a department, this is clearly dependant on the broader organizational context at a smaller scale. Communication could be more direct and informal between the members of a department compared to the whole formal structure of the company. Clearly the way people communicate in the professional environment is influenced by the organizational context.

Next we are going to analyse communication in this group after a management change occurred. The autocratic manager retired and she was replaced by a younger member of the department who had a different approach, but at the same time, was not really prepared for her new position. At the beginning of her activity she was still guided by the former management whose advice she was seeking. However, this advice came in conflict with the views of the top management of the institution so she decided to stop asking for advice.

On the other hand people's expectations from the new head of department were unrealistically high. They wanted a total change and wanted it to happen immediately; this shows how much their knowledge competency was affected by the previous management style as they could not understand such changes would take a long time. As their sensitivity competency had also been affected, they showed no empathy towards their new boss regarding her lack of experience and started criticising her for the smallest mistake. Here comes another element: their field of experience. As they had been used only to an autocratic management style, they were suspicious of every action the new manager performed and interpreted many things in the wrong way believing that all her actions were still influenced by the former manager's advice.

Communication between the members of the department also changed; again, the fact that their knowledge and sensitivity competencies had been affected, made them adopt inappropriate communication styles. Everything they couldn't say in the previous years, all their frustrations and resentments towards others, all the fake behaviours turned into an aggressive way of communication which sometimes exceeded the boundaries of politeness and common sense. People started quarrelling during meetings, even shouting at each other, some left the meetings in tears and conflicts seemed to exist everywhere. Some were between department members, however the majority were between the new head of department and members. Unfortunately, she seemed unable to deal with the situation in a proper way.

3.1 Suggestions for improving communication in the department

An important step in solving the communication issues in this department is to identify all the issues. This should be done through a communication audit conducted by an external party e.g. a consultant or a consultancy company. The audit should use quantitative and qualitative methods which would reveal all the problems people are confronted with. A questionnaire would be recommended plus focus groups or individual interviews. Once the problems are identified, the auditor should come with recommendations. Such recommendations might be trainings and team building to create a sense of community and develop team spirit or other specific actions.

However what is clear just from observation and discussions is that the members' field of experience influences their current behaviour and communication style and in addition to that, their sensitivity and knowledge competencies have been affected and they need to regain these competencies in order to recreate their overall communication competency.

How can one regain these competencies? We thought that one possible solution is the practise of nonviolent communication, an approach developed by Professor Marshall Rosenberg in the 1960's.

What is nonviolent communication? It is "a way of communicating that leads us to give from the heart. NVC is founded on language and communication skills which strengthen our ability to remain human, even under trying circumstances. NVC guides us in reframing how we express ourselves and hear others" (Rosenberg, 2003:5) Even from the definition we can clearly see that this approach is about compassion and empathy and this is what can help people regain their sensitivity competency in order to become better communication both in their professional and personal lives.

How does the process work? It has four stages: observation, feelings, needs, request. "First, we observe what is actually happening in a situation: what are we observing others saying or doing that is either enriching or not enriching our life? The trick is to be able to articulate this observation without introducing any judgment or evaluation – to simply say what people are doing that we either like or don't like. Next, we state how we feel when we observe this action: are we hurt, scared, joyful, amused, irritated etc? And thirdly, we say what needs of ours are connected to the

feelings we have identified. An awareness of these three components is present when we use NVC to clearly and honestly express how we are." (Rosenberg, 2003 : 6)

We consider that input into nonviolent communication techniques would greatly help the members of this department regain their sensitivity competency and be able to communicate without being influenced to such a great extent by their field of experience. The least they could do would be to read Rosenberg's book, but also bringing in a trainer specialized in NVC to hold a workshop would certainly improve the situation.

If the members of the department applied the principles of nonviolent communication, they would be able to regain their sensitivity competency and be less influenced by their field of experience. For example, when the head of department asks someone to do something, they should just observe first, without making a judgment such as "She is acting like the old boss". They could also clarify their feelings: "when she tells me to do things using this tone, I feel she is ordering me around in the same way the former boss did and nothing is changed. I feel irritated and confused" Then, an honest expression of needs should be recognized for example "I need more respect". Finally a polite request should be expressed to the superior. The employee might say: "I need you to express your demands in a more polite way and on a lower voice".

This is just an imaginary scenario. Such exchanges can take place between the manager and the subordinates or between colleagues. The practice of these techniques will definitely make a difference between the way people are communicating now and how they should communicate in a professional environment.

4. Conclusions

A common mistake many people make is to forget about the context of their communication acts. The organizational context shapes the communication context; one cannot but consider the professional context as the background for their interaction. Once you behave as if you were in a personal context, the quality of your professional communication decreases.

Developing the communication competency among professionals is essential for their activity and the well-being of the company. When one of the parts of the communication competency is affected or missing the entire ability is damaged.

We have also seen the great influence the management style has on the communication competency. As Peter Drucker used to say: "Culture eats strategy for breakfast". You may be a new manager with a new vision and you want to change things in your department or in your company. However, one of the great enemies will be your people's field of experience. It is difficult to fight with the past and to change mentalities and habits. It is a long-term process and the key to success is not changing one's experience (which is impossible) but changing perspective through effective communication. You, as a manager, you may not be the best communicator, but you can bring in specialists and learn together with your colleagues. The development of the communication competency will help people work better and connect better. And, we dare say, the sensitivity competency is the most important side of the overall communication competency. It is the one which reminds us to remain human at all times, no matter the context. This is actually the competency which is not context-bound. Showing empathy, putting yourself into the other one's shoes are essential elements of successful communication in all life contexts, not just in the professional context. And so is the case with the use of nonviolent communication techniques: not judging and being responsible for one's feelings in order to understand what you really need and to express your request in the correct way will improve communication in all contexts.

The same ideas are expressed more poetically in the lyrics of a song M. Rosenberg quotes in his book:

"I feel so sentenced by your words

I feel so judged and sent away

Before I go I've got to know

Is that what you mean to say?

Words are windows, or they're walls,

They sentence us or set us free,

When I speak and when I hear,

Let the love light shine through me."

Ruth Bebermeyer

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INCREASING (VOLUN)TOURISM THROUGH SOCIAL ENTREPRENEURSHIP – THE CASE OF CROATIA

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Abstract

Social entrepreneurship is a relatively new topic of interest within the academic and the literature on it is limited. With the increase of interest in recent years from various interest groups the concept of social enterprise has become much more widespread. The purpose of this paper is to explore the link between social entrepreneurship and voluntourism, as one of the types of special interest tourism, and to examine the Croatian context in this regard. Voluntourism is a combination of volunteering and tourism. Unlike the rest of the European market, the Croatian development of voluntourism is still at the beginning. Voluntourism, according to the concept of sustainable community development, relate all the stakeholders of such development. Moreover, social entrepreneurship focusing on the creation of innovative products and procedures that would benefit the entire local community could become an important vehicle for sustainable development of destinations.

This paper proposes that niche tourism products and more specifically, voluntourism projects, under the prism of social entrepreneurship, can become the means towards Croatian product diversification and long-term environmental, social and economic sustainability. Quantitative research was conducted and the methodology entails a case study approach that includes a thorough review of the related literature and of any existing Croatian sources of social entrepreneurship in voluntourism projects to determine the state of the Croatian industry in this regard. Results indicate that there are limited number of projects concerning social entrepreneurship in voluntourism in Croatia and also that discussed projects are not recognized or there is a lack of awareness of them. This study assessed the situation in Croatia and although it was comprehensive under conditions of limited data availability, it cannot speak to social entrepreneurship in voluntourism globally, but it can offer foundation for future research in this area.

Keywords: *case of Croatia, sustainability, social entrepreneurship, voluntourism*

Track: *Entrepreneurship*

Word count: *6.039*

1. Introduction

Social entrepreneurship incorporates innovative thinking and creative conceptualization to spread improvements in a social context, in contrast to individual entrepreneurship. Still, it is a relatively new topic of interest within the academic and the literature on it is limited. This paper tries to explain the relationship between social entrepreneurship and voluntourism, as one of the types of special interest tourism, and their mutual impact on sustainable community development. This is accomplished through a critical analysis of the literature on social entrepreneurship in order to understand the possible link with voluntourism and community development and also to examine the Croatian context in this matter.

In other words, this paper proposes that niche tourism products and more specifically, voluntourism projects, under the prism of social entrepreneurship, can become the means towards

Croatian product diversification and long-term environmental, social and economic sustainability. Quantitative research was conducted and the methodology entails a case study approach that includes a thorough review of the related literature and of any existing Croatian sources of social entrepreneurship in voluntourism projects to determine the state of the Croatian industry in this regard. To illustrate how social entrepreneurship along with voluntourism practice can encourage sustainable development of local community, a conceptual framework integrating the mentioned concepts is proposed.

2. Social entrepreneurship and social entrepreneur

During the last fifteen years, there is a growing acknowledgement of social entrepreneurship, and social enterprises in particular, on a local, national and international level, in comparison to previous decades where the concepts were less discussed (Defourny and Nyssens, 2010). According to research presented by Weerawardena and Mort (2006) there is a plethora of definitions and interpretations around the term social entrepreneurship. Some authors speculate that social entrepreneurship is only an idea of solving social problems using business methods (Peredo and McLean, 2006; Austin et al., 2006), while others believe that social entrepreneurship is just a nonprofit activity (Williams and K'nife, 2012). Dacin et al. (2010) counted 37 definitions of social entrepreneurship or social entrepreneurs, while Bacq and Janssen (2011) noted 17 different definitions of "social entrepreneurs", 12 definitions of "social entrepreneurship" and 18 definitions of "social enterprise", "social entrepreneurial venture" or "social entrepreneurship organization".

According to Mort et al. (2003), social entrepreneurship is a multidimensional construct involving the expression of entrepreneurially virtuous behavior to achieve the social mission, a coherent unity of purpose and action in the face of moral complexity, the ability to recognize social value-creating opportunities and key decision-making characteristics of innovativeness, proactiveness and risk-taking. Mair and Marti (2006) define social entrepreneurship as a process consisting of the innovative use and combination of resources to explore and exploit opportunities, that aims at catalyzing social change by catering to basic human needs in a sustainable manner. Austin et al. (2006) view social entrepreneurship as an innovative, social value creating activity that can occur within or across the nonprofit, business, or government sectors. Zahra et al. (2009) suggest that social entrepreneurship encompasses activities and processes undertaken to discover, define, and exploit opportunities in order to enhance social wealth by creating new ventures or managing existing organizations in an innovative manner. Dees (1998) proposed three dimensions of social entrepreneurship: (1) sociability: solving a social problem and creating social value; (2) innovation: being innovative, breaking patterns and changing systems; (3) market orientation: being entrepreneurial, taking advantage of opportunities, accepting risks, being resourceful, and practicing leveraging.

Finally, for the purpose of our research we will use the definition by the Organization for Economic Cooperation and Development (OECD). OECD describe the term social entrepreneurship as the entrepreneurship that has as main goal to address pressing social challenges and meet social needs in an innovative way while serving the general interest and common good for the benefit of the community. In a nutshell, social entrepreneurship targets to social impact primarily rather than profit maximization in their effort to reach the most vulnerable groups and to contribute to inclusive and sustainable growth.

Authors including Dees (1998), Light (2006), Mair and Martí (2006), and Martin and Osberg (2007) concluded in their papers that all definitions of social entrepreneurship focus on four key

factors: first one is the characteristics of individual social entrepreneurs, second one is their operating sector, third one is the resources used by social entrepreneurs, and the last fourth one is the primary mission and outcomes associated with the social entrepreneur.

One of the most commonly used definitions about social entrepreneur was provided by Dees (1998). Dess (1998) define social entrepreneurs as change agents in the social sector. Social entrepreneur by Dess (1998) is someone who plays the role of change agents in the social sector by: (1) adopting a mission to create and sustain social value (not just private value); (2) recognizing and relentlessly pursuing new opportunities to serve that mission; (3) engaging in a process of continuous innovation, adaptation, and learning; (4) acting boldly without being limited by resources currently in hand, and (5) exhibiting a heightened sense of accountability to the constituencies served and for the outcomes created. Brinckerhoff (2000) defines social entrepreneurs as those, who: (1) are willing to take reasonable risk on behalf of the people that their organization serves; (2) are constantly looking for new ways to serve their constituencies and add value to existing services; (3) understand that all resource allocations are really stewardship investments; (4) always keep mission first, but know that without money, there is no mission output. According to the Dess (2008) and Brinckerhoff (2000) literature review, about social entrepreneur we find out these three components in common: (1) entrepreneurship spirit; (2) personality and (3) social value.

2.1 Social entrepreneurship in Croatia

Social entrepreneurship in Croatia is a rather new phenomenon and is still poorly developed. The term appeared in the public discourse rather late, in 2006, and since then has increased to the point where a strategy for social entrepreneurship has been initiated. In April 2015 Croatia adopted a Strategy for Social Entrepreneurship Development in the Republic of Croatia for the period 2015-2020, which introduced a new definition of social enterprise. In the document social entrepreneurship is defined as: business based on the principles of social, environmental and economic sustainability, in which generated profit is entirely or largely reinvested for the benefit of the community. Today, almost five years after the adoption of the Strategy we can conclude that theory has not been followed by practical implementation. The present state of the development of the social entrepreneurship in Croatia is reflected in the passive approach towards meeting the Strategy objectives, the lack of institutional infrastructure and legal framework, and the lack of long-term financial support that would ensure stability and planned development of the sector (Šimleša *et al.,* 2019).

Even if social entrepreneurship in Croatia is still in its early stage of development, it is dominantly generated by the associations, particularly since 2014 when new legislation (Law on Associations, Official Gazette 70/2014) opened that sector for commercial activities, with the social aspect being the dominant one. The number of social entrepreneurship actors is shown in the table below, along with their distribution according to their legal status.

It is evident from Table 1. that the number of Social entrepreneurship actors in Croatia is growing, especially among associations and cooperatives (Šimleša, Puđak and Bušljeta Tonković, 2019). Still, scientific institutions in Croatia[12] have to support more development of education and awareness of social entrepreneurship.

[12] Scientific institutions in Croatia that supported development of social entrepreneurship are: Faculty of Law, University of Zagreb – the Chair of Social Policy; Faculty of Economics, University of Osijek; University of Applied Sciences VERN in Zagreb; Zagreb School of Economics and Management; and Faculty of Economics and Tourism "Dr. Mijo Mirković" in Pula (EMS, 2014).

Having taken into consideration the fact that there is small number of empirical research in social entrepreneurship in Croatia, we decided to conduct one to explore the link between social entrepreneurship and voluntourism, as one of the types of special interest tourism, and to examine the Croatian context in this regard.

Table 1: Social entrepreneurship actors (2013, 2014, 2015)

Legal entity	2013.	2014.	2015.
Associations	45	44	57
Cooperatives	36	31	39
Companies	13	13	15
Institutions	1	2	1
Total	95	90	112

Source: Šimleša, D., Puđak, J. and Bušljeta Tonković, A. (2019). Social Entrepreneurship in Croatia: Its Future, the Actors Database, and the Strategy // Social Entrepreneurship in South East Europe - Three Countries Analysis / Šimleša, Dražen (ur.). Zagreb: Institut društvenih znanosti Ivo Pilar, 27-44.

3. Sustainable tourism development

Tourism, as one of the most significant phenomena of modern society, is at the same time one of the world's largest industries and hence the main form of global economic expansion (Fletcher *et al*., 2019). According to UNWTO (2019), the tourism industry is forecasted to continue to grow dramatically in the future based on the development aspirations of many low- and high-income countries alike. However, despite the fact that tourism is recognized as a vital contributor to job and wealth creation, economic growth, environmental protection and poverty alleviation, its negative effects at a social, environmental and economic level are increasingly emphasized. This is the reason why the tourism industry should be paid attention in order to ensure sustainable development.

The most commonly cited definition of sustainable development, which is often transmitted to the sustainable development of tourism, presupposes development that meets the needs of the present without compromising the ability of future generations to meet their own needs. UNEP & WTO (2005) defined sustainable tourism more precisely as tourism that take full account of its current and future economic, social and environmental impacts, addressing the needs of visitors, the industry, the environment and the host communities.

The fragmented nature of the tourism industry requires necessity of coordination and collaboration of many different stakeholders that have interests in the process of tourism development. The stakeholder in the tourism industry is implied as anyone who is impacted on by development positively or negatively, and as a result it reduces potential conflict between the tourists and host community by involving the latter in shaping the way in which tourism develops (Aas *et al.,* 2005). According to Heitmann (2010), stakeholders fall into different categories depending on their levels of interest and their potential to influence in the decision-making process of the tourism destination.

It seems that local community is the main stakeholder in the sustainable tourism development process. The full involvement of local communities in the tourism sector, not only benefits them and the environment in general, but also improves the quality of the tourism experience. Local communities benefit from sustainable tourism through economic development, job creation, and infrastructure development. Tourism revenues bring economic growth and prosperity to attractive tourist destinations which can raise the standard of living in destination communities. Increase in

tourism revenue to a destination acts as a driver for the development of increased infrastructure. As tourist demands increase in a destination, a more robust infrastructure is needed to support the needs of both the tourism industry and the local community. Projects imposed from outside and motivated by the pursuit of rapid economic growth often override local needs, conditions and resources, and result in unacceptable environmental, social and cultural costs (Kilipiris, 2005).

However, a variety of stakeholders can and should play the role in the development and implementation of sustainable development in the tourism sector. The private sector is responsible for producing and sustaining quality tourism products and services such as accommodation, food and beverages, local tours, transportation facilities, and recreational activities (Turker *et al.,* 2016). It is the bearer of tourism development in general, so it wouldn't be possible to develop sustainable tourism without it.

Governments of the states which determine the rules of conduct by law are the most important in shaping sustainable tourism policy (Nsizwazikhona *et al.,* 2015). It should be noted the influence of government institutions on change encouraging through incentives such as tax breaks or changes in the legal framework. But, a primary challenge for local governance both today and in decades ahead, is to steer increasingly external, global forces on local development so that development achieves the shared vision of the local population. However, if tourism development by the government of a particular destination is not aligned with the wishes and needs of the local population by legal and other regulations, it is possible to expect the local population's resistance to tourism development.

Also, non-governmental organizations are one of the stakeholders in supporting sustainable tourism development. They can be involved in the provision of consultancy services in designing campaigns, investment projects or gaining public support for a series of particular causes (Iorgulescu *et al.,* 2005).

4. Voluntourism – a sustainable form of tourism

On the global scale, voluntourism is one of the fastest growing examples of alternative travel experiences that respects dimensions of sustainable tourism. Voluntourism can be viewed as a development strategy leading to sustainable development through balance between natural resource qualities, local community and the visitor that all benefit from tourism activity (Butcher *et al.,* 2010).

Voluntourism can be considered as an integrated organized combination of volunteer service at tourist destination and specific tourism activities, which are performed in one's spare time, out of a place of residence, in home country or abroad and that is beneficial not only for voluntourists, but also for local communities and the environment (Pompurová *et al.,* 2018). The volunteer tourist pays for the costs of his travel and stay in the destination and moreover the fee for the opportunity to be involved in project. Unlike volunteers who participate in volunteer projects in their local communities, volunteer tourists leave a mark in communities that are often far from their homes, they work in an unfamiliar environment that involves new people, unknown or lesser-known cultures, a different tradition and different living conditions. Volunteer tourists through well-organized volunteer programs help to provide basic services that are lacking or not sufficiently available in the local community, mobilize people and influence changes and attitudes in areas such as environmental protection or sustainable consumption, and strengthen capacities by transferring knowledge and experience.

The direct benefits of the local community are reflected in the increased manpower engaged on programs that aims the needs of the community itself, as well as direct financial support through

placements, while the indirect benefits include increased local employment and improved quality of public facilities and infrastructure (Morgan, 2012). Volunteering helps to activate local communities by involving people in the planning and implementation of sustainable development goals, but also contributes to the local economy as volunteers spend part of their time getting to know the area they are in.

Volunteering also provides new opportunities for tourism companies. The development of voluntourism creates the need for partnerships beyond the traditional tourist supply chain participants (i.e. accommodation providers, airline companies etc). We need to emphasize the important role of tour operators and travel agencies that offer travelers an opportunity to participate in an optional excursion that has a volunteer component, as well as cultural exchange with locals (Wearing, et al., 2013). On the other side they should actively participate, in partnership with local NGOs, not only in promotion and distribution, but also in creating volunteer products. It allows them to stay in touch with large segment of voluntourist consumers while also enable them that both the local community and their customers recognize them as a company that is active in the area of corporate social responsibility. However, because of commercial component of volunteer programs, the critiques of voluntourism often arise, aimed not only at exploiting the local population for the purpose of achieving personal goals through short-term tourism-motivated engagement, but also at targeting profit rather than community well-being (Verardi, 2013).

Conducted research in the field of voluntourism mostly investigate environmental, humanitarian and development projects in less developed countries, whose cultures are significantly different from voluntourists' cultures. However, the perception of voluntourism as a combination of travel and volunteering only in developing countries is short-sighted and too simplistic owing to the diverse array of opportunities available in today's market (Pompurová *et al.,* 2018). Voluntourism projects in developed countries are becoming more and more popular. They create opportunities for collaboration of different stakeholders in the local community, and they can include different segments: teaching, conservation, preserving tradition, protection of cultural heritage, research etc.

4.1 Tourism social entrepreneurship – support for the development of voluntourism

For the successful development of any tourism product, it is necessary to understand its complex structure. Kotler (2001) defined a product as any offering that can satisfy a need or want, such as one of the 10 basic offerings of goods, services, experiences, events, persons, places, properties, organizations, information, and ideas. Applying this concept to a tourism product, it can be differentiated as: material products (guides, maps, souvenirs), services (transport, gastronomy, recreational services etc.), local tourism facilities (castles, churches, monuments, museums, recreational centers), events (exhibitions, cultural events, sports championships, even sightseeing with a guide), personalities and groupings (i.e. famous residents or their birthplaces, characteristic ethnic groups, artists), thematic trails (walking, cycling, water trails), places (viewpoints, national parks, landscapes) and finally "ideas" (exploring the cultures of other nations, living and resting closer to nature). All these product categories are destination related and they jointly connect to create the complex final product (Lipianin-Zontek, et al., 2017).

The biggest challenge in developing a tourism product stems from the fact that some different enterprises are responsible for each component of a complex tourism product, giving tourism enterprises a critical role in delivering desired community development outcomes. Since the implementation of the traditional profit-oriented approach to entrepreneurship in tourism has shown numerous negative effects on the local community and the environment, the pursue of new social values and inducing societal transformation at large, leads to the development of the concept

of social entrepreneurship and its application in tourism. Since social entrepreneurship is designed to facilitate social value creation, social innovation and sustainability, the tourism industry is a rich ground for social entrepreneurs (Aquino et al., 2018). This is especially true for niches such as voluntourism, social tourism or cultural heritage tourism, that are the result of the vision to foster innovative and, more importantly, sustainable tourism practices that balance the economic, social, cultural and environmental outcomes for local communities.

Social tourism entrepreneurs are defined as those who conduct tourism business activities that inspire and encourage local communities to participate in carrying out business activities travel. Here there is a strong effort from one to change himself and others by doing tourism business activities (Reindrawati, 2018). It is represented by the establishment of the innovative environment, which ensures tourism entrepreneurial projects that do not present value added only for the tourist, but also for all the local stakeholders (Alkier *et al*., 2017).

Due to the complex structure of the tourist product and the specific way of selling it on the market, implementation of social entrepreneurship in tourism requires social enterprises that offer a variety of products and services while also implementing social innovation strategies. Day and Mody (2017) categorize tourism social enterprises into three types based on enterprises' functions, roles, contributions and product offerings within the tourism value chain. The first type relates to a "suppliers to the tourism experience" and it includes tourism social enterprises that offer tangible products (e.g. food, souvenirs) to tourists. Often, this type adopts a social innovation where technical expertise is transferred to community beneficiaries in order to develop the local skills and knowledge to produce such goods.

The second type includes a "providers of the tourism experience", respectively social entrepreneurs which organize and involve the wider community, identify community needs, and develop local capacity to address these needs through human resource development and tourism training. And the last type refers to an "intermediaries of the tourism experience". They involve travel-market intermediaries (e.g. travel agencies) which sell sustainable tourism products and thus promote and educate travelers in more responsible tourism practices, emphasize the need to change travel behavior, and support social causes at the respective destinations they 'sell'. These social enterprises exist to influence public views on social issues through their commercial activities (Aquino et al., 2018).

From the above, it is evident that the opportunities for the implementation of social entrepreneurship in tourism are huge, so different local communities can cherish different examples of social entrepreneurs who contribute to the development of tourism products each in their own way, but also different forms of collaboration with other stakeholders in the community. In that regard, the conceptual framework proposed in this paper is developed from the described concepts of sustainable community development, social entrepreneurship and voluntourism, as shown in Figure 1.

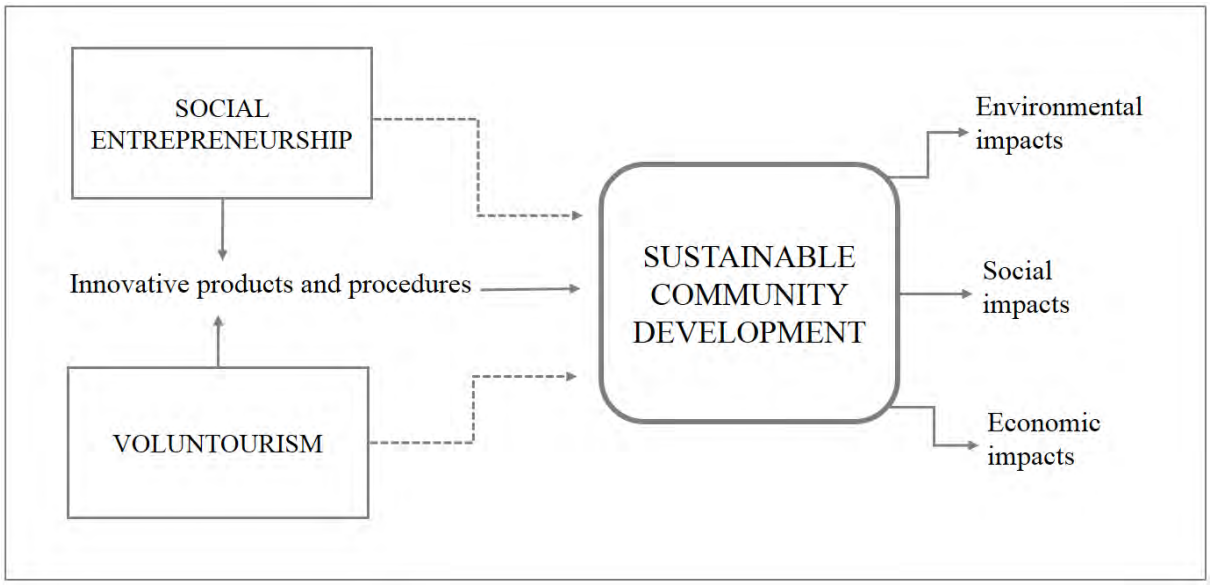

Figure 1: Social entrepreneurship and voluntourism impact on sustainable community development: A conceptual framework proposition

4.2 The role of social entrepreneurs in the development of volunteerism: The case of Croatia

Croatia has been an unavoidable tourist destination for many travelers from all over the world in recent years. This is evidenced by data from the Croatian Bureau of Statistics (2019), which registered nearly 90 million overnight stays in 2018. However, the data also show that more than 85% of the total overnight stays were realized in the four months of the peak season. This indicates that the dominant model of tourism development is still summer bathing tourism with marked mass characteristics. Considering all the negative effects arising from the development of this tourism model, it is evident that there is a need to develop an alternative tourism model that will support sustainable development. One of the alternative models of tourism development are focused on selective forms of tourism, and this paper analyzes the contribution of social entrepreneurship to the development of voluntourism in the Republic of Croatia.

Although there is great potential for the development of voluntourism products, since, on the one hand, there is a need for local communities to involve more people with volunteer preferences, and on the other, there is a growing interest of tourists for this type of holiday, the development of volunteer products in Croatia is relatively modest.

The pioneering project of raising public awareness about the possibilities of development voluntourism products in Croatia, with an emphasis on finding and connecting stakeholders who could support its development, was carried out by the MI-Split Association in cooperation with partners. The project „Open up borders for adventure and new travel opportunities" was designed for organizations operating in the field of tourism, non-profit civil society organizations and representatives of local administrative units, and implemented under the EU program on cross-border IPA component II, the Program on Cross-Border Cooperation Croatia – Montenegro 2007 – 2013, and the anticipated duration of the project was 18 months (from April 2016 to October 2017). The overall objective of the project was to contribute to the promotion of Croatian and Montenegrin tourist potentials as an integral tourist destination, improving the environment for the establishment of new tourism products based on sustainable development of the program area and improvement of social connections in the cross-border area. On the other hand, the specific objective of the project was to strengthen the cooperation between the public, profit and non-profit

sector by developing voluntourism as an innovative and distinctive tourism product on joint tourism territory of Croatian-Montenegrin border areas.

Within the project activities, two workshops were held on volunteering management and social entrepreneurship, as well as development of voluntourism products. Also, the first Croatian Conference on Voluntourism was held on June 2nd 2017 in Dubrovnik, where the voluntourism innovations, best practices, as well as examples and ideas that resulted from the project's activities, were presented. Since one of the objectives of the project was to develop at least two pilot voluntourism products/activities in the cross-border area, three such examples were presented at the conference: Frano Vlašić (Luški puti j.d.o.o.) and Leo Žanetić (Otočki sabor) presented their idea of including tourists in volunteering efforts on the island of Korčula during the summer season, while Julija Milanović from the Animal Welfare Association in Cetinje and Željko Starčević from the Orjen Protection Agency in Herceg Novi presented ideas for voluntourism projects in Montenegro (Matošević Radić, Buljan Barbača, 2018).

Also, in recent years, projects, that have great potential to grow into voluntourism programs, are invented and implemented. For the last few years, the City of Nin has been working with volunteers (biologists and ornithologists) in the fields of 'Solana Nin', where volunteers work as educators on the European Bird Counting event, which aims to inform citizens and tourists and promote the exceptional biodiversity of the salt pans and lagoons. This area is listed in the Natura 2000 habitat, ecological network of nature protection areas for preserving endangered species and habitats. The volunteer role in bird watching involves tourists and all interested (mostly amateur) photographers who come to the lagoon to photograph the birds and then donate the created photos for the purpose of promoting the destination, which are then posted on the destination's Instagram profile (Lekić, 2017). In this way, the satisfaction of tourists and the local community is achieved, and free materials for promotional purposes are obtained, which again has the effect of increasing tourist demand.

An interesting idea for a volontourism product was developed on the island of Korčula, that has an exceptional natural and cultural-historical heritage. One of the interesting features of the island is the drywall, which, in addition to being the boundary between the land plots, is today also nominated as a cultural property of the Republic of Croatia, protected by the Ministry of Culture (Vlašić, 2017). The idea of a volunteer program was triggered by the desire to include tourism activities in the restoration of the Korčula drywall. The itinerary includes a seven-day stay, during which the volunteer tourists will have the opportunity to learn about the history and culture of the island of Korčula through four days of hiking trips, and then actively participate in a volunteer project of construction and restoration of drywall, mosaic and various sculptures creation related to the island tradition. The project also includes cooperation with the European Ramblers Assocciation (ERA), which promotes and supports all European pedestrian paths, pedestrian walking programs, etc.

For the further development of voluntourism in Croatia, it is necessary to encourage the development of social entrepreneurship, in order to develop products that respect all dimensions of sustainable tourism development. The presented examples show that there are interested stakeholders on both the suppliers and the providers travel experience, but at least one serious intermediary of the tourism experience is still missing. Its role is crucial, since voluntourism development needs the incorporation of volunteer projects into high quality tourism products that tell the stories about the locals, cultural heritage and rich traditions of the host destination while encouraging both the sustainable development of the local community and the personal development of the voluntoutists.

5. Conclusion

This paper proposes that niche tourism products and more specifically, voluntourism projects, under the prism of social entrepreneurship, can become the means towards Croatian product diversification and long-term environmental, social and economic sustainability. Moreover, this paper demonstrated the connection between social entrepreneurship and volutourism and proposed a relatively coarse framework that integrates the effects of voluntourism and social entrepreneurship, through innovative products and procedures, thus affecting the sustainable development of local community through its environmental, social and economic dimension.

This research, in regard to theoretical contribution, has connected the literatures on social entrepreneurship, voluntourism and sustainable development of the local community, thus explaining the conceptual linkage between them. On the other hand, this paper offers practical implications that make contributions to the voluntourism literature, since the lack of implementation of this concept.

The focus was on the Croatian context and results indicate that there are limited number of projects concerning social entrepreneurship in voluntourism in Croatia and also that discussed projects are not recognized or there is a lack of awareness of them. The empirical work was exploratory because of the novelty of the subject and limitations related to data availability. Research assessed the situation in Croatia and although it was comprehensive under mentioned conditions, it cannot speak to social entrepreneurship in voluntourism globally, but it can offer foundation for future research in this area.

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INTRODUCING FAIRNESS AND TRANSPARENCY FOR BUSINESS USERS OF ONLINE PLATFORMS

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Abstract
Online intermediation services are becoming indispensable in the field of online economy and are a crucial step for the success of businesses using these services as they enable them to attract more consumers. Being aware of the dependence on their services, service providers can impose harmful commercial practices on business users and therefore significantly affect the results of their transactions generated through the use of their services. On 20 June 2019, the European Parliament and the Council adopted the Regulation on promoting fairness and transparency for business users of online intermediation services. It seeks to ensure a legal framework that guarantees fair and transparent commercial practices for business users of online intermediation services and online search engines. The aim of this paper is to present and explain the solutions representing the new legal regime of the use of online platforms, define the reasons for adopting these rules at EU level and determine their position within the system of unfair competition law, particularly in B2C and B2B (business-to-consumer and business-to-business) relations.

Keywords: *online intermediation services, online platform economy, online search engines, unfair commercial practices, unfair competition*

Track: *Entrepreneurship*

Word count: *8.226*

1. Introduction

Today, we are witnesses of the time when the Internet has a significant impact on our daily lives, both private and business. We use internet applications, search engines, social networks of different profiles and for different needs.[13] Digital environment seems particularly convenient for trading and the Internet is becoming a common place of connection for a seller or service provider and a client. This connection is most commonly done by online platforms, because they easily combine supply and demand and thus act as intermediaries, representing "access points to the market and consumers".[14]

[13] Eg. Google Search, Yahoo!, Bing, Amazon, eBay, Alibaba, Uber, BlaBlaCar, Airbnb, Booking.com, Facebook itd.
[14] Explanation of the Regulation Proposal of the European Parliament and of the Council on promoting fairness and transparency for business users of online intermediation services (COM(2018), 238 final, 2018/0112(COD), further: Proposal for a Regulation), point 1 states that *"currently, over one million businesses in the EU trade through online platforms to reach their customers and it is estimated that approximately 60% of private consumption and 30% of public consumption of goods and services related to the digital economy as a whole are done through online intermediaries. "*

Moreover, it can be said that they create markets,[15] because they represent the place where supply and demand meet, which goes beyond the existing legal framework of contract law[16], so the necessity of special legal regulation is created.

Online intermediation involves a variety of services, like business users advertising, facilitating their communication and booking, conducting cash transactions between business users and consumers, price comparison etc.[17] Online platforms are a source of data-driven innovations that enable businesses to be online, as well as they provide citizens with easier access to information, offer social and creative content, affect the increase of consumer choice, improve the efficiency and competition of businesses as well as they can strengthen civic participation in society.[18] Creating and shaping new markets by collecting, processing and editing large amounts of data, using information and communication technology, business in multilateral markets with varying levels of control over direct interaction between groups of users, creating a network that is more user-friendly when it has more users, and creating digital value by accumulating data, enabling new business ventures and creating new strategic relationships are common to all online platforms.[19]

In the digital market, which knows no geographical boundaries, significant market power is concentrated on a smaller number of online platforms, which have a large number of users. That is why the success of small businesses is increasingly dependent on collaboration with these leading online platforms. It creates an addiction of businesses with low bargaining power to online platforms that have strong bargaining power. Due to the dependence of business users on service providers and their imbalance in the bargaining power, there is a possibility of unfair business practices.[20]
In 2017 and 2018, studies were conducted to analyse the practices and business conditions of online platforms[21].

To prevent the unfair business practices of ISPs, or to achieve the overall goals of a fair, predictable, sustainable and reliable online business environment[22], European Union adopts Proposal for a Regulation of the European Parliament and of the Council on promoting fairness and transparency for business users of online intermediation services, in addition to which it adopted the Decision on the establishment of a group of experts for the Observatory of the

[15] So does Twigg-Flesner, Christian, The EU's proposals for Regulating B2B Relationships on Online Platforms - Transparency, Fairness and Beyond (September 17, 2018). (2018) 7, p. 1. Journal of European Consumer and Markets Law (Forthcoming). Available at SSRN: https://ssrn.com/abstract=3253115.
[16] In the Republic of Croatia, the brokerage contract is regulated by Art. 835 to 848 of the Law on Obligations (Official Gazette 35/05, 41/08, 125/11, 78/15, 29/18).
[17] See Proposal for a regulation, rationale, point 1. See also typology of online platforms in the OECD (2019), An Introduction to Online Platforms and Their Role in the Digital Transformation, OECD Publishing, Paris, https://doi.org/10.1787/53e5f593-en.
[18] Communication of the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, online platforms and the digital single market, Opportunities and challenges for Europe, 25.5.2016, COM (2016) 288 final, point 2. The internet platforms importance increases in the digital economy.
[19] Ibid.
[20] § 6 Introductory statement (EU) 2019/1150, OJ no. 186, 11.7.2019, p. 57-79.
[21] de Bas, Patricketal. (2017): Business-to-Business relations in the online platform environment. FWC ENTR/300/PP/2013/FC-WIFO: Final report, ZEW-Gutachten und Forschungsberichte, ISBN 978-92-79-68950-5, European Commission, Brussels, http://dx.doi.org/10.2873/713211, EY, Study on contractual relations between online platforms and their professional users- Final report, European Commission, FWC JUST/2015/PR/01/0003/Lot1-02, Final Report, 23rd April 2018, available at: https://op.europa.eu/en/publication-detail/-/publication/b3d856d9-4885-11e8-be1d-1aa75ed71a1/language-en.
[22] Justification of the Regulation Proposal, point 1, § 31 of the proposal for a recital (later § 51 of Regulation 2019/1150).

Economics of Online Platforms, for the purpose of consulting and conducting expert analysis of that branch of the economy, as well as monitoring the effects of the application of the Regulation.[23] Regulation (EU) 2019/1150 of the European Parliament and of the Council on promoting fairness[24] and transparency for business users of online intermediation services was adopted on 20 June 2019 and will apply from 12 July 2020. [25]

2. Adoption of Regulation on Promoting Fairness and Transparency for Business Users of Online Intermediation Services as an application of a B2B relations legal framework as a restriction against unfair competition in the EU

Regulation on Promoting Fairness and Transparency for Business Users of Online Intermediation Services that was adopted by the European Commission, may be perceived as yet another act of unfair competition law. In the EU, there is no exact regulation on unfair competition as there is the regulation on competition. However, there was an attempt at harmonizing the unfair competition law in 1968 when the European Commission requested a comparative study of national regulations of Member States[26], which was to be conducted by Max Planck Institute in Munich. The integral harmonization failed: the EU decided on a step-by-step procedure against unfair competition[27]. The very first directive on unfair competition that was adopted was the Council Directive 84/450/EEC of 10 September 1984 relating to the approximation of the laws, regulations and administrative provisions of the Member States concerning misleading advertising.[28] Soon followed the Directive 97/55/EC of European Parliament and of the Council of 6 October 1997[29] amending Directive 84/450/EEC concerning misleading advertisings as to include comparative advertising. Both directives defined B2B and B2C relations. Division of law on unfair competition relating to B2B and B2C relations, however, was imposed by the adoption of the Directive 2005/29[30]. Thus unfair business practices were defined by introducing comprehensive ban exclusively for B2C relations.[31] Consequently, codified version of the Directive 2006/114/EC of European Parliament and of the Council of 12 December 2006 was adopted concerning misleading and comparative advertising, which applied exclusively to B2B relations.[32] The necessity for further harmonization of regulations on unfair competition concerning B2B relations has recently

[23]Justification of the Regulation Proposal, point 5 according to Art. 18 (4) of Regulation 2019/1150, the Commission is required to take into account the opinions and reports of this group when carrying out an evaluation of the Regulation every three years (Article 18 (1) of the Regulation).

[24]It would be more legal to use the term "fairness", in the sense of the principle of conscientiousness and fairness, on which these particular rules are based upon (§ 2. Introductory Statement of the Regulation), as a translation of the English version of "fairness".

[25]OJ no. 186, 11.7.2019, p. 57-79.

[26] Head of the project, Professor Eugen Ulmer, proposed that the European regulations concerning unfair competition were based on the Paris Convention but with minor changes. See: Ulmer E., Intellectual Property Rights and the Conflict of Laws, Deventer; Kluwer, Commission of the European Communities, 1978

[27] Study by Institut für EuropäischesWirtschafts- und Verbraucherrechte. V., Study for Health &Consumer Protection DG, Volume III, 2000, http: // europa. eu. int/ comm/dgs/health_consumer/library/surveys/sur21_vol3_en. pdf, p. 9.

[28] Council Directive 84/450/EEC of 10 September 1984 relating to the approximation of the laws, regulations and administrative provisions of the Member States concerning misleading advertising expired on 11 December 2007, OJ L 250, 19 September 1984, p. 17 - 20

[29] Directive 97/55/EC of European Parliament and of the Council of 6 October 1997 amending Directive 84/450/EEC concerning misleading advertisings as to include comparative advertising, expired on 11 December 2007, OJ L 290, 23 October 1997, p. 18–22

[30]Directive 2005/29/EC of European Parliament and of the Council of 11 May 2005 concerning unfair business practices in B2C relations within the European market and amending Directive of the Council 84/450/EEC, directive 97/7/EC, 98/27/EC and 2002/65/EC of the European Parliament and the Council,, as well as the Regulation (EC) no. 2006/2004 of the European Parliament and the Council (*Directive concerning unfair business practice*), OJ L 149, 11 June 2005, p. 22–39, Special Croatian Edition: Chapter 15, Volume 008, p. 101 – 118

[19] Integral harmonization

[32] OJ L 376, 27 December 2006, p. 21–27, Special Croatian Edition, Chapter 15 Volume 022 p. 96 – 102

arisen in light of e-commerce expansion, investment and innovation protection and, finally, the change in retail terms. Directive (EU) 2016/943 of the European Parliament and of the Council of 8 June 2016 on the protection of undisclosed know-how and business information (trade secrets) against their unlawful acquisition, use and disclosure was the first to be issued.[33]

It was followed by the Directive (EU) 2019/633 of the European Parliament and of the Council of 17 April 2019 on unfair trading practices in business-to-business relationships in the agricultural and food supply chain.[34] The European Union identified another type of unfair trading practices that were predominantly generated by the use of digital technologies – misleading marketing practices.[35] Those were discussed in the context of amending Directive concerning misleading and comparative advertising 2006/114/EEC. So far no statutory regulations have been passed within the Union.[36]

As for B2B relations, there is no comprehensive ban on unfair business practices within the EU legal framework as is the case with the Directive 2005/29 concerning B2C relations. Defined regulations within B2C relations cannot form the basis for the protection from unfair practices in terms of online intermediation services within the scope of B2B relations.

This is elaborated in the Proposal for the Regulation of the European Parliament and of the Council on promoting fairness and transparency for business users of online intermediation services. The Proposal highlights limitations of the Directive of unfair business practices 2005/29, as well as Council Directive 93/13/EEC on unfair terms in consumer contracts. Both put an emphasis on the high level of transparency and professionalism exclusively in B2C transactions. On the other hand, it is underlined that the Directive 2006/114/EEC applies to B2B relations exclusively in the sphere of advertising. However, they do not apply to unfair trading practices that result from the existing contractual relationships between online platforms and their business users.[37]

As for the unfair business practices within the food supply chain as well as unfair practices of online platforms in relations to business users, the key issue lies in the dependence of business entities on stronger partners. Stronger partners, however, may not be stronger in terms of fair competition regulations. In other words, these regulations are applicable in cases of the breach of fair competition, e.g. the abuse of power reflected through unfair pricing, other unfair trading practices, application of different terms for identical business practices, which makes fair competition impossible.[38] Therefore, the acts of the abuse of superior bargaining position can be perceived as „minor acts of competition law breach“, i.e. the amendment of this law, when the abuse of power is not considered as the abuse of the leading position on the market within

[33] OJ L 157, 15 June 2016, p. 1–18
[34] OJ L 111, 25 April 2019, p. 59–72
[35] Misleading marketing practices include misleading advertising and marketing techniques that cannot be included in the definition of advertising contained in the Directive 2006/114 on misleading and comparative advertising. This mainly refers to mass online cross-boundary fraudulent marketing activities, such as misleading practices of companies directory services, invoicing for services that have not been ordered, billing in the name of public entities, internet domains prolongation offers, fraudulent offers for the stamp protection prolongation in other states, et al.
[36] See Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions protecting businesses against misleading marketing practices and ensuring effective enforcement, 27 November 2012, COM/2012/0702 final.
[25] Point 1of the Regulation Proposal

[38]Art. 102 of the consolidated version of the Treaty on the European Union and Treaty on the Functioning of the European Union; Treaty on the European Union (consolidated version), Treaty on the Functioning of the European Union (consolidated version); Protocols and Annexes to the Treaty on the Functioning of the European Union, Statement annexed to the Final Act of Intergovernmental Conference at which the Treaty of Lisbon was adopted and signed on 13 December 2007 Tables of equivalents, OJ C 202, 7 June 2016, p. 1–388

competition application.[39] The Article 1(5) of the Regulation 2019/1150 provides that this abuse does not undermine fair competition law, which means that if an entrepreneur (an online platform) that holds a leading position imposes retroactive changes to terms and conditions of use, the regulations regarding competition law will by no means be applied, regardless of the Regulation provisions. Although unfair business practices by online platforms may not result in the breach of competition, the intervention on the part of the Union was necessary in accordance with principles of subsidiarity and proportionality due to transboundary effects and impacts on a large number of business users.

From the statement of reasons of the Regulation Proposal in which online platform practices are compared with regulations below that define unfair competition law, titled ″consistency with the existing regulatory policies“, it can be perceived that analysed rules and regulations contained in the Regulation 2019/1150 belong to the same same legal area.
However, the Regulation does not refer to unfair competition as such, but unclearly addresses fair competition, e.g. § 30 of the introductory statement and the point (d) of Article 18(2), in relation to competition between business users and online platforms. [40] Some authors question the existence of unfair competition law within the area of the EU. [41] Although the Union selectively regulates unfair practices, without strictly defined material legal and procedural references, these regulations are integral to unfair competition law. So far, there have been several attempts at regulating B2B relations on the part of the Union. E.g. § 8 of the introductory statement of the Directive 2005/29 on unfair business practices in B2C relations states: *"The Commission should thoroughly examine the need for action in the area of unfair competition that is not contained in the Directive, and, if necessary, draft a proposal that would contain other aspects of unfair competition*“. In addition, § 17 of the Directive 2016/943 concerning trade secrets, states, "*While this Directive does not aim to reform or harmonise the law on unfair competition in general, it would be appropriate that the Commission carefully examine the need for Union action in that area.*“

Therefore, since fairness is mentioned in the title of the Regulation, its application represents its very aim in accordance with the Article 1, this regulation may be understood as the integral part of the heterogeneous legal system concerning unfair competition within the EU. Consequently, it represents a step further in the process of harmonisation of unfair competition law.

Since the area of unfair competition law in B2B relations is only partially regulated by the Regulation 2019/1150, § 8 of the introductory statement of the Regulation defines the subsidiary application of the laws valid in Member States providing sanctions and prohibition against unilateral conduct of unfair business practices to the extent that the relevant aspects are not covered by this Regulation. This means that Member States have freedom to prohibit unfair business practices in relations between online platforms and business users that are not covered by this Regulation.

3. Method, need and objectives of regulation of the online intermediation services sector

The European Union has decided to act because the existing legal rules cannot provide protection against the specific behaviour of online platforms. Solely voluntary initiatives are not considered

[39]According to the Law of unfair trading practices within the food supply chain, all public law proceedings are under the jurisdiction of Competition Agency. This confirms the link between these practices, whilst there are no specific regulations concerning private law enforcement.

[40] Point (d) of Art. 18 (2) provides that the first evaluation of the Regulation is conducted for *the purpose of investigating whether the competition between goods or services offered by a business user and goods or services offered or controlled by a provider of online intermediation services constitutes fair competition and whether providers of online intermediation services misuse privileged data.*

[41]Henning-Bodewig F., Unfair Competition Law, European Union and Member States, Kluwer Law International, Hague, Netherlands, 2006

to be suitable for creating a functionally independent legal protection mechanism and rules of fairness, as evidenced by combating harmful trade practices in the food supply chain. It is therefore concluded that these unfair business practices can only be effectively addressed by a legislative instrument[42]. The legal basis is the same as with other regulations in the field of unfair competition, and that is art. 114. TFEU, which prescribes shared jurisdiction between the Union and the Member States for the establishment and functioning of the internal market. As online services are cross-border in nature and different national legislation causes fragmentation of the single market, Union action is necessary for the establishment and proper functioning of the internal market, in accordance with the principles of subsidiarity and proportionality[43]. However, unlike the aforementioned acts of unfair competition, the Union decided to control this area by regulation rather than by directive. Therefore, these rules are directly applicable in the Member States.[44] The Regulation Proposal states that the Regulation is *"the most appropriate solution, as it is directly applicable in the Member States, it establishes the same level of obligations for private parties and allows consistent application of the rules in inherently cross - border internet intermediary trade and internet search. This will also address and prevent fragmentation of the Digital Single Market."* Furthermore, the growth will be allowed, compliance costs will be reduced and legal certainty will increase according to common rules.[45].

The Regulation Proposal justifies compliance with the principles of subsidiarity and proportionality. It cites that Member States cannot achieve the targets on their own in an effective way, as online intermediation providers, who have access to almost the entire population of the Union, have a place of establishment in one Member State. Union action is therefore the only way to apply common, appropriate and effective rules to the providers and users of the services concerned, irrespective of the legislation and the forum, which is determined by the general conditions. The principle of proportionality is justified by a combination of *"relatively general principles-based Union rules, with significant potential for industry action and targeted monitoring"*. It is emphasized that a better business environment will be created, while at the same time freedom for service providers will be retained so that they may establish their general conditions and shape their good business practices with codes of conduct, within the set principles.[46]

All regulations in the field of unfair competition, which impose a duty of fair competition, to the extent that they limit the freedom of enterprise laid down in Union law by Article 47 of the Charter of Fundamental Rights of the European Union.[47] Therefore, in order to prevent this freedom from being unduly restricted, it is essential that the rules are proportionate to the objectives pursued. In this regard, an attempt was made to strike a balance between the demands of honesty and the preservation of the innovation potential of online platforms. The justification for the restriction on the freedom of enterprise of online platforms lies in the fact that there is a dependent position of business users in relation to the service providers.[48] This is particularly affected by the use of pre-formulated terms of use, which are unilaterally determined by the service provider.[49] By balancing

[42] Justification of the Regulation Proposal, point 2, choice of instrument.
[43] Art. 5(3) and (4) of the Treaty on European Union.
[44] Art. 288(2) TFEU provides: "*The Regulation shall have general application. It shall be binding in its entirety and directly applicable in all Member States*."
[45] Justification of the Regulation Proposal, point 2, proportionality.
[46] Ibid.
[47] OJ C 202, 7.6.2016, p. 389-405. According to Art. 49(1) and (2) of the Constitution of the Republic of Croatia, the foundations of the economic organization of the Republic of Croatia are entrepreneurial and market freedom, and the reasons for limiting entrepreneurial freedom are the protection of the interests and security of the Republic of Croatia (general interest), nature, the human environment and human health. However, this right, as well as other constitutional rights and freedoms, may be restricted by law to protect the freedoms and rights of other people and to legal order, public morals and health.
[48] Regulation 2019/1150, Introductory statement, § 12.
[49] Ibid, §14.

the position of business users with respect to online platforms through safeguard provisions, the Regulation provides entrepreneurial freedom for service users. As entrepreneurial freedom is a fundamental principle from the Article 47 of the Charter, there must be no disproportionate restriction on the freedom of enterprise of online platforms in any case. The Regulation therefore emphasizes that the purpose of the Regulation is to respect the right to an effective legal remedy and a fair trial, which should be achieved by these rules, but also to promote the application of entrepreneurial freedom as a fundamental principle.[50]

The Regulation Proposal in Article 1 laid down the objectives related to ensuring appropriate transparency and effective legal protection for business users. However, in the Article 1 of the Regulation, firstly the purpose of the Regulation referring to proper functioning of the internal market, was introduced, which is understandable given that the legal basis for the adoption of this regulation is 114 TFEU, and secondly, fairness, as mentioned for the first time in Union's legislation on unfair competition, appears as the objective of the regulation itself.[51] The proper functioning of the market also leads to better and increased consumer choice.[52] In addition to the above mentioned objectives, the economic objectives are the protection and contribution to innovation, increased data sharing and the creation of a common European data space,[53] but also a fair distribution of surplus among online platforms, business users and consumers.[54]

4. Subjects of protection

The Regulation 2019/1150 on Promoting fairness and transparency for business users of online intermediation services regulates online intermediation services in B2B relationships. More specifically, the relationship between online platforms and users is also referred to as a P2B relationship [55]. According to the Regulation, direct protection is enjoyed by business users [56] and corporate users of online sites,[57] who have their place of establishment or residence in the Union and who, through these online intermediation services or search engines, offer goods or services to consumers located in the Union.[58]

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[50] Ibid, § 33.

[51] Eg. Directive 2005/29, although it exclusively regulates unfair commercial practices in Art. 1 states as its aim: *„The purpose of this Directive is to contribute to the proper func-tioning of the internal market and achieve a high level of con-sumer protection by approximating the laws, regulations andadministrative provisions of the Member States on unfair com-mercial practices harming consumers' economic interests."*

[52] Regulation 2019/1150, Introductory statement, § 8.

[53] Ibid, § 8 and 35.

[54] de Streel, Alexandre, Online Intermediation Platforms and Fairness: An Assessment of the Recent Commission Proposal (September 6, 2018). Available at SSRN: https://ssrn.com/abstract=3248723 or http://dx.doi.org/10.2139/ssrn.3248723, p. 22

[55] See for example the study: Néstor Duch-Brown, Platforms to Business Relations in Online Platform Ecosystems, JRC Digital Economy Working Paper 2017-07, JRC109186.

[56] According to point 1 of Art.2 (1) of Regulation 2019/1150 a business user is "*any private person acting in a commercial or professional capacity, or any legal person, offering goods or services to consumers through online intermediation services for purposes related to their own commercial , business, craft or professional activity.* "

[57] According to point 1 of Art. 2 (7) of Regulation 2019/1150 a corporate online user is "*any natural or legal person using the Internet interface, or any software, including websites or some parts of them and applications, including mobile applications, offering consumers goods or services for purposes related to their own trade, business, craft or professional activity.* "

[58] Paragraph 9 of the introductory statement states that consumers should be located in the Union but do not have to be residents of the Union or be nationals of a Member State.

This Regulation emphasizes the protection of weaker market players, which is one of the objectives and one of the remaining regulations in the field of unfair competition rights[59], for both consumers and micro, small and medium-sized enterprises.

In the introductory statement of the Regulation 2019/1150, great attention is given to consumers, although they are not directly addressed by these provisions, they only enjoy indirect protection. In point 4 of Article 2(1) as well as in the rest of the Union's acquis communautaire, a consumer is defined as *"any physical person acting for purposes which are outside his trade, business, craft or professional activities"* .The introductory statement of the Regulation points out that online intermediation services enable consumers to take advantage of the internal market, by increasing their choice of goods and services and by having access to more competitive prices. However, it also emphasizes the need to ensure legal safety and responsible behaviour of companies[60]. As a reason why this Regulation does not apply to consumers, it is stated that they are directly covered by the Union law in the field of consumer protection, but it is acknowledged that these rules will indirectly contribute to improving their confidence in the economy of online platforms[61]. However, direct protection is not provided to consumers, it is only provided to B2C relationships. Specifically, business users in relation to online intermediation providers enjoy protection only when they offer goods or services to consumers who are located in the Union, not if their offer is aimed only at business entities, i.e. when mediated in a B2B relationship. The stated reason is that the dependent position of business users has been observed primarily in relation to services that serve as a point of access to consumers.[62] Therefore, an intermediary relationship which enjoys protection under this Regulation, could also be described as a *platform – business user - consumer* (P2B2C). By doing so, the Union once again limited its involvment in exclusive relations of business entities in the field of unfair competition, thereby giving priority to the freedom of entrepreneurship.

Micro, small and medium-sized enterprises are provided with direct protection, along with other business users and corporate online users, but it is possible to notice that SMEs are more dependent on online business services in relation to other users, in order to connect with consumers [63]. Namely, the reason for the adoption of this Regulation is the existence of the great economic power of certain online platforms, which, due to greater negotiating power in relation to their weaker partners, can impose unfair business practices. However, no special rights are granted to SMEs, they enjoy protection because the rules for promoting fairness and transparency are being introduced into this area, which should be reflected in their more successful business activity.

On the other hand, if online service providers are SMEs, then they are not subject to all obligations, as are their stronger competitors. Thus, SMEs are exempted from the obligation to set up an internal system for dealing with complaints and determining mediators, because of the costs that they may have. [64].
The Regulation does not apply to relationships between competitors or peer-to-peer online intermediation services without the presence of business users[65].

5. The scope of the Regulation

[59] See: M. Rodin, 2019, New Theoretical Positions of Law Against Unfair Competition, University of Zagreb, Faculty of Law, Zagreb, Chapter 3.6. Unfair competition in order to protect a weaker market participant in European law.
[60] Regulation 2019/1150 / EEC, introductory statement, §§ 1 and 3.
[61] Ibid. § 3.
[62] Ibid, § 12.
[63] Ibid, § 2.
[64]See Regulation 2019/1150, § 38 and § 41, points 5 and 11, point 7 of Art. 11.
[65] Ibid, Introductory statement § 11.

5.1. Geographical scope

The Regulation 2019/1150, as a document of the Union, should apply to the territories of the Member States. Regarding business users and corporate website users, they need to have their place of establishment or residence in the Union, and, through the provision of online intermediation services and online search engines, should offer goods or services to consumers located in the Union. Therefore, consumers should be located in the Union, but do not need to have their place of residence in the Union nor have the nationality of any Member State.[66]

Furthermore, this Regulation should apply irrespective of the place of establishment or residence of the providers of those services, namely, online platforms whose actions are not restricted by national borders. These rules are congruent, and as stated in the Regulation, it is irrelevant which law is otherwise applicable to a contract.[67] Apart from online platforms that have their place of establishment in the Union, this Regulation should also apply to those service providers outside the Union that operate in the Union, although they don't have their place of establishment within the EU territory.

5.2. The substantive scope

5.2.1. Types of services within the scope

Multi-sided services based on the same ecosystem-building business model and online intermediation services between business users and consumers, fall within the scope of this Regulation.[68] The definition of services covered by this Regulation should be precise and technology-neutral. Therefore, irrespective of the technology used to provide online intermediation services, the introductory statement of this Regulation explains that those services could also be provided by means of voice assistant technology.[69]

As the Regulation states, there are two types of relevant services; online intermediation services and online search engine services.

Online intermediation services fall within the scope of the Regulation 2019/1150 if three cumulative requirements are met: firstly, they should refer to information society services according to point (b) of Article 1(1) of the Directive (EU) 2015/1535 of the European Parliament and of the Council[70], secondly, they should allow business users to offer goods or services to consumers in order to facilitate the initiating of direct transactions between those business users and consumers, irrespective of where those transactions are ultimately concluded[71], and thirdly, they should be provided to business users on the basis of contractual relationships between the provider of those services and business users which offer goods or services to consumers.[72]

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[66] Ibid, § 9.
[67] Ibid, introductory statement, § 9. and Art. 1(5)
[68] Ibid, introductory statement, § 10.
[69] Ibid, § 10., 11 and 13.
[70] Point (b) of Art. 1(1) of the Directive (EU) 2015/1535 of the European Parliament and of the Council of 9 September 2015 laying down a procedure for the position of information in the field of technical regulations and of rules on Information Society services (codified text), OJ L 241, 17.9.2015., p. 1–15, defines „service" as: „any service normally provided for remuneration, at a distance, by electronic means and at the individual request of a recipient of services. For the purposes od this definition: i. „at a distance' means that the service is provided without the parties being simultaneously present, ii. „by electronic means" means that the service is sent initially and received at its destination by means of electronic equipment for the processing (including digital compression) and storage of data, and entirely transmitted, conveyed and received by wire, by radio, by optical means or by other electromagnetic means, iii. „at the individual request of a recipient of services" means that the service is provided through the transmission of data on individual request.
[71] § 10 of the introductory statement of the Regulation 2019/1150 explains that it is irrelevant whether the transactions are concluded online, on the online portal of the provider of online intermediation services in question or that of the business user, offline or not at all.
[72] Regulation 2019/1150, point 2, Art. 2,

The introductory statement of the Regulation states that online intermediation services should include e-commerce, online software application market places and online social media services.[73]

Online search engine means "*a digital service that allows users to input queries in order to perform searches of, in principle, all websites, or all websites in a particular language, on the basis of a query on any subject in the form of a keyword, voice request, phrase or other input, and returns in any format in which information related to the requested content can be found*"[74] Search engine providers determine the ranking of websites through which corporate website users offer their goods and services to consumers.[75]

5.2.2. Services outside the scope

The Regulation 2019/1150 precisely determines which services are not applicable.[76] This Regulation should not apply to online payment services, since they are rather inherently auxiliary to the transaction for the supply of goods and services to the consumers concerned.[77] Online advertising tools as well as online advertising exchanges, which are not provided with the aim of facilitating the initiation of direct transactions with consumers, should also not be covered by this Regulation. Furthermore, the introductory statement of the Regulation states that it should also not apply to search engine optimisation software services as well as services which revolve around advertising-blocking software. Technological functionalities and interfaces that merely connect hardware and applications should not be covered by this Regulation because they do not fulfil the requirements for online intermediation services. However, such functionalities or interfaces can be directly connected or ancillary to certain online intermediation services and where this is the case, they should be subject to transparency requirements.[78]

5.2.3. Obligatory legal relationships within the scope

One of the requirements that online intermediation services have to meet is the fact that they should be provided to business users on the basis of contractual relationships between the provider of those services and business users.[79] It is considered that a contractual relationship between the providers and business users which offer goods or services to consumers should exist if *"both parties concerned express their intention to be bound in an unequivocal manner on a durable medium, without an express written agreement necessarily being required."*[80] Therefore, the Regulation provides that it is a consensual and informal contract between a service provider and a business user, although that is stated only in the introductory statement of the Regulation. This Regulation should neither define the contract on online intermediation services and provision of search engine services nor specify the obligations of the parties arising from the concluded contract, i.e. it should not completely go into aspects of contract law. Therefore, provisions of national law should apply to obligatory legal relationship between service providers and users, in matters outside the scope of this Regulation.[81] Namely, the aim of this Regulation was not to arrange this contractual relation, but only to regulate the part which refers to ensuring fairness and transparency, that, as already mentioned, belongs to unfair competition law.

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[73] Ibid, § 11. introductory statement.
[74] Ibid, point 5, Art. 2(1)
[75] Ibid, § 4. introductory statement.
[76] Ibid, Art. 1(3)
[77] Ibid, § 11. introductory statement.
[78] Ibid.
[79] Ibid, point (c), Art. 2(2)
[80] Ibid, § 10. Introductory statement.
[81] Point 4, Art.1 of the Regulation provides as follows: "*This Regulation shall not affect national civil law, in particular contract law, such as the rules on the validity, formation, effects or termination of a contract, in so far as the national civil law rules are in conformity with Union law, and to the extent that the relevant aspects are not covered by this Regulation*."

This Regulation provides that the request for fairness and transparency should refer to the provider of online intermediation services, and the contract between a business user and a consumer doesn't have to be concluded, for online intermediation services to be covered by this Regulation. [82] Therefore, this Regulation should apply to the contractual relationship between a provider of online intermediation services and a business user, regardless of whether there is a contractual relationship between a business user and a consumer.

This Regulation should contain provisions that refer to the content of the contractual relationship (for example, necessary information in the general terms and conditions). In addition, this Regulation should also apply to the pre-contractual stage of the contractual relationship, to the behaviour during that relationship as well as to the period after termination of the contract. For example, this Regulation states that providers of online intermediation services shall ensure that their terms and conditions are easily available to business users in the pre-contractual stage of their commercial relationship.[83] Furthermore, this Regulation determines that providers of intermediation services shall include in their terms and conditions a description of the access to the information provided by the business user, which service providers maintain after the expiry of the contract.[84] Therefore, it can be concluded that this Regulation shall apply to practices before, during and after the concluded contract and to minimum content of contractual relationship, but only to aspects provided by this Regulation.[85] Mutual regulation of unfair contractual terms (which is covered in B2C relationships of the Directive 93/13) and unfair business practices (covered in B2C relationships of the Directive 2005/29), namely, the content and actions in B2B relationships in the law on unfair competition, is provided in the Directive (EU) 2019/633 on unfair commercial practices between companies in the agricultural and food supply chain.[86]

In relation to services of online search engine providers which rank websites, there is no need for a contractual relationship. Therefore, this Regulation should, in terms of those services, apply to the contractual and extra-contractual relationships. In other words, this Regulation provides that, even in the absence of a contractual relationship with corporate website users, providers of online search engines can behave unilaterally in a way that can be unfair and that can be harmful to the interests of corporate website users. [87] Thus, this Regulation should cover the contractual relationships between business subjects as well as the extra-contractual relationships to some extent, in which unfair business practices might occur, that can be harmful to the users' interests.

5.2.4. Transparency as an aspect of the principle of conscientiousness and fairness

The Regulation 2019/1150, as well as the Directives 93/13/EEC and 2005/29/EC, among other things, makes the principle of conscientiousness and fairness more concrete. Although there is no general clause which provides that principle, as in the Directives 93/13/EEC [88] and 2005/29/EC[89],

[82]Regulation 2019/1150, introductory statement, § 10.
[83] Ibid, § 14. and 18., point (b), Art. 3(1)
[84] Ibid, point (c), Art. 8(1)
[85] In B2C relationship Directive 2005/29 is also applied before, during and after the concluded contract, Art. 3 (1) of the Directive 2005/29.
[86] Art. 1(1) of the Directive (EU) 2019/633 provides that it should combat practices that grossly deviate from good commercial conduct that are contrary to good faith and fair dealing and that are unilaterally imposed by one trading partner on another. See more in M. Rodin, New theoretical assumptions of law against unfair competition, op. cit., chapter 4.2.6.2. Unfair commercial practices.
[87] Regulation 2019/1150, § 4. introductory statement.
[88] Art. 3(1) of the Directive 93/13/EEC provides as follows: *"A contractual term which has not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer*."
[89] A commercial practice is unfair: (a) if it is contrary to the requirements of professional diligence; and (b) if it materially distorts or is likely to materially distort the economic behaviour with regard to the product of the average consumer whom it reaches or to whom it is addressed, or of the average member of the group when a commercial

the principle of conscientiousness and fairness is mentioned in Article 8 of the Regulation, from which it is apparent that the Regulation should ensure that contractual relations between providers of online intermediation services and business users are conducted in good faith and based on fair dealing. The principle of conscientiousness and fairness refers to the duty of conscientious and fair dealing in establishing obligatory relationships and exercise of the rights and obligations of those relationships.[90] That principle requires that, not only one's own interests have to be taken into account, but one should act in accordance with the other party as well.[91] One of the functions of the principle of conscientiousness and fairness is an additional function which implies the imposition of special duties apart from the main duty, and could fall within the duty of information provision.[92] The Regulation 2019/1150 mostly imposes positive duties to providers of online intermediation services designated as: "*any natural or legal person which provides, or which offers to provide, online intermediation services to business users*"[93] , and to providers of online search engines designated as: "*any natural or legal person which provides, or which offers to provide, online search engines to consumers.*"[94] As the Regulation provides, they have to act in a transparent way by following the principles of simplicity, intelligibility, easy accessibility, timeliness and completeness. This refers to the aspect of the principle of conscientiousness and fairness because it contributes to openness, honesty and successful cooperation at the moment of entering into the contractual relationship, during that relationship and after the expiry of the contract. Those are mostly positive duties in terms of business conditions, suspension and termination of business relation, online ranking of business users, different actions towards business users, data access, restricting the offer through other means.

Estimated effect of the Regulation is preventive. This results from paragraphs § 2 and 6 of the introductory statement which discusses potentially unfair and harmful business practices.[95] Therefore, in relation to the existing regulations in the field of unfair competition which ban unfair business practices, this Regulation should not ban misleading claims or omissions and other unfair practices, but impose positive duties to online platforms in order to avoid unfair business practices. The exception to this can be found in point (a) of the Article 8(1) which states that the providers of online intermediation services mustn't impose retroactive changes to terms and conditions.

5.2.5. Types of unfair business practices between the online platforms and business users

The regulation does not identify specific types of unfair practices and does not give them a specific name, as is the case with unfair B2C business practices, unfair commercial food chain practices, unfair marketing practices for which there is a regulatory initiative. Examples of potentially harmful business practices in the Regulation proposal[96] are: *"unexplained changes in the terms of use of the service without prior notification, withdrawal of goods or services from the offer and suspension of accounts without clearly stating reasons, lack of transparency related to the order of goods and services and the companies which offer them; unclear conditions of access and use of data collected by service providers, lack of transparency in favouring the competitive services of the service providers themselves, and the so-called most favoured nation clauses that limit the*

practice is directed to a particular group of consumers. Pursuant to point (h) of Art. 2. „professional diligence" means the standard of special skill and care which a trader may reasonably be expected to exercise towards consumers, commensurate with honest market practice and/or the general principle of good faith in the trader's field of activity.

[90] Art. 4 of the Civil Obligations Act (Official Gazette 35/05, 41/08, 125/11, 78/15, 29/18).

[91] V. Tomljenović, S. Petrić, E. Mišćenić, Unfair contract terms, European standards and Croatian implementation, Faculty of Law of the University of Rijeka, Rijeka, 2013.

[92] For remaining functions, : V. Gorenc, Komentar Zakona o obveznim odnosima, RRIF, Zagreb, 2005, p. 9. and 10.

[93] Regulation 2019/1150, point 3 of Art. 2 (1).

[94] Ibid, point 6 of Art. 2(1).

[95] But, unfair practices have already been seen in practice, e.g. see: Communication from the Commision to the European Parliament, the Council, the European economic and social Committee and the Committee of the regions, Online Platforms and the Digital Single Market, Opportunities and Challenges for Europe, op. cit., p. 9.

[96] Point 1 of the explanation.

ability of businesses to offer more attractive terms through channels other than the online intermediation service. "

Furthermore, there are problems related to general search engines, which can also affect the commercial success of users of corporate online sites, i.e. those who supply their goods or services online in the internal market. The problem is that search engine providers determine the ranking of websites, including pages through which businesses offer their goods and services to consumers. Therefore, search engines have an important influence on consumer choice and thus on the commercial success of these corporate web site users.[97]

Any prohibition of dishonest dealing implies a duty of fair dealing and vice versa. The decree acts as an introduction to stipulation of transparent business rather than an imposition of prohibitions on unfair practices.

In general, the Regulation introduces the principles of simplicity, intelligibility, easy accessibility, timeliness. These principles are prescriptive in relation to the terms of use of the online intermediation service providers[98] and to descriptions of parameters that those providers need to determine in the process of ranking the online search engines.[99] Furthermore, the Regulation prescribes minimum information requirements to be included in these acts,[100] including the terms of use of the online search engine providers[101]. The Regulation also stipulates the obligation of the online platforms to inform users on a durable medium of changes in terms of use, restrictions, suspensions or discontinuation of services[102], the right of business users to terminate the service [103] including the right to be properly informed about the access to information provided by business users and consumers .[104]

The legal consequence of non-compliance with the prescribed obligations in respect to the conditions of use is the absolute nullity of the conditions of use or of its individual provisions[105]. Finally, an online intermediation service provider needs to ensure the visibility of the identity of a business user. [106]

In the following pages we will depict and analyse the prescribed solutions to counteract targeted unfair practices.

5.2.5.1. Unexplained changes to the Terms of Service without prior notice

Providers of online intermediation services are required to provide notice on a durable medium of any proposed changes to their terms of use. A notice period is introduced, and it has a delayed

[97] Regulation 2019/1150, introductory statement, § 24.
[98] Ibid, Art. 3.
[99] Ibid, Art. 5(2)
[100] According to points (c-e) of Article 3(1) of the Regulation 2019/1150 the terms of use of the online business mediation should include reasons for decisions to suspend, terminate or otherwise restrict, in part or in whole, the provision of their online business services to business users; information on additional distribution channels and potentially related programs through which online business mediation services place goods and services offered by business users on the market; general information on the effects of terms of use on the ownership and control of intellectual property rights of business users.
[101] According to Article 7(2 and 3) of the Regulation 2019/1150 search engine providers, in their terms of use, provide a description of different practices, access to personal or other user and consumer data, a description of rankings or other settings applied by the provider that affect consumer's access to the goods or services offered by other users; a description of any direct or indirect fee charged for the use of the online intermediation services or search engines and for the use of services or functionality or technical interfaces.
[102] Regulation 2019/1150, Art. 3(2) and Art. 4(1 and 2).
[103] Ibid, point b, Art. 8.
[104] Ibid, Art. 9.
[105] Ibid, Art. 3(3).
[106] Ibid, Art. 3(5).

effect on the application of the proposed amendments. It lasts for at least 15 days in which the business user has the right to terminate the contract with the service provider before the expiry of this period, and the termination takes effect within 15 days from the receipt of the notice of the proposed changes. The business user may also waive the notice period, either explicitly or tacitly. Tacit waiver is considered to be the offering of new goods or services through online intermediation services, with the exception of a deadline exceeding 15 days.[107] The notice period is not applied only in exceptional situations.[108] The legal consequence of non-compliance with the prescribed obligations is the nullity of changes to the conditions of use.[109]

5.2.5.2. Withdrawal of goods or services from the offer and suspension of the account without clearly stating the reasons

Provider of online intermediation services is required to provide on a durable medium a statement of reasons for limiting or suspending the online intermediation services before or at the time of the restriction or suspension.[110]. Only exceptionally a statement of reasons is not required. [111] In the event of complete termination of the provision of the online intermediation services, the notice period for providing the statement of reasons shall be 30 days before the termination takes effect, with the provided exceptions.[112] In all cases, the right of the business user to clarify the facts and circumstances of the internal complaints procedure is introduced. If a service provider revokes a restriction, suspension or termination, he/she is obliged to provide the service again to the business user without undue delay.[113]

5.2.5.3. The lack of transparency associated with the order of goods and services and the companies that offer them

In addition to providers of online intermediation services, ranking provisions apply to providers of search engines who are required to determine the most important parameters for determining ranking and the reasons for these parameters. The providers of online intermediation services determine them in their terms of use while the providers of search engines establish them in an up-to-date, easily and publicly available description on search engines, compiled in a simple and understandable language[114]. Where direct or indirect payment is possible to influence the

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[107] Ibid, Art. 3(2).

[108] According to Article 3(4) of the Regulation 2019/1150 the notice period shall not apply where a provider of online intermediation services: *"(a) is subject to a legal or regulatory obligation under which it is obliged to discontinue the provision of the online intermediation services to a particular business user where compliance with that notice is impossible; or (b) exercises its right of termination on imperative grounds of national law which is in conformity with Union law; (c) can prove that the business user has repeatedly breached the valid conditions of use, resulting in the termination of the provision of the relevant online mediation services in full. "*

[109] Regulation 2019/1150, Art. 3(3).

[110] According to Article 4(5) of the Regulation the statement of reasons includes: „*a reference to the specific facts or circumstances, including contents of third party notifications, that led to the decision of the provider of online intermediation services, as well as a reference to the applicable grounds for that decision referred to in point (c) of Article 3(1)."*

[111] According to Article 4(5) of the Regulation the online mediation service provider need not provide a statement of reasons if: *"it is subject to a legal or regulatory obligation not to provide the specific facts or circumstances or the reference to the applicable ground or grounds, or where a provider of online intermediation services can demonstrate that the business user concerned has repeatedly infringed the applicable terms and conditions, resulting in termination of the provision of the whole of the online intermediation services in question."*

[112] Article 4(4) of the Regulation 2019/1150 provides that the notice period does not apply if the online intermediation service provider: *"(a) is subject to a legal or regulatory obligation which requires it to terminate the provision of the whole of its online intermediation services to a given business user in a manner which does not allow it to respect that notice period; or (b) exercises a right of termination under an imperative reason pursuant to national law which is in compliance with Union law; (c)can demonstrate that the business user concerned has repeatedly infringed the applicable terms and conditions, resulting in the termination of the provision of the whole of the online intermediation services in question. "*

[113] Regulation 2019/1150, Art. 4(3).

[114] Ibid, Art. 1 and 2.

ranking, the provider is required to describe both such options and the effects of such rank. [115] The descriptions provided must clarify whether the ranking mechanism has, and to what extent, taken into account the features of the goods and services, the relevance of these features to consumers, and relating to search engines, the design features of web pages.[116] When a ranking is changed or a particular website is removed from search results after a third party notification, the service provider offers the corporate website user the possibility to view the content of the notification.[117]

The Regulation does not require providers to disclose algorithms or information that could be used to manipulate the search results, or to disclose business secrets as per Directive 2016/943 on trade secrets.[118]

Accordingly, the lack of transparency associated with the ranking is eliminated by imposing the necessity to describe the reasons for ranking. This will encourage the online platforms to define the terms for ranking. However, there is no ban on unfair business practices (e.g. ranking against established parameters) or sanctions in case the online platforms fail to meet the prescribed conditions. Nonetheless, the Commission has committed to adopt accompanying guidelines to achieve harmonization and transparency.[119]

5.2.5.4. The lack of transparency in giving preference to competing services providers

The introductory part of the Regulation recognizes the risks of unfair competition when a provider directly competes with its non-controlled customers in relation to certain goods and services in such a way that it can use its control to give technical or economic advantage to its tenders or tenders of users under their control. [120] However, the Regulation does not prohibit giving unfair advantage to the proprietary services of the providers of online intermediation services and providers of search engines over the services of users, but imposes obligations on providers to describe different practices in their terms of use. [121] The Regulation specifies which descriptions should be included.[122] However, no specific legal consequences are foreseen and there is no warranty that transparency will ensure fair and equal treatment between the providers of these services and users.

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[115] Ibid, Art. 5(3).
[116] Ibid, Art. 5(5).
[117] Ibid, Art. 5(4).
[118] Ibid, Art. 5(6).
[119] Ibid, Art. 5(7).
[120] Ibid, introductory statement, § 30 and 30.
[121] See Regulation 2019/1180, Art.7(1 and 2)
[122] According to Article 7(3) of the Regulation 2019/1150 if applicable, the descriptions particularly include: "various actions by way of specific measures taken by an online intermediation service provider or online search engine provider relating to any of the following:

(a) access that the provider, or that the business users or corporate website users which that provider controls, may have to any personal data or other data, or both, which business users, corporate website users or consumers provide for the use of the online intermediation services or the online search engines concerned or which are generated through the provision of those services;

(b) ranking or other settings applied by the provider that influence consumer access to goods or services offered through those online intermediation services by other business users or through those online search engines by other corporate website users;

(c) any direct or indirect remuneration charged for the use of the online intermediation services or online search engines concerned;

(d) access to, conditions for, or any direct or indirect remuneration charged for the use of services or functionalities, or technical interfaces, that are relevant to the business user or the corporate website user and that are directly connected or ancillary to utilising the online intermediation services or online search engines concerned.

5.2.5.5. Prohibition of imposing retroactive changes to terms and conditions

The Regulation governs this action in a manner customary to the Unfair Competition Law. Namely, prohibition is imposed on retroactive changes to terms and conditions and is drawn from the principle of good faith and fair trading.[123] The exceptions to this prohibition are only applied if they are necessary to comply with a specific legal or regulatory obligation or when retroactive changes are beneficial to business users. These provisions do not contain a specifically prescribed legal consequence in the case of non-compliance with this prohibition.

5.2.5.6. Nontransparent requirements for access to and use of data collected by service providers

Referring to this action, the Regulation, by requiring transparency, seeks to prevent fraudulent and unauthorized data use, including personal data, in such a way as to impose an obligation on providers of online intermediation services to include in their terms and conditions a description of the technical and contractual access, or absence thereof, of business users and consumers to any personal data.[124] The Regulation contains a minimum list of these descriptions.[125] There is also no specific legal consequence in the case of failure to comply with the prescribed rules.[126]

5.2.5.7. Restrictions to offer different conditions through other means

Even with reference to this action, the Regulation does not prohibit unfair restrictions imposed on users to offer more attractive conditions through other means. The Regulation only imposes an obligation on providers of online intermediation services to include the grounds for the restriction on the ability of business users to offer the same goods and services to consumers under different conditions through other means. Those gounds must include the main economic, commercial or legal considerations.[127]Prescriptive descriptions appear to be general and vague and provide justification for online platforms to impose restrictions, without guaranteeing that this standard will prevent potential unfair practices. Since such restrictions may be prohibited by the application of other acts, e.g. Act on competition rules when other conditions are fulfilled, the Regulation stipulates that these obligations do not affect prohibitions or restrictions prescribed by other acts.[128]

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[123] Regulation 2019/1180, point (a) of Art. 8 and introductory statement § 32.

[124] Ibid, Art. 9(1)

[125] Art. 9(2) of the Regulation 2019/1150 provides as follows: *"providers of online intermediation services shall adequately inform business users in particular of the following:*

(a) whether the provider of online intermediation services has access to personal data or other data, or both, which business users or consumers provide for the use of those services or which are generated through the provision of those services, and if so, to which categories of such data and under what conditions;

(b) whether a business user has access to personal data or other data, or both, provided by that business user in connection to the business user's use of the online intermediation services concerned or generated through the provision of those services to that business user and the consumers of the business user's goods or services, and if so, to which categories of such data and under what conditions;

(c) in addition to point (b), whether a business user has access to personal data or other data, or both, including in aggregated form, provided by or generated through the provision of the online intermediation services to all of the business users and consumers thereof, and if so, to which categories of such data and under what conditions; and

(d) whether any data under point (a) is provided to third parties, along with, where the provision of such data to third parties is not necessary for the proper functioning of the online intermediation services, information specifying the purpose of such data sharing, as well as possibilities for business users to opt out from that data sharing."

[126] The application of the Regulation 2019/1150, according to Art. 9(3), does not affect the application of Regulation (EU) 2016/679 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, Directive (EU) 2016/680 on the protection of natural persons with regard to the processing of personal data by competent authorities for the purposes of the prevention, investigation, detection or prosecution of criminal offences or the execution of criminal penalties, and on the free movement of such data i Directive 2002/58/EC on privacy and electronic communications.

[127] Regulation 2019/1150, Art. 10 (1).

[128] Ibid, Art. 10 (2).

6. Implementation of rules

Rules and regulations, established in the Union unfair competition law, stipulate the enforcement in a different way.[129] This Regulation, contrary to previous rules and regulations, places the greatest emphasis on self-regulatory protection ensured through the internal system for handling the complaints of business users established by providers of online intermediation services and implementation of codes of conduct as well as mediation that providers of online intermediation services, with the exception of small enterprises, are required to apply.[130] The Regulation also provides for civil-law protection, namely collective protection. Although no specific provisions on individual protection are included, it is explicitely stated that taking a collective legal action does not affect the rights of business users and corporate website users to start any legal action on an individual basis.[131] The Regulation does not contain any provisions on public-law enforcement. However, the European Commission shall closely monitor the impact of this Regulation by conducting an evaluation of compliance with the obligations, effectiveness of the Regulation and any potential needs for further regulation every three years. Also, Member States shall lay down the rules setting out the measures applicable to infringements of this Regulation and shall ensure that they are implemented. The measures provided for shall be effective, proportionate and dissuasive.[132] Accordingly, the Regulation contains minimum provisions on enforcement.

The Regulation stipulates an obligation for providers of online intermediation services to have an internal complaint-handling system. It is considered to be faster, more flexible and more effective legal protection.[133] In any case, it does not prevent any judicial protection.[134] It is based on principles of transparency and equal treatment applied to equivalent situations.[135] It should therefore be easily accessible, free of charge, effective and swift and allow business users to lodge complaints directly regarding any issues raised[136] as well as to receive information on the outcome individually in a simple and comprehensible language.[137] Providers of online intermediation services shall establish and make easily available to the public information on the functioning and effectiveness of their internal complaint-handling system including the total number of complaints lodged, the main types of complaints, the average time period needed to process the complaints and aggregated information regarding the outcome of the complaints.[138]

Mediation is seen as an alternative to potential lengthy and costly judicial proceedings[139] although it shall not affect the providers of online intermediation services and business users to initiate judicial proceedings at any time before, during or after the mediation process.[140] Providers of online intermediation services shall identify in their terms and conditions two or more mediators

[129]Directive 2005/29/EC concerning unfair business practices provides collective protection (Art. 11(1)), public law (javnopravnu) enforcement ensured by governing bodies (Art. 11(2 and 3)) and does not exclude self-regulatory enforcement (Art. 10), the same as Directive 2006/114/EC concerning misleading and comparative advertising (Art. 5 and 6). Directive (EU) 2016/943 on trade secrets stipulates individual enhancement (chapter III), Directive (EU) 2019/633 on unfair trading practices in the agricultural and food supply chain provides for public law enforcement (Art. 4 - 6) and promotion of mediation (Art. 7).
[130] Ibid, Art. 11(5) and Art. 12(7).
[131] Ibid, Art. 14(9).
[132] Ibid, Art. 15(1 and 2).
[133] Ibid, introductory statement, § 37 and 38.
[134] Ibid, § 37.
[135] Ibid, § 37 and Art. 11(1).
[136] According to Art. 11(1) of the Regulation 2019/1150, the issues relate to: *"(a) alleged non-compliance by that provider with any obligations laid down in this Regulation which affects the business user lodging the complaint ('the complainant'); (b) technological issues which relate directly to the provision of online intermediation services, and which affect the complainant;(c) measures taken by, or behaviour of, that provider which relate directly to the provision of the online intermediation services, and which affect the complainant."*
[137] Regulation 2019/1150 Art. 11(2), point (c).
[138] Ibid, Art.11(4).
[139] Ibid, § 40.
[140] Ibid, Art. 12(5).

with which they are willing to engage to attempt to reach an agreement with business users on the settlement, out of court, of any disputes between the provider and the business user arising in relation to the provision of the online intermediation services concerned, including complaints that could not be resolved by means of the internal complaint-handling system.[141] According to the Regulation, the mediators shall meet the following criteria: they should be impartial, independent, their services affordable, they should possess knowledge of the language of the terms and conditions and be easily accessible either physically or remotely using communication technologies, they should be capable of providing services without delay and of understanding general commercial relations between business subjects.[142] With reference to the total costs, providers of online intermediation services shall bear a reasonable proportion, on the basis of a suggestion by the mediator, in particular by taking into account the relative merits of the claims of the parties to the dispute, the conduct of the parties, as well as the size and financial strength of the parties.[143]The Commission shall encourage providers of online intermediation services to set up one or more organisations providing specialized mediation services.[144]

Furthermore, it also provides for collective protection, i.e. judicial proceedings initiated by organizations and associations that have a legitimate interest in representing users and public bodies set up in Member States. In these proceedings, the above mentioned subjects shall have the right to stop or prohibit any non-compliance by providers of online intermediation services or by providers of online search engines, with the relevant requirements laid down in this Regulation, in accordance with the national law of the Member State concerned.[145]

Collective protection does not prevent the individual protection of business users or corporate website users, i.e. their rights to start any action before competent national courts in accordance with the rules of the law of the Member State where the action is brought, to settle disputes arising in relation to the non-compliance by providers of online intermediation services with the relevant requirements laid down in this Regulation. The rules regarding these procedures are established by national laws.[146] Under Croatian law, business subjects could bring an action for compensation according to the general rules of mandatory law, however they are not granted the right to require the cessation or prohibition of practices that are detrimental to them or could harm their interests contrary to the Regulation.
Moreover, the Commission shall encourage the drawing up of codes of conduct intended to contribute to the proper application of this Regulation and shall particularly encourage the providers of online intermediation services to implement sector-specific codes of conduct.[147]

7. Conclusion

The principles of simplicity and comprehensibility of general conditions, as well as their additional duty to inform, have long been part of consumer protection rights.[148] However, these rules are a novelty in the law of unfair competition in B2B relationships.[149] Similarly to consumer protection, the Regulation seeks to balance the position of the contracting parties in relation to the information

[141] Ibid, Art. 12(1).
[142] Ibid, Art. 12(2).
[143] Ibid, Art. 12(4).
[144] Ibid, Art. 13.
[145] Ibid, Art. 14.
[146] Ibid, Art. 14(9).
[147] Ibid, Art. 17.
[136] See, for example, Art. 5. Directive 93/13 / EEC and the judgment of the Court of Justice of the EU C-186/16 - Andriciuc and Others of 20.9.2017, ECLI: EU: C: 2017: 703.
[149] Article 169 (1) TFEU provides that "*the Union shall contribute to the protection of the health, safety and economic interests of consumers, as well as to the promotion of their right to information, education and organization for the protection of their interests.*"

available to them when making a business decision and during a contractual relationship. Furthermore, it seeks to achieve a balance in the negotiating power of online platforms and users, as well as a balance of relationships in general, all this should lead to diminished market and economic power of users and their dependence on doing business with an online platform.[150] The Regulation also mentions users' fear of retaliation because of the dependancy relationship, [151]the so-called *fear factor*.

Although businesses, as opposed to consumers, are professionals who should have a sufficient level of knowledge and diligence, there is a growing need to protect SMEs as weaker market players. This Regulation does not introduce special protection for SMEs, but it clearly aims to protect weaker business entities by binding their stronger partners to a duty of transparency, timely and complete notification to make an informed and deliberate decision for their users, and, as the Regulation emphasizes, the aim of which is to ensure contractual relations in good faith and on the basis of fair dealing.[152] In doing so, the protection of weaker market players is gradually being extended and strengthened with respect to businesses as well, in order to indirectly protect SMEs in the first place, similarly to consumers.

But the question is whether the Regulation will succeed in achieving its goal and prevent unfair practices of online platforms towards weaker users.

Namely, the strictly prescribed duties of transparent action ensure that the user is aware of the provider's business rules, but does not guarantee that the rules will be fair and that the provider will interpret and apply them in accordance with the principle of conscientiousness and fairness. Therefore, apart from achieving transparency that undoubtedly contributes to less recourse to unfair practices due to lack of rules, it is questionable how much the Regulation actually ensures the implementation of the principles of conscientiousness and fairness in other aspects, as well as other fundamental principles applicable in the Law on unfair competition, such as the principle of equality. prohibition of causing harm, equal value of acts and prohibition of abuse of rights. Therefore, the Regulation has a limited scope in battling unfair business practices.[153] The provisions of the Regulation 2019/1150 are not flexible and cannot cover all current or possible new unfair business practices and contractual provisions arising from the development of the digital market. In particular, a general clause is missing - general prohibition of unfair practices that would serve as a safety net that could cover all unfair practices that may arise in P2B relationships. In this sense, the Regulation, in addition to the prescribed positive obligations as a minimum list of acts (the so-called gray list), missed the opportunity to generally prohibit all actions/practices and contractual provisions allowing online platforms to violate professional due diligence.[154] Professional due diligence should include the duty of online platforms to act in accordance with the ability and diligence of professionals, and the duty to act in accordance with all fundamental legal principles. One of the conditions is that the economic behaviour of a user is significantly impaired by the use of due diligence. In other words, in the absence of a contractual

[150] Regulation 2019/1150, introductory statement, § 2 states that there is an increased dependency of users, especially SMEs, on online platforms for access to consumers. Greater negotiating power, in practice, is thought to allow online platforms to act unilaterally in a manner that may be unfair and damaging for the legitimate interests of their business users. Furthermore, online platforms could unilaterally impose on business users practices that deviate significantly from good business manners or are contrary to the principle of good faith and fair dealing.
[151] Ibid, § 5. and 44.
[152] Ibid, Article 8
[153] A. de Streel, Online Intermediation Platforms and Fairness: An assessment of the recent Commission Proposal, already cited., pages. 20. and 21 who adds that transparency solves some problems of information asymmetry but not the problems of market power and dependency.
[154] For example in B2C relations under Art. 2 point h, professional attention means: "a standard of special skill and attention that is reasonably expected of a trader in relation to consumers, in proportion with fair market practice and / or the general principle of good faith in the trader's area of activity."

relationship (such as in the case of online search engine services) it is necessary to prohibit acts that may objectively or very likely cause harm to the economic interests of users by violating professional diligemce. Certainly, with the application of the principle of equality in order to prevent excessive restrictions of the freedom of entrepreneurship. The Regulation already recognizes that this area is incomplete and may not be adequately addressed, so Art. 18 (2) leaves room for further rules.

In relation to implementation, it has been missed to define in greater detail, at Union level, uniform rules on individual protection as well as the protection of public law. Although the Commission has had the obligation to evaluate the implementation of the Regulation, it has not been given any authority to impose sanctions or co-operate with national authorities in order to remove identified discrepancies.

The final thing, but not less important for the Law on unfair competition is the novelty that this area is regulated by a regulation rather than a directive, and, after the Directive 2019/633 (potentially unfair) procedures or practices, are being regulated again as well as (potentially unfair) contractual provisions.

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FACTORS THAT EXPLAIN ENTREPRENEURIAL FAILURE OF MOROCCAN SMES, AN EXPLORATORY STUDY

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Abstract
The entrepreneurial failure of SMEs involves considerable socio-economic consequences. Yet entrepreneurship research has focused particularly on the success factors of SMEs without further highlighting the multiple factors of their failure. By adopting a multidimensional perspective of entrepreneurial failure, the objective of this article is to contribute to the study of this phenomenon in the Moroccan context. We conducted a qualitative analysis of academic research and public and private surveys, in order to explore and contextualize the factors of the entrepreneurial failure of Moroccan SMEs. The results reveal that the essential determinants of the entrepreneurial failure of the Moroccan SME are its organizational and managerial specificity, the role and profile of its entrepreneur and the constraints imposed by its macroeconomic and institutional environment, as well as the competitive forces of its industry and the external financing of its activity.

Keywords: *Entrepreneurial Failure, Morocco, SME Entrepreneur, SME External Environment, Specificity of SME*

Track: *Entrepreneurship*

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1. Introduction

Failure is a dynamic, multidimensional and complex issue. It has aroused the interest of researchers and practitioners since the 1929 crisis. Some authors judge it from the discontinuity of entrepreneurial activity (Singh, Corner & Pavlovich, 2007), others appreciate it on the basis of the company's economic failure.

While SMEs are experiencing alarming failure rates, entrepreneurship research has paradoxically focused more on success factors than on recent failure factors (Smida & Khelil, 2010). In addition, existing studies have instead used predictive models of economic or financial factors for failure (eg Abdullah, Ahmad, Zainudin, & Rus, 2016; Altman, 1968; Beaver, 1966) and have hardly integrated those linked to the specificities of the SME and its environment.

In Morocco, the rate of SMEs failure is enormous (eg. More than 8000 SMEs went bankrupt in 2017 according to FRISK), without however drawing enough attention from academic researchers. Indeed, very little research has focused on identifying the causes of the failure of Moroccan SMEs from a global and integrative perspective. In addition, reports from public bodies often simply list the weaknesses of SMEs without explaining how they can cause their failure.
Based on these observations, the objective of this article is to contribute to the study of the phenomenon of entrepreneurial failure of SMEs in the Moroccan context.
We have adopted a multidimensional perspective of failure that considers both endogenous and exogenous factors. Through a qualitative analysis of secondary data on the failure of Moroccan

SMEs (academic articles and private and public surveys), we tried to answer the following question: "What are the factors of entrepreneurial failure of Moroccan SMEs? ".
Our research is exploratory and descriptive, the aim is to bring together in a single analytical framework the different factors of entrepreneurial failure of Moroccan SMEs.

Our work is structured as follows: First, we start with a literature review around the concept of entrepreneurial failure and the explanatory factors of entrepreneurial failure of SMEs. In a second step, we will present and discuss the results of the main studies relating to the entrepreneurial failure of Moroccan SMEs. Finally, the limits and perspectives of this work will be developed in conclusion.

2. Literature review

2.1. Defining Entrepreneurial failure

Entrepreneurial failure is a vague, polysemic and multidisciplinary concept. To describe it, the authors use different terminologies such as business death, termination, bankruptcy, insolvency or closure (G. Beaver, 2003). Even if these terminologies may appear synonymous, confusion in their meanings prevents the emergence of a consensual definition of entrepreneurial failure (G. Beaver, 2003; Mellahi & Wilkinson, 2004). From an academic point of view, each author apprehends failure according to his research subject and the theoretical approach used (Smida & Khelil, 2010). Entrepreneurial failure occurs when the business becomes insolvent, ceases to operate, and liquidates assets to pay creditors. Entrepreneurship research has generally used more specific criteria to define failure, and a literature review highlights at least four main definitions that approach entrepreneurial failure differently (J. Watson & Everett, 1993).
The first refers to the discontinuity of the business for any reason. In this situation, the company's resources are reallocated to more profitable alternative opportunities (J. Watson & Everett, 1993). This may include businesses sold by their owners who wish to retire due to age or health considerations; businesses sold to make a profit or those sold because the owner simply wants to start another activity (Fredland & Morris, 1976). The discontinuity is sometimes due to a change of owner and of the management method (Mitchell, 1994) or a voluntary closure of the business (Cardozo & Borchert, 2003).
The second is the sale or liquidation of the business to prevent further losses (Ulmer & Nielsen, 1974). The company is prepared to close its doors to avoid further future losses that may affect the owner's capital. Therefore, a business could be considered to have failed, even if there was no loss to the creditors.
For the third definition, entrepreneurial failure means the inability to make the business profitable (Cochran, 1981). According to this definition, companies fail when their rate of return on invested capital is significantly lower than the rates prevailing on similar investments, or do not meet other profitability objectives set by the owner (Altman, 1968; Cochran, 1981).
Finally, the fourth definition concerns bankruptcy or loss for creditors (Dun & Bradstreet, 1979; Massel, 1978). Failure occurs when the business that is bankrupt ceases to operate and creates losses for creditors. Bankruptcy can be triggered by legal actions, or by voluntary compromises with creditors.

2.2 SMEs' failure factors

The factors of entrepreneurial failure of SMEs are very numerous and difficult to define. Their relative importance will depend on the specificities of the SME and the characteristics of its environment. They are therefore both endogenous and exogenous.

2.2.1 Internal factors of SME's failure:

a- Age

According to several studies, young SMEs are systematically at the greatest risk of failure (N. A. H. Abdullah et al., 2016; Everett & Watson, 1998; Honjo, 2000; Mellahi & Wilkinson, 2004; John Watson, 2007). This is due to the fact that they have less experience and less social capital. They are also forced to bear high costs during their organizational learning processes to create organizational routines (Mellahi & Wilkinson, 2004), efficient management structures (Freeman, Carroll, & Hannan, 1983) and to quickly install some organizational stability (Freeman & Hannan, 1989).

b- Size

Generally, SMEs start out small and are burdened with an inherent size disadvantage. The small size of SMEs does not allow them to cover their fixed costs, which can sometimes force them to leave their sector of activity (G. C. Hall & Tu, 2004). Actually, there is a positive relationship between the size of the SME and its performance in terms of growth, profitability, survival and internationalization (Campbell, Heriot, Jauregui, & Mitchell, 2012; D. A. Williams, 2016). The increase in the size of SMEs is a factor in reducing the mortality rate according to Mellahi & Wilkinson (2004).

c- Organizational structure

The establishment of an inadequate organizational structure negatively affects the survival of the SME (P. L. Jennings & Beaver, 1995). Such a structure includes a set of constraints such as the absence of a clear division of labor, the low efficiency of internal and external communication, the predominance of control, the lack of organizational flexibility due to its mechanistic nature and the poorly structured work procedures (PL Jennings & Beaver, 1995; Temtime & Pansiri, 2004).

d- Management skills

In order to reduce operating costs, some SMEs' owners tend to manage multiple operational activities on their own and by themselves (Tushabomwe-Kazooba, 2006). If they do not have proven managerial competence, the risks of failure become very high. According to Khan & Rocha (1982), SMEs face problems meeting managerial expertise criteria in four main functional areas, namely marketing, accounting, inventory management and cash flow management. In particular, Jennings & Beaver (1997) discuss the lack of quality management practices as another major cause of the failure of SMEs.

e- Marketing skills

Requirements for a successful marketing of SMEs are inherently different from those of large companies. Hall (1992) explicitly considers that the adoption of an ineffective marketing strategy is a cause of the failure of SMEs. Ropega (2011) points out that among the marketing errors most committed by SMEs, there is an offer that is inappropriate to market needs, and an inappropriate pricing policy that does not reconcile the real cost structure with the perceived value of the offer and prices charged by direct or indirect competition. The situation worsens with the lack of recourse to market research, demand forecasting and commercial promotion activities for products (Temtime & Pansiri, 2004).

f- Financial management skills

Several authors have linked the entrepreneurial failure of SMEs to the ineffectiveness of their financial management (Bruno, Mcquarrie, & Torgrimson, 1992; Ropega, 2011). Lack of managerial skills in the financial field, including accounting, inventory control and cash flow management, can jeopardize the chances of survival of SMEs (Khan & Rocha, 1982). For Temtime & Pansiri (2004), poor management of working capital explains the failure of SMEs. Specifically, these are credit and overdraft management issues, poor inventory and liquidity management. Tushabomwe-Kazooba (2006) adds that overinvestment, especially in fixed assets, for personal considerations of the manager leads to the collapse of many SMEs.

g- The owner's skills

The personality traits and behaviors of owner-managers have been mentioned by some authors to explain the entrepreneurial failure of SMEs (Gaskill, Van Auken, & Manning, 1993). The owner-managers of SMEs show less initiative, dynamism, enthusiasm and entrepreneurial orientation. Also, entrepreneurs in SMEs are often unable to separate social capital from personal capital and resort to recruiting family members despite their inexperience (Tushabomwe-Kazooba, 2006).

2.2.2 External factors of SME's failure

According to the theory of organizational ecology (Hannan & Freeman, 1977), failure depends more on the evolution of the environment in which the company operates. This means that the macroeconomic context, the political and institutional environment and the market or industrial conditions can strongly determine the entrepreneurial failure of SMEs.

a- The global economic context

According to the literature, the factors for the failure of SMEs in the economic context are very varied. Interest rates and the unemployment rate are the main determinants of what could be considered forced default (Everett & Watson, 1998). Other factors are also to be considered, especially those relating to the economic policies of the country leading, for example, to the variety of taxes, high tax rates, rampant inflation, and unsuitable regulations or deregulation for certain industries. (Ihua & Siyanbola, 2012; Tushabomwe-Kazooba, 2006). Temtime & Pansiri (2004) also discuss exchange rates, the size of the internal market, the purchasing power of customers, limited access to new technologies, market policy, fiscal policy and price control measures. The economic recession, the tight labor market, the high cost of labor (Ropega, 2011) and unfair competition from the public sector, large companies and imports (Edmunds, 1979), are also factors that can negatively affect SMEs. uncontrollable economic factors causing the failure of SMEs.

b- Access to external financial resources

Most SMEs find it difficult to obtain external funding. Often, the entrepreneur is forced to mobilize personal savings, the income generated during the operating cycle (Liao, Welsch, & Moutray, 2009) or even "love money" financing. This situation perpetuates the inability of the SME to honor its financial commitments, that is to say, no longer being able to repay its current liabilities with its available assets. As a result, its financial structure is affected, which leads it to critical levels of solvency (Cultrera, 2016) and an obligation to declare bankruptcy (Honjo, 2000).

c- The institutional environment

The absence, insufficiency or inadequacy of government institutional support are the problems that SMEs often encounter in many countries, especially those in the process of development (Gagoitseope & Pansiri, 2012). In this sense, the failure of SMEs has its origins in the long duration of the procedures for obtaining public funding, the insufficiency of financial support, the poor orientation of public aid (Ropega, 2011), and the lack of specific training, advisory and support programs for SMEs (Everett & Watson, 1998).

d- Industry or market conditions

Besides the role of the political and institutional environment, the survival of the SME may be threatened by an unfavorable situation in the industry. Weak industry dynamism does not offer growth potential for SMEs. In the extreme case, the risk of failure may be higher than the chances of success in a fast-growing or highly competitive industry, since market conditions in such an industry can be turbulent (Honjo, 2000) . Turbulence implies uncertainty and therefore difficulties in forecasting and making strategic decisions (Mellahi & Wilkinson, 2004).

Ultimately, the literature review reveals three types of entrepreneurial failure factors for SMEs: the external environment, the specific managerial and organizational aspects and the entrepreneur. These factors are not independent and can interact perfectly. The factors of failure linked to the external environment influence those relating to the entrepreneur and the specificities of the SME. For example, high interest rates (exogenous factor) force the entrepreneur to call on financing by his family members or by using personal savings (entrepreneur's behavior) which reinforces the inability of the entrepreneur to separate between social capital and personal capital, and makes the financial management of the company very difficult (specifics of the SME). The factors of entrepreneurial failure in relation to the entrepreneur and the specificities of the SME can be in reciprocal interaction. Thus, the managerial incompetence of the entrepreneur (profile of the entrepreneur) or of these collaborators can negatively affect strategic decisions in terms of growth of the SME which further reinforces the lack of financial resources at home (specificities of the SME). On the other hand, the scarcity of financial resources (specificities of the SME) can dissuade entrepreneurs from getting training in management and consequently his managerial incompetence becomes a structural defect (entrepreneur profile). The figure below shows these different factors and their interaction.

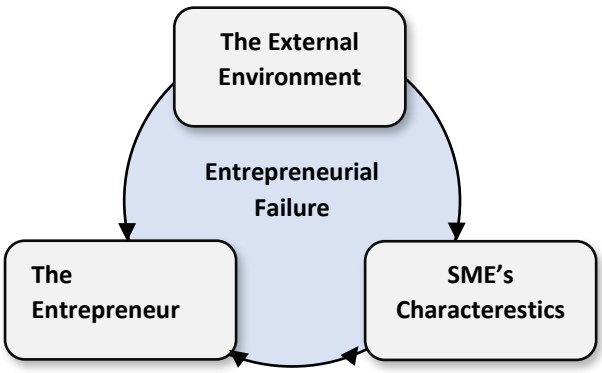

Figure SEQ Figure * ARABIC 1 : SMEs'

Figure 1: SMEs' Failure Factors

3. Empirical Studies on the entrepreneurial failure of Moroccan SMEs

3.1. SMEs in Morocco

In Morocco, the economic fabric is made up of small and very small businesses, or even micro-businesses. Small and medium-sized enterprises (very small and medium-sized enterprises) and large enterprises constitute the two main poles of the productive fabric. The number of mid-sized companies (20 to 50 employees) is very limited (OECD, 2017, p.123). SMEs participate 40% in the creation of global added value and carry out 30% of exports and 40% of private investments (Inforisk, 2016).

Despite the predominance of SMEs in the Moroccan economy, there is no uniform definition of what constitute an SME. The National Agency for the Promotion of SMEs, Maroc PME, in collaboration with the General Confederation of Enterprises in Morocco (CGEM) has adopted a definition consistent with the support systems for SMEs. This new definition considers the sole criterion of turnover and does not include the number of employees. According to this definition, a very small enterprise is one that has a turnover of less than 3 million dirhams; a small business is one that has a turnover between 3 and 10 million dirhams; for a medium-sized enterprise, the turnover must be between 10 and 175 million dirhams.

The SMEs' default rate has been increasing steadily in recent years. In 2017, the rate reached 11.5% with more than 8,088 going bankrupt, while this number hovered around 4,000 in 2009 (Euler Hermes, 2005). Between 2009 and 2015, the bankruptcy rate increased by 16%. Still according to the same source, over the past three years, defaulters registered an increase of between 8% and 10%. The consequences of SME bankruptcies are very worrying given the drop in the growth rate of the Moroccan economy (2.9% in 2019, against 3.1% in 2018 and 4.1% in 2017) and the rise in the rate of unemployment, which reached 9.4% in the third quarter of 2019.

Such failure cannot be avoided or at least reduced without a perfect understanding of the causes leading to it.

3.2. Research Methodology

Given the exploratory nature of this study and our research objective, we used secondary data in the form of academic research, studies carried out by national, international private and public organizations (Cowton, 1998; Thiétart, 2003). Among the main advantages of using secondary data is the low cost of obtaining it, thus allowing the researcher to focus more closely on the theoretical aspects and the substantive questions of the study rather than on the practical and methodological problems of the collection of new data (Cowton, 1998). In addition, relying on secondary data can effectively benefit the development of the theory (Hakim, 1982).

We started by searching the official websites of public and private organizations for studies on the entrepreneurial failure of Moroccan SMEs. For academic articles, we carried out a keyword search on the Google Scholar site using the following search string: ("failure" OR "bankruptcy" OR "failure") AND ("Moroccan SMEs").

After this step we identified 33 documents and we retained 12 documents; an investigation carried out by a public body, 2 investigations of two firms recognized at the national and international level and 9 articles; the research objective of which relates directly to the entrepreneurial failure (see table 2 in the appendix). The eliminated articles are those which do not clearly explain their research methodology, and those which do not consider failure in its extreme form which is the closing of the company.

The processing of our secondary data is done through a thematic content analysis. The purpose of this analysis is to provide knowledge and understanding of the phenomenon studied. It is an intellectual process that involves categorizing qualitative textual data into clusters of similar entities or conceptual categories in order to identify patterns and consistent relationships between variables or themes (Given, 2008).

The analysis of the studies collected took place in two stages. During the first stage, several in-depth and critical readings of each document were carried out individually by each author. The

goal was to analyze their content and highlight all the factors of failure that emerged in the results of each study. Subsequently, a collective work of comparison of the factors of failure identified by each author was started to lead to a final census of these factors.
In the second stage, the causes of failure identified were the subject of a two-step coding process: open coding and axial coding (Miles, Huberman, & Saldaña, 2014; Strauss & Corbin, 1998). In order to facilitate the coding process, we used the ATLAS.ti v7.5.7 qualitative analysis software.
Open coding has allowed the analysis, comparison, conceptualization and categorization of the causes of entrepreneurial failure identified to construct subcategories of factors. During this first stage, we went back and forth between our codes and literature. Then, the axial coding consisted in a grouping of these sub- categories of factors into conceptually similar factors. To limit the risks of subjectivity in the results of the coding process (open and axial), we made sure that the coding work is carried out individually under the ATLAS.ti software followed by a collective discussion of the results by the authors.

4. Results

Table 1 shows in detail the categories of factors, the subcategories of factors and the factors of entrepreneurial failure of Moroccan SMEs.

Table 1: Factors of entrepreneurial failure of Moroccan SMEs (Asli & al. 2019)

Categories of factors	Sub-categories of factors	Failure factors	Refernces
	Organizational structure	Informal working relationships. - Undefined functions. - Poor organization of the company. - Rigid organizational structure.	Abriane & Aazzab (2016) ; Zahra (2014).
Characteristics of the SME	Organizational climate	- Unstructured communication system. - Poor communication between internal partners. - Disputes between the partners. - Lack of a climate of cooperation within the SME. - Internal social problems. - Absence of a managerial culture.	Bellihi & Agy (2008) ; Abriane & Aazzab (2016).
	operational management	- Deficiencies in the operational management of the SME. - Lack of innovation and quality management efforts. - Lack of forward-looking management and tendency towards short-term management. - Low level of productivity.	Inforisk (2016) ; Euler Hermes (2015) ; DEPF (2008).
	Financial management	- Under-capitalization (very low start-up capital).	Inforisk (2016) ; Euler Hermes (2015) ; Bellihi &

Categories of factors	Sub-categories of factors	Failure factors	Refernces
		- Devastating shock on the cash cycle especially for small businesses. - Poor management of working capital requirement. - Financial difficulties, poor management of financial resources, non-payment of customers. - Deficient accounting system.	Agy (2008) ; Zahra (2014) ; Kherrazi & Ahsina (2016) ; Hassainate (2016) ; Sefiani & Bown (2013) ; Maniani (2014).
	Human resources	- Low-skilled and generally poorly paid workforce. - Weak recourse to training. - Difficulty attracting qualified human resources. - Unclear rights and duties of employees in the workplace. - Compensation and promotions not based on skills and qualifications, but influenced by family, friendship and personal considerations. - High HR management expenses and fees.	Inforisk (2016) ; DEPF (2008)
	Marketing	-Poor diversification of the client portfolio (decrease in order books) - Insufficient commercial profitability.	Inforisk (2016) ; Kherrazi & Ahsina (2016) ; Hassainate (2016).
The Entrepreneur	Skills and experience	- Lack of entrepreneurial experience. - Poor management by entrepreneurs. - Insufficient managerial and functional skills. - Low level of education.	DEPF (2008) ; Sefiani (2012).
	Management Style	Self-centered management style among managers. - Low delegation of power. - Limited search for support by experts (absence of a culture of advice). - Lack of a strategic vision, knowledge and managerial culture.	Euler Hermes (2015) ; Kherrazi & Ahsina (2016) ; Hassainate (2016).

Categories of factors	Sub-categories of factors	Failure factors	Refernces
	Personal factors of the entrepreneur	- Low tolerance for ambiguity. - Strong risk aversion. - Factors related to human attitudes (lack of trust in partners, conflicts with partners, dishonesty of partners). - Age. - Leadership crisis. - Family history. - Gender: women entrepreneurs often suffer from a lack of technical and managerial expertise. - Inadequacy of the entrepreneurial profile to the specificities of the SME. - Insufficient need for entrepreneurial success.	Bellihi et Agy (2008) ; Zahra (2014) ; Sefiani (2012).
External factors	**Global Economic Situation**	- Low economic growth rate. - Slowdown in domestic demand. - Slowdown in growth sectors, especially real estate. - Crisis in the main economic partners. - Decline in public investment. - Soaring commodity prices.	Inforisk (2016); Euler Hermes (2015); Abriane & Aazzab (2016); Sefiani (2012).
	Industrial factors	- Abnormally long payment terms (difficulty in applying Law 32-10 in force since 2013) - Significant creation of companies in the sector. - Difficult economic conditions in the sector. - Strong competition and unfair competition from the informal sector. - Difficulty accessing commercial networks, customers and suppliers.	Inforisk (2016) ; Euler Hermes (2015) ; Bellihi & Agy (2008) ; Zahra (2014) ; Abriane & Aazzab (2016) ; Ibourk & Aazzab (2016).
	Institutional environment	- Malfunction of legal provisions in terms of inter-company loans. - Lack of official commercial and financial	Euler Hermes (2015) ; Zahra (2014) ; Sefiani (2012).

Categories of factors	Sub-categories of factors	Failure factors	Refernces
		information for decision-making. - Lack of long-term support for the entrepreneur. - Rigid administrative context. - Rare offer of specific training for the entrepreneur. - Weak state support for innovation. - Regulation of foreign trade favoring the volatility of domestic prices. - Significant tax burden. - Difficult relationship with public administration. - Weak support for access to land.	
	Access to External financial resources	- Difficult access to bank credits (reluctance of the banking sector). - Lack of banking support when the SME is facing financing problems. - Difficulties accessing the capital markets.	Inforisk (2016) ; Euler Hermes (2015) ; DEPF (2008)[155] ; Sefiani (2012).

Through the results of the content analysis carried out, we organized the factors of the failure of SMEs in the Moroccan context into three categories, namely, the external environment, the specificities of SMEs, and the entrepreneur (Figure 3). We believe that the entrepreneur is an important factor in explaining entrepreneurial failure and which should be studied in a separate category.

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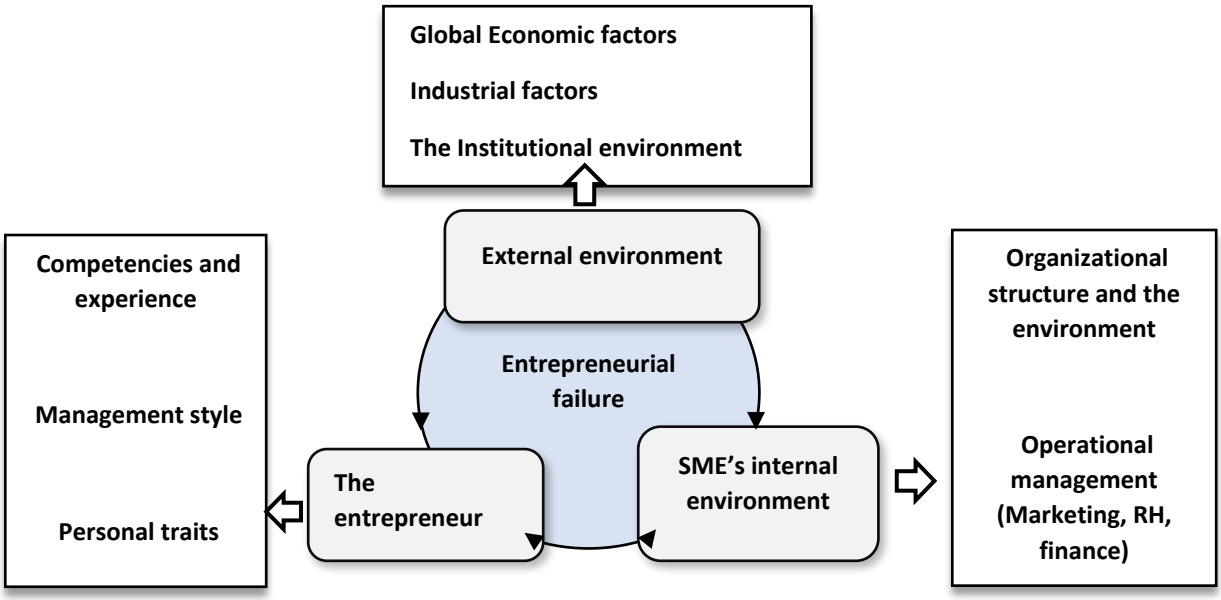

Figure SEQ Figure * ARABIC 2 : Factors of entrepreneurial

Figure 2: Factors of entreprenuerial failure of Moroccan SMEs

4. Discussion of the results

As shown in table1, the factors of entrepreneurial failure of SMEs have been divided into three categories. The discussion of these results will be carried out in three sections, each devoted to one of the categories listed in the table.

4.1. Factors of entrepreneurial failure linked to the specificities of Moroccan SMEs

a- Organizational structure and climate

The failure of SMEs can be attributed to their organizational specificities (Julien & Marchesnay, 1988; Torres & Julien, 2005). In terms of organizational structure, the studies reviewed show that Moroccan SMEs that fail are characterized by poor work organization, a rigid structure, undefined functions within the company; and a rather informal working relationship. These companies often have a poorly formalized hierarchical structure (El Houmaidi, 2011). Such a structure results in a predominant role of the owner-manager compared to the other members of the company, because he takes charge of both strategic and operational responsibilities. This is in line with Temtime & Pansiri (2004) who reveal that most SMEs in developing economies do not have a formal organizational structure. In addition, failed Moroccan SMEs reported having difficulties resulting from unstructured communication between internal partners, governance problems reflected in disputes between partners and a lack of formal framework for internal cooperation.

b- The management of the Moroccan SME

According to several empirical research, management problems in the fields of finance, HR, marketing and management of operational activities are major causes of failure of SMEs (Bennett, 2016; Temtime & Pansiri, 2004). For Moroccan SMEs, the difficulties of operational management reflected by the low level of productivity, the lack of forecast management and short-term management jeopardize their survival (Benabdeljlil, 2007). This confirms the results of Ropega (2011), showing that the lack of managerial skills in one of the aforementioned areas reduces the chances of survival of SMEs.

In the financial field, the failure of Moroccan SMEs is mainly linked to problems of liquidity and internal cash management. This result is in line with that of Bruno et al, (1992) who showed that the failure of the SME is often attributed to poor financial management of the company. In several Moroccan SMEs, managers lack skills in corporate finance and often make decisions without any solid financial information.

The failure of the Moroccan SME is strongly determined by its marketing capabilities. According to Ailli (2011), the function of marketing in Moroccan SMEs remains dispersed within the organization due to the absence of a specialized marketing department. Even when such a service exists, it reduces marketing to its operational dimension by underestimating its strategic aspect. Consequently, very few Moroccan SMEs carry out a market diagnosis and an analysis of consumer needs. The segmentation, targeting and positioning marketing approaches are not a common practice in all Moroccan SMEs, and the 4Ps of the marketing mix often lack consistency and homogeneity. Also, in accordance with Tushabomwe-Kazooba (2006), we can especially explain the poor development of marketing activities of Moroccan SMEs by the inability of their financial structure to bear the prohibitive costs of these activities. Generally, the inadequacy of the marketing effort of failing Moroccan SMEs is not compensated by the establishment and improvement of a quality management system capable of retaining customers and improving commercial profitability. This confirms the results of Jennings and Beaver (1997), who explain the failure of SMEs by the lack of a quality management system.

Certain dimensions of HRM also contribute to the explanation of the failure of Moroccan SMEs. One element which seems important to us is the low level of qualification of the workforce as well as the low salaries. Moroccan SMEs do not invest enough in continuous training for employees. Liouaeddine (2009, p.11) notes that "most Moroccan SMEs invest very little in the training of their workers and focus on activities in sectors with low added value in which the demand for skills is low. Barely 20% of Moroccan SMEs organize training cycles for the benefit of their employees." By international standards, this rate is considered to be extremely low. In terms of vocational training, the High Commission for Planning (HCP) declares that in 2014, only 1.6% of employees benefited from training paid for by the employer. Such a situation explains the difficulties experienced by several managers of Moroccan SMEs in training and transforming their employees into real partners, and by attributing, from time to time, a strategic dimension to the HR function. As a result, interpersonal conflicts, indicators of limited HR management, strongly contribute to the deterioration of the social climate and cause remarkable decreases in productivity (Bacq, Giacomin, & Janssen, 2009; Smida & Khelil, 2010; Singh et al. , 2007). From the above, it seems that the failure of Moroccan SMEs is strongly linked to the weakness of the strategic dimension at the level of all management functions (HR, Marketing, Financial Management, etc.). Often this imperiousness of strategic management (especially in terms of growth strategies) has its origins in the managerial behavior and personality traits of the Moroccan entrepreneur, director of the SME.

4.2. Factors related to the Moroccan SME entrepreneur

The Moroccan entrepreneur is largely imbued with the windfall mentality (Boutti, 2010) giving rise to the notion of the venture capitalist entrepreneur (called in Moroccan dialect "Bouchkara". This mentality translates into a refusal to commit to strategic (innovation, TQM) and societal (CSR) investments. More specifically, the entrepreneur's difficulty in promoting innovation and implementing quality management reduces the possibilities of upgrading, thus causing a loss of market share and accentuating the risks of failure for pure commercial causes.

In the Moroccan SME, the entrepreneur often engages in several functional tasks. This commitment strengthens short-term management of the SME and hampers its performance and sustainability. The salient result of our study is that the failure of the SME is strongly determined by a limited level of managerial skill or expertise of the Moroccan entrepreneur. This result corroborates research revealing that the lack of managerial experience is a source of SME failure (Bacq, Giacomin & Janssen, 2009; Smida & Khelil, 2010). Indeed, this inexperience reduces the effectiveness of management (operational and strategic) and conditions the nature of the

management style. Inexperience is sometimes combined with a low degree of entrepreneurial preparedness (Cope, 2005) within the Moroccan SME's entrepreneur. This situation means that the entrepreneur is unable to support and manage the managerial constraints of the SME, which leads to failure (Saunders, Gray, & Goregaokar, 2014).

The management style of the Moroccan entrepreneur remains largely influenced by the standards of the tribe or region of origin, the social class, the work of the father and the traditional and religious values inherited from the parents (Ali & Wahabi, 1995; Tahirou & Une, 2013). According to Ali & Wahabi (1995), the management style of the Moroccan entrepreneur is predominantly "self-centered". That is to say, he concentrates his efforts on his own interest and adopts an authoritarian -even aggressive and ruthless-behavior without worrying too much about the feelings of others. Such an attitude creates social tensions and increases the aversion to the growth of SMEs among employees, considered as a reason why most SMEs go bankrupt (Clark, Berkeley, & Steuer, 2001).

4.3. Factors of entrepreneurial failure linked to the external environment of Moroccan SMEs

a- The Moroccan economic situation

Studies in developed countries show that the effect of the macro-economic environment is evident on the violent disappearance of SMEs (Liefooghe & Zopounidis, 1990, cited by Kaba, 2007). This effect is even more present in the case of developing countries (Ihua, 2009; Temtime & Pansiri, 2004), where bankruptcies of SMEs are more linked, on the one hand, to the variability of their GDP and another side to the structure of their industrial fabrics. In general, Moroccan SMEs operate in the context of moderate and volatile economic growth (4% on average) and slowing domestic demand (OECD, 2017, p.66). Thus, short-term SME failures are highly sensitive to changes in economic conditions (Ibourk and Aazzab, 2016). According to these authors, the short-term decrease in GDP of around 1% leads to an increase in bankruptcies of SMEs by 1.5%.
At the level of the Moroccan industrial fabric, the industrial acceleration plan 2014-2020, favored the establishment of certain large contractors from the main economic partners of Morocco (such as France and Spain) with the 'objective of developing a network of subcontracting SMEs. Nevertheless, Moroccan subcontracting SMEs find themselves in a situation of dependence (frequently exclusive) vis-à-vis their prime contractors., having suffered from the global financial and economic crisis of 2008, the latter accelerated the failure of some subcontracting SMEs because of the drop in order books.

b- The Moroccan institutional framework

Some laws that directly affect the activity of SMEs delay the proper implementation of the law. For example, law 32-10 relating to payment periods remains difficult to apply due to the diversity of business-to-business relations and the absence of regulatory texts concerning the calculation of late payment penalties. This situation further deteriorates the financial situation of Moroccan SMEs and increases the risks of their failure. Today, the extension of payment terms is considered an important factor in the failure of SMEs. In addition, some illegal business practices make the justice system ineffective, mainly due to corruption (Ihua & Siyanbola, 2012). In this sense, a study by the World Bank (2013) indicates that 21% of Moroccan companies, especially the small ones, declare that corruption is the first obstacle they face. For example, when obtaining an import license, 58% of entrepreneurs make informal payments of money or gifts (World Bank, 2016).
The institutional environment is also marked by the insufficiency and irrelevance of public support to finance SMEs. Despite the existence of certain public funding programs (eg Imtiaz, Moussanada), they are not entirely within the reach of SMEs due to the lack of information and the cumbersome administrative procedures for filling in and preparing documents and applications. The issue of cumbersome procedures is consistent with the results of Ropega (2011),

which focuses mainly on the procedures for obtaining public funding. The lack of public support also affects long-term support for entrepreneurs, which remains very limited.

c- Industry

Moroccan SMEs that have experienced failure are often affected by the poor development of the sector, the competitive intensity, and more particularly the long delays in payment of debts.
Late payments are behind 25% of Moroccan SMEs' bankruptcies (Inforisk, 2016). In fact, the lengthening of payment periods for inter-company claims, which can reach on average ten months, weighs heavily on the cash flow of Moroccan SMEs and exalts their vulnerability (Inforisk, 2016). Obviously, it is VSEs that suffer even more from this deterioration in the payment period, the average duration of which has increased by 70 days since 2010 (Inforisk, 2016). For example, for VSEs in the construction sector, the deterioration in payment terms is greater since they have lengthened by more than 4.4 months for four years (Inforisk, 2016). This is explained by the balance of power more in favor of large companies which impose their payment terms on SMEs which in turn pass them on to very small businesses. By being the weakest link, VSEs and SMEs play the role of the banker for large companies (CFCIM, 2016).
Poor development or sometimes crises in the SME activity sector can accelerate their failures. This is explained by the reactive attitude of SMEs faced with the determinism of their industrial environment which does not guarantee them growth opportunities. Conversely, when the sector is prosperous, it can give rise to a high level of competition which weakens SMEs. In sectors such as agri-food, textiles and manufacturing industries, Moroccan SMEs face stiff competition from national or foreign companies in terms of cost, quality and productivity, this confirms the work of Honjo (2000) and Temtime & Pansiri (2004) who showed that SMEs operating in highly competitive sectors are more prone to failure.

Competition from the informal sector is another factor that weakens the financial structures and commercial performance of Moroccan SMEs. In Morocco, the share of the informal sector fluctuates between 11.5% and 33% of GDP (HCP, 2007; CGEM, 2014) and concerns several practices such as smuggling, under-invoicing and non-declaration of employees.

d- Access to external funding

The loan share granted by banks to SMEs in 2016 is between 35% and 37%, the rest being allocated to large companies. Banks impose tough conditions to grant loans to SMEs. They may sometimes request warranty relating to the personal property of the managing owner, which represents the most discouraging form of condition for entrepreneurs. According to the banks, the overly restrictive conditions for granting credit to SMEs are justified by their structural fragility, the insufficient quality of the credit files presented and the lack of transparency of the financial statements. The rigid behavior of banks vis-à-vis companies in difficulty accelerates their failure, a finding corroborated by Bloch, Bourdieu, Colin-Sedillot & Longueville (1995). In addition, SMEs also experience great difficulties in accessing the stock market given the complexity of stock market mechanisms and rules due to their limited means. This exacerbates the shortage of external financial resources and blocks the materialization of investment projects of Moroccan SMEs.

5. Conclusion

Entrepreneurial failure is a global phenomenon affecting SMEs and large companies (Omri & Frikha, 2011). In developing countries, such as Morocco, entrepreneurial failure is under- studied, fragmented and devoid of a holistic and integrated vision of the factors that determine it. Therefore, the objective of this study is to fill this gap through an exploratory analysis of academic articles

and national and international surveys, private and public, on the entrepreneurial failure of Moroccan SMEs.

The study implies that the causes of the failure of SMEs in Morocco are numerous, but can be reduced to three categories of interdependent factors. First, the external environment of SMEs in relation to the country's economic situation, the institutional framework, the conditions of industry, and lack of access to external financial resources. Secondly, the factors inherent in the specificities of SMEs that affect the internal environment and organizational structure, the management of the SME (Marketing, Finance, HR etc.). And finally, there are factors relating to the SME's dependence on the owner-manager (or the entrepreneur), his experiences, his skills, his management style and his personality traits.

Understanding these categories of factors explored and synthesized in the context of this work can be very useful for owner-managers of SMEs. The latter can have a fairly broad idea of the different factors behind the failure of SMEs and consequently design the strategies necessary to prevent any scenario of failure of their businesses. The results of this study can also help government institutions and private organizations (as well as training centers for entrepreneurship and management of SMEs) to better implement policies or programs to support the growth process of SMEs.

However, this study has a number of limitations which constitute avenues for future research. First, the secondary data used only partially covers our research question since it does not reveal other possible factors of entrepreneurial failure (for example the effect of Morocco's free trade agreements with several foreign countries , the variables the Moroccan national culture or the psychological dimensions of the entrepreneur). Second, the heterogeneity of the studies on which our analysis is based does not allow the generalization of our results, because they relate to SMEs belonging to different Moroccan regions and operating in various sectors of activity. In fact, it would be interesting to conduct a national survey that would touch different regions and sectors, and consider other factors of failure to arrive at a fairly complete explanation of this phenomenon. Third, this research does not define the SME and the concept of failure in the same way, and above all does not specify the age of the SMEs studied, which does not allow the results to be distinguished between already established and newly created SMEs. Future research can focus on failure factors according to the age of SMEs, while adopting a single definition of entrepreneurial failure, the same theoretical frameworks and the same definition of SME in order to allow for results generalizability. Still, deeper understanding of the issue of SME's failure can be reached through qualitative longitudinal research, complemented by quantitative approaches. This will provide an in-depth investigation of the evolution of the process of entrepreneurial failure of SMEs, the degree of importance of each of these factors and the level of their interaction.

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COMPARATIVE ANALYSIS OF FACTORS INFLUENCING EVOLUTION OF RURAL ENTREPRENEURSHIP IN RUSSIA AND CROATIA

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Abstract
The paper compares genesis of functional components and variables of rural entrepreneurship in Croatia and Russia. Rural entrepreneurship is for a long time in the focus of considerable theoretical and political interest in Russia and the European Union alike. Rural entrepreneurship stands not only as a vehicle of achieving sustainable food supply and improving the quality of life in rural communities but also plays an important part in the efforts to preserve country's cultural identity. We propose that the key aggravating features of today's development of rural entrepreneurship in Russia and Croatia alike can be found in history of economic development of these countries. Examination and comparison of antecedents of rural economic development in observed countries are traced back to the last decades of 19th century up until present day, and encompass five key categories: infrastructure, individual factors, social and cultural factors, economic factors and finally, administrative and legal factors. By analyzing and comparing key events and elements of economic development of rural areas we want to achieve better understanding of the present situation in order to devise a better approach to further fostering of rural entrepreneurship in Russia and Croatia.

Keywords: *Rural Entrepreneurship; Rural Entrepreneurship Development; Rural Socio-Economic Development*

Track*: Entrepreneurship*

Word count: *3.749*

1. Introduction

According to Schumpeter, an entrepreneur is willing and able to turn a new idea or invention into a successful innovation (1976). Entrepreneurship employs what Schumpeter called the "creative destruction" to replace, in whole or in part, the inferior supply in markets and industries, while simultaneously creating new products and new business models. In that way the "creative destruction" is largely responsible for long-term economic growth. According to Drucker (1985) entrepreneurship is a pattern of behavior, not a matter of personality. Drucker is especially keen to emphasize the need to educate entrepreneurs, because entrepreneurial success depends on the knowledge of entrepreneurial settings and theory of entrepreneurial behavior.

Entrepreneurship is also seen as a crucial factor in creating national wealth. In doing so, the entrepreneur is exposed to a certain personal risk, he invests his capital and expects a reward in the form of financial and other kind of benefits. As Drucker puts it (1985, 73) entrepreneurship is about maximizing the possibility of avoiding fatigue and mediocrity while ensuring constant movement with new energy. This thought is very important because it points to one of the most important factors of entrepreneurship and economy in general, and it is the economic dynamism is that *conditio sine qua non* of a market economy. This fact is also noticed by Timmons and Spinelli (2003) when they say that entrepreneurship is transforming an idea into a business

opportunity. Therefore, market-oriented economies are entrepreneurial economics. The fact of high entrepreneurial risk, and that of a mindset of a person who starts the business with his or her personal capital, should be respected by the state by developing a support network for start-up and other similar support programs. In the same way,, rural development approximated by improvement of quality of life in rural areas, is the key factor of sustainable growth of agricultural production and social stability in rural area.

Main proposition of the paper is that historical knowledge is not only essential to understand the territorial ecosystem of agriculture, and to forecast its development; it is also an important component in the management of the territorial development, particularly in the sphere of regional food security (Thomas Herzfeld et al, 2014). In order to address similarities and differences of rural entrepreneurship ecosystems in Croatia and Russia we propose five key categories which we analyses through description of historical antecedents of rural development in observed countries: infrastructure, individual factors, social and cultural factors, economic factors and finally, administrative and legal factors.

In overall economic perspective, according to the 2018 data, Croatia was in the penultimate position among the countries of the European Union (EU) in terms of real individual consumption and gross domestic product (GDP) per capita, ahead of Bulgaria (EUROSTAT). Croatia is at 36% with Latvia, Romania and Greece, in the group of countries whose GDP per capita is more than 30% below the EU average.

Beeing a part of Eruopean Union Rural Development in Croatia is managed nationally through one Rural Development Programme (RDP), funded under the European Agricultural Fund for Rural Development (EAFRD). The RDP sets out priority approaches and actions to meet the needs of the specific geographical area it covers. To achieve policy goals by the EU standards, Croatian agriculture has to solve its long time preoccupation with a production of basic food supply, resulted from size and technological structure of business entities in agriculture (Franić, Jurišić, Gelo, 2014). Goal of rural development in Croatia is to accomplishing the highest level possible of self-sufficiency in agricultural production (now within the Common European market), production competitiveness, acceptable food prices with respect towards health regulation, achievement of environment protection standards, good agricultural practice codes and contribution to the public goods.

Although there are vast differences between Russia and Croatia in respect to size and economic position and preferred economic policy in respect to development of rural entrepreneurship there are many similarities. Russian rural areas (populated areas outside towns and cities) occupy two thirds of the country territory. Practically all Russian constituent regions have rural areas, though varying by their share in a region's total area and by their population number. In the Southern and European Russia and Siberia the former reaches 50%. In the Non-Black Earth Zone it is under 20%. The total population of rural areas is 39,2 million, which is 27% of the country population (Petrikov, in Petrick, Weingarten (ed.), 2004).

Nowadays, the existing system of food production and rural development in Russia cannot be termed sufficient and productive (Goldman, 1992). Modern requirements of the living standards in rural regions and rural poverty reduction cannot be achieved within the post-Soviet type of rural policy. To reach the goal of improving and to change the declining trends of living standards in rural regions, it is necessary to develop rural entrepreneurial ecosystem to ensure the priority of social goals over economic development, because providing higher standards of rural livelihood will inevitably lead to sustainable development of rural economy.
Population and economic changes in rural regions, the exploration and development of economic opportunity drift beyond just traditional agriculture. Entrepreneurial development of communities

in rural regions, designed to support the development of new social and sustainable economic opportunities, is esteemed by many researchers to be the unique opportunity and driving force that will generate sustainable regional development and foster economic security. Entrepreneurial ecosystem formation for economic development of communities in rural regions has significant academic importance, serving as foundation for creation of rural entrepreneurial ecosystem approach, which is called to be agriculture system of the 21th century and practical importance, serving as the foundation for political decisions for regional development.

Many Russian experts (for example Lisova, Erokhin, Ivolga, 2016) acknowledge the systemic crisis in agriculture, which is partly a result of economic reforms, occurred in Russia in 1990-2000s, partly a consequence of global tendencies of growing population and issues of food security.

2. Antecedents of development of rural entrepreneurship in Croatia and Russi

In the 19th century Croatia was still fragmented and divided into countries that often changed their principals from the Habsburg Monarchy, Hungary, Italy and even France. As Karaman (1972) states, in the mid-19th century the development of Habsburg monarchy was quite fast, but the Croatian countries within the monarchy did not participated significantly in this development. A somewhat more noticeable development of the economy of Croatian occurred only after 1873, after the abolition of feudal relations, that is, when more intensive industrialization begun in Austria, the Czech Republic and Hungary. Analyzing the middle of the second half of the 19th century, Karaman concludes that economic development in Croatia was accompanied by the construction of railway lines, the opening of banks, and the operation of the Chambers of Commerce in Zagreb and Osijek. This development was short-lived because it was stopped by the crisis of 1873. It was a period of mass emigration of the population from Croatia. Fisheries, arable farming and animal husbandry were the predominant industries, but technologically underdeveloped and could not market their products to non-local markets but were a source of livelihood for the local population (Karaman, 1972).

According to Stipetić (2012), Croatia had 42,450 business entities in 1870, which he estimates as a huge increase in respect to previous years. It is interesting to notice that in 1957. Croatia had only 15,850 business entities (Stipetić, 2012, 142). Until 1910, Croatian agriculture did not change significantly within 5,659 thousand hectares of arable land. At the same time, in Dalmatia the area of traditional vineyards and olive groves gradually decreased in the period from 1870 to 1914 (Stipetić, 2012, 176), while the livestock production of Croatia increased during the same period. With his research, Stipetić answered the dynamics of the development of large and important countries and economies of Europe at that time. The development was observed through the dynamics of the per capita source structure and came to the following results.

As it can be seen from the data on per capita exports of the four core countries of west Europe and Austria-Hungary in the period from 1830 until 1910 (Table 1) the development of England was very steep. Germany and France share similar growth, although France has a wider market than Germany. Also, Italy and Austria-Hungary have similar dynamics even though Austria-Hungary, after Russia, is the largest European country.

Table 1: Relative per capita exports of the four core countries and Austria-Hungary 1830-1910

State	1830	1860	1880	1910
Austria-Hungary	1	4	8	9
France	3	11	15	29
England	8	22	30	48
Germany	3	11	16	27
Italy	2	4	7	11
Europe average	3	…	12	18

Source: Heywood, C. (1992). The Development of French Economy, Cambridge, p 47

At the same time internal structure of Austria-Hungary is extremely conservative and underdeveloped, and its political and economic system is sluggish and inefficient in relation to countries of western Europe. All this led to the fact that the Austrian Hungary Monarchy is called the periphery of Europe. Even in relation to the average of Europe, Austria-Hungary is lagging behind and unable to solve its internal problems, which will eventually prove to be one of the main reasons for World War I. In all of this, Croatia is the most backward country of Austro-Hungary, therefore Croatia is a periphery of the periphery. The period before the start of World War II was marked by various trends, for example unemployment was around 25%, although population growth from 1921 to 1948 took place at an average annual rate of only 0.65% (Stipetić, 2012, 240). As a result of unemployment and high demand for labor, Croatian workers are moving to Germany, which is rapidly expanding its industry. At the same time, agriculture was stagnant, the livestock stock declined until 1951, and from 1910 to 1949 the output of basic agricultural products (grain, milk and meat) per capita (in kg) did not develop. By the time of the Second World War, Croatian industry, crafts and related trade were stagnating, as was the production and consumption of cement, but with the notion that oil and gas production had been increasing steadily since the beginning of the Second War until 1950 (Stipetić, 2012, 236- 279). What is positive is education, which, despite the difficulties Croatia has been experiencing during this period, has seen a steady, which grew from an average rate of 6.2% between 1930 and 1950. The first post-war period, in the new communist totalitarian country Yugoslavia, did not mean for Croatia any improvement, but continued economic stagnation.
Interesting discussion on the state of rural development in Croatia was given by Bičanić before the second World War which can be summed up within these three points (Bičanić, 1939, pp. 103-105):

(1) “We are a peasant country with a relatively poorly developed national economy. Our peasant economy, of which 80% of our population lives, is unable to compete with other countries as it is economically unorganized and unprepared for modern management."
(2) "We are economically one of the most disorganized countries in Europe" and concludes "The question is whether we will organize our economic forces ourselves or foreigners will organize it for us."
(3) "The state government has not shown "the sense and ability to properly and modernly organized economy, which is a precondition for settling of political issues".

These conclusions are still worth discussing. Validly of these remarks was confirmed by the change of GDP from 1913 to 1950 (Stipetić, 2012, 240). The period from 1950 to 1973, in economic terms, was marked by slow growth in production and livestock production, but more significant growth of industry. At the same time, entrepreneurship was ideologically opposed to communist society and almost disappeared, and small craftsmanship remained at the same level throughout this period. The period, from 1973 until the end of the Croatian war for independence, did not change significantly in economic and social terms for Croatia. And after the end of the war, in 1995, Croatia found itself in an extremely difficult state. As a result of those killed in the war and because of the destroyed economy, the number of employees from 1989 to 2005 more than halved (Stipetić, 2012, 339).

Rural entrepreneurship was destroyed in Russia during the Soviet period, rural inhabitants were pressed to work only in agriculture, and today the traditionalist approach for organization of economy, business and social life, that cause obstacles for rural social development (O’Brien, 2002, 2012).

The rural entrepreneurial ecosystem has to be closely related to the climatic conditions of the region in question and to its historically-developed way of life and human activity; therefore, it

should rely not only on agricultural traditions but also on those of food consumption (Zalivcheva O., 2013). The significance of the exploration of entrepreneurial ecosystems is proved by the necessity of research of community economic development in rural regions, spatial innovative development aiming theoretical explanations of trends and threats of rural development. It is proved by many researches based on analysis in rural development in different countries in various geographic regions that traditional agricultural profile of rural economy has no sufficient potential to increase living standards of rural population. The contemporary approach to solution of this problem is based on formation of special innovative ecosystems implementing different types of economic activities for population providing living standards comparable to urban ones.

The suggested ecosystem can be considered suitable for the rural entrepreneurial ecosystem of an industrial northern region, since the principles which this ecosystem is based on are fundamental for any industrial region. The expected outcome, after the realization of the rural entrepreneurial ecosystem, is an increase in food security and an improvement of living standards for the rural population. To achieve this, the following principles should be realized:
The first principle is that the rural entrepreneurial ecosystem must consider the interests of all social groups of the given industrial region, and it should be aimed at increasing the public welfare of all groups.
Secondly, the ecosystem must be targeted at the development of the specific advantageous features of the agricultural producers of Sverdlovsk region, but not at the expense of competition with external producers. The third principle is that, rather than focusing on changes in benchmarks for the development of Sverdlovskaya Oblast, the ecosystem should strengthen the economic growth of the region by improving food quality for the population.
The fourth principle is that the ecosystem develops not only the economic potential of the rural territories but, primarily, social growth. The ecosystem points out the importance of the multifunctional development of rural localities, which, in turn, is bound to affect the standards of living in the rural localities in Sverdlovskaya Oblast. The weakness of the suggested ecosystem is a possible lack of political initiative on the part of local authorities (Kirsti Stuvøy, 2014). The current political system in Russia does not give sufficient power to municipal administrations. To implement this ecosystem municipal administrations are required to take political responsibility for the level of living standards and food security of the population.

Increase in migration to rural localities, stimulated by creating jobs in agrifood enterprises, and the creation of a favorable rural community, will lead to long-term stable regional economic development (Sergei Shubin, 2006). Thus, the agrifood system ecosystem developed for Sverdlovskaya Oblast meets the basic requirements for rural entrepreneurial ecosystem of industrial regions and can be applied in other northern industrial regions of the Russian Federation. The research results revealed a deteriorating trend in agricultural production and rural social development in Sverdlovskaya Oblast. To reach the goal of maintaining regional food security and to address the issue of the downward trend in food production it is necessary to ensure the priority of social goals over economic development.

3. Comparative analysis of key categories of rural entrepreneurship development in Russia and Croatia

In order to address comparison of rural entrepreneurship ecosystems in Croatia and Russia we propose five key categories which we analyze through presentation of antecedents of rural development in observed countries: infrastructure, individual factors, social and cultural factors, economic factors and finally, administrative and legal factors.

Being a part of European Union Rural Development in Croatia is managed nationally through one Rural Development Program (RDP), funded under the European Agricultural Fund for Rural Development (EAFRD). In order to increase the volume of farming output and productivity, which

is currently far below EU average, as is the absorption of funding for EU rural development programs, Croatia's farming sector needs to be regionalized to ensure a stronger role of subsidies in efforts to increase competitiveness. It remains to be seen how it will develop in the future, will the opportunity be utilized.

Because of its size, there is whole range of differences between rural areas in Russia. Internal regional differences are sometimes even stronger, than the interregional ones (Lisova, Erokhin, Ivolga, 2016). That very much depends on a number of factors, including economic, social, environmental, geographic, historic, cultural, and ethnographic.
From the perspective of individual factors influencing development of rural entrepreneurship the generational gap is very important issue in Croatia, since more than 50% of agricultural holders are over 60 years old. However, the share of young farmers puts Croatia high at the EU level, averaging at 6 percent. Year by year, young farmers are increasing in numbers, although growth is still slow.

Rural population in Russia is decreasing and accounts around 35 mil people, which is about 26% of total population. Working-age rural population is 21.4 mil people. There are 153.1 thousand settlements located in rural territories; over 133.7 thousands of them are permanently inhabited. Herein, 73% of rural settlements have less than 200 inhabitants, while settlements with over two thousand residents account only 2% (State Council of the Russian Federation, 2014).

Concerning social and cultural factors we can conclude that providing higher standards of rural livelihood will inevitably lead to the sustainable development of agricultural production both in Croatia and in Russia. Our study determined the conceptual foundations of sustainable development of rural localities of the Russian industrial regions, to be accomplished through the creation of decent living conditions and the participation of the rural population in quality food production. Particular attention is given to the mechanism of interaction and coordination among federal and regional governments, local governments and commercial organizations engaged in food production in rural areas. On the basis of the described theoretical propositions, the conceptual ecosystem of the innovative development of rural areas in an industrial region, namely Sverdlovskaya Oblast, aimed at quality food production for the population of region, is presented.

From the overall economic perspective, in Croatia, over the first ten months of 2018, compared with the same period in 2017, the country's farming and food exports increased by 5 percent to €1.64 billion, while imports rose by 4 percent to €2.55 billion. Coverage of imports by exports increased from 63 to 64 percent in the same period. Croatia still has large deficits in meat, milk, and dairy products, fruits, and vegetables.

In Russia, in recent years the dollar gap between food imports and food exports has closed considerably from $27 billion in 2013 to $3.9 billion in 2018 (Wegren, 2020, 7). Figure 1 shows value of Russia's food exports from 2001 through 2018 expressed in billion US dollars. The data in the figure represent not only a significant increase in Russia's food exports, but also a narrowing of the net difference in the value of food imports and exports.

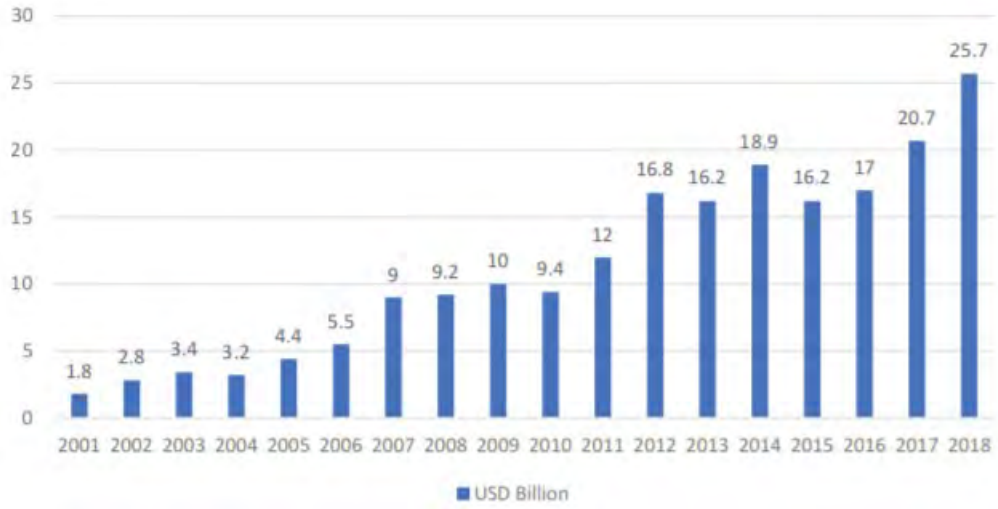

Figure 1: Value of Russian food export 2001-2018
Wegren, S. (2020), Can Russia's food exports reach $45 billion in 2024?, Post-Communist Economies, 32:2, p. 7

Finally, in respect to administrative and legal factors the results show that despite a highly centralized economic policy in the Russian Federation and Croatia alike, regional food security and rural development can be achieved by encouraging municipal authorities and entrepreneurs to take on a more responsible and active role.

4. Conclusion

A theoretical model of the regional entrepreneurial development, which will allow to determine the perspectives for innovative development, cannot be built without an analysis of development of the social and economic system in rural regions, especially when it comes to a predominantly northern one, and to our opinion it must be based on the concept of rural entrepreneurial ecosystem.

The concept of entrepreneurial development of rural regions has become well established both in scientific world and in public administrations. Despite the deep attention to the problems rural social and economic systems development there is no consistent ecosystem of multifunctional rural development that can lead to the solution of this problem.

Today more and more attention is given to development of rural territories as a source of agricultural commodities and food. However, current situation cannot be changed at once in Croatia or Russia alike. Attractiveness of rural areas and effectiveness of agricultural production cannot be increased with just a bigger amount of investments. Rural way of life is a social paradigm, which is developed under an influence of a whole set of non-economic factors: social, cultural, historical, ethnic, etc (Lisova, Erokhin, Ivolga, 2016)

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UNDERSTANDING OF SOCIAL CROWDFUNDING: THE CASE OF AN ITALIAN PLATFORM

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Abstract
Crowdfunding is a distinct form of venture financing that has recently experienced high growth rates. The collection of resources through this alternative channel has involved both profit-oriented companies and non-profit organizations (NPOs). This paper investigates the emerging practice of social crowdfunding focusing on the role played by an Italian social crowdfunding platform owned by a banking foundation. Examining 140 projects hosted between 2016 and 2018, the study analyzes how the platform acts in enhancing and facilitating the interaction between NPOs and private investors willing to participate in the financing of innovative social projects. In this context, the study also explores the role the Foundation plays in making more virtuous the social investing process aimed at creating a multiplier effect of its traditional philanthropic activity. Our findings help both to assess the effectiveness of a social crowdfunding platform and to identify the conditions that could make the traditional philanthropic activity of an institutional force such as the banking foundation more effective.

Keywords: *banking foundation, crowdfunding platform, reward mechanism, social investment, social leverage*

Track: *Entrepreneurship*

Word count: *3.962*

1. Introduction and relevant literature

Social enterprises play three roles in the promotion of community-friendly initiatives: the offering of innovative solutions to unsolved social problems, the centering of their corporate mission on the concept of shared social value, and their intention of contributing to the progress and sustainability of the global economy (Nel and McQuaid, 2002). Unfortunately, social enterprises suffer the lack of funding opportunities because there are limited sources of financing available to them as they have problems in securing loans and raising equity: they are not profitable or growth-oriented enough to access traditional financial markets, which results in a financial-social return gap (Bugg-Levine et al., 2012). The scarcity of funds allocated to welfare policies has led to address the necessity of identifying innovative funding models capable of attracting private financial resources to be channeled towards the improvement of the sustainability of welfare systems (Azemati et al. 2013).

McKenny et al. (2017) view crowdfunding as a distinct form of venture financing worthy of specific attention. Crowdsourcing favors the co-creation of value through digital technologies (Howe 2006). The use of the web platform and online communities facilitates access to financial resources for businesses, profit and non-profit organizations (NPOs), which need to raise funds through non-traditional channels (Belleflamme et al. 2014; Ordanini et al. 2011; Schwienbacher and Larralde 2010). Through a mechanism of interaction between different actors, crowdfunding links funders with an investment funder platform that can provide financial capital. The Internet-based brokerage platform acts as an alternative financial market in which it is possible to raise private capital to support commercial ideas or projects of a social nature.

Crowdfunding has emerged as a promising new option for securing large numbers of small

donations from the socially conscious crowd for the needs of projects run by both established non-profit organizations as well as socially focused startups (Clarkin, 2014; Clarkin et al. 2016; Parhankangas et al. 2017). For Renko et al. (2018) social crowdfunding helps social initiatives to test the appeal of new feasible minimum products that they want to launch and can integrate other sources of financing in the initial phase that are generally difficult to find. It is important to emphasize that for socially focused organizations, crowdfunding can be used to create momentum and excitement around a common cause, to build a community around the organization by activating current donors, in addition to finding new ones.

In this context, the present study has the aim to investigate the emerging practice of social crowdfunding. Our research focuses on the role played by an Italian social crowdfunding platform and the screening process that this platform performs in enhancing and facilitating the interaction between not-for-profit organizations seeking to raise funds and private investors willing to participate in the financing of innovative social projects.

Examining the first 140 projects hosted by the crowdfunding platform Meridonare between January 2016 and September 2018, our work analyzes how the platform was able to promote philanthropic activities and obtain a multiplier effect on the intervention of a specific banking foundation (FBN - Foundation of Bank of Naples).

The different reports used by the platform over the years and the profound interaction with Meridonare managers represent our main data sources in order to explore the context of social crowdfunding and to investigate the relationship between the crowdfunding platform and the banking foundation. In particular, we are interested in exploring the role the Foundation and Meridonare play in the social investing process. A key point is to study how institutional forces, such as the FBN, influence the functioning of social crowdfunding and increase the potential of this funding channel. In this perspective, the research questions are as follows:

H1: How does the relationship between Meridonare and the banking foundation influence the functioning of social crowdfunding?

H2: What are the benefits for the Foundation to use the crowdfunding platform as a tool of its philanthropic activity?

Our work highlights that the presence of the banking foundation strongly influences the activity of the platform differentiating it from the behaviors of the competing platforms both for its way of relating to fundraisers and backers and for its internal organization. In addition to playing an important role in connecting and matching fundraisers and investors, the Meridonare platform was able to create greater legitimacy for social enterprises by promoting the early interaction and participation of all the actors involved confirming the findings of Presenza et al. (2019). As a result, the use of the platform as a tool in favor of the philanthropic mission of the Foundation has permitted to generate a social multiplicator of 300 per cent in addition to the traditional philanthropic annual activities.

Our paper contributes to the literature assuming explanations for what is observed by drawing on unique qualitative data and testing our research hypotheses through rigorous empirical work. Since most of the existing literature is of a descriptive nature, we see the need to conduct a convincing analysis that investigates the effects of the synallagma between two important actors operating in the area of social crowdfunding. Social investments have become an important trend that has actually attracted capital flows for philanthropic reasons and sustainability. As social investing flourishes, it has real world impact on business practices, philanthropic foundations and the behavior of investors. Our document aims to understand the consequences of social investments made through a new channel such as the crowdfunding

platform. It will help to evaluate the effectiveness of a specific donation investing practices and will help to assess under which conditions social crowdfunding is best applied and where the practice could be rethought.

The rest of the paper is organized as follows. The *Methodology and data analysis* section presents the sources of data and gives an overview of the methodology. The *Findings* section presents the main research results, while the final section presents some *Discussion* on the implications of the study.

2. Methodology and data analysis

Given the inductive nature of the research questions, the study adopts a qualitative, case- based approach that enables the exploration of a phenomenon within its context (Yin, 2003). Data analysis will carry out by following a four-step procedure adapted from Easterby-Smith et al. (2012): (i) we carefully read the evaluation forms in order to familiarize with data; (ii) we express judgments by evaluating collected data in light of prior literature related to the topic of social crowdfunding platforms and social investment; (iii) we identify a set of variables considered relevant to address our original research questions; (iv) we formulate an analytical framework where the principal implications of our work can be traced.

Meridonare and FBO: a brief description

The Meridonare crowdfunding platform operates as a limited liability company (Meridonare Ltd.) characterized by the Startup Innovativa a Vocazione Sociale (SIAV) legal form. Meridonare was established in November 2015 and is led by Banco di Napoli Foundation, which considers it as an instrument for enhancing its social interventions. Meridonare's mission is to plan and develop its capital raising activity through innovative financial instruments, such as crowdfunding, aimed at promoting social well-being and the development of local communities. Through the use of the crowdfunding platform, it aims to become the reference point for those who plan social, cultural or civil interventions aimed at promoting a new way of understanding active citizenship in local urban areas. Meridonare intends to support the ideas and projects aimed at promoting the culture of philanthropic giving, the sense of community and the creation of strong and cohesive social ties, having as its main reference South Italy, its resources, its talents and its unlimited potential.

Italian Banking Foundations are defined by the Italian Constitutional Court (sentence No. 300/2003) as “private subjects, non-profit, participating in the construction of the common well-being" and use their assets to promote philanthropic activities in the territory to which they belong. Today, the Foundations of Banking Origin (FBO) system consists of 87 foundations originally made up of banks and savings banks to exercise direct philanthropy. In the 1999s, with the aim of separating the credit activity of the banks from the philanthropic activity, the role of the FBOs has been specially structured by Legislative Decree 153/1999. The FBOs have been assigned the task of remaining important institutional investors (in the portfolio they still have over 30% of the national banking system today) and of using the profits of financial investments for the socio-economic development of places of settlement through the supply of philanthropic resources to the system of third sector operators and to public institutions. FBOs cannot make donations to commercial enterprises. Despite being private entities, the FBOs are subject to the supervision of the Ministry of Economy and Finance (MEF) in order to strengthen the role of institutional investors and regulate the aims of social utility, collective interest and economic development of their location region through resources generated by the prudent investment of financial assets.

The Meridonare operating model and its evolution

In 2015 the main crowdfunding operators in Italy were: DeRev, Produzioni Dal Basso,

BuonaCausa and PlanBee. None of these operators was, however, specialized in social activities

but rather on innovative ideas. The FBO has entirely financed the launch of the Merdionare platform, including the hiring of the first three employees. They were selected both on the basis of their IT skills and because they were founders of a former local social platform.

To facilitate access to the platform for social project proposers, who often lacked specific IT, marketing and social media skills, Meridonare has chosen to offer its users various support services free of charge: the video presenting the request, the strategic study of the campaign, the organization of events to present the crowdfunding campaign, banking assistance for the opening of a dedicated current account, the use of a multimedia totem (donamat). The donamat is a tool that allows to illustrate the video of the campaign and, at the same time, to collect the donations in order to facilitate the collection during special events (such as, for example, the one held at the San Carlo Theatre in Naples). To support the dissemination of knowledge of the campaigns present on the platform, Meridonare has developed an online journal (Meridonare news) which contains various editorial activities including interviews with associations/organizations promoting social projects.

The fundamental contribution to the development of the crowdfunding platform was the instrumental relationship with the Foundation of Bank of Naples. In addition to financing the start-up phase of the project, the FBN has been, from the earliest stages, the main financier of the Meridonare as part of a strategy that saw the crowdfunding platform the ideal channel to promote the social interventions of the Foundation.

Data analysis

The research database is composed of the information contained in the evaluation form (Social Report) compiled by the Meridonare operators at the end of each crowdfunding campaign. The evaluation and reporting activities involve the various phases of the crowdfunding campaign and covers the entire spectrum of activities (online and offline) ranging from the project submission phase to the end of the crowdfunding campaign. In the pre- campaign phase, Meridonare analyzes the project in terms of completeness, potentiality and social impact by assigning its own evaluation judgment. The preliminary assessment of the project aims to decide whether to place the request on the platform without the assignment of a score to be communicated to the donors. In the final phase, namely, at the end of the campaign, Meridonare assesses the social impact of the campaign on the community and evaluates the social report of the funded project.

The evaluation process is not a black-box, but is shared with the applicants right from the planning phase of the proposal (Gallucci et al, 2018). The sharing of the evaluation mechanisms helps to implement effective and efficient behaviors and actions for the following: the financial target of the crowdfunding campaign (funding); the implementation of the intervention (output) controlled by Meridonare, then publicized on the platform; the evaluation of the social impact (outcome) made by the Foundation, published annually in the social balance sheet.

Table 1 illustrates the variables that have been identified following the three initial phases of our analysis process (Easterby-Smith et al. 2012).

Table 1: The key variables of Meridonare's crowdfunding activity

3. Findings

The quantity and quality of information in the report has changed over time.

Initially the report consisted of a simple form which, starting in 2017, was transformed into an evaluation sheet of the social impact of the campaign. In particular, Meridonare transmits to the board of the Foundation a report which identifies the capacity of the association to develop relationships - both personal and through social media - with new donor subjects sensitive to the theme of charity and philanthropy.

The analysis of the results obtained from the campaigns published on the crowdfunding platform stimulated, at the end of the first year of activity, the revision of the Meridonare operating model.

The observation of the data contained in the evaluation forms has contributed to grasping the two main changes on Meridonare's operating methods and, therefore, to giving an answer to our first research question (*H1*).

The first important change concerned the verification of the social purposes pursued by the applicant association to the platform for fundraising. The identification of a set of key variables ennobles the role of the crowdfunding platform which, acting as a hub that raises the sharing of knowledge, lays the foundations for the creation of an ecosystem of high-impact social initiatives. In this context, the Meridonare operators carry out an evaluation of the congruity of the requested amount in relation to the social objective pursued (e.g. the money necessary to purchase a minibus to accompany children to school) to obviate a detected tendency to make requests too high. The lack of congruence between the request for funds and the funds actually necessary for the realization of the project is one of the main causes of failure of the crowdfunding campaign.
The second change has been the introduction of a reward mechanism in order to avoid that the failure campaigns determine a use of the collection not in line with the social objectives pursued. The reward mechanism works in the following way (Gallucci et al. 2018):

- if the crowdfunding project collects less than 15% of the funds, the NPO will not receive the funds, and the funds will be devolved to another project on the platform indicated by the NPO itself:
- if the crowdfunding project collects between 15% and 50% of the funds, the applicant organization ought to modify its proposal to persuade both Meridonare and the Foundation that the additional funds will contribute significantly to the finalization of the project (e.g., the NPO wants to buy a 9-seater bus, but, alternatively, chooses to buy a 6-seater bus or to acquire a bus by recurring to debt capital and then using the funds collected and the incentives to extinguish the payments).
- if the crowdfunding project collects more than 50% of the funds, then resources are available for the NPO.
- if the crowdfunding project collects at least 100% of the funds (funding target achieved), it receives an incentive from the Foundation, which determines the amount of resources to be transferred (which range from 7% up to 15%) in accordance with the score obtained.

The FBN has reviewed, improving them, the methods of participation in the financing of the most deserving proposals. From an intervention of a preventive nature, the contribution of the Foundation's has turned into successive and rewarding. The reward mechanism actually makes it possible to establish specific priorities with reference to those projects that can be proposed

for additional funds. The incentive program provides eventual financial intervention by the Foundation only for projects that have exceeded the financial target set out for the crowdfunding campaign.

This circumstance has produced two benefits (*H2*): the lower amount of financial resources and greater control over the social impact of the financed projects. The combined effect of these two benefits has produced a multiplier effect. In quantitative terms, Meridonare's activity has determined an important social leverage effect. For each euro of contribution to the projects paid by the Foundation, more than three euros were mobilized by non-institutional donors. Faced with 410,800 euros of financing from the FBO, the crowdfunding platform has collected and supported the various 140 projects with over 1 million and 190 thousand euros.

In this perspective, Meridonare's role is not merely to act as a standard crowdfunding platform, but to facilitate interactions and relationships between various stakeholders in order to raise the chances of fundraising. The platform operates in order to broaden the charitable activities in the area by involving the support of donators who otherwise would not have participated.

The multiplier effect underlines the importance of overcoming that instrument of philanthropic activity of the Foundation and, therefore, justifies the support to the development of the platform through the coverage of the management costs and the support in the selection of human resources. The FBN plays a key role in allocating resources in a rational and strategic way on projects that really contribute to maximizing the social impact. In this perspective, the Foundation has identified in Meridonare not only a tool to attract donations, but also a means to monitor, evaluate and leverage the efficacy of its own social intervention (Gallucci et al. 2018).

4. Discussion and conclusion

The understanding of social investment activities carried out by a crowdfunding platform such as Meridonare can only take place if the role and methods of intervention of the Italian foundations of banking origin are analyzed. The FBOs are bound to very structured and regulated procedures for defining the budget and choosing the recipients of the charitable interventions. This often determines the impossibility of effectively supporting worthy projects of social utility as they are too small in size or excessively fragmented. The creation of a social crowdfunding platform allowed the Banco di Napoli Foundation to expand its sphere of intervention in favor of a large number of small-scale social projects. The multiplier effect that has been created has increased the intensity of philanthropic activity, contributing, among other things, to spreading the culture of investment with a social impact.

Thanks to the feedbacks coming from the evaluation forms and the continuous interrelationship between Meridonare and the Foundation, the platform's operating methods have evolved over time. The development of specific internal skills aimed at optimizing the use of social media and a better understanding of fundraising techniques has encouraged greater coherence between the request for funds and the actual investment needs of the project and the introduction of a reward mechanism. These interventions have produced a double result. First, the propensity to donation of thousands of local subjects was developed by offering them selected proposals and the possibility of participating in a guided and verified process of social support. Second, it consolidated Meridonare's role as a functional tool for the Foundation's philanthropic activity. Meridonare strengthens the effectiveness of FBO interventions in the third sector by favoring the allocation of resources in a rational and strategic manner on efficient projects compliant with the vision and mission of the Foundation. Social crowdfunding makes it possible to establish specific priorities with reference to those projects which, due to their size or fragmentation, may not be part of the

ideal objective of the Foundation's charitable activity.

Given the wider social, political and economic impacts of social investment, the development of an analytical framework is of enduring concern to regulators, practitioners and academics. The drivers useful to increase the return of social investment are expected to be different from those that lead to financial choices. The examination of the relationship between the crowdfunding platform and the bank-originated foundation is functional in order to evaluate the capability to survive in a long-term challenge of sustainability (Cornée, 2017).
The philanthropy sector in Italy is characterized by the presence of the FOBs which largely satisfy the NPO charity demand. Faced with the significant volumes of annual payments (over € 1 billion), the assessment and reporting system for the activities carried out is still not adequate. Attention to the transparency of the processes, which is met through the mandatory publication of the payments made, prevails over the assessment of the social impacts of the disbursements themselves (not required by any legislation). Meridonare's initiative and its instrumentality in the mission of FBN represents an innovative modality in the operating model of banking foundations. The drivers of success turned out to be the innovative use (for the sector) of the crowdfunding tool, the wide offer of online and offline services, the technical skills of the team and the intense relationship between the Foundation and the platform that led to periodic improvements in the operating process including the introduction of the reward mechanism. The main benefits of this approach are represented by the growth of social interventions in the territory, by the multiplier effect on the philanthropic activity of the Foundation and by the diffusion of solidarity values among a wide audience of private subjects.

The present work highlights the set of key points useful in order to support worthy social initiatives and increase their rate of success in raising funds. In this context, the drivers useful for increasing the return on social investments should be different from those that drive the competitiveness of a social crowdfunding platform compared to other crowdfunding platforms.

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FOOD FOR THOUGHT: IVE4FSG - INTERNATIONAL VIRTUAL EXCHANGE FOR FOOD SECURITY GOVERNANCE

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Abstract

Food security involves global awareness and efforts addressing resources, access and consumption of nutritious and balanced meals which sustain each individual in its own needs. In this paper, we share experiences regarding an international virtual exchange and highlight how food security is perceived throughout different cultures and perspectives.

BRaVE/UFPE and COIL/SUNY are virtual exchange initiatives in Brazil/UFPE and USA/SUNY. In 2019, about 60 students from both countries engaged in collaborative study focusing on UN's Sustainable Development Goals. FSG is a broad concept and because of that it often raises confusion instead of promoting clear guidelines for healthy eating, production and consumption.

The Brazilian Ministry of Health issued a Food Guide for the Brazilian Population which suggests Ten Steps for Healthy Eating. Students in New York state and in Pernambuco state had these Ten Steps in an icebreaker session at separate times when each group selected those most challenging items from easy ones to follow regularly.

FSG pillars by WHO: resources, access and consumption

Food… A person has the ability to...

■ ***Resources: …*** *secure sufficient financial resources to purchase enough nutritious food to support a healthy diet on a consistent basis.*

■ ***Access: …*** *obtain affordable, nutritious, and culturally appropriate foods safely and conveniently.*

■ ***Consumption: …*** *prepare and store healthy meals, and the knowledge of basic nutrition, food safety, and cooking.*

Linking the Ten Steps to Healthy Eating to FSG's three pillars it was noticed that consumption, more often than resources and access, plays a strong role emphasizing that the "ability to prepare and store healthy meals, and the knowledge of basic nutrition, food safety, and cooking" is a main skill for healthy eating.

This finding supports the understanding that FSG request a complexity approach more than jumping into seemingly easy and fast solutions. While most of responsible consumption studies look at behavior patterns and changing habits, there is an urgent need which is more than food for thought.

Keywords: *Healthy Eating, Food Security Governance, FSG, International Virtual Exchange*

Track: *Governance Management & Leadership Entrepreneurship Education*

Word count: *3.856*

1. Introduction

The present study looks at stated eating habits via an ongoing survey which we plan to present partial results given the OFEL submission deadline. It is part of a larger International Virtual Exchange program between Brazil and U.S.A., called BRaVE for Brazilian Virtual Exchange and COIL for Collaborative Online International Learning. In 2019 joined initiatives took place evolving over 100 students (UFPE, 2019).

Healthy eating is a buzz-word related to slow food, veganism, or not skipping breakfast (NHS, 2020), giving some short illustrations.

1.1 BRaVE/UFPE and COIL/SUNY

BRaVE/UFPE and COIL/SUNY are both virtual exchange programs ran by universities. These initiatives allow people to gain access to high-quality international and cross-cultural education through the internet (VIRTUAL EXCHANGE COALITION, 2019). BRaVE stands for Brazilian Virtual Exchange and it's managed by the directory of international relations at the Federal University of Pernambuco, a university based in Recife, Brazil. COIL stands for Collaborative Online International Learning, and it's managed by the State University of New York, at New York, United States of America. This article has arisen from a collaboration between three different classes: Recife, Brazil - UFPE; Caruaru, Brazil - UFPE and Brockport, United States of America - SUNY. This cooperation allowed the students from each of these classes to unleash themselves from their realities regarding food security governance, mainly by interacting in specific assignments, through videoconferences and computer-supported collaboration, such as Google Suite.

1.2 The Brazilian Ministry of Health's Ten Steps to Healthy Eating

The Brazilian Ministry of Health's "Nourishment Guide for the Brazilian Population" was used throughout the discipline to define which healthy eating habits were important to this population. Inside the guide, readers are able to find ten steps that summarize good practices when choosing a healthier lifestyle. These are called, in free translation, the "Ten steps to adequate and healthy nourishment", or our "Ten Steps to Healthy Eating".

These are:

1. Try adding mostly natural state (unprocessed) and minimally processed foods to your food pyramid's base.
2. When seasoning and cooking food, (only if really needed) use oil, fat, salt and sugar in small quantities.
3. Limit the consumption of processed foods.
4. Avoid the consumption of ultra processed foods.
5. Eat regularly and attentively, in appropriate settings and, if possible, with company.
6. Shop in stores that offer great variety in natural or lowly processed foods.
7. Improve, nurture and share your cooking skills.
8. Plan your schedule so you can give your meals the appropriate time they deserve.
9. Give preference to eating facilities where fresh food is served.
10. Be critical regarding information, advices and messages about nourishment offered in commercials.

1.3 World Health Organization's Three Pillars of Food Security

Another material used in the discipline was regarding the Three Pillars of Food Security Governance, by the World Health Organization, which defines the ability a person has to:

■ **Resources: …** *secure sufficient financial resources to purchase enough nutritious food to support a healthy diet on a consistent basis.*

■ **Access: …** *obtain affordable, nutritious, and culturally appropriate foods safely and conveniently.*

■ **Consumption: …** *prepare and store healthy meals, and the knowledge of basic nutrition, food safety, and cooking.*

1.4 Relating the Three Pillars of Food Security to the Ten Steps to Healthy Eating

After observation, it was noticeable to the authors that there were many parallels regarding the relationship between the ten steps to healthy eating and the three pillars of food security, illustrated by the presence of at least one pillar in each step to healthy eating. It was visible that most, but not all of the steps fit into the triad of resources, access and consumption. Only four of those ten did not fit the criteria for the three pillars: #2, #5, #7 and #8, with #7 being related to both access and consumption, but not resources, while the rest only had ties to the pillar of consumption. With that said, six steps out of ten have to do with the three pillars, which involve resources, access and consumption.

Approximately 25% of the population of Brazil lives below the poverty threshold, with 6.5% living in extreme poverty, according to World Bank's standards. Even people who are considered to be above these thresholds aren't that better off, with 60% of brazilian workers earning less than a minimum wage per month. Seeing that these are steps meant to be followed by the majority of population, which does not have access or resources, it's concerning that so many of these habits proposed by the Brazilian Ministry of Health do not reflect the reality of the majority of the population, nor are they easily reachable by them.

Sources: IBGE apud Estadão (2019) and IBGE apud Época Negócios (2019).

1.4.1 Synthesis of relationship between the ten steps to healthy eating and the three pillars of food security

Healthy Eating Habits	Resources *Financial*	Access *Convenience*	Consumption *Prepare, Store and Cook*
1 - Try adding mostly natural state (unprocessed) and minimally processed foods to your food pyramid's base.	X	X	X

2 - When seasoning and cooking food, (only if really needed) use oil, fat, salt and sugar in small quantities.			X
3 - Limit the consumption of processed foods.	X	X	X
4 - Avoid the consumption of ultra processed foods.	X	X	X
5 - Eat regularly and attentively, in appropriate settings and, if possible, with company.			X
6 - Shop in stores that offer great variety in natural or lowly processed foods.	X	X	X
7 - Improve, nurture and share your cooking skills.		X	X
8 - Plan your schedule so you can give your meals the appropriate time they deserve.			X
9 - Give preference to eating facilities where fresh food is served.	X	X	X
10 - Be critical regarding information, advices and messages about nourishment offered in commercials.	X	X	X

1.4.2 Detailed Analysis of the relationship between the ten steps to healthy eating and the three pillars of food security

1. Try adding mostly natural state (unprocessed) and minimally processed foods to your food pyramid's base.

This step relates to the three pillars of food security.

2. When seasoning and cooking food, (only if really needed) use oil, fat, salt and sugar in small quantities.

This step regards the pillar of consumption, as the dosage of these condiments are an active choice people can make when consuming food.

3 and 4. Limit the consumption of processed foods and avoid the consumption of ultra processed foods.

Both of these steps are covered by the three pillars of food security. In the resources realm, one can argue that for some populations, it's cheaper to get processed and ultra processed foods than something fresh when eating out. As for the access pillar, there are places in which consuming fresh food isn't as easy, such as remote areas with harsh climates. Finally, regarding consumption, there is the convenience of processed and ultra processed foods through the form of packaged goods that makes them an attractive choice for people today.

5. Eat regularly and attentively, in appropriate settings and, if possible, with company.

This step relates to the consumption pillar, as it's determined by how and in what settings a person will consume food.

6. Shop in stores that offer great variety in natural or lowly processed foods.

In this case, the three pillars fit into the step. Similarly to steps 3 and 4, shopping for natural and lowly processed foods requires resources for this, as many organic produces are actually more. People also need to have easy access to fresh food markets, which are not available everywhere. Regarding consumption, people need to be inclined to consume these fresh foods and have the urge to go after them when shopping.

7. Improve, nurture and share your cooking skills.

This step relates to the pillars of access and consumption. For people to be able to improve, share and nurture their cooking skills, first they need to acquire access to a cooking setting, something that many people don't have access to (e.g. college students who live in dorms). It also has to do with consumption as cooking is a process of preparing food for consumption.

8. Plan your schedule so you can give your meals the appropriate time they deserve.

The step fits into the consumption pillar, as arranging time for meals is related to how one consumes food.

9. Give preference to eating facilities where fresh food is served.

This relates to the three pillars, for the same reasons stated in 3, 4 and 6.

10. Be critical regarding information, advices and messages about nourishment offered in commercials.

This step relates to the three pillars as thinking critically about this type of information has to do with consumption, but also with resources and access, as these are basic pillars to empowering people to make their choices.

2. Methodology

Mixed method makes this study as it started with a literature review, discussion in international classrooms, which took us to develop an online questionnaire aiming at an international survey with closed and open questions to be deeper discussed via focus groups in different settings with BRaVE/COIL partners and others who show support to taking part in the study.

Building the questionnaire required not only specific choices regarding the formats of the questions as open and closed, but also respecting respondents' privacy. After many discussions we decided to apply an online questionnaire 'open to all', assessing the risks related to having anyone entitled to answer it no matter its gender, age, education and occupation as closed options, but none as obligatory, to be followed by open questions regarding main educational background and city/country of residence.

For this particular OFEL paper, we look into quantitative analysis of the survey with some qualitative illustrative analysis from the answers to open questions which followed the closed ones on the online questionnaire available as an attachment to this international conference paper submission.

In order to provide an exploratory descriptionary analysis we use basic descriptive statistics applied to 189 answered questionnaire by Brazilian population in Recife the Metropolitan Area which include municipalities of Recife, Olinda, Jaboatão dos Guararapes and /Pernambuco. This number - 189 answers - was achieved within one week of the questionnaire online, from Saturday 18th January to Saturday 25th, and we resummed the presented analysis to this number as sufficient estimate of Brazil's Pernambuco state population mostly based in its capital, Recife, and the large metropolitan area. For January 2020, 10 million inhabitants is an estimated number of Pernambuco's population based on 2018 numbers (IBGE apud G1, 2018). And about half of it lives in 10 larger cities as Recife, Jaboatão dos Guararapes, Olinda, Paulista, Cabo de Santo Agostinho, Camaragibe, Igarassu, São Lourenço da Mata and Abreu e Lima. If Recife alone has about 2 million inhabitants today, we can state that our survey when restricted to Recife's respondents would have

Pernambuco's population in 10 most populated cities, according to IBGE in 2018

Recife - 1.637.834; Jaboatão dos Guararapes - 697.636; Olinda - 391.835; Paulista - 329.117; Cabo de Santo Agostinho - 205.112; Camaragibe - 156.736; Igarassu - 115.640; São Lourenço da Mata - 112.362; Abreu e Lima - 99.622 and Ipojuca - 94.709.

Source: IBGE apud G1 (2018).

3. Applied study

A survey has been applied, in Portuguese, addressed mainly (but not only) university students, with the objective of understanding how the ten steps to healthy eating were perceived and applied in these people's daily lives. The survey bore questions such as the three perceivably most difficult and easiest steps to follow, the frequency in which these steps were present in the respondents' routines, and left some space for non-mandatory qualitative answers, especially regarding their perceptions as to why some habits are easier or harder to follow. The formulary also had a section for the respondent's socio-economic profile, which was non-mandatory as well.

The survey was promoted through online channels such as Facebook and email listings, as well in real time, gathering a number close to 200 respondents in total, most of them from Recife's metropolitan area in Pernambuco, Brazil.

4. Data analysis with discussion

For this exploratory analysis we present and discuss the two main questions which involve those items pointed out: the easiest steps to healthy eating to follow regularly and the opposite, those which are hard to achieve.

4.1 The Stated Easy Healthy Eating Habits

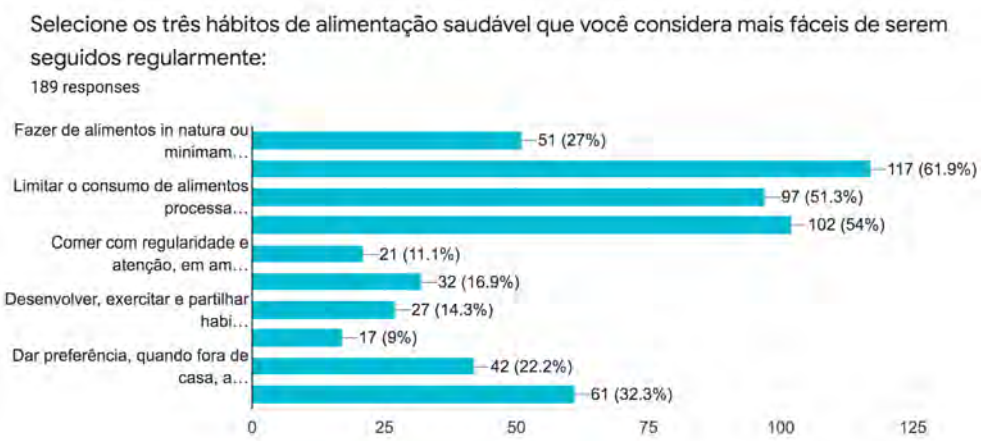

Figure 1: Graphic representation of the three easiest healthy eating steps to follow.

The figure below shows the graphic representation of the quantitative answers to the question: "Which habits do you find easier to follow?"

Provided the ten actions for healthy eating habits, respondents as a group seem quite clear about the three easiest practices when pointing out items 2, 3 and 4, copied below:

> 2 - When seasoning and cooking food, (only if really needed) use oil, fat, salt and sugar in small quantities.
>
> 3 - Limit the consumption of processed foods.
>
> 4 - Avoid the consumption of ultra processed foods.

From the FSG analytical perspectives of Resources, Access and Consumption we can raise as questions how each plays a role to the three most answered alternatives as easier than others. These three items 2, 3 and 4 strongly relate to the definition of Consumption in food security when it is about preparation and storage of healthy meals, and the knowledge of basic nutrition, food safety and cooking. While knowledge of highly processed and ultra processed foods is required, it seems that most respondents are aware of that. This particular aspect can be raised as a limitation of the online survey answered by those who participate in the digital economy and therefore literacy.

The figure below illustrates a WordCloud mapping highlighting the words Time, Practicity and Facility - tempo, praticidade and facilidade, in Portuguese.

Figure 2: In Portuguese language, the easiest steps to follow's word cloud, gathered from all qualitative answers regarding the question minus.

Interestingly enough, "access", "resources" and "consumption" appear organically in the word cloud, further exposing how the ten steps to healthy eating relate to FSG's Three Pillars of Food Security.

4.2 The Big Challenges

As for the most difficult to follow, the steps 5, 6 and 8 were elected:

5 - Eat regularly and attentively, in appropriate settings and, if possible, with company.

6 - Shop in stores that offer great variety in natural or lowly processed foods.

8 - Plan your schedule so you can give your meals the appropriate time they deserve.

As the three most difficult habits to follow, more than in the easy habits previously appointed, knowledge plays a strong role and it seems that it is not lack of knowing how important they are. They strongly relate to routine and the act of making time for meals.

The figure below illustrates the most difficult steps to follow according to the respondents:

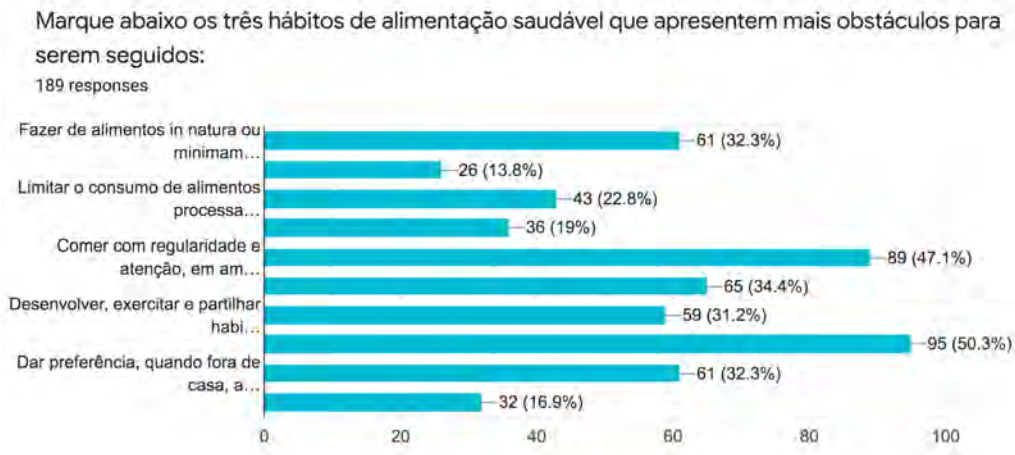

Figure 3: Graphic representation of the three most difficult healthy eating steps to follow.

Below, we also have a figure of the WordCloud for the qualitative answers regarding these steps:

Figure 4: In Portuguese language, the most difficult steps to follow's word cloud, gathered from all qualitative answers regarding the question minus.

One of the most mentioned words in the answers reported was "time", mentioned over 60 times throughout all qualitative answers. The main usage of the word was when referring to the difficulties of maintaining healthy habits while having to deal with time, especially when fast-food is an alternative time-saver. Routine and work, mentioned 14 times each, also revolve around the fact that it's hard to eat healthily and fit these habits into short on time routines.

The similar words “price” (14 times), “cost” (9 times), “financial” (4 times), “resources” (4 times), “expensive” (7 times) and “money” (6 times) were used to expose the fact that maintaining healthy habits is expensive and not accessible to the majority of the population as well.

4.3 Respondents Daily Habits

When directly asked about their most common habits we used 'Always' + 'Often' to highlight practices mentioned as 'daily' when compared to others. By visual aid, as the charter available below, we recognize a group of respondents who show (#10) critical perspective when targeted for industrialized food commercials. And it supports the idea that our respondents are educated regarding healthy eating. And also the habit of seasoning with small portions of sugar, salt, oil and fat (#2) also show here. Avoiding ultra processed food (#4) has a high number of respondents making more than ¾ of answers each of these practices highlighted.

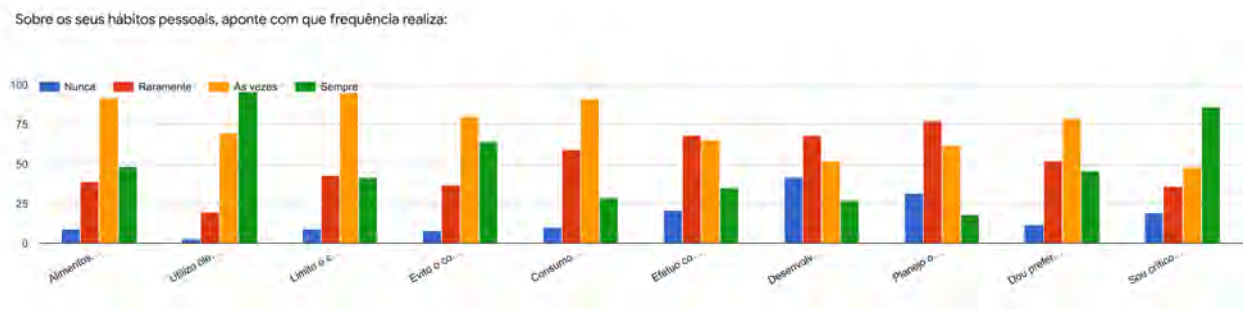

Figure 5: Frequency, in graphic form, of the most practiced healthy eating habits by the respondents.

Some unexpected results worth sharing here in this exploratory study is that our choice to offer an open questionnaire, or mixed questionnaire with some open questions, is that a good number of replies was achieved and two respondents included their email voluntarily offering to be contacted. One stated concerns regarding food safety when eating out and other commenting to have written its graduation thesis on the subject of food security.

4.4 Socio-economic analysis

Gender: 0.5% of the respondents were non-binary, 30.2% were men, and 69.3% were women

Age range: 43.9% were between 16 to 24 years old, 28.6% were between 25 to 34 years old, 13.2% were between 35 and 49 years old, 12.7% were between 50 and 64 years old and 1.6% were over 65 years old.

Occupation (multi-selection): 49.3% were students, 22.9% worked part-time, 44% worked full-time, 2.7% were retired.

Education: 39.7% had incomplete bachelor’s degree, 17.5% had complete bachelor’s degree, 13.8% had graduate’s course degree complete, 8.5% had master’s degree incomplete.

5. Main findings

Dear Watson, and so what? Further studies are requested if one wants to gather into conclusions. What can be learned from this simple survey with almost 200 respondents in Brazil does not necessarily add to what is known, but it reinforces the need to support initiatives which recognize and take action, aiming at improving basic education on food security involving cooking. Have students and workers facilities provided cooking tools and collective cooking activities? Storytelling competition, when did I last cook for my family and friends? To grandparents who often provide us all with great food memories, shall we cook together?

Summarizing the main findings based on Brazilian responses answered in January 2020, to those - over 50% - who answered that easy practices involved (a) seasoning and cooking food with small amounts of salt, sugar, fat and oil; (b) limited processed food consumption; and (c) ultra processed food avoidance; one can suggest that we address highly educated people in food security even though one respondent suggested that the questionnaire should be followed by a glossary. The concerns go to those almost other half who do not define these items as the easiest to follow, but the hardest - ranging from 14% to 25% in these same three items #2, #3 and #4.

For large number of respondents, the hardest practices to be followed are #5, #6 and #8. Planning seems to be the key challenge for a healthy eating by far when compared to other nine items. With over 50% of responses this is the most mentioned item and it does not depend necessarily on resources, access nor knowledge as suggested in FSG three pillars literature. A mindset to take responsibility for their own feeding could make a new agenda for healthy eating.

Finally and corroborating with the internal validity of the questionnaire as a research tool, the lack of planning for healthy eating is also answered as the least often practice undertaken by respondents with only 12 'always' and 50 'often'. On the other hand, those practices pointed as the easiest are also answered as the most commonly undertaken - #2 - 60 + 75; #3 - 74 + 36; and #4 - 67 + 53. Also #1 and #10 are pointed out as practices with over 100 answers as 'sometimes' and 'always'.

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PROMOTING ENTREPRENEURIAL THINKING AND ACTING OF STUDENTS THROUGH COMPETENCY-BASED LEARNING

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Abstract

Encouraging students to think and act entrepreneurially requires complex skills and competencies. To convey these skills, most of the university efforts so far have focused on extracurricular entrepreneurship education. The University of Applied Sciences HTW Berlin (HTW) has already launched numerous curricular and extracurricular programs and projects in the field of awareness raising and entrepreneurship promotion – from individual and project courses to lecture series, etc. Up to date, however, there is no holistic approach for entrepreneurship trainings in higher education.

The present proposal addresses this research gap by developing a flexible and modular entrepreneurship-training programme for universities of applied sciences. Building on a literature review on entrepreneurship trainings in higher education and the case of University of Applied Science HTW Berlin a training concept regarding the necessary skillset for entrepreneurial thinking and acting, including a guideline for its implementation will be developed. Overall, the paper will provide a systematic view on how to develop a modular and curriculum-based entrepreneurship-training concept in academia. In this regard, it could also be implemented in other universities and educational institutions.

Keywords: *competency-based learning, entrepreneurship education, modular entrepreneur-ship-training, promoting entrepreneurial thinking*

Track: *Competency based learning*

Word count: *5.085*

1. Introduction

If we look at current studies, *helping individuals and organizations of all kinds to create, cope with and enjoy change and innovation* (Gibb 2000, S. 89; Bijedic 2013, p. 37) is one of the principle aims in entrepreneurship education. In this understanding, entrepreneurship can be taught. Or more specifically, obviously different assets and approaches to think and act entrepreneurially can be defined and passed on to learners (in this case prospective founders) as best practices or guidelines for future behavior.

Nowadays, researchers assume that entrepreneurial thinking and acting can be achieved particularly well by trying, experimenting and learning about one's own experience (see theoretical background section). In this understanding, mere informing and learning about entrepreneurship and its components is not enough within entrepreneurship education. This is why, other approaches, such as project based learning, action based learning and experiential learning (for more information see theoretical background section) in this context become more and more important.

All in all, teaching and learning entrepreneurship in higher education is as complex as the skills required for entrepreneurial thinking and acting. But, in view of the challenges graduates are confronted with during their future professional careers, entrepreneurship training is more important than ever and of particular importance at the practice-oriented universities of applied

sciences. Competencies such as the allocation of resources for a specific project, teamwork and creativity (for an overview of entrepreneurial skills see section 4) are required in every professional context - regardless of whether graduates are looking for a self-employed activity or a salaried job position. Universities should generally offer their students extensive training that encourages them to think outside the box. For most, however, holistic educational concepts have not yet been established - and least of all is training for entrepreneurial thinking and acting considered.

The research question of the present paper is therefore how the entrepreneurial thinking and acting of students can be promoted through competency-based learning in higher education. It aims to develop a flexible and modular entrepreneurship training plan for universities of applied sciences. Building on a literature review on entrepreneurship in higher education and the case of University of Applied Science HTW Berlin a training concept is developed that conveys the necessary skills for entrepreneurial thinking and acting. In addition, some implications in order to implement the concept into the students' curricula will be given by the author.

2. Theoretical background

This paper and especially the theoretical background section draws on the status quo of entrepreneurship education research in academia. Over the past two decades research on this topic has become highly relevant. This is due to the fact that universities are more than ever forced to rethink, expand and structure their transfer activities. An important area here is the interaction with the private market place, e.g. in the nature of the entrepreneurial activity of students, staff etc. (Mars and Rios-Aguilar 2010, p. 441).

In Germany, higher education is largely determined by the research assignment or the practical relevance of the respective educational institution. While the classical universities primarily fulfill their research mandate, the universities of applied sciences focus on practical relevance within their activities and programmes. The cooperation with companies, extensive and numerous phases for the acquisition of professional experience, for example internships, characterize the study course at universities of applied sciences as well as the professional experience that their teachers bring to teaching and research. Teaching entrepreneurship therefore is of great importance to the latter.

Entrepreneurship training at universities in a German context usually takes place as follows: there is a startup center set up as a service center, to which students interested in the subject can turn. Extracurricular and free workshops and training courses for further education in this area are also offered here. Possible topics of the events are the financing of a startup project, the registration of patents, tax aspects etc. Increasingly - at least in Germany - events are also provided in the area of sustainability; social entrepreneurship is a particularly popular topic here. Startup projects are no longer only supported in a profit-oriented area, but also beyond.

However, extracurricular events and individual consultations usually dominate the reality of entrepreneurship education at universities. As a logical consequence, the activities of the startup centers only reach students who are already planning to start their own startup project or at least have already thought of this idea. But what about all those students who have never thought of this before? Whose environment is barely entrepreneurial and who may have never learned the confidence in their own abilities, which are necessary for a startup? Those students are usually not part of traditional entrepreneurship education efforts at universities.

Common entrepreneurship courses also usually remain with offers in which you can learn about entrepreneurship. However, newer approaches in research on entrepreneurship in higher education

assume that entrepreneurship can only be achieved by trying, experimenting and learning about one's own experience (see Ebbers 2004). First and foremost, it is important to motivate students to become and/or think as entrepreneurs. And the least you can convey motivation through learning about mere content. In order to do this and to enhance entrepreneurial thinking and acting, the learning environment must be designed differently and include, for example, inspiring personalities and successful startup examples, but also opportunities to make the requirements of starting a business tangible. For this, newer approaches and creativity methods, such as design thinking become more important within entrepreneurship education.

Experiential learning nowadays is also widely used within the context of entrepreneurship education (Lackeus and Williams Middleton 2018, p. 20). Experiential learning is particularly about the creation of processes with open results. Action and project based learning are additional approaches when it comes to teach entrepreneurship in academia. „Project based learning places students in realistic contextualized problem-solving learning environments“ (Blumenfeldt et al. 1991, p. 372). The advantage of this approach is that it is interdisciplinary and thus allows a broad view of a topic and its context. In addition, the overall problem as well as the structure are determined by the students themselves. Action based learning, on the other hand, is based on real life experiences, for example in a real-life venture creation environment, but within the protected framework of the respective university. Failure is allowed and widely accepted (Lackeus and Williams Middleton 2018, p. 28, 29).

Ideally, entrepreneurship education combines all of these concepts in a way that builds on each other. To sum up, entrepreneurship education shouldn´t be only about the subject itself, but should widen the view on methods and instruments used by successful entrepreneurs. Therefore, not only the roles of students who take responsibility for their own learning environment and learning goals, but also those of the lecturer or teacher has to change. The latter now rather assume the role of a trainer or moderator, who only intervenes structurally in the learning process.

According to Schulte (2002), entrepreneurship education in an university context takes place – in order to also pick up those students who have not yet considered self-employment – in a process that comprises the following five phases: naivety, awareness, interest, action, company formation and success. In order to enable students to go through all these phases, the role of the university lies in providing information, in motivating, qualifying, advising and training their students through appropriate offers (p. 269). In the following, the current state of entrepreneurship training offers in practice is to be determined using the example of the University of Applied Sciences HTW Berlin.

3. The Case: Entrepreneurship education at University of Applied Sciences HTW Berlin, Germany

The University of Applied Sciences HTW Berlin (*Hochschule für Technik und Wirtschaft Berlin*) has more than 14,000 students, about 300 professors, 800 lecturers and approx. 450 employees in administration and, therefore is the largest university of applied sciences in Berlin, Germany. It offers more than 70 undergraduate and postgraduate study courses in the fields of technology, IT, business, law, culture and design. The programmes form part of the five faculties: 1) School of Engineering – Energy and Information, 2) School of Engineering – Technology and Life, 3) HTW Berlin Business School, 4) School of Computing, Communication and Business, 5) School of Design and Culture. In addition to classic disciplines, in the meantime there have also been set up many new courses in, for example, health tech or game design.

The interdisciplinary profile of the HTW Berlin particularly leads to research projects and business startups in the following areas: Health research, renewable energies and energy efficiency as well as cultural and creative industries and digital economy. Startup support at University of Applied Sciences HTW Berlin often focuses on foundations in the cultural and creative industries, such as freelance web and communication designers as well as fashion designers etc. Even if these foundations provide jobs for the founders themselves, they usually remain limited in growth. So far, teams with a complementary competency profile have rarely teamed up to found a startup-company.

The HTW Berlin has already launched a large number of extracurricular events, such as the weekly semester programme "Startup Tuesday" (a total of 27 events in 2018, counted by the author), offers those interested in founding a startup-company the opportunity to find out more or to work on their own ideas. Furthermore, the *Startup-Kompetenzzentrum* (startup service center of HTW Berlin) supports students in the pre-startup phase with individual advice (a total of 85 coachings in 2018, counted by the author) for the further development of ideas and the development of business models. In addition, formats such as the summer university offer workshops for around 50 participants on the topics of business modeling and business planning, marketing, taxes and law as well as soft skills on an extracurricular basis.

All students and graduates interested in founding a startup can also use the prototyping lab at HTW Berlin and the numerous laboratories in the individual faculties to test initial ideas. As a part of the general supplementary subjects HTW Berlin each semester offers around five seminars related to entrepreneurship in general which can be selected by students from different disciplines during the course of study. So far, there is no binding specification by the university management regarding the number of these university-wide offers per semester.

For professors and teachers in general who want to integrate the topic of entrepreneurship more closely into their own teaching, an interest group for entrepreneurship was founded. It is up to the teachers themselves to integrate entrepreneurship-related teaching content into their events. The proportion of such content in the course of study depends to a large extent on the commitment of the respective lecturer; there are no binding requirements for this. An entrepreneurship advisory board is also to be set up shortly, consisting of professors from all 5 schools as well as startup founders and experts from the startup scene in Berlin. A position for entrepreneurship education was also set up from project funds.

4. Holistic entrepreneurship training-programme in higher education

In order to achieve the objective of the present paper, an analysis of the specific skills and competencies required for being entrepreneurial is carried out. Overall, in order to foster students to think and act entrepreneurially, a set of complex skills and competences is needed. So far, many definitions of entrepreneurial skills and competencies have been raised. Man et al. (2002), for example, see the existence of entrepreneurial skills above all in the fact that someone successfully acts as an entrepreneur. Other definitions are somewhat more detailed regarding the components and details of entrepreneurial skills and in some cases also contain a list of individual skills and abilities. In addition, social skills are required to develop the ability to deal with partners, customers and employees correctly and to assume responsibility.They are highly required when it comes to customer acquisition and negotiating (Klapper and Tegtmeier 2010, p. 555).

This is why a flexible and modular entrepreneurship-training plan for higher education especially focusing on social skills shall be developed. With regard to the considered skillset and competency-profile the author draws on the ASTEE dimension of entrepreneurial skills. The

ASTEE tools have been developed for the assessment of entrepreneurial competences of pupils and students across different educational levels. The entrepreneurial skills dimension consits of *Exploration* through creativity, *Evaluation* through planning and financial literacy and *Exploitation* through marshalling of resources, managing ambiguity and teamwork (Moberg, Vestergaard, Fayolle et al. 2014, p. 37).

The competencies mentioned above will be described in the following. Creativity in an entrepreneurial context can be defined as „the ability to think in new and imaginative ways" (Moberg, Vestergaard, Fayolle et al. 2014, p. 16). This ability is related to the "exploration" subdimension as it makes a major contribution to identifying and discovering new business ideas, which is an essential part of being entrepreneurial. Design Thinking is an important tool for learning creativity in the context of entrepreneurship. In essence, this approach serves to develop products and services that are oriented towards people and their needs (Grots and Pratschke 2009, p. 18). Design thinking can be seen as a creativity method that is used to create innovative and human-centered solutions for societal problems; in order to gain new ideas the group composition shall be as heterogeneous as possible.

Planning is a typical project management skill that can be defined as the ability to plan and structure tasks related to a certain project (Moberg, Vestergaard, Fayolle et al. 2014, p. 16). If we see a company as a project, it becomes clear why this ability is also of crucial importance for entrepreneurs. Business planning has a long tradition within entrepreneurship education, and university support for developing a business plan is generally fairly common. Even though there are a lot of offers in this area at universities as well as at non-university institutions (chambers of industry and commerce, regional business plan competitions etc.), the creation of business plans within the framework of entrepreneurship education has proven to be a relatively complex content to teach. Especially for students who have gained only little or no business knowledge during their studies, it can be easier to start by creating a business model in the form of a business model canvas. "A business model describes the rationale of how an organization creates, delivers and captures value" (Osterwalder and Pigneur 2010, p. 14). The business model canvas as a tool is particularly suitable for students from creative fields due to its clarity and the possibility of iterative use (Heinze 2019, p. 14).

Financial literacy is "the ability to understand financial statements and budgets" (Moberg, Vestergaard, Fayolle et al. 2014, p. 17). Even if external parties are usually consulted for the financial planning of young startups, it is still important to have basic financial knowledge in view of persuasiveness in front of potential supporters and customers. It is part of every business plan to prepare financial and cost planning; it also forms an integral part of setting up a business model (see comments on the business model canvas above). As well as planning, financial literacy is a cognitive skill that can be taught easily in an educational setting (Moberg, Vestergaard, Fayolle et al. 2014, p. 17). For this, conventional learning contexts in the classroom are suitable.

The marshalling of resources can also be seen as a key element of project management. It desribes „the ability to assemble and organise resources in order to exploit a business opportunity" (Moberg, Vestergaard, Fayolle et al. 2014, p. 17). Without the ability of marshalling resources, a business opportunity could not be exploited properly. The best way to train this competence is through project work. This is part of many courses at universities of applied sciences anyway. It is important here that the students themselves are responsible for independently working on a specific problem or topic by planning and using human, time and other resources themselves.

The skills of marshalling of resources and of managing ambiguity are closely linked. The future is highly unpredictable. This means that the resources currently available for a project may not be available tomorrow or at a different price. Managing ambiguity is therefore understood as: "The ability to manage and cope with uncertainty and ambiguity in the process of implementing and exploiting a business idea" (Moberg, Vestergaard, Fayolle et al. 2014, p. 17). Both of the abilities mentioned above – collecting resources and dealing with ambiguities – are non-cognitive skills and therefore difficult to convey. In order to learn them it requires a practice and hands-on environment in which students can experiment and try themselves out (for more details on experiential learning see theoretical background section).

Good teamwork is also required to take advantage of a business opportunity. Teamwork can be seen as "the ability to reach goals and achieve assignments through collaboration, as well as building effective relationships with others" (Moberg, Vestergaard, Fayolle et al. 2014, p. 17). Working in a team and contributing your own skills, but also recognizing the perspectives and approaches of others can be learned very well during the studies, especially through project work. Cooperation with representatives of other disciplines, which can sometimes not be smooth and conflict-free, can already be tried out and improved within the protected framework of a university. Conflict ability is also an important skill when being an entrepreneur.

From a students' perspective, learning soft skills from the first semester on is particularly desirable. Startup-sensitized students – such as those who are involved in a student association at HTW Berlin that accepts and processes real orders in the field of communication design – have a precise sense of what competencies they did not learn during their studies and what they would have needed in order to feel prepared now for a "business owners" life. In their opinion, learning team and conflict skills, knowledge on how to set up a business model and at least one good pitch training would be essential for every student, regardless of the subject area (interview conducted on December 13th 2019 at HTW Berlin).

5. Implications for the implementation of the programme at universities of applied sciences

From the entrepreneurship competencies presented in the previous section and the outlined necessary framework conditions and prerequisites associated with their teaching and learning, implications for the implementation of the holistic entrepreneurship training-programme in higher education can be derived.

As outlined above, creativity can be learned through experiencing the design thinking process. At the beginning of the studies, for example as part of the introductory week, such a course could be offered under the heading "innovation" (which is a highly relevant topic in any field of studies) in a compulsory way for all first semesters on one day. For example, this is already recognized practice at the University of Applied Science Hochschule der Medien (HdM) Stuttgart. In this context, university-related questions and problems of students could be dealt with and innovative approaches could be developed. In this way, the university gets a fresh external view of its respective organizational structures and suggestions for improvement (one possible topic here could be the registration process for the studies and the question of how it could be improved from a students´ perspective).

It would also be conceivable to make a mandatory regulation in the general supplementary subject area, so that all students have to attend a course with entrepreneurship relevance or a subject in which innovative solutions are developed using design thinking as a method at least once in the course of their studies. Since no specific previous or specialist knowledge is required for design thinking, creativity can be trained from the author's point of view right at the beginning of the

studies. It is important that the respective course is offered and carried out in a multidisciplinary manner (across all offered courses at HTW Berlin) so that interdisciplinary teams can be formed.

In contrast to creativity, planning and financial competence require some basic knowledge in the areas of organizational structuring and financing. Good knowledge of the industry in which an idea is to be implemented is also required for the preparation of the financial and cost planning. From the author's point of view, it would therefore be advisable to learn these skills later in the course of studies when subject-related content has already been imparted and knowledge of market prices, sales volumes and a good assessment of future market trends has already been gained. Since, as shown above, these competencies can be taught well in a conventional classroom setting, you can work across courses of study here, but this is not absolutely necessary.

Writing a business plan or establishing a business model requires good supervision and guidance from a trainer who has experience in assessing such plans and models. Courses in business modeling could therefore be offered and carried out in cooperation with the startup service center of HTW Berlin. At the HTW Berlin, it has also proven to be sensible to hire external trainers. In the communication design programme at HTW Berlin, such a business model canvas-course, carried out by an external provider, is regularly offered before starting the final thesis phase. Students who deal with a topic that suggests that the content in the long run could be used economically will be trained to make realistic assessments of the market success of their ideas. Other students who want to deal with a more theoretical question as part of their thesis are encouraged to put their topic through their paces again in a business model canvas-course before they immerse themselves in the actual writing phase.

In view of marshalling of resources, managing ambiguity and teamwork, things are a little more complex. As already explained above, a somehow different learning context is necessary than with the other entrepreneurship skills. Thus, project-related experience is required for all three. As an educational institution with proven practical relevance, project work is an integral part of the training of students at universities of applied sciences. It should be compulsory that at least one, better two, cross-semester projects must be completed as part of each course of study at HTW Berlin. The earlier they start, the better. From the author's point of view, the project work can already be applied in the second semester after learning the first subject-related basics.

As an increased level of difficulty in advanced studies, projects could also be offered across disciplines (interdisciplinary work) and, depending on the subject, external players (transdisciplinary work), such as companies, startups, scientists from other universities, etc. could also be included. To aquire the ability of managing ambiguity also experiential learning is important. Therefore, project work is carried out a little further than usual (subject or question is given by the trainer, resources are available and limited in terms of time, human resoures, etc.). It would be advisable that there are hardly any guidelines given for working on the project that go beyond the mere assignment of over-topics.

As part of the team academy-approach, as it is already successfully applied at the University of Applied Sciences Hochschule Bremerhaven in the bachelor's degree course “Foundation, Innovation, Leadership”, the team is put together by and the determination and selection of the resources necessary to deal with a specific topic is entirely up to the students themselves. Here experimenting and trying out is an inherent part of the learning setting. Failure and a new starting can be tried out in the protected environment of the university before students start their later professional career, in which such skills are of crucial importance - regardless of whether they are looking for a self-employed activity or a purely salaried position.

Even if the recommendations for implementing the concept were presented here especially for the University of Applied Science HTW Berlin, it can also be transferred to other universities of applied sciences based on the information given on the location of the courses during the course of studies.

6. Conclusion

In the present work, the author developed a holistic concept for a competency-based training programme for entrepreneurship in higher education. In addition, implications for implementing the programme at universities of applied sciences have been given on the example of HTW Berlin. The starting point was the following observation: At the University of Applied Science HTW Berlin, a variety of individual projects and events related to entrepreneurship and entrepreneurship education in particular are offered. So far, however, there was neither a consecutive integration of these individual activities in curricula nor a systematic review in terms of pedagogical aspects and the status quo of research in entrepreneurship education.

The present contribution addressed this gap of research and, based on the current state of research on entrepreneurship trainings in higher education outlined in the theoretical background section and the analysis of different skills related to entrepreneurial activity developed a holistic concept for training entrepreneurship skills in academia. The main components of the entrepreneurship training-programme are the following:
1) A course on design thinking at the beginning of the studies with students from other courses and disciplines and/or as part of the general supplementary subject area within the course of studies in order to train creativity.
2) A business model canvas-course later in the course of studies when some subject-related content has already been imparted in order to gain planning and financial competence. This course should be completed at the latest before the start of the final thesis phase.
3) Through the completion of at least one, better two, cross-semester projects as part of each study course at HTW Berlin especially marshalling of resources, managing ambiguity and teamwork can be trained. For this, project based work and experiential learning are key.

With regard to the concept presented, a few limitations can also be stated. In view of the University of Applied Science HTW Berlin it can be said that the faculties and schools manage themselves to decide on their offers in the area of general supplementary subjects. For this reason, it is difficult to get an overview of the entire range in this area or to ensure that all students must have attended at least one course within their studies related to entrepreneurship or in which design thinking is used as a method. Here, binding regulations that apply across all schools would have to be drawn up by university management. Furthermore, it is certainly also a question of money whether all schools can afford an extra business model canvas-course for their students, but eventually it would be possible to offer one within the elective area of the study courses - and here many courses have modules related to business administration - as part of one other broader course.

All in all, the presented framework for a holistic entrepreneurship training-programme can only be one part of a comprehensive training in entrepreneurial thinking and acting at universities of applied sciences. Apart from students entrepreneurial activity in a near future could also be enhanced among faculty members, PhDs, post-docs, and professors and teachers. Thus, the success of entrepreneurial training in a university context also depends on the overall university environment being entrepreneurial.

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IS LEARNING WITH VIRTUAL TECHNOLOGY STIMULATIVE OR DESTIMULATIVE?

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Abstract
The goal of the paper is to present the results of the primary research which has been carried out at University of Dubrovnik, Department of Economics and Business and refers to the students' perceptions towards virtual technology (VR) application in learning process. For testing students' attitude the Pine & Gilmore model has been used. According to the Pine and Gilmore model four basic elements have been included in the process of exploring students' attitudes towards virtual technologies, so their perception is classified into four domains, that is in the area of Entertainment, Education, Esthetic and Escapist. Entertainment component referes to the action of occupying a persons' attention agreeably. Educational component refers to the consumers' active participation through interactive engagement of one's mind or body. The consumer absorbs and by doing so increases skills and knowledge. Esthetic component referes to the consumers' passive appreciation and does not alter the nature of the environment. The consumer is immersed in or surrounded by the environment.Esthetic experiences entail customer enjoyment of an enriched, unique physical design. The customer enjoys passively appreciating or "just being in a setting" of the business.Escapist element referesto the consumer active participation. He is immersed in an actual or virtual environment. The consumer is been active actor or participant in events or activities. The four experiences vary based on the customer's active or passive participation and on absorption or immersion in the experienceAccording to the results of the primary research which has been carried out in 2020., using the method of personal interview and including the sample of 150 students it is visible that students have positive attitudes towards virtual (VR) and augmented (AR) reality and their implementation in education. There is no significant difference in attitude between students in Erasmus + Mobility Program and students of University of Dubrovnik, Department of Economics and Busines. The research provides the framework for further activities and planning based on virtual tecnology involment.

Keywords: *attitudes, Dubrovnik, education, students, virtual technology*

Track: *Education*

Word count: *4.713*

1. Introduction

The implementation of virtual tehnology in the process of learning is just in the beginning in education. The goal of virtual technology (VR) is to create a digital environment which students feel immersed. The goal of the paper is to present the results of the primary research which has been carried out at University of Dubrovnik, Department of Economics and Business, refers to the students' attitudes towards virtual technology (VR) application in learning process. The primary research has been carried out in 2020., including the sample of 150 students. For the purpose of this paper the main hypotheses has been stated:

H1. The students have positive attitudes towards virtual technology implementation and they prefer learning with elements of entertainment.

For analyzing data the descriptive statistics has been used. For exploring the students' attitudes the Pine & Gilmore Model has been used.

Brand Experience Model has been presented in 1999. by Pine and Gilmore.The model shows the relationship between the addition of experiences on products and services and successful branding. The theory is that an experience contributes to a positive internal and external brand experience. A positive brand experience contributes to the top-of-mind position of the brand, so people know and trust the brand.

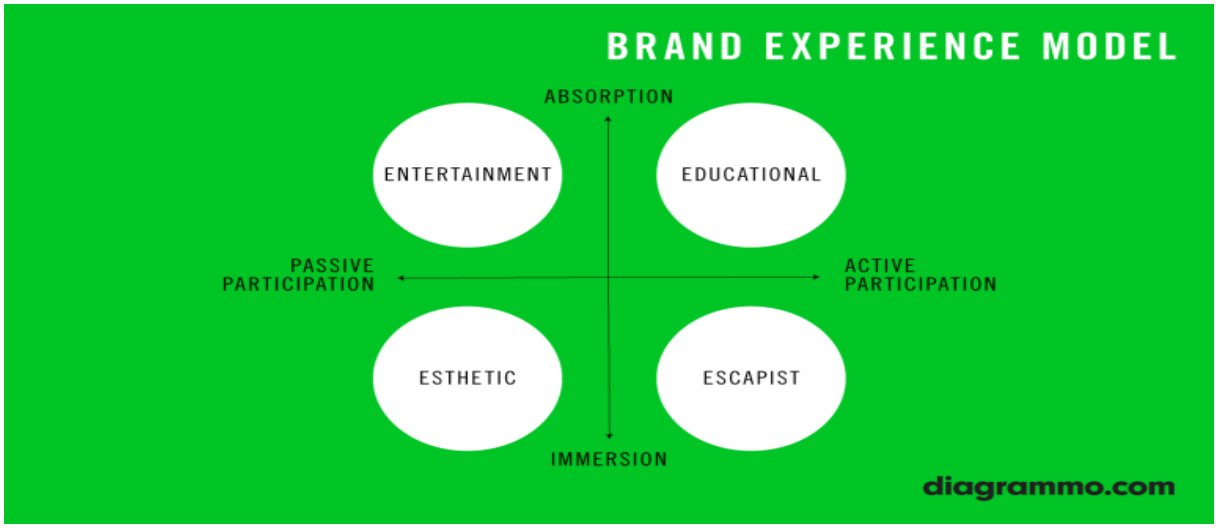

Figure 1: Pine and Gilmore model elements
Source: http://www.diagramo.com

According to the Pine and Gilmore (1999) there are four realms or dimensions of experience differentiated by level and form of learner involvement (Gupta, Singh, 2020, p 205).

So, as it is visible in the matrix experience is classified into four domains, termed the '4ES' that can contribute to strengthening a brand experience. These domains are placed on a matrix divided by an active-passive involvement axis and absorption-immersion dimensions axis that together produce quadrants. The four domains are: Entertainment, Educational, Esthetic, Escapist.Entertainment component referes to occupying a persons' attention agreeably**.**The Educational component refers to the consumers' active participation through interactive engagement of one's mind or body. The consumer absorbs and by doing so increases skills and knowledge. Esthetic component referes to the consumers' passive appreciation and does not alter the nature of the environment. The consumer is immersed in or surrounded by the environment. Esthetic experiences entail customer enjoyment of an enriched, unique physical design. The customer enjoys passively appreciating or "just being in a setting" of the business. Escapist element referestot the consumer active participation He is immersed in an actual or virtual environment. The consumer is been active actor or participant in events or activities (http://www.srdc.msstate.edu).

The four experiences vary based on the customer's active or passive participation and on absorption or immersion in the experience. Active–passive participation entails the level of customer involvement in creation of the experience. For instance, the customer can actively participate in a product trial or passively watch a product demonstration performed by a staff member. Absorption is "occupying customers' attention by bringing the experience into the mind" and immersion is "becoming physically or virtually a part of experience itself" (Pine, Gilmore, 1999, p. 31).

Passive participation of the customer in an experience offered by the business characterizes the Entertainment and Esthetic dimensions, while active participation characterizes Educational and Escapist experiences. The customer who passively participates in an experiential activity or setting does not directly affect or influence these experiential offerings, whereas an active participant will personally affect these activities and settings. The customer typically "absorbs" Entertainment and Educational experiences and "immerses" in Esthetic and Escapist experiences **(**http://www.srdc. msstate. edu. com**).**

Although in real word, the boundaries between these four dimensions are amorphous and not every clear in technology (AR) enhanced learning environments one colud see that various pedagogical tools appeal to a specific dimension (entertainment, education, aesthetic, escapist) of the learner/student. This helps by giving the educator the ability to tune/adjust the active /passive participation (by gamification of AR learning environment) and also the degree to which the learning environment is immersive. This would help in simulating near-real business scenarios and thereby imparting augmented learning to future managers (Gupta, Singh, 2020, p. 205)

According to the statistics, China has planned aim to grow Artifical Intelligence (AI) contribution to GDP to 26% and UK by 10% by 2030. Japan has estimated the economic impact of AI application at JPY to be 1.1. trillion by 2045. The India's digital learning was valued at $ 2 billion in 2016 and it is projected to grow at a compound annual growth rate of 30%, reaching $ 5,7 billion in 2020 as per estimates from Technopak, wherein AI and connected other information and communications technology, such as AR will be a key part of the growth. One of the most important reasons could be capacities of AI and AR technologies in imparting quality education to India's globally linguistically diverse population.New products based do these technologies will make projects such as smart classrooms with digital contents as reality. Strategic investment in and commitment to AI and AR will increasingly become one of the ways that campuses will differentiate themselves in a competitive environment (Gupta, Singh, 2020, p. 207.).

2. Virtual technology (VR) in education

Virtualization technology is possibly the single most important issue in IT and has started a top to bottom overhaul of the computing industry. The growing awareness of the advantages provided by virtualization technology is brought about by economic factors of scarce resources, government regulation, and more competition. Virtualization also provides high availability for critical applications.Virtualization can simplify IT operations and allow IT organizations to respond faster to changing business demands (http://www.software.intel.com.). Virtualization is technology that lets us to create useful IT services using resources that are traditionally bound to hardware. There is no sharp line delineating a frontier between augmented (AR) and Virtual (VR) reality. AR can be considered as an extension of VR, which mixes a vision from real world with virtual elements to create a real-time mixed reality (Martinez-Gutierrez et al., 2017, p. 473.)

Rosemblum & Cross (1997), indicate three basic key aspects linked to any VR system: Immersion, Interaction and Visual Realism. Immersion is created by surroundings the user with virtual technology e. g. virtual glasses, HMDs, sounds and other element creating sensorial stimuli, so usement of virtual tecnology stimulates the presence of the user in the virtual environment. Interaction as a cycling process of communication acts and their interpretations (Hornbaek, Oulasvirta, 2019)**.**Visualisation is any technique for creating images, diagrams, or animations to communicate a message. Visualization through visual imagery has been an effective way to communicate concrete ideas.Visualization helps to tell stories by curating data into a form easier to understand, highlighting the trends and outliers. A good visualization tells a story, removing the noise from data and highlighting the useful information (http://www.tablau.com).

Different categories of immersive reality (AR, VR, MR) involving different types of equipment have potential to establish a contextual relationship between users, reality, and virtuality and enable collaboration and engagement in virtual environments. In recent years, Augmented Reality (AR), Virtual Reality (VR), Augmented Virtuality (AV), and Mixed Reality (MxR) have become popular immersive reality technologies for knowledge dissemination. The different situations are defined by factors refer to the technology's or the interaction method's potential and/or demonstrated capability to: (1) establish a contextual relationship between users, virtual content, and learning context, (2) allow collaboration between users, and (3) enable engagement with the context in the virtual environments and the virtual environment itself (Bekele, Champion, 2019).

Interaction between users and virtual content is a crucial element of any immersive visualization environment. This is even more true for VH applications where leaning is impacted by the interaction with virtual content. The common types of interaction methods are: tangible, collaborative, device-based, sensor-based, multimodal, and hybrid interaction methods.Tangible interfaces allow direct manipulation and interaction with virtual information through physical objects.Collaborative interfaces often use a combination of complementary interaction methods, sensors, and devices to enable a co-located and/or remote collaboration among users. Device-based interfaces use GUIs and conventional devices, such as mouse, gamepad, joystick, and wand to enable interaction and manipulation of virtual content.Sensor-based interaction interfaces use sensing devices to perceive users' interaction inputs. The common types of sensors include motion trackers, gaze trackers, and speech recognisers. Multimodal interfaces are a fusion of two and more sensors, devices, and interaction techniques that sense and understand humans' natural interaction modalities. This interface group allows gestural, gaze-based, and speech-based interaction with virtual content. Multimodal interfaces are closely related to sensor-based interfaces. However, the former combines multiple modes of interaction. Hybrid interfaces integrate a range of complementary interaction interfaces to devise a method that combines different characteristics from the above categories. For instance, a combination of collaborative, and multimodal interfaces (Bekele, Champion, 2019. p. 4)

In the next text the exampleof ViaTechnik programms will be explained. VIATechnik's preferred tool for highly polished virtual reality experiences. It is free for the architecture industry and is frequently used to visualize spaces and render architectural models in immersive environments. This tool enables engineers and architects to design and build in a virtual reality environment by means of a powerful editor toolset and the interaction models that have been specifically designed for VR world building. The outcome is a believable immersive experience built upon natural motions and interactions.Translating CAD or BIM models into virtual reality experiences used to take considerable time and programming know how. With the advent of the Unity gaming engine, bringing Revit/3D models into a virtual reality space becomes much easier. Any AEC professional can take their Revit model, bring it into Unity, and create a VR experience. With a bit of programming knowledge, the VR models can also be heavily customized. This powerful, intuitive and flexible tool ensures rapid iteration and fluid workflow, thus allowing engineers and architects to create stunning, interactive walkthroughs and provide clients with a realistic sense of how it would feel like to actually live in the simulated environment.Twinmotion is a powerful and simple visualization engine that takes in various AEC models. Developed for architectural, construction, urban planning and landscaping professionals, regardless of the size and complexity of their project, their equipment, their computer skills or their modeler, Twinmotion is a simple to use tool powered by Unreal Engine that generates amazing graphics in a short amount of time.Oculus Rift's headset is traditionally seen as a tool for gamers. However, in the AEC space, it makes working in virtual environments so much easier. Through the 3D experience combined with motion tracking capabilities, it becomes a lot easier to move around 3D models and look around corners than using a mouse and keyboard. There is no wonder that more and more architecture companies are deciding

to experiment with using the Rift technology for visualisation and design. Rift allows architects to get a real glimpse of how their buildings will look like and understand the scale, something that is impossible to achieve on a traditional monitor (http://www. viatechnik.com).

One of the challenges faced by VR/AR companies was creating less complex and more affordable hardware, which is a key factor to popularize virtual technologies. Latest hardware developed by these companies is classified into three categories : smartphones mounted on headsets, dedicated head mounted displays and augmented reality glasses. Mobile devices like smartphones have actually processors powerful enough, to make them suitable for VR/AR visualization (Martinez-Gutierrez et al., 2017, p**.** 476). For instance, one of the recent HMDs "Microsoft HoloLens," which is built mainly for an AR/MR experience, can also be used for VR scenarios (http://www.microsoft.com).

Generation Z born between 1995-2005 is disrupting the way learning typically happens in higher education. Most of generation Z have used Internet since younge age and they are generally comfortable with tecnology and engaging these tech-savvy studrents in the learning process with their preferred learning style is a challenging task (Azhar, Salman, 2018, p.3720)

There are studies in academic literature refer to the benefits of virtual technology on learning performances.Virtual Reality is motivating for students and they have positive attitudes towards using VR in learning process (Mikropoulos et al., 1998).

Table 1: Students' performance data

Student	Control group	Control group	Control group	VR Group	VR Group	VR Group
	Accurancy Hazzard in Detection (%)	Accurancy in selecting the correct mitigation plan (%)	Time taken to complete the exercise (minutes)	Accurancy Hazzard in Detection (%)	Accurancy in selecting the correct mitigation plan (%)	Time taken to complete the exercise (minutes)
1	78	87	38	91	93	19
2	83	87	32	100	90	21
3	74	91	29	95	96	18
4	74	74	41	95	94	21
5	78	83	34	100	90	23
6	86	87	38	97	93	21
7	83	74	41	97	96	18
Mean	79%	83%	36 min	96%	93%	20 min

Source: Azhar, Salman, 2018, p.3723.

Table 1. shows the students' performance data on correctly identifying hazards and selecting the most suitable mitigation plan as well as time taken to complete the exercise.These results clearly indicate that the VR based safety games/trainings can play a positive role in improving students' understanding, knowledge and interes tin the construction safety education. (Azhar, Salman, 2018, p.3723)

For instance the students in building construction programs learn to analyse the design for building projects and plan their construction by reviewing 2D project drawings (Messner, et al., ,http://www.resesarchgate.net). Using a VR environment educators can effectively instruct students about identyfying and minimizing some factors/situations. The students which have been

involved in experiment „360 panoramic virtual Field trips through the immersive environment could visually „feel“ the jobsite hazards without visiting a jobsite. They were able to interactively discuss possible hazards and develop specific safety plans. The students' interest and understanding oft he course material has been increased. The concept oft his experiment was created using a Ricoh Theta S 360 camera. The camera is capable of obtaining a 360 panoramic digital photograph that could later upload to a VR head mounted device. The VR head mounted device chosen fot this study was the Oculus Go, primarly chosen for the capability zo instantly view 360 panoramic digital images without the need for futher processing for a virtual reality environment. In this way students have had opportunity to experience multiple virtaul reality site .They were given as much time as they wanted to explore the virtual project site and were encouraged to ask queastions to the instructor during their time with the VR headset (Azhar et al., 2018., p. 3727). The Science Center to Go project is based on education by experimenting with virtual objects. (http://www. sctg.eu).

According to the SWOT anaysis of VR/AR technologies in education given by Azhar, Kim & Salman (2018) it is vible that the main strengths are: accurate depiction of real scenarios, interactive, improve knowledge retention,improve students interest, reduce dependence on fields visits, matches life style of generation Z. The main weakness refer to next elements: imaturate technology, substantial time commitment in the development stage, not suitable for allinstructors, motionsickness, high costs. Opportunities provided by virtual technology implementation are: effective platform for the 21 st century education, suitable in both education and training, technology is becoming cheaper and affordable, encourage active learning. According to the Azhar, Kim & Salman (2018) there are also next threats: less sustainable, not suitable in a traditional classroom, multiple support platforms „confuses“ users (Azhar et al., 2018, p.3728).

Martin Gutierrez et al. (2017, p. 480) define four main aspects regarding the advantages of using virtual technologies:

1.Virtual technologies increase students' motivation and engagement. Students have immersive experience and feel as protogonist, while studying 3D models that enhance their learning experience.
2. Virtual technologies allow a constructivist approach of learning. Students are free to interact with virtual objects and students. As a result, students can investigate, experiment, and obtain feedback, resulting in an experience that improves their learning.
3. Virtual technologies are now affordable and accessible. Recent technological advances ease access to VR/AR with smartphones, tablets, and videogame devices. Complex devices are not required anymore and students can access to shared VR contents through common online platforms such as YouTube.
4. Virtual technologies allow than conventional learning materials and by using VR/AR students feel immersed while interacting with concepts, objects and processes by using headsets, tactile gloves and motion sensors. This immersion permits to experiment environments with realistic objects that can not be accessible otherwise**.**

They also point out some limitations of using virtual technologies in education such as:

1.Studens are not competent using technologies in educational environment (margaryan, Littlejohn & Vojt, 2011)
2.The use of newer innovative technologies does not involve necessarily pedagogic innovations (Martin Gutierrez et al. 2017, p. 482).
3.It is required to design Virtual Learning Environments (VLEs) beginning with pedagogical affordance to maximize learning outcomes (Fowler, 2015).

4.The pedagogical scaffolding of VLEs requires academic staff to be involved actively when designing virtual learning scenarios to obtain maximum learning benefits (Martin Gutierrez et al. 2017, p. 482). In the next text the results of the primary research refer to students' attitudes toward VR technology implementation in learning processes will be shown.

3.The results of the research

The primary research has been carried out in 2020., at University of Dubrovnik, Department of Economics and Business, including Croatian students and student in Erasmus+ mobility program. The method of personal interview has been used for exploring students' attitudes towards Virtual tecnology. The sample of 150 students has been choosen.

The share of 70% of students consider that virtual technologies generally is very important., 10% think VR technology is important and 20% consider it is neither important, nor unimportant.

Table 2: Students' interest towards virtual technology in education

Interest Technology	High	Middle	Little	No interest
Without VR	10%	60%	25%	5%
With VR	70%	15%	15%	-

The next table refers to the students' attitudes towards different types of technologies and their importance in education.According to the results oft he research given in table 2. it is visible that studentds show the higer level of interes for education including virtual tecnology implementation.

Table 3: The importance of each type of the virtual technology in education

Importance Type of technology	Very important	Important	Neither important nor unimportant	It is not important
2D	25%	60%	10%	5%
3D	12%	68%	20%	-
4D	20%	65%	15%	5%
5D	55%	25%	15%	5%

According to the result of the research carried out at University of Dubrovnik, Croatia, including the the sample of 150 students it is visible that the largest number of respondents,that is 60% of them consider that 2D technology is important and 25% think it is very important in education. The share of 10% consider that VR tecnologies are neither important, nor unimportant and for 5% of them think it is not important. From the data given via table 3. it is visible that 68% of students think that 3D technologies are important and 12% that it is very important, 20% consider it neither

important, nor unimportant. The share of 65% think that 4D technology is important, 20% find out that it is important, 15% think it has middle level of importance and for 5% of them it is not important . The situation is just a little bit different with 5D technologies where 55% of students think that it is very important, 25% it is important, 15% consider it neither important, nor unimportant and 5% think it is not important.

According to the result of the research carried out at University of Dubrovnik, Croatia, including the the sample of 150 students it is visible that the largest number of respondents,that is 70% of them consider that virtual technology has high level of importance in educational organizations in the area of entertainment, while 30% think it is neither important, nor unimportant. The situation is the same with VR influence at the element of education, but just a little bit different in case of the esthetics. The most of students, 53% of them consider that the virtual tecnology is neither important, nor unimportant for educational organizations in the area of esthetics, 35% of them think that it is important and 12% consider that it is not important at all. The results of the research refers to the area of escapism shows that 42 % of students consider that it has high level of importance for educational organizations, and 58% find out it has middle level of importance.

Table 4: Importance of VR technologies based on Pine & Gilmore model elements

Importance Elements	High	Middle	Small	Not at all
Entertainment	70%	30%	-	-
Education	70%	30%	-	-
Esthetics	35%	53%	-	12%
Escapism	42%	58	-	-

Table 5: The influence of each type of VR technology ccording to the Pine & Gilmore model-4E on the students' satisfaction with education

Influence Elements	High	Middle	Small	There is no influence
Entertainment	76%	12%	12%	-
Education	76%	12%	12%	-
Esthetics	35%	53%	-	12%
Escapism	63%	20%	12%	5%

For exploring students' perception towards their satisfaction with learning process in the areas defined by Pine &Gilmore the Mehrabian-Russell model has been used. Mehrabian Albert and Russell James (1974) have given environmental psychology model based on three different states: pleasure-displeasure, arousal-nonarousal, dominance-submisivness. For the purpose of this paper the fist state has been taken, so the students have marked the influence of VR technologies on the satisfaction/dissatisfaction with learning process in 4 stated areas. According to the result of the

research carried out at University of Dubrovnik, Croatia, including the the sample of 150 students it is visible that the largest number of respondents,that is 76% of them consider that virtual technology has high level of influence on their satisfaction with educational organizations in the area of entertainment, while 12% think it is neither important, nor unimportant and 12% find out it has small level of influence. The situation is the same with VR influence on the element of education, but just a little bit different in case of the esthetics. The most of students, 53% of them consider that the virtual tecnology has middle level of influence on the satisfaction with eduaction in the area of esthetic and 35% of them think that VR technologies have high level of influence on the satisfaction with eduactional processes int he area of esthetic. The results of the research refers to the area of escapism shows that 63% of students consider that it has high level of influence on the satisfaction level with educational services , 20% consider that it has middle level of influence, 12% think that influence on their satisfaction with learning processes is small in the area of escapism, and 5% think that it does not influence at all on their satisfaction with education.

The students have stated the main advantages and disadvantages of VR technology implementation in education. Acording to the students' opinions the main advantages of VR technology implementation are that education is very interesting, there is a possibility to „go inside the situations“ and make them to be be „alive“, the interaction with the other persons of virtual team, to learrn without physical visit, it encourages the young people to educate them without attending the buildings.On the another site there are some dissadvantages and the main of them according to the students' opinion are costs, the knowledge about VR and how to use it as well as access to VR , addaption of universities to the new ways of teaching based on VR or AR reality.

4. In conclusion

According to the result of the research carried out at University of Dubrovnik, Croatia, including the the sample of 150 students it is visible that the studnts consider that 2D technology is important in education, and they find out the most important 3D. They think that 4D and 5D are less important than 2D and 3D.

Testing based on 4E given by Pine & Gilmore (1999) has provided the next conclusions. They find out that implementation of these tecnologies is especially important in the area of entertainment and education, but it is has significant role and in the area of esthetics and escapism. According to the Getz (2012, p.192)) making education fun as an „edutainment“ is an effective approach**.** It is aslo important to mention that the students which have been included in the research are studying at the Department of Economics and Business, so their preferences could be different comparing the students who are studying in some other area.

The students have stated that virtual technology implementation influence on the satisfaction with learning process and they found out that it is very important in the area of entertainment, eduaction and escapism and just a little bit less important in the area of esthetic. The results of the research refers to the area of escapism shows that the significant share of students (63% -76%) consider that it has high level of influence on the satisfaction level with educational services. The educators have ability to tune/adjust the active /passive participation (by gamification of AR learning environment) and also the degree to which the learning environment is immersive.

The students are aware of advantages and disadvantages of digitalization and VR/AR technology usement in the learning process, but they have positive attitudes towards digitalization and they are willing to accept it. There is a wide range of interaction methods helping to integrate users in virtual environment. It has not been included in the resarch, but it should be considered as the subject of the futher researches, and also can be considered as the limitation of the research, as well as it is limited number of students.The findings refer to the forms of of immersive reality and interaction methods could be important path for improving the learning processes. The main

challange is to adapt the universities to the new realities based on virtual and augmented technologies usement. Opportunities provided by virtual technology implementation are effective platform for the 21 st century education, suitable in both education and training. Technology is becoming more affordable what encourage active learning based on virtual technolgy implementation, although there are disadvantages which should be overcome.

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