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PUBLIC UTILITY AS ECONOMIC CATEGORY

UŻYTECZNOŚĆ PUBLICZNA JAKO KATEGORIA EKONOMICZNA

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Summary: The aim of the article is an attempt to present more enhanced characteristics of the concept of public utility. It is a term that is also used in economic literature to describe a particular type of economic activity in the public sphere. However, despite the legal definition the category of public utility is not satisfactory and variously interpreted. The discussion conducted in the article is twofold. First, it refers to the formula of public utility enterprises; secondly, it refers to the analysis of the essential characteristics of this sphere of activity. To achieve this goal the author used literature review and legal acts. As a result, the findings concerning the conditions for the functioning of the public utility were presented and the author made an attempt to redefine the term. The article highlights the merits of the enterprise model in a separate legal regime, appropriate to the specific nature of public utility as derogation from the logic of the market.

Keywords: public interest, public utility, public service, authority, enterprise, collective needs.

Streszczenie: Celem artykułu jest próba bardziej pogłębionej charakterystyki pojęcia *użyteczność publiczna*. Jest to termin stosowany również w literaturze ekonomicznej do opisu szczególnego typu działalności gospodarczej w sferze publicznej. Mimo definicji prawnej, kategoria użyteczności publicznej jest mało satysfakcjonująca i różnie interpretowana. Prowadzone w artykule rozważania przebiegają dwutorowo. Po pierwsze nawiązują do formuły przedsiębiorstwa użyteczności publicznej; po drugie odnoszą się do analizy istotnych cech tej sfery działalności. Do realizacji celu wykorzystano przegląd literatury przedmiotu oraz akty prawne. W rezultacie autor przedstawił wnioski dotyczące warunków funkcjonowania sfery użyteczności publicznej oraz pokusił się o redefinicję użyteczności publicznej. W artykule podkreśla się zasadność modelu przedsiębiorstwa funkcjonującego w odrębnym reżimie prawno-ekonomicznym, adekwatnym do specyfiki użyteczności publicznej, jako odstępstwa od logiki rynkowej.

Słowa kluczowe: interes publiczny, usługi komunalne, władza, przedsiębiorstwo, potrzeby zbiorowe.

1. Introduction

Every economic concept requires a proper context. So does the term of public utility, which appears in the regulations, the literature on public administration and relatively rarely, in economic literature¹. Using it in a practical sense indicates that its interpretations are not clear and cause a lot of confusion and various developments of content. The term is also used to indicate the grounds of relevant decisions and some questionable ones from a social point of view as well as those economically irrational ones.

The aim of the article is an attempt to describe this synthetic concept, which should be regarded as an economic category. The author analyzes various elements of the concept of public utility from the economic and time perspective. The recognition and application of general interest in the Polish regulations are not satisfactory. The article as a whole is a theoretical reflection about this interesting and forgotten term, whose economic importance is really significant. At the end of the discussion the proposal of changes in the Polish law is recommended.

2. Characteristics of public utility

The category of public utility in Poland dates back to the interwar period and is associated with the conduct of entrepreneurship by local government. At that time, abundant literature devoted to the issues of functioning of municipal enterprises was created². These entities were treated as a key form of general objectives of public tasks. Local governments led dual entrepreneurship: in the form of public utility and focused on increasing budget revenues. The first group of enterprises provided public services on the basis of technical infrastructure, the second included service, commercial, industrial enterprises as well as building the construction of the commercial nature. In the structure of enterprise the prevailing entities were public utility with a high level of profitability. Then, a surprising situation emerged which showed that the greater benefits for the budget were brought by public utility enterprises than by the profit oriented ones. Next, the characteristics of public utility enterprises included the entities fulfilling two conditions: meeting specific social needs (elementary), widely noticeable and entities of monopolistic position in the market. The common element in the organization of municipal enterprises was municipal property transferred to enterprises as assets or transferred for use only.

In order to explain the nature of public utility it will be helpful to connect it to the category of infrastructure and public enterprises. Many economists highlight this context, which is then translated into the economics of economic entities performing

¹ E. Wojciechowski explains the category wider in [Wojciechowski 2005, pp. 276-282].

² The leading authors include: K. Krzeczkowski, S. Włoszczowski, K. Romaniuk, H. Dembiński, H. Biegeleisen.

services of public utility³. The issue of public utility enterprises has a long tradition and an abundant literature referring to the conditions of European and American institutionalism. In Europe, the category of the enterprise was connected with the public property and activities for the local government. In the US, from the very beginning the dominance of the conditions of natural monopoly as a specific characteristic of public utility was emphasized [Jeżowski 1991, p. 130]⁴. By analyzing the public utility enterprise one should take into account the fundamental differences that are indicated between the American and European system [Dziembowski, Sadowy 1992, pp.34-38]. In Poland there was strong opposition that derived from the neo-liberal circles, which questioned the legitimacy of the public utility, due to legal and financial privileges⁵.

The question that arises is what attributes characterize public utility for the purpose of its separation from the economic activity and assigning a special status. The answer is quite simple, it is a type of economic activity, which, due to its specific nature is a derogation from the logic of the market. Differences in public utility are closely related to social, technical and economic conditions of economic activity [Piątek 1986, p. 155]. As S. Piątek puts it, public utility is associated with the category of primary needs whose satisfaction requires a special management mechanism taking into account the technical and economic specificities of this activity and the social objectives [Piątek 1986, p. 155]. Some authors link the public utility with the areas in which there are market failures (public goods, externalities, economies of scale) [Szablewski 1992, p. 399]. Others indicate that the source of public utility are the assumptions of the concept of perfect competition [Jeżowski, Kruszewski 2000]. Social conditions are associated with the actions for the public good by providing services to meet elementary needs. These services are in the public interest, and therefore should be supported and financed with public money [Szablewski 1990, p. 94]. Referring to the social nature of needs, public utility is strictly associated with the public interest mentioned above (business affected with public interest) or becomes a matter of public interest (a matter of public concern) [Kahn 1988, p. 10].

Technical conditions are combined with the functioning and development of devices of technical infrastructure, mainly networking systems. The elements of social infrastructure are scattered and are related to the point. Z. Dziembowski notes that the features related to public utility enterprises coincide with the economic characteristics of the technical infrastructure. These characteristics are: daily and basic needs, the nature of the service, external benefits for recipients and longevity. They may require substantial investment (technical atomicity), the high proportion

³ The dependence is indicated by, among others: [Ginsbert-Gebert 1984, pp. 37-40; Dziembowski 1974; Sadowy, Piątek (eds.) 1986, p. 35].

⁴ The main researchers of this issue are J. Bonbright, P. Garfield, W. Lovejoy.

⁵ Among others [Mazewski 1990, p. 10]. In Poland the status of public utility belonged to several nationwide companies. The joint-stock company of the State Treasury "Polish Post" still has it. In turn, "Polish Oil and Gas Company" lost this status in 1996.

of fixed costs and uneven demand [Dziembowski 1985; 1974]. Longevity of devices results from their technical (physical) durability, which in conjunction with the capital intensity creates a new feature of infrastructure defined by J. Goryński as “capitality” [Goryński 1970, p. 81].

Economic considerations determine the organization of the market, and the purpose of activity. Enterprises providing public services operate under the exclusivity given by law. The aim of the operation is not the desire to maximize profits, but to meet the needs in the best possible way. According to D. Bös, the basic feature of the public utility enterprise is orientation to needs, not profit [Bös 1986, pp. 14-15]. Non-profit orientation does not mean the exemptions from the obligation to respect the principle of profitability. Even if an enterprise starts to generate a lower profitability, the activity in this area can still be attractive because it will be compensated by stable sales services. As it was noted by D. Głuszczyk in this situation optimum relationship between the interests of social and economic logic emerges. According to him, the principle of profit maximization is overridden by the principle of economy, focusing on the possible lowest cost of activity [Głuszczyk 2009, pp. 400-401].

Ownership of the property, through which public utility services are performed, does not prejudice calling public utility – public activity. Also, nor does financing these services from public funds. Public utility services may be provided by different entities, regardless of the form of ownership. In Anglo-Saxon countries, especially in the US, the role of private enterprise in the deregulatory model dominates in this area. For the defense of public interest, public utility commissions are organized and they affect the level of prices, scope, territory and investment policy⁶. On the other hand, in Europe, local authorities prefer their own enterprises in the field of public utility. Their activity is also subject to administrative regulations, as well as separate, independent regulatory institutions⁷.

3. Public utility in the Polish regulations

The concept of public utility appeared only in 1981 in the *Act of State-owned Enterprises* [Ustawa z dnia 25 września 1981 r....]⁸. The Act distinguished public utility enterprises and enterprises operating on a general basis. The regulation adopted a standard business model of the state enterprise based on the principles of independence, self-governance and self-financing, which, in relation to a group of

⁶ These committees are called in most states *Public Service Commission* or *Public Utilities*.

⁷ Elements of regulation of activities of general interest are characterized by [Woźniak 1991; 1990]. In the UK the national market regulator separates works water supply – OFWAT (Office for Water Supply). In Poland, a similar regulator on the energy market is the Energy Regulatory Office.

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public utility enterprises were subject to modifications dictated by the specificity of action. These enterprises were aimed at current and continuous meeting the needs of the population. They ran production or service activity mainly in the field of public utilities, understood objectively. The concept of public utility appeared again in [Ustawa z dnia 8 marca 1990 r....] and in connection with the introductory provisions of the act. The catalog of the commune's own tasks suggested that they had a public utility character. In fact, the situation appeared highly complex because on the one hand, public tasks of the municipality as a public utility were determined, and on the other shortly after the beginning of the process of communalization of state property the transformation of the acquired enterprises and establishments started to be carried out. It should be emphasized that the category of public utility has become important because additionally it legally sets the limit of running commercial activities by local governments.

In 1996 the category of public utility was found in the [Ustawa z dnia 20 grudnia 1996 r....], in connection with a clarification of the organizational framework of public tasks and the completion of the transformation of municipal enterprises. What is worth mentioning is the context of ongoing discussion about the limits of economic activity of local governments and significant interpretation of the Constitutional Court [Wykładnia Trybunału Konstytucyjnego...]⁹. The Court stated that the performance of the tasks of a public utility *relies on meeting the social needs of a general nature, none of which is focused to maximizing profits*. The tasks of this nature have been recorded quite extensively and can be identified with public tasks, the implementation of which falls on government and local administration.

Since 1997 the statutory definition of public utility appears twice: in the acts on local self-government, county and province, and in the act of communal economy. Public utility has been defined in purposeful terms and in the way of its achievements *as ... current and uninterrupted satisfaction of the collective needs of the population through the provision of universal services* [Wykładnia Trybunału Konstytucyjnego...]¹⁰. The features that arise from such a specific structure of concepts reflect the content of each element, and their sum results in the general perception of the term of public utility. These elements include:

- the goal of public utility: current and continuous meeting the needs of the population,
- the nature of the needs – collective ones,
- the method of implementation: organization and provision of services,
- the nature of services – widely available ones.

The current nature of the process of meeting the needs means that they are elementary in human life and according to Maslow's pyramid are located on the

⁹ Parliament in 1992 passed a ban on business activity by municipalities outside the sphere of public utilities.

¹⁰ Parliament in 1992 passed a ban on business activity by municipalities outside the sphere of public utilities.

bottom. Satisfying these needs creates the basic living conditions of people. Satisfying the needs in a continuous manner means that the process is ongoing, stabilizing many activities that make up the standard of life. A way to meet collective needs is, as the definition states – providing commonly available services. Legislators probably meant the availability of services in terms of space, or the possibility of using them in a certain organizational and technical system [*Wykładnia Trybunału Konstytucyjnego...*]¹¹. What was also at stake was another kind of accessibility – this time economic accessibility.

The feature of social nature imposes some rigors in the organization of activities since public services and other entities must act permanently, ensuring adequate supply and structure of services covered by the regimes of ownership. Satisfying the natural needs is connected with the obligation to provide services in a safe way, without jeopardizing the health and lives of consumers. Disruption or interruption of a service process can occur only in crisis situations, such as breakdowns. The definition indicates that the recipient of public utility services are people. It is narrowing a circle of consumers because such services are also used by other entities (private, NGO's). The tasks of public utility cater only to a specific type of social needs. As it is apparent from the definition, these needs are collective i.e. they are shown in the following ways: group or mass ones. It follows that the needs are public as well social, which means that satisfying them falls into the category of public interest (the public good). The consumption of public utility services is beneficial from a social and economic point of view, therefore, public authorities should encourage and offer the supply of this type of service that is adequate to the needs.

While assessing the statutory definition of the public utility one can pay attention to two elements. Firstly, it is not precise, full or rewarding. The nature of public utility refers only to the part of the local government's own tasks. Secondly, local governments undertake also activities that go beyond the tasks of public utility under certain conditions. For this reason, one should see quite precisely the border area dividing public utility from remaining types of undertaken economic activity. Numerous external controls (e.g. NIK) in their reports highlight the frequent cases of crossing the border illegally, especially by utility enterprises.

The adoption of a very broad interpretation of the concept of public utility impacts the scope of the communal economy, including all tasks of public utility. Assuming that the communal economy is identical with the self-government, which is also focused on the realization of public service tasks characterized by law, to defend the social interests the activity of public utility requires the intervention of the administrative factor. We can say that public utility is a regulated activity, and entities performing services within it are subject to public control of varying intensity. The logic of the market is within certain limits replaced by the regulatory regime for

¹¹ Parliament in 1992 passed a ban on business activity by municipalities outside the sphere of public utilities.

stimulating pro-efficiency behavior. Non-profit activity attitude does not mean giving up achieving profitability. In this perspective, the entities performing tasks of public utility are closer to companies defined as *not-for-profit organizations*. This is a category of companies that operate in the traditional system of economic efficiency, but they are not focused on profit-making. They form a set of operators of a hybrid, combining social and economic objectives. Studying the efficiency of economic entities, municipalities in the context of local government, three levels of economic evaluation can be distinguished. In the first one it is advisable to obtain a profit, which expresses a normal situation in a market economy ensuring self-financing. If the conditions do not ensure this, then the objective of a business is to strive for a result oscillating around zero. When it also turns impossible, then with the financial loss operating costs must be rationalized at the most. This formula is used e.g. in local governments in Germany.

Based on the arguments one could attempt to submit a new economic form of public utility activity. An accurate definition of the public utility is important in the economic life, as economists and managers often create solutions and make decisions in the areas of economic activity where market mechanisms do not apply to the full extent. It is assumed that the definition of public utility should be coherent and give meaning only to the relevant properties. What therefore, must be considered as the **public utility is an economic activity aimed to meet collective needs (public interest) non-profit target-oriented, led in conditions of monopolistic or quasi-monopoly in the market based on technical infrastructure**. This approach takes into account four essential elements of action, i.e. the nature of the need, the purpose of public economy, the type and base of activity. Other features of the public utility are derived from them.

The concept of public utility is not a synthesis of its parts, but the sense of this type of activity. As it was shown earlier, economic activity determined by this name has a clearly outlined specificity, which requires to look at economic operators from a different perspective. The sphere of public utility, yet of a smaller scope than the typical activity in a market economy, however, is an exception to the major rule. Functioning in this field does not relieve owners and managers of the obligation to maintain economy efficiency in achieving public objectives. The sphere of public utility is very sensitive to the rise in prices in public utility services, therefore, the poorest groups of the population should be protected against the effects of these increases. According to the World Bank the services working in the field of general interest should be able to maintain their own thanks to revenue from the sale of public services [Hume 1993]. Two fundamental consequences arise from this definition. First, the public utility concerns the nature of the activity, rather than as the name of the terms suggests – property. Service activity dominates within this activity. Economic activities conducted under these conditions operate in a separate financial-economic regime. Operators of this type are under special control of public authorities. Secondly, public tasks in the field of public utility can be carried out by

operators of various ownership. To carry out public tasks other entities apart from municipal bodies may be involved: the private sector and the social sector. The common denominator is to offer service to people and other entities, not to work to achieve maximum profit.

4. Conclusions

The abovementioned considerations present an interesting and complex picture of the activities called public utility. Therefore, one is tempted to formulate important conclusions of a general character specifying the content of this controversial and not really correctly understood concept.

1. The public utility is a part of the economic activity in general, therefore, activity in this area may be considered a form of entrepreneurship in the economy. Its separation from overall economic activity is dictated by the specific difficulties it faces, ordering separate treatment in system solutions. Public utility shows the deviation from the logic of the market that is generally applicable in the economy. Its peculiar nature is supported by relevant circumstances resulting from social, political, organizational, economic, technical and economic activities related to the implementation of important public tasks in the state. The analysis shows that the main premise in the economic activities which are recognized as public utility is a social need. The potential profit is only accompanying and providing a method of realization of the public goal. The main purpose of public utility is, in fact, to maximize the utility while providing services to people and other entities.

2. This article attempts to describe a new definition of the public utility in a more universal dimension. The activity of public utility occurs throughout the whole economy, i.e. in local government and on macroeconomic scale. Private and social entities have different economic and financial status which does not rule out their participation in the realization of public tasks with features of public utility. A new look at public-benefit activities is based on the visibility of the significant features of its nature and the natural combination thereof. It can be argued that public utility is an economic category, an important interpretation of the processes and phenomena occurring in the public economy. An accurate definition of public utility has practical importance. It shows a legal limit defining initiating economic activities beyond this area.

3. The development of market economy in Poland and the dominance of mainstream liberal economic theory caused somewhat a removal of the concept of public utility to the background, and even its obscurity. Public utility constitutes a derogation in the logic of the system aimed at pro-efficiency behavior of participants in a competitive market. Another segment of the economic activity within public utility, despite its justification is something undesirable in a pure market economic doctrine. Meanwhile, there are many economic activities whose injecting into the

framework of acute economic struggle is unreasonable and illogical, and what is more, to the detriment of the public interest.

4. Determination of the characteristics of public utility is pragmatic because legal solutions create different variants of business activity by local governments. The commune may implement activities beyond public utility under certain conditions, and the region as well. In turn, the county does not have such a possibility. The definition of public utility, therefore sets the dividing line between such activities and the remaining economic activity, which is credited with commercial characteristics.

5. In Poland, local government bodies do not have much of a choice of organizational form of economic activity in order to perform public duties by their own bodies. Besides budgetary unit that proves most relevant in practice, local authorities have a choice of only two extreme forms: factory budget and the municipal company. Each of these forms is guided by different logic operations and has different solutions of the economic system in which it operates. What seems closest to public utility is factory budget because the municipal company functioning in the rigors of market is a form of calculated profit. The law is not adequate to the characteristics of public utility as a form of implementation of public tasks. As for the entity it concerns the subject having other form of organisation legal and economic-financial system having another legal organization form and economic-financial system which is an intermediate form between the factory budget and municipal company. In the Polish law, there is no enterprise with the status of public utility, which is a handicap because the factory budget and the company do not fit into the separation of economy in the formulation of public utility. Therefore, a return to the concept of municipal utility enterprises appears to be fully justified.

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