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State of Business in Kosovo: Challenges and Opportunities for Doing Business in Kosovo

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Kosovo Foundation for Open Society's project



Input for the Progress Report 2014



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Foreword

The Kosovo Foundation for Open Society has supported Kosovo's European integration process since 2006, when it founded the European Integration and Good Governance program. Since then, the Foundation has constantly supported the non-governmental organizations' engagement in the process with their analysis, monitoring of policy developments, public discussions, and advocacy processes. The support has resulted in numerous analyses through the years and acquisition of essential knowledge and expertise over the processes by Kosovo's civil society organizations. Hence, in joint effort with a number of organizations already active in certain segments of integration process, the Foundation initiated the project "Civil Society for the Progress Report 2014" through which it offered the organizations an opportunity to channel their contribution to the upcoming Progress Report and the current Stabilization and Association Process Dialogue through focused and well-informed analysis, built on their multi-year experience and engagement.

Each analysis produced within the project addresses a specific segment of the current dialogue between Kosovo and the European Union, informing about the current situation, from the civil society's point of view, followed by the recommendations on the needed improved performance.

We hope that this exercise has produced will be of value not only to Kosovo's civil society organizations for further amplification of their voice within the integration process, but also to the European Union and the Government of Republic of Kosovo towards building of a standing cooperation with this segment of the state-building process. Ultimately, we hope that as a result of all the stakeholders' engagement, Kosovo's European integration process will accelerate, overcoming all the political barriers that stand on our way to this destination.

Iliriana Kacaniku
European Integration and
Good Governance Program

Acknowledgements

The American Chamber of Commerce would wish to express its gratitude towards Kosovo Foundation for Open Society for offering its generous support for this project. In addition, the completion of this study would have been impossible without the help of all member and nonmember companies, whom we thank for taking their time to respond to our survey. AmCham also dearly thanks the interviewees, who have, without any hesitation offered their insights and expertise on the state of business in the country. Finally, we thank DC Consulting Company for their help in collecting the survey responses.

Introduction

In the postwar period, Kosovo has implemented numerous reforms that in one way or another were aimed to have an effect on the economic development of the country, and ultimately pave country's path towards the European Union integration. These reforms included improvements in the doing business environment through improvement of national legislation, fiscal policies, and fighting corruption. However, regardless of all the work that has been done in narrowing the gap between Kosovo and other regional countries with regards to doing business, unfortunately this gap is still very much evident, and Kosovo businesses still face challenges and problems of different nature. In this context, the American Chamber of Commerce in Kosovo has conducted a Study on the Opportunities and Challenges of Doing Business in Kosovo, with the aim of conducting a comprehensive analysis of the state of businesses, and then based on the findings of the study, the appropriate recommendations can be offered to respective institutions, that are responsible for tackling of potential problems that the private sector faces.

The central and local level of governance remains a key source of the challenges and problems of the private sector in the country. The main issues that cause discontent include bureaucratic processes, which are not efficient, presenting difficulties in business operations, and discouraging businesses from following these procedures, while making Kosovo less attractive for foreign investments. A perceived lack of transparency, deficiencies in rule of law and the judiciary, create space for the occurrence of corruption, a phenomena perceived and reported to be present at large in Kosovo¹.

The study focuses primarily fiscal environment, namely on tax declaration and customs clearance procedures, tax rates, transparency level, recent decisions of the Tax Administration of Kosovo and Kosovo Customs, to facilitate business and the efforts being taken by all the institutions to fight high perceived level of informal economy. The study also contains the most recent figures illustrating the international trade and a comparison of these figures throughout the recent years.

The study further presents the perception of businesses regarding public procurement, one of the largest problems that Kosovo private sector has faced through the years despite the relatively good legislation in place.

1 See Corruption Perceptions Index 2013, 2013

Other areas in which the study focuses as well, include obtaining of construction permits, issues of rule of law, perception of corruption, access to public documents, and the access to finance, which is considered to be a great challenge of doing business in Kosovo, particularly for the small and medium sized companies

Finally, the study measures the level of optimism and expectations of the business community about the future economic development and growth of the country in general, and the private sector in specific. In order to maintain a balance between the views of the private sector and those of the public officials and independent experts, the study contains interviews conducted with the latter ones.

Methodology and Survey Sample

With the aim of assessing the state of business and challenges that private sector faces in its daily operations, challenges that derive from public policies and law enforcement, AmCham conducted a state-wide survey, covering more than 7 regions of Kosovo. In total, 652 businesses participated in this survey, whereas the distribution of the sample across regions was done proportionately with the number of registered businesses in that particular area. For example, if Prishtina accounts for 40 percent of registered businesses in Kosovo, than roughly 40 percent of collected surveys come from Prishtina. 603 questionnaires were conducted in person by visiting respondent companies, while an additional 49 surveys were collected through a web based survey platform. The following graph provides an overview of the location of businesses that participated in the survey:

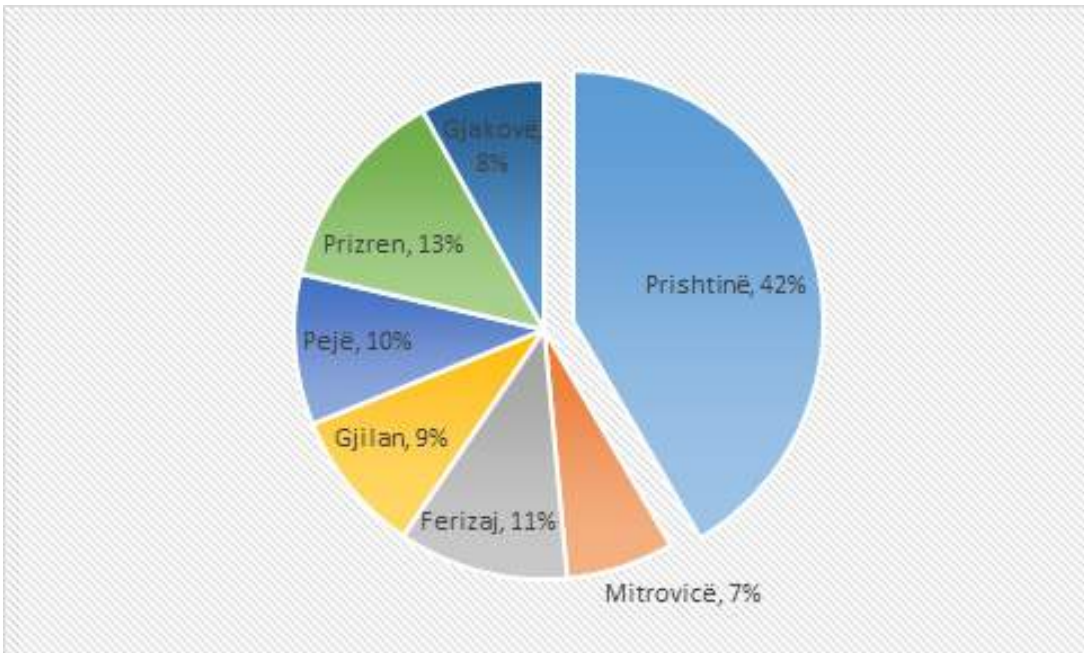


Figure 1 Respondents according to location

In order to understand the main business activity of these companies and their contribution to overall employment in the country, companies were asked to provide the number of employees as well as the industry they belong to. The following two graphs depict the composition of the sample according to these two aforementioned elements:

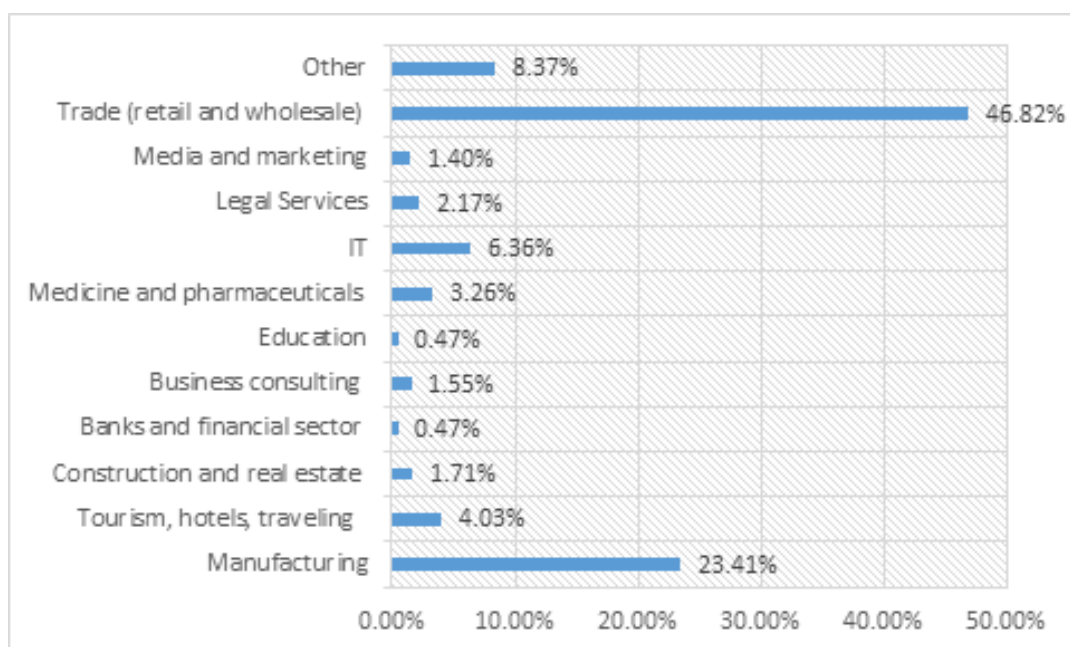


Figure 2 Respondents according to industry²

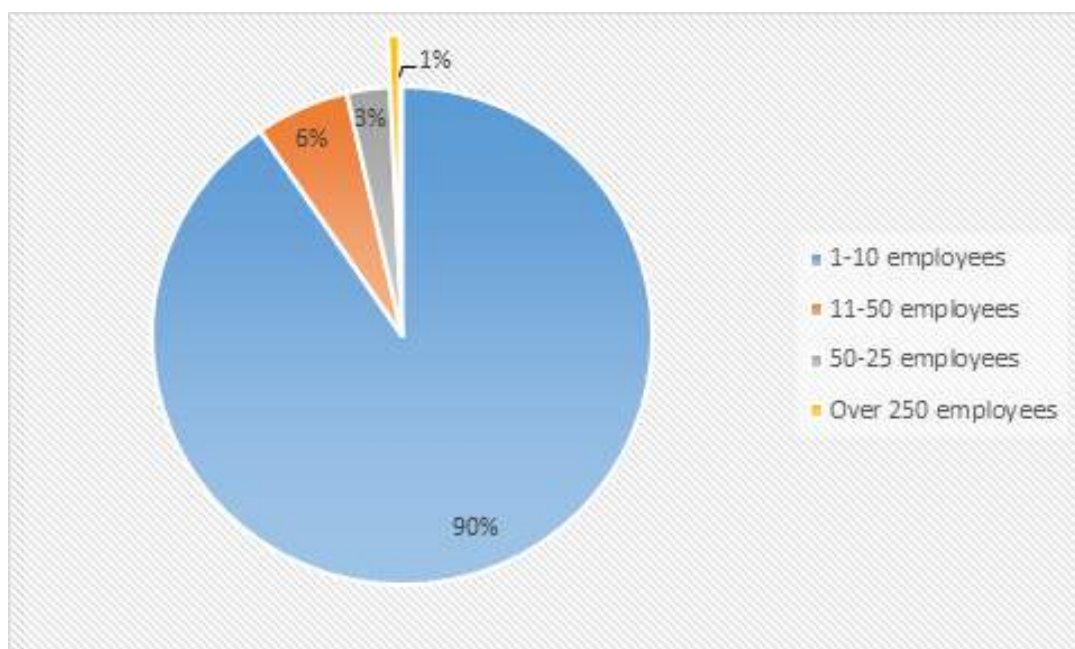


Figure 3 Businesses according to the number of employees

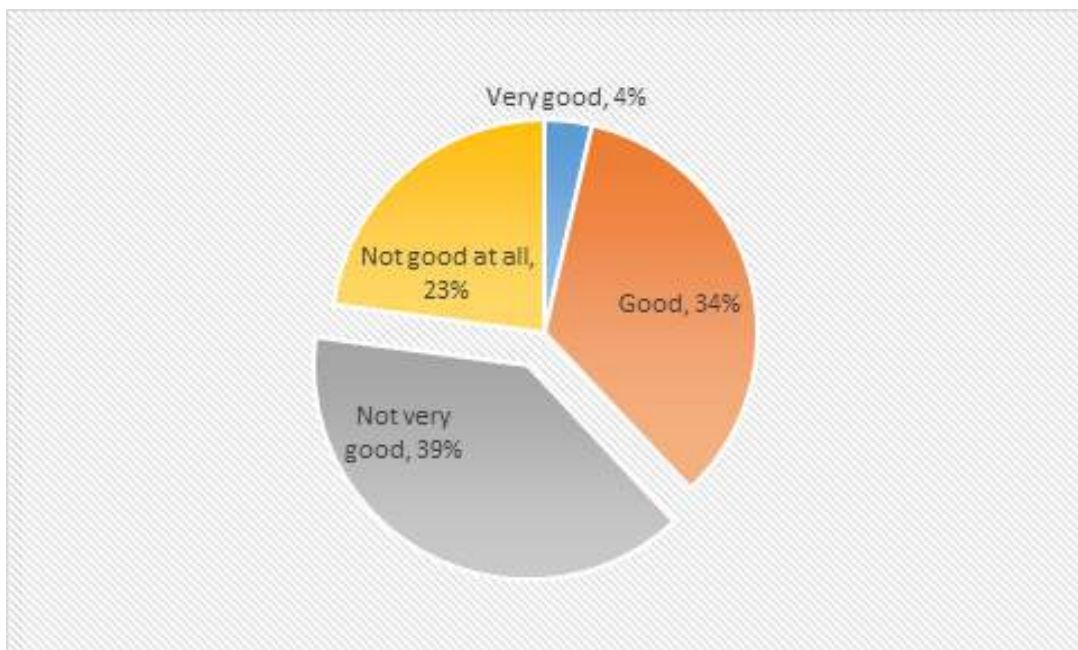
² "Other" includes industries that were not given as options, or companies that had more than 1 activity (e.g. manufacturing and trade, accounting and consultancy etc.)

Another thing measured by the survey is the most common type of businesses in terms of registration forms. Results show that 83% of surveyed companies are individual businesses, 8% are limited liability companies, 7% are general partnerships, while only 2% of interviewed companies are registered as joint stock companies.

In addition to the responses collected from businesses, the study also included three interviews conducted with relevant officials and independent experts, Behxhet Haliti, Director of Tax Administration of Kosovo, Agron Demi, Executive Director of GAP Institute for Advanced Studies, and Terrence Slywka, Chief of Party of USAID Partnership for Development Project in Kosovo. While Behxhet Haliti provided his insights on developments affecting the tax environment in the country, Agron Demi shared the work of GAP Institute for Advanced Studies in the area of doing business environment. Finally, Terrence Slywka, who was also former chief of party of USAID Business Enabling Environment Program shared his thoughts on recent developments affecting the private sector and the steps forward.

Fiscal Environment

This section provides an insight on the perception of businesses regarding the overall fiscal environment in the country, including tax rates, tax legislation, implementation of laws, efficiency of administration implementing the legislation, etc. While having attractive tax rates is encouraging to businesses, the overall fiscal environment encompasses much more than that. A study conducted by AmCham Kosovo in 2011, titled Kosovo Business Agenda 2011 concluded that the main issues that businesses face in terms of taxes are: (1) collection of VAT at the border crossing points, (2) complicated procedures for VAT reimbursement, (3) registration/inspection of stocks conducted during working hours, (4) informal economy, (5) lengthy procedures in processing of tax statements, (6) VAT exemptions for specific products, (7) problems emerging from fiscal cash registers, (8) lack of information, etc³. Because the study was conducted in 2011, some of the issues mentioned have already been addressed (such as the timing needed to process tax statements or the availability of information which has been improved thanks to the customer-friendly brochures and leaflets prepared by TAK); however, the findings remain as a solid starting point for the purpose of this study. Businesses that participated in the survey provided the following assessment on the overall fiscal environment:



3 See Kosovo Business Agenda 2011, pp. 18-21

Figure 4 Businesses' evaluation of the fiscal environment

According to the responses portrayed above, 38% of businesses are satisfied with the overall fiscal environment, 39% do not think the environment is very good, while 23% find the fiscal environment as not good at all. Similarly, businesses were asked about their opinion about the applicable tax rates in the country, with 37% of respondents claiming that the tax rates are appropriate to the level of economic development, while 61% claim that taxes are high. However, it should be noted that tax rates in Kosovo (Corporate and Personal Income Tax, VAT etc.) are actually quite low and competitive to those of the region. The perception of businesses that the tax rates are high might stem from difficulties that businesses face in their operations. Only 1 percent of businesses claim that tax rates are low:

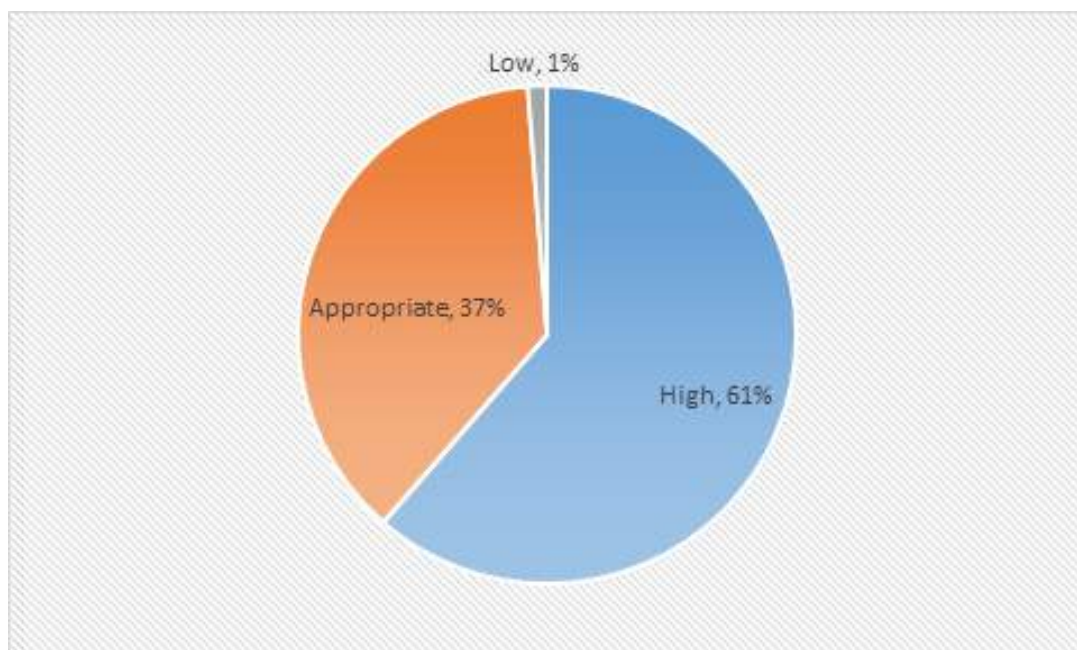


Figure 5 Businesses' view on tax rates

In addition, AmCham also wanted to identify whether the businesses find procedures for declaring and paying taxes easy or not, especially considering the overall governmental efforts to reduce bureaucracy. Results from this question were more encouraging, with a large number of respondents claiming that they find this procedure easy and appropriate as illustrated below. Furthermore, as Haliti points out in his interview, Kosovo has marked a significant improvement in the "Easiness of Paying Taxes"

indicator in World Bank's Doing Business Report, jumping from 47th to 43rd position. A major part of this improvement should be attributed to the digitalization of the tax declaration system that has also resulted in an increased voluntary compliance rate for taxpayers (from 78% to 87% in 2013).

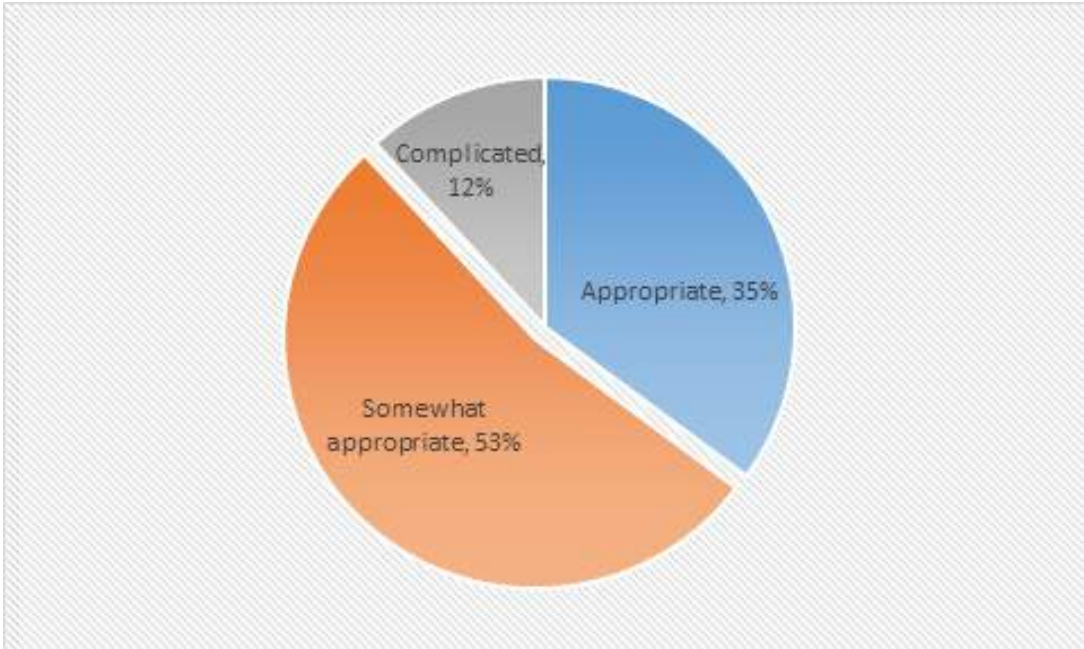


Figure 6 Easiness of declaring and paying taxes

In addition to finding out the views regarding the legislative framework and the procedures, we also wanted to find out the level to which businesses believe this framework is being implemented properly by the Tax Administration of Kosovo, as similarly to other fields, often complaints refer to the enforcement of laws, rather than the content and quality of the law itself. Roughly 19% of respondents believe that TAK officials do not interpret the law properly, while 59% say that the interpretation is somewhat fair:

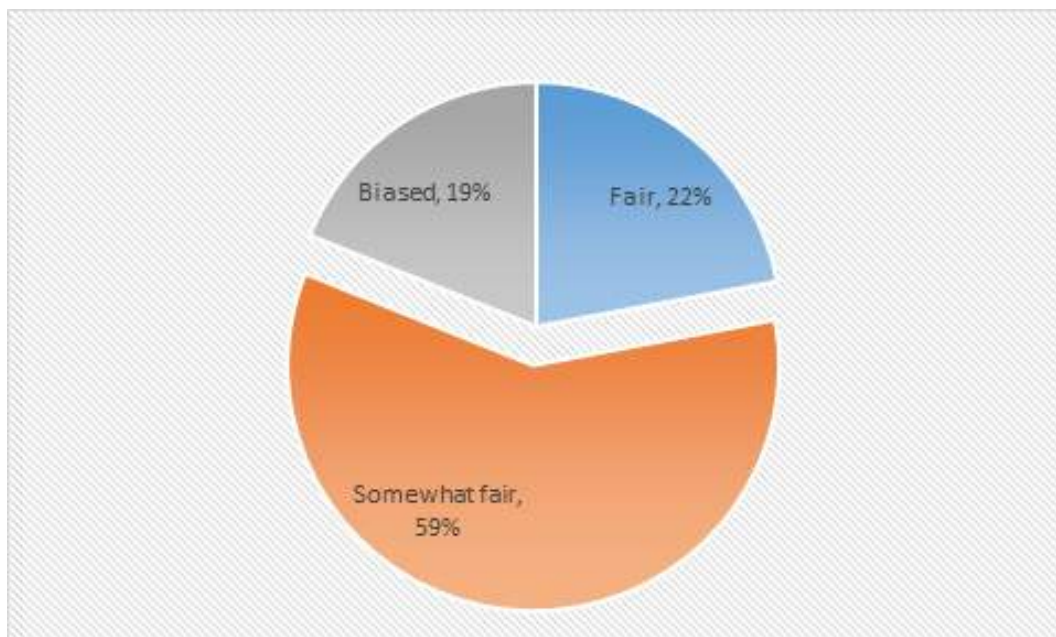


Figure 7 Businesses' view on TAK's Legal Interpretations

While the lack of proper statistics in this field is a known phenomenon, all institutions agree that the level of informality is very high in Kosovo. Depending on the source of information, informality in Kosovo ranges from 35-45%. The government has recently adopted a new National Strategy for Reducing Informality, however it is still too early to measure its effects on the ground. One thing that is certain is that this negative phenomenon damages those businesses that abide by the laws and pay their obligations regularly. The graph below summarizes the perception of respondents regarding the willingness of TAK to address this issue:

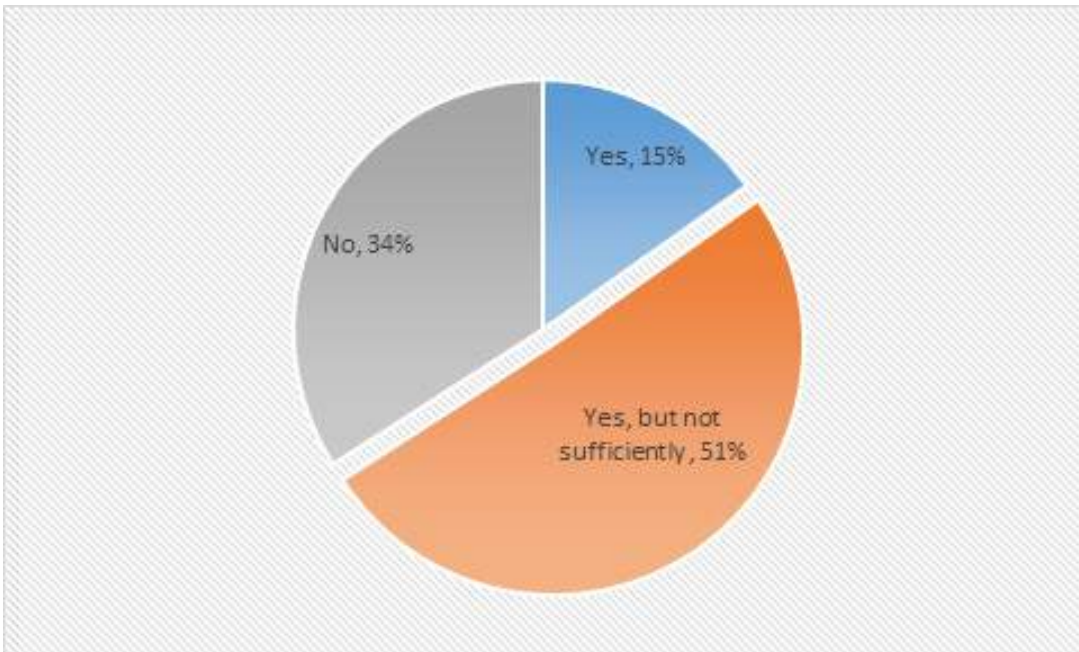


Figure 8 Addressing of informality by TAK

As the graph reveals, 34% of respondents do not believe that informality is addressed at all, while 51% believe that more should be done in this regard. On the other hand, Haliti explains that while previously TAK used to treat informality on an ad-hoc, case-to-case basis, in the last three years it has created a systematic approach, based on the OECD model, which is mainly directed towards understanding the behavior of the taxpayers. In terms of addressing informality, Terrence Slywka, Chief of Party of the USAID Partnerships for Development Program, suggested that the government should focus government actions or policy decisions that create disincentives for people to engage in the formal economy and needs to have a holistic approach to solve that issue, with all government officials working towards a joint set of reforms and goals. According to him, market mechanisms provide their own incentives including: property protection, ability to grow, developing a credit history, access to loans/financing, ability to enforce contracts, trade, and other protections under the law. Slywka emphasizes that while enforcement plays a role at the margins, to significantly address informality, all administrative actions should be considered as they contribute to the collective burden that is outweighing market benefits.

Similarly to above indicator, the opinion of businesses is largely positive regarding their perception about the level of transparency of Tax Administration, as one of the most important public institutions that businesses deal with. Establishment of the Consultative Council of TAK-Customs-Business Community aimed at providing a mechanism that would enable a further increase of transparent decision-making by TAK and Customs. Businesses were also asked whether they have encountered any corruption in this institution, with only 9% of respondents claiming to have actually encountered this negative phenomenon.

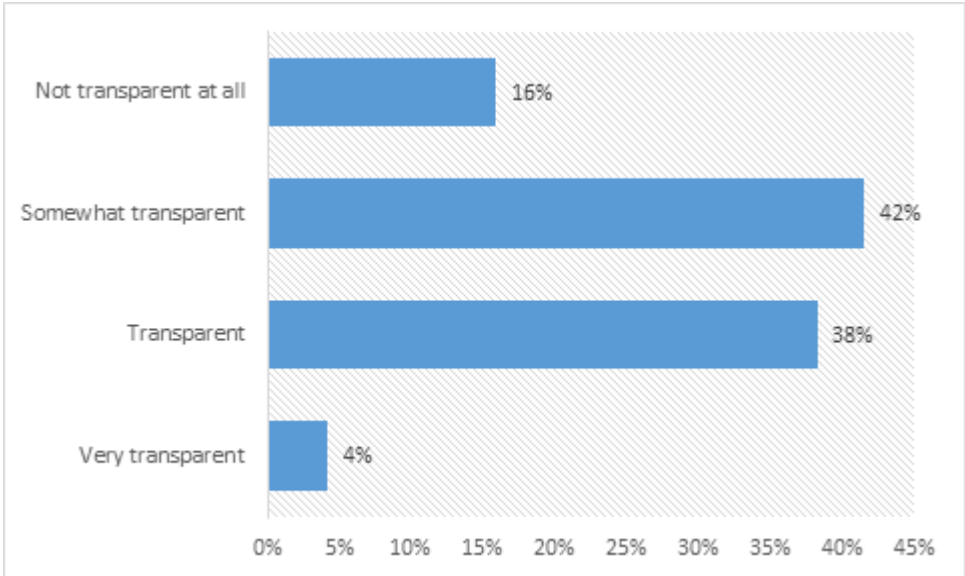


Figure 9 Businesses’ view on the transparency of TAK

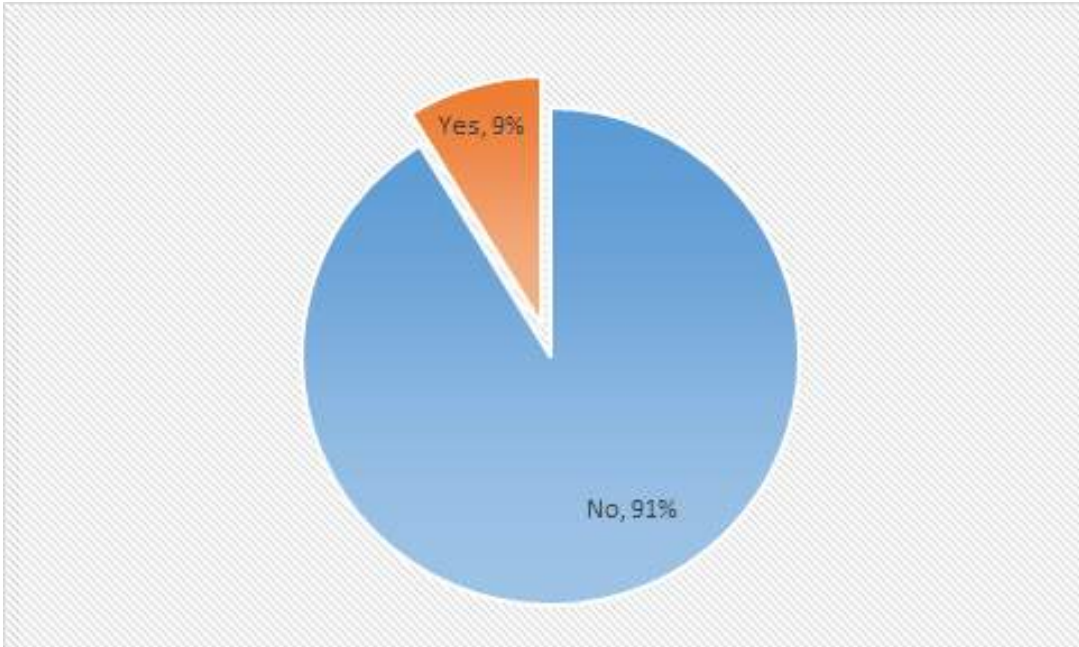


Figure 10 Corruption occurrence in TAK based on respondents' claims

Companies that report to have encountered corruption in TAK were asked to provide more information on their claims. According to their response, they have encountered this phenomenon with tax inspectors or other lower ranking officials of the administration, usually in the form of bribery.

Customs and Trade

Six years after the declaration of its independence, Kosovo's economy remains largely dependent on imports. Kosovo faces extremely huge trade deficit as a result of poor manufacturing sector. According to Kosovo Statistical Office, while imports in 2013 amounted to € 2.45 billion, exports totaled to € 294 million only, meaning that only 12 percent of imports were covered by exports⁴ . In addition, AmCham's Kosovo Business Agenda 2011 identified 6 concrete problems that trading companies face in their activities, (1) non-acceptance of the value of invoices by Customs officers, (2) non-recognition of original prices due to differences from prices foreseen in Customs Integrated Tariffs Code (TARIK), (3) non-acceptance of discounted purchases, (4) lengthy and time consuming appeal procedures, (5) non-consistency of the customs in decision making, and (6) lack of clear description of goods in Customs Code and regulations⁵ . Similarly to tax issues, some of these problems have already been addressed by Customs; however, a lot remains to be done to address challenges in this sector.

It should be noted that only 38% of surveyed businesses deal with Customs, whereas the following tables summarize their views on this topic. It should also be noted that 10% of these companies benefit from procedures with economic impact such as the authorization for Customs Bonded Warehouses, Simplified Customs Procedures, etc.

Speaking about how complicated the Customs Clearance procedures are, 31% of respondents that deal with Customs view these procedures as complicated, while 24% think that the procedures are appropriate. Slywka mentions the adoption of the electronic Asycuda system by Kosovo Customs and the decentralization of customs services from a single Prishtina office to regional branches for improved access by citizens as positive developments in the customs that have facilitated international trade procedures.

⁴ See External Trade Statistics, Statistical Office of Kosovo, December 2013, p. 10

⁵ See Kosovo Business Agenda 2011, American Chamber of Commerce in Kosovo, pp. 12-15

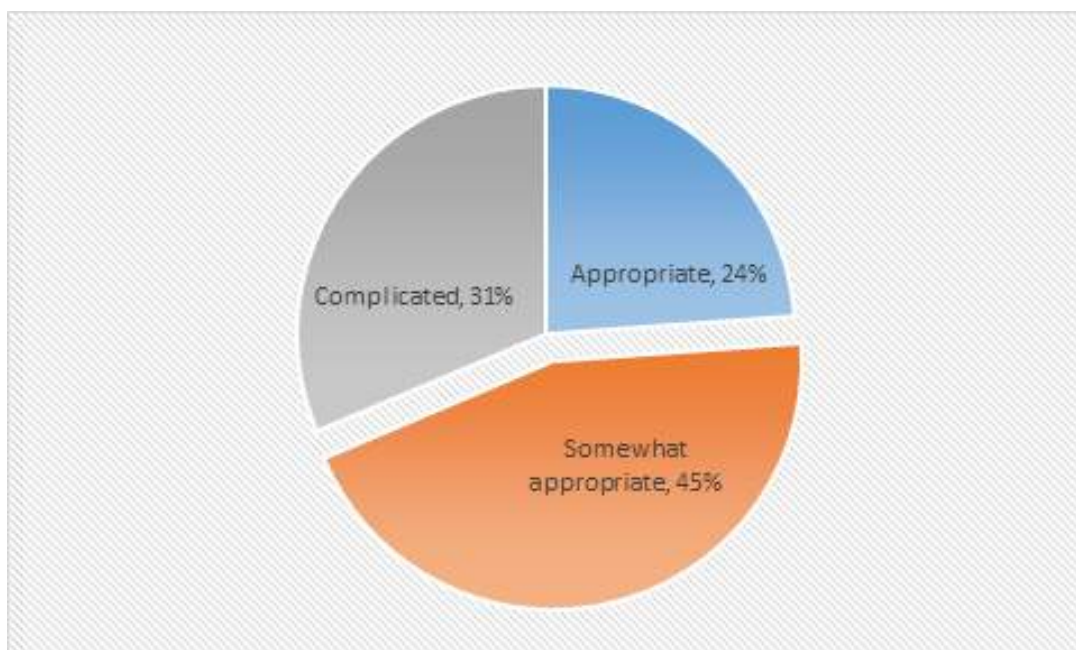


Figure 11 Businesses' evaluation of Customs procedures

Businesses believe that Customs make no difference from other institutions, such as Tax Administration of Kosovo, when it comes to the interpretation of the respective legislation by this institution, with only 17% of respondents claiming that the interpretation is fair, while 32% of them believe that the interpretation of laws is biased. Some of the issues related to legal interpretation were raised by the representatives of business associations through Consultative Council of TAK-Customs-Business Community.

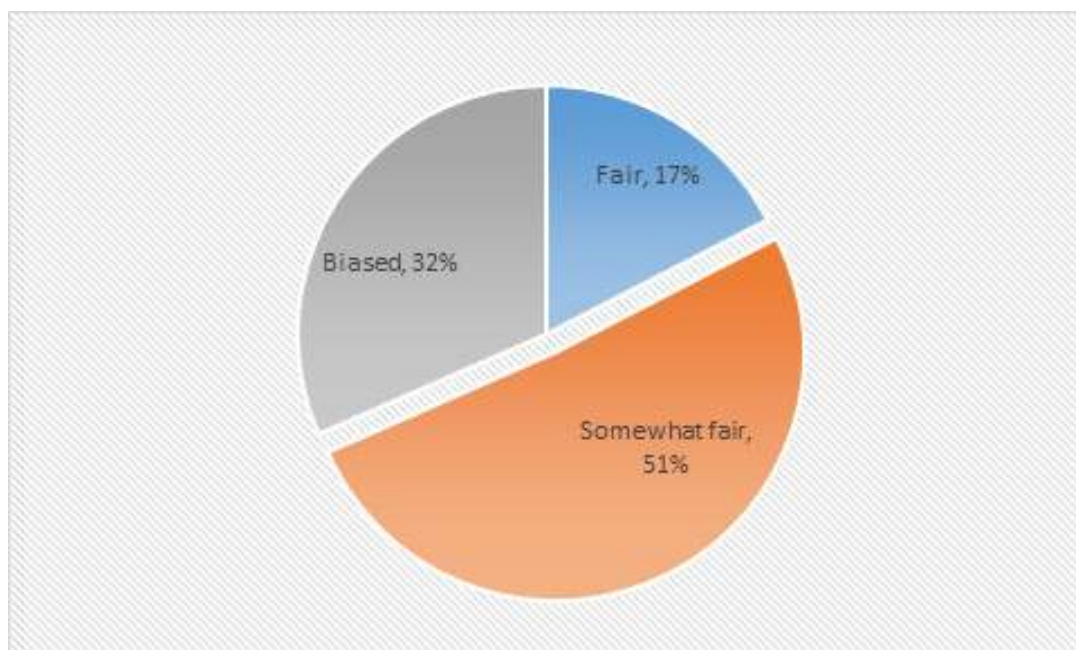


Figure 12 Businesses' view on Custom's Legal Interpretations

Compared to the data on Tax Administration where 19% of respondents claimed that its legal interpretations are not fair, this number is higher when it comes to customs. This may be due to the fact that the Customs is also authorized to do the revaluation of goods being imported, in cases when they believe that the goods are under-declared. Businesses have frequently expressed their concerns regarding the discretion of Customs officers in revaluating the goods. This issue was reported in the Kosovo Business Agenda 2011 as well.

As depicted in the previous section, informality is causing problems to regular taxpayers. Another issue that is very much related to informality is the smuggling of goods. Respondents were also asked to provide their thoughts in this topic. On this topic, responses do not differ greatly from the similar issue in the fiscal section, although it should be noted that the efforts of Customs to fight and prevent the smuggling of goods have increased significantly, and part of this effort was also the detection of fraudulent activities of Customs officers as well. The business perception about the efforts of fighting and prevention of smuggling may suggest an improper information by Customs on this regard.

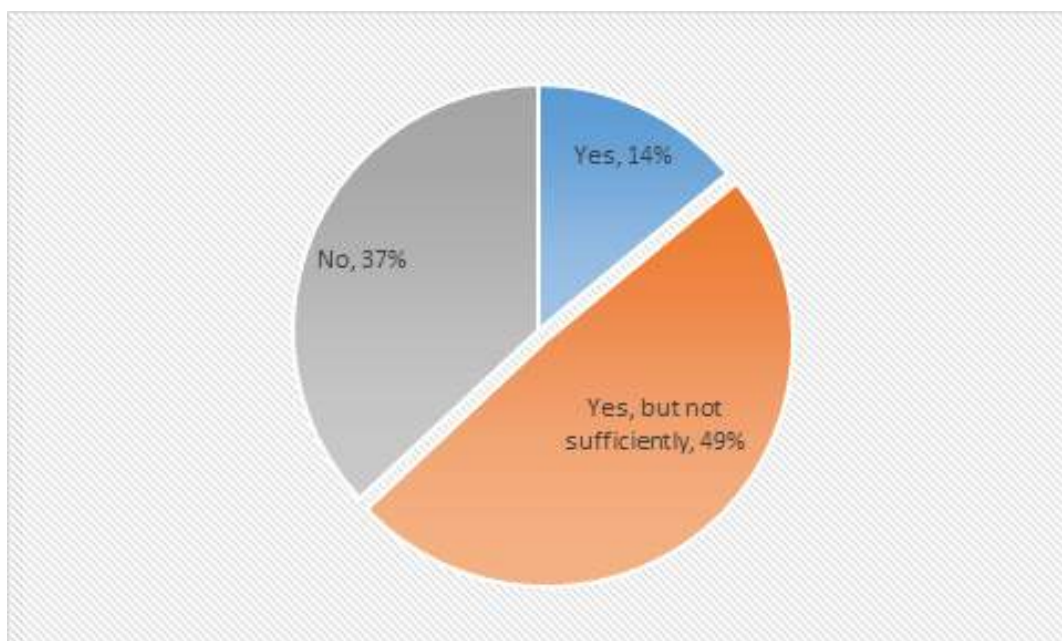


Figure 13 Fighting of smuggling

As one of the main public institutions that businesses deal with, respondents were asked to present their perception regarding the level of transparency of Customs administration as well as the prevalence of corruption in this institution:

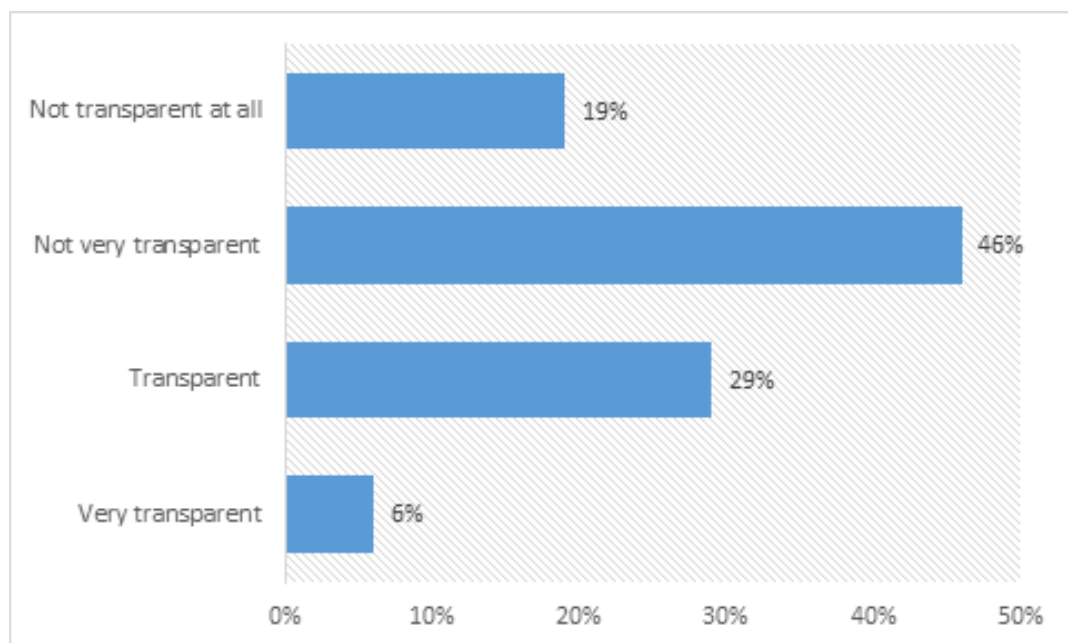


Figure 14 Businesses' view on the transparency of the custom

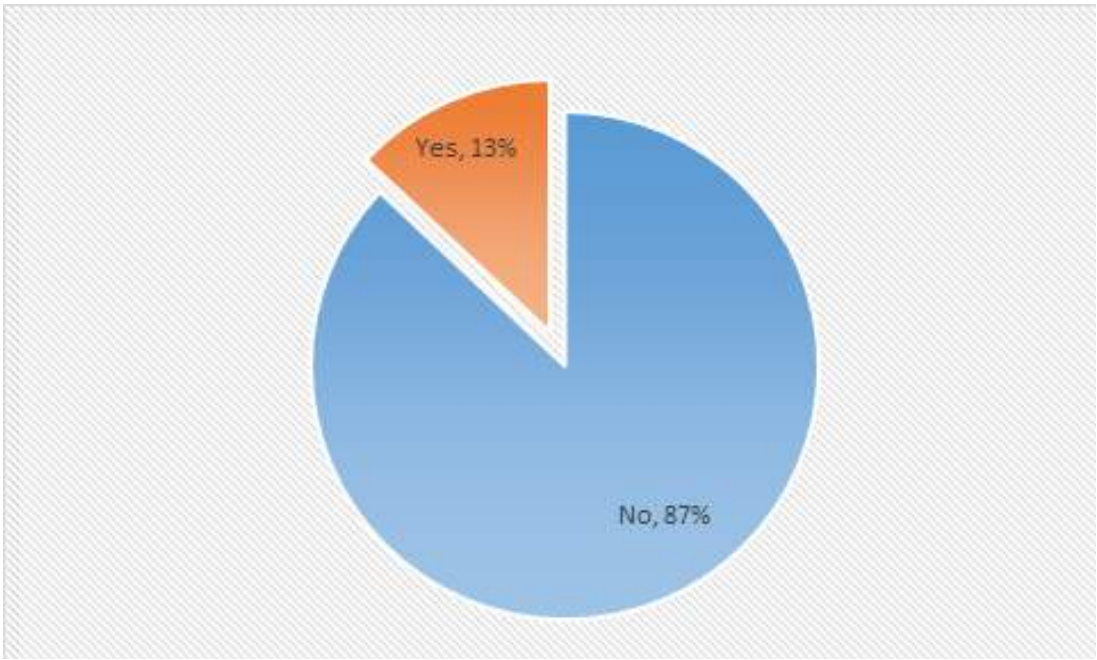


Figure 15 Corruption perception in Customs

While transparency levels are more or less the same based on the results, the percentage of people claiming to have encountered corruption in custom (13%) is slightly higher compared to TAK (9%). But again, just like with Tax Administration of Kosovo, the perception of corruption is extremely lower compared to the initial years when the Customs Service was set up. Respondents claim that they are facing this issue during import of goods, and again mainly by lower ranking officials.

Municipal Regulations

Pursuant to the Law No. 03/L-040 on Local Self Government and Law No. 03/L-049 on Local Government Finance, Municipalities have a much more significant role in doing business environment. In addition to being responsible for issuing construction permits (one of the fundamental indicators in opening a business), municipalities have a wide range of other policies at their availability that can affect the doing business environment. Specifically, Article 10 of the Law on Local Government Finance, foresees competencies of municipalities for the imposition of Business Activity fees. There were claims by foreign investors in Kosovo that certain municipalities have imposed discriminatory fees, by asking the foreign companies to pay higher fees compared to the local businesses.

AmCham's Kosovo Business Agenda 2011 lists three main problems that businesses have identified in 2011 regarding problems that emerge from municipal level of governance: (1) Municipal permits procedures are costly and lengthy, (2) Submission of documents to receive work permits and (3) Procedures for obtaining construction permits are lengthy and burdensome. While the first two issues have been addressed and resolved by the Ministry of Trade and Industry through the amendment of the Law on Internal Trade, the third issue has been addressed only last year, with the new Law on Construction.

The survey results suggest that 56% of businesses believe that municipalities indeed have a very important role to play in business activities, while 31% of respondents believe that the role of municipalities is limited. Moreover, businesses were asked about their opinion on municipal tariff rates, where 50% of respondents claimed that these tariffs are high.

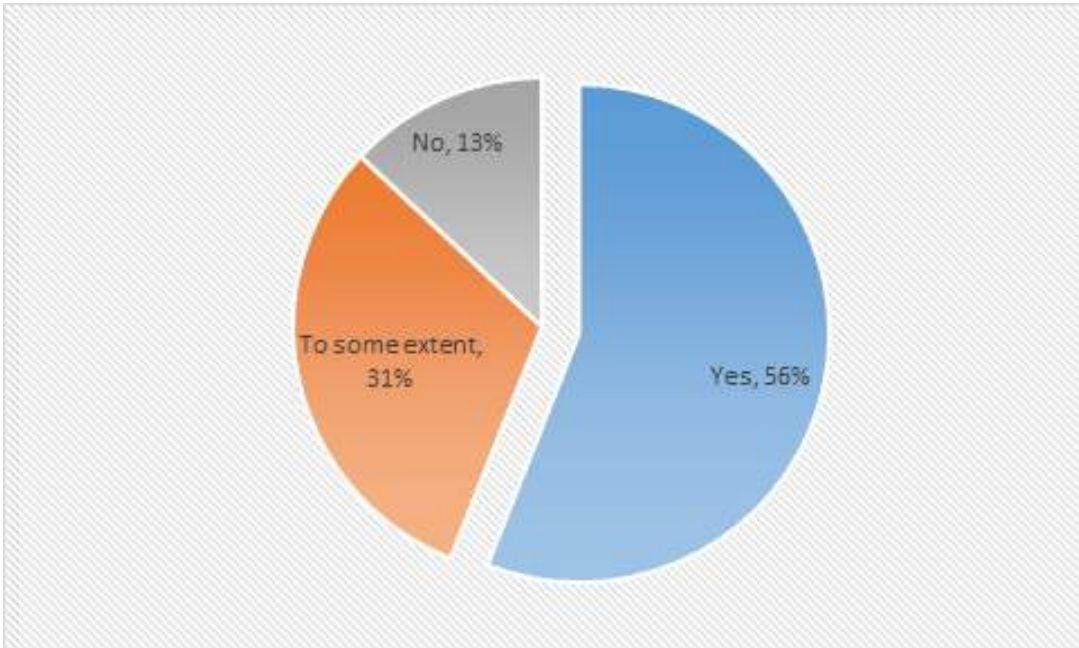


Figure 16 Do municipalities have a role in the doing business environment?

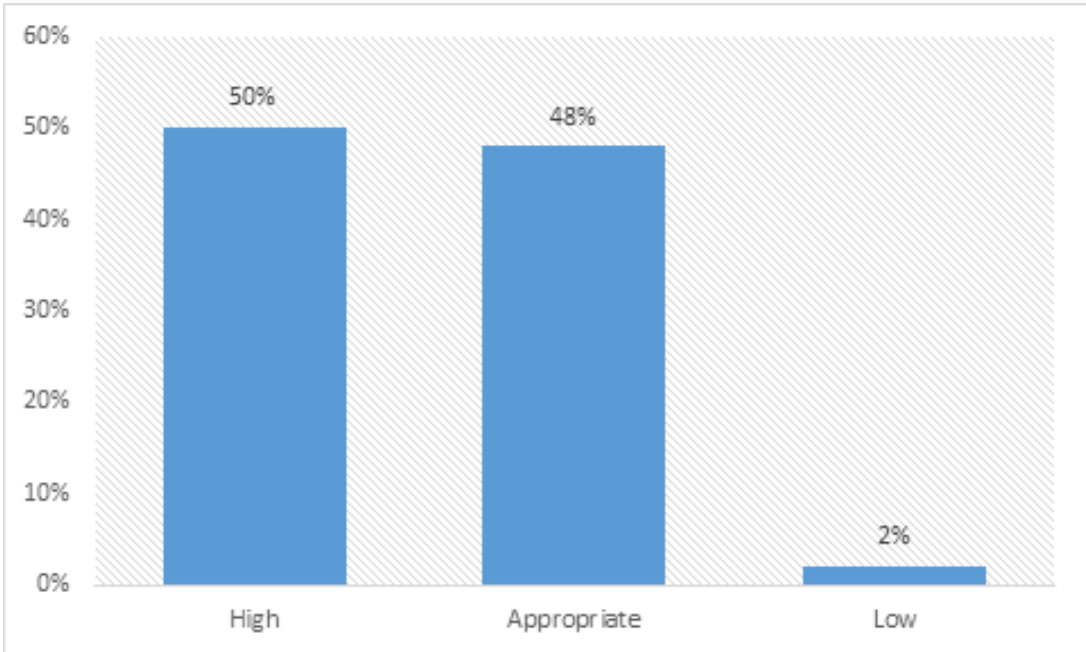


Figure 17 Businesses' thoughts on municipal tariff rates

As mentioned above, another important role that municipalities have is issuing construction permits. In the past, businesses have continuously raised their concerns regarding how the burdensome and time-consuming procedures they face when trying to obtain a construction permit. With the adoption of the new Law on Construction, where the input and expertise of the previous USAID Business Enabling Environment Program was very valuable, we wanted to see whether the procedure for obtaining a permit has been simplified in terms of time requirement. Out of 14% of respondents who have applied for a construction permit, 65% of applied for a Construction Permit before 2013, while 35% of them applied after 2013 (after the adoption of the new law).

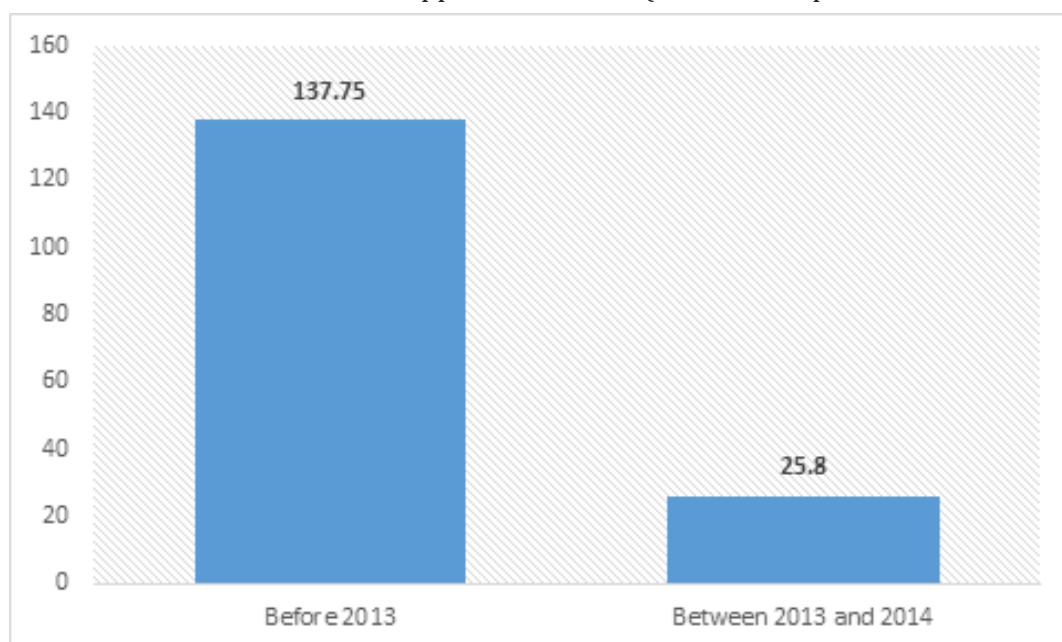


Figure 18 Number of days for obtaining a construction permit

The responses provided by businesses in this questions are promising. A very important point that needs to be made here is that a major part of this improvement can be attributed to the fact that the law includes the consent by silence principle, meaning that if the municipality does not respond to your request for permit within the legal deadline, than the application is considered as approved. As regards construction permits and the Law on Construction, Slywka asserts that a proactive approach from Kosovo Government has led to numerous reforms, including decrease of the permit fee (putting on a cost-recovery basis), the ongoing work towards consolidation of plans and zoning maps and so on.

Just like with Tax Administration and Customs, the respondents were also asked to present their perception regarding the level of corruption in municipal level, as well as the level of transparency.

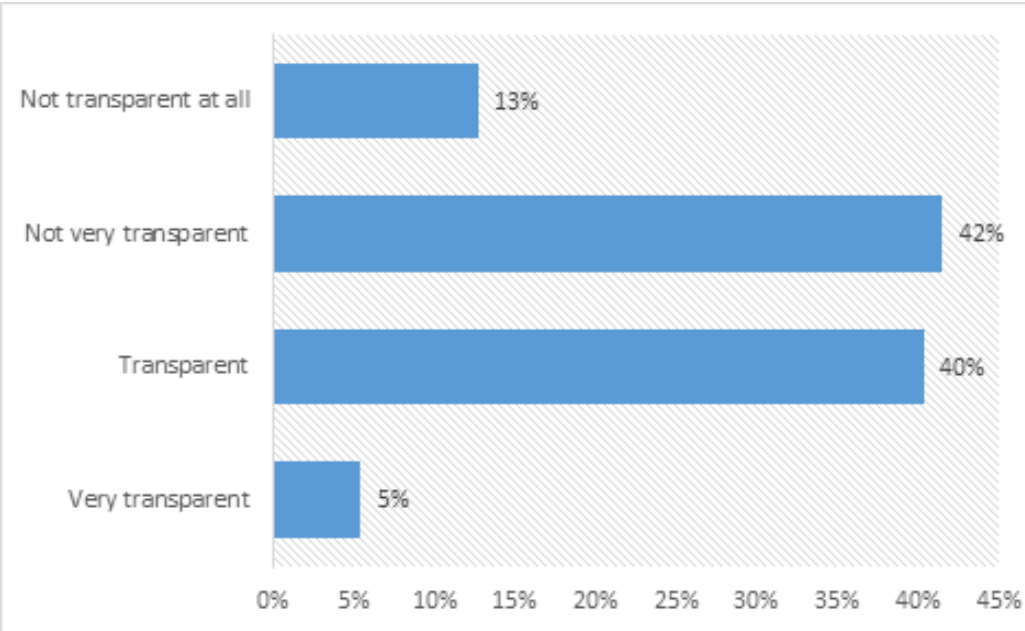


Figure 19 Transparency in Municipality according to respondents' perception

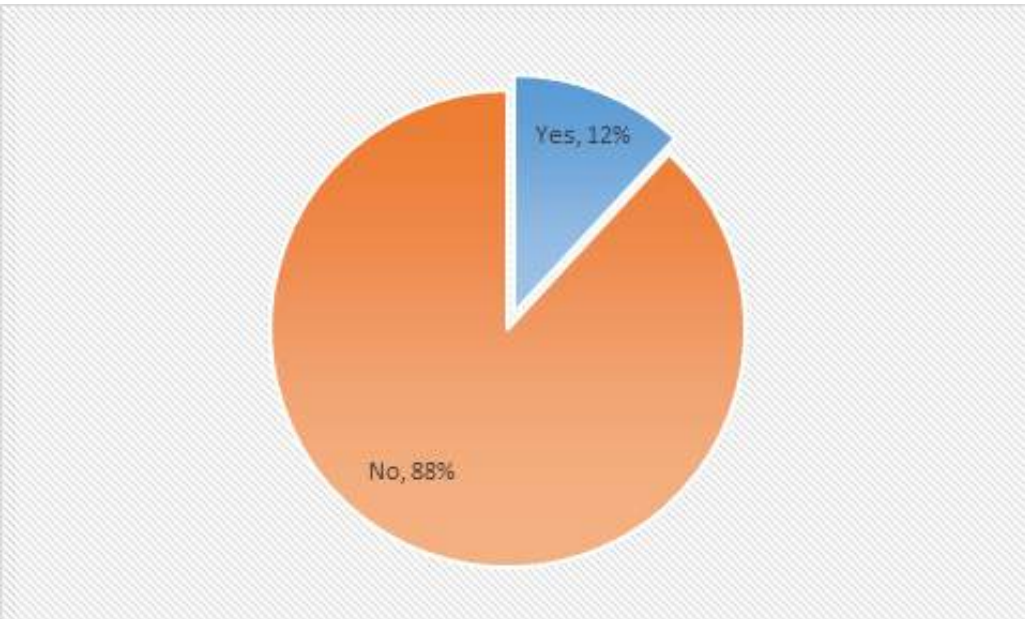


Figure 20 Corruption presence according to respondents' claim

Respondents that claim to have encountered corruption in municipalities say that this is done for getting access to certain administrative services, obtaining of any document, registering of property etc.

Public Procurement

Historically, public procurement has been an area that has triggered a lot of negative attention from the entire society in Kosovo, especially in terms of the perceived presence of corruption. The number of companies whose existence is largely dependent on tenders is relatively high, and at the same time, given that the public sector is the largest buyer of products and services in the country. Several reports from the civil society have demonstrated and identified numerous problems and challenges related to procurement, and yet very few improvements have been marked in this field. In 2012, AmCham published a report on Public Procurement which at that time presented a comprehensive situation in this area. This section provides the experience of 10% of respondent companies that are involved in public procurement activities. Out of that number, 46% claim to have encountered with irregularities in public procurement activities.

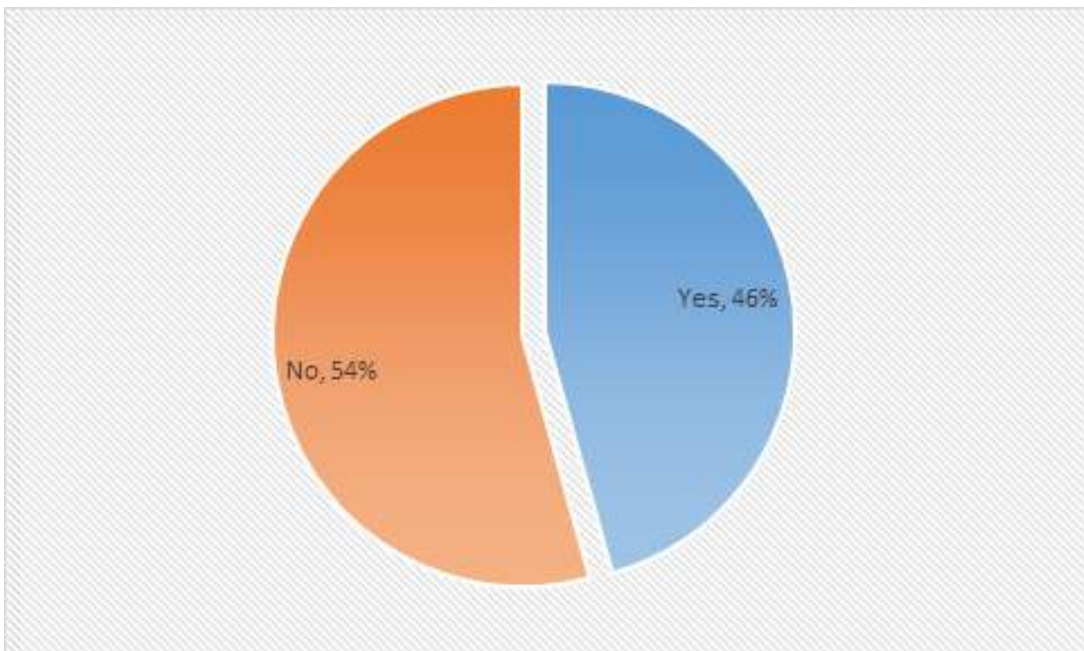


Figure 21 Have you encountered a problem in a procurement process

In this questions, the responses that respondents have provided regarding the type of problems they have encountered are various (to name a few: Illegal documentation; Low quality documents; Biased tender specifications; Illegal decisions; PRB very often

takes illegal decisions, corruption etc.)⁶.

Despite these evident irregularities, only 27% of respondents have actually submitted a complaint to respective authorities, namely to the Procurement Review Body (PRB). The 2012 AmCham’s Study on Public Procurement found that businesses avoid appeals on irregular public procurement activities as they are concerned that they might face problems with public procurement authorities in future tenders.

The degree to which businesses were satisfied with how the case was handled by the independent Procurement Reviewing Body, which is often referred as ‘Tenders’ Court’ are presented below:

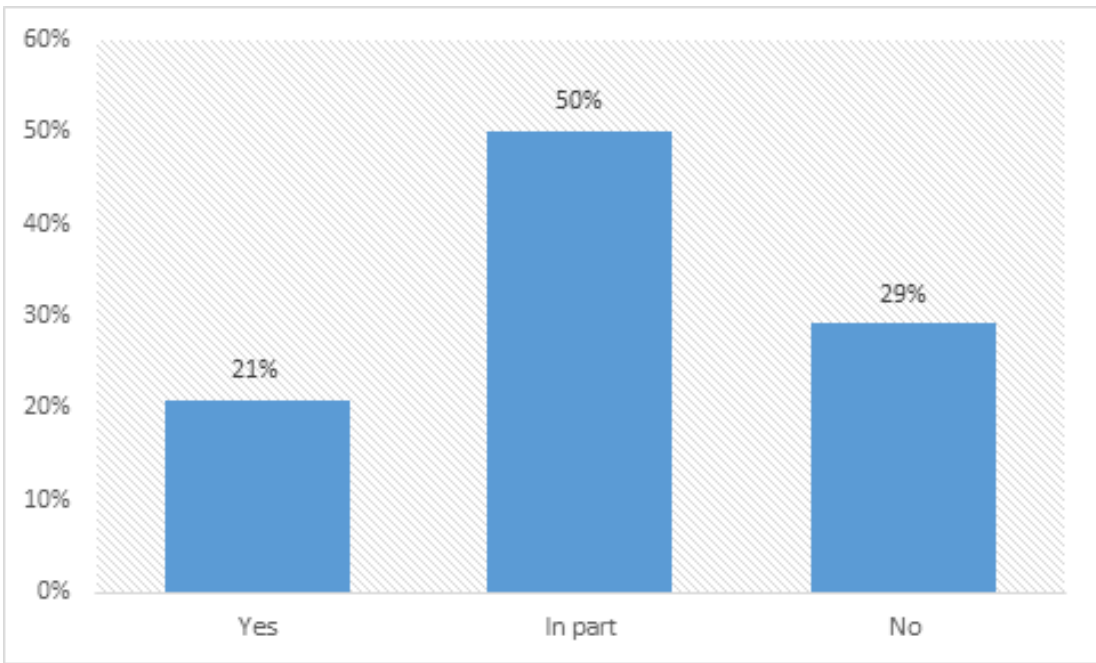


Figure 22 Satisfaction with the Procurement Review Body

As shown below, the perception of corruption in public procurement activities is at a relatively high rate.

⁶ For a more detailed analysis of the procurement system and problems in Kosovo, please refer to Public Procurement in Kosovo: Challenges of the Business Community study of AmCham

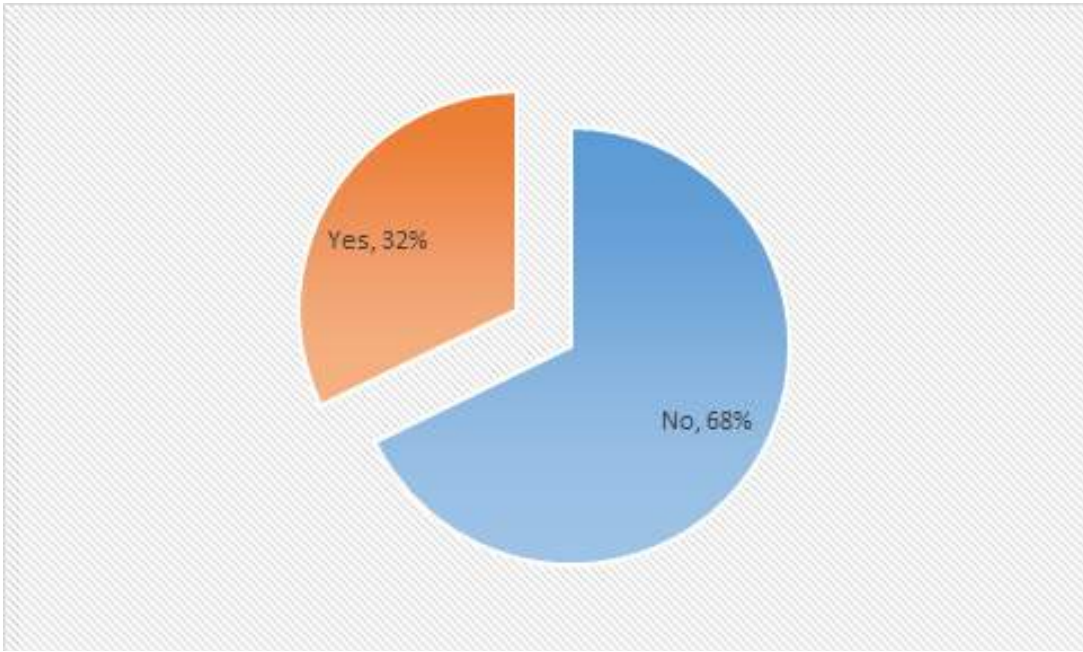


Figure 23 Have you encountered corruption in public procurement

Rule of Law

A trustworthy and efficient judicial system is a backbone of a strong and stable economy. This issue has been repeated times and times again by public institutions, private sector and the civil society. Efficient contract enforcement mechanisms are among the most important elements that an investor looks for when looking for a destination of his/her investments. Yet, despite the fact that Kosovo has marked significant improvements in many indicators of World Banks Doing Business Report, no significant improvement has been shown with regards to indicators related to contract enforcement. Agron Demi from GAP Institute of Advances Studies states that regardless of the reforms and great amount of work that has been put into law enforcement, the country still suffers from a relatively weak rule of law, which causes for Kosovo’s attractiveness in the eyes of potential investors to decrease. In this aspect, Demi emphasizes that also further improvement of legislation (especially in fiscal legislation) are necessary especially to remove contradictions between laws, which makes the work of the judiciary more difficult. In this direction,

This section of the study analyses the perception of respondent companies about the rule of in Kosovo.

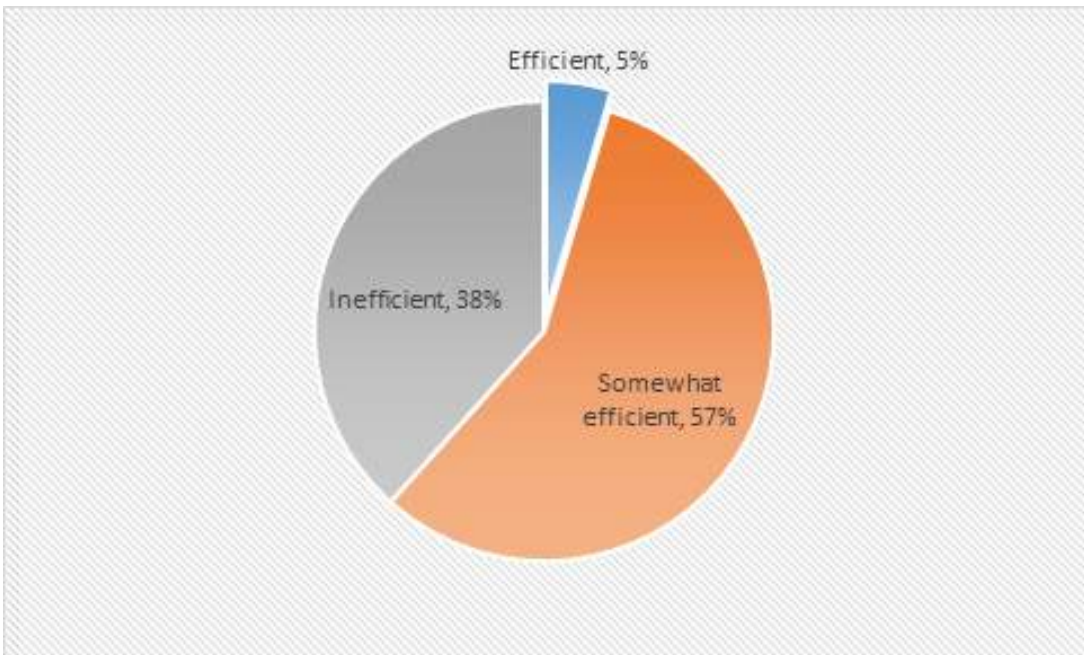


Figure 24 Respondents’ perception about the rule of law

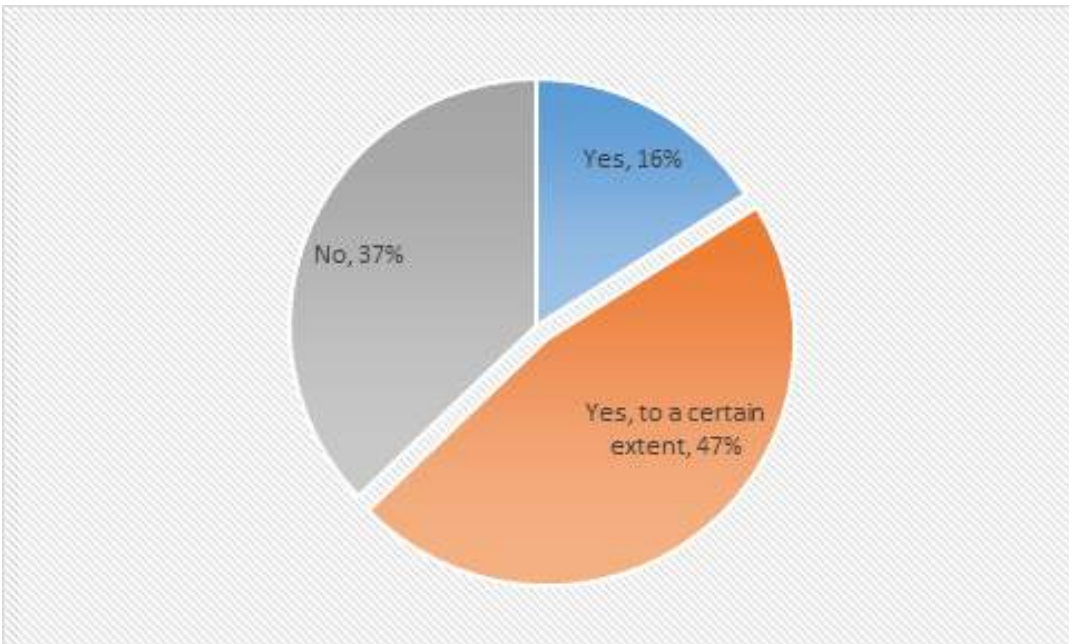


Figure 25 Trust in the judicial system

As the graphs reveals, only 5% of respondents believe that rule of law mechanisms are efficient and functional, while 38% claim the system to be inefficient. The perception about the efficiency of the rule of law mechanisms has influenced a significantly low trust by businesses on the judicial system, with only 16% of respondents claiming they trust the judiciary, while almost 40% of them claim a lack of trust. As Slywka mentions, the introduction of private bailiffs -a mechanism that has proved successful in many countries in the region- should help in improving Kosovo's situation with regards to rule of law, and contract enforcement particularly.

While the judicial system is only one of many actors in the war against corruption, AmCham also wanted to find out whether respondents believe that this system is efficient in this aspect. As depicted below, 48% of respondents do not believe that the judicial is doing a good job in fighting corruption:

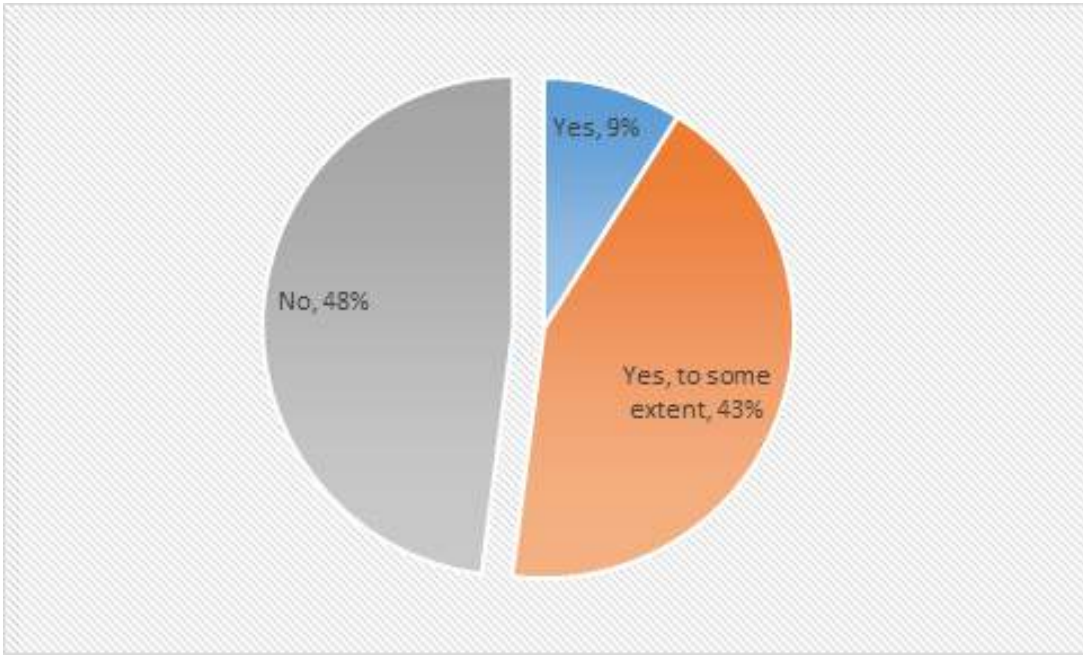


Figure 26 Judicial system war against corruption

Moreover, some respondents claim that the judicial system is engulfed in corruption itself, and the simplest evidence to support this is the fact that no major case of corruption has been found or punished by the institutions of this sector.

Access to Public Documents

Access to public documents is a fundamental right provided by the effective legislation in Kosovo. While only a minor percent of business respondents (9%) have made a request to access a public document, the results from these cases are very concerning. The degree to which respondents were able to gain access to requested documents is depicted below:

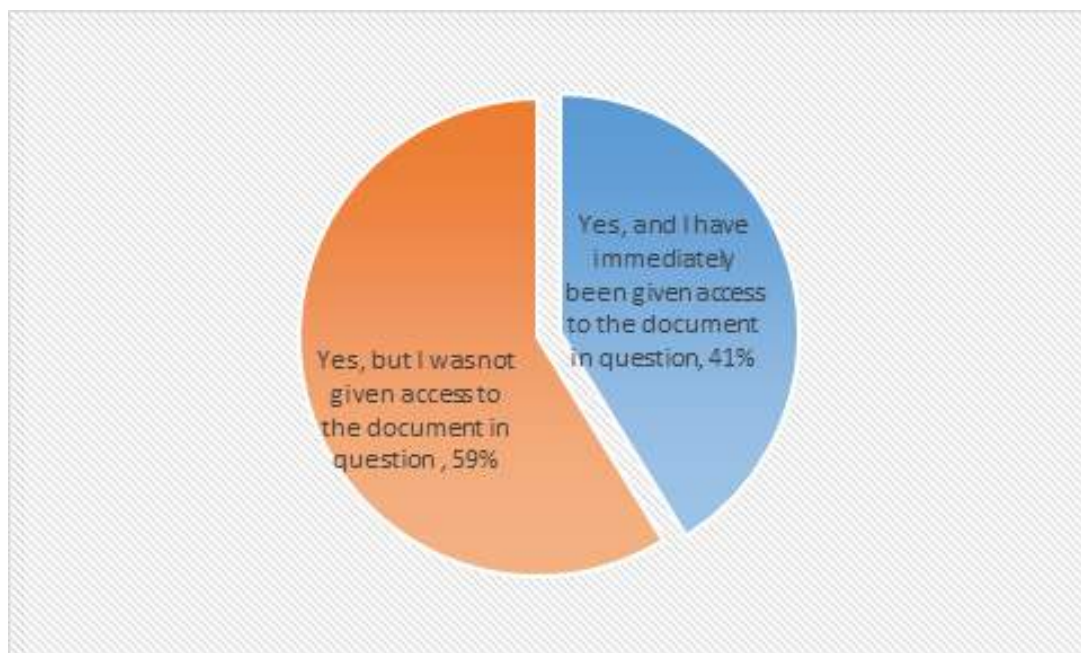


Figure 27 Accessing public documents

Most of the requests from business respondents to access public documents relate to procurement projects, while other requests concern urban planning documents, property registry, registration documents etc. Respondents that have not managed to get access to a desired public document claim that the denial is a clear indicator of corruption. Moreover, Demi stressed that access to public documents continues to be a major challenge and that sometimes institutions are hesitant to respond to requests from the civil society, although such an action represents a clear violation.

Access to Finance

Sound financing opportunities and favorable lending conditions are crucial elements for a normal business functioning and growth. Businesses borrow for various reasons, be it for liquidity or investment plans. AmCham conducted a study in 2010 that analyses the access to finance for Kosovo businesses in more details; however, this section of the study also gives an updated overview of the challenges and issues that businesses face in accessing finance. In this regard, Demi mentions access to finance as a major challenge for small and medium enterprises in Kosovo, stressing out that this is mostly a result of unfavorable financing conditions and the extensive documentation requirements from loaning institutions. The table below provides a picture of the most common source of financing among the respondent businesses:

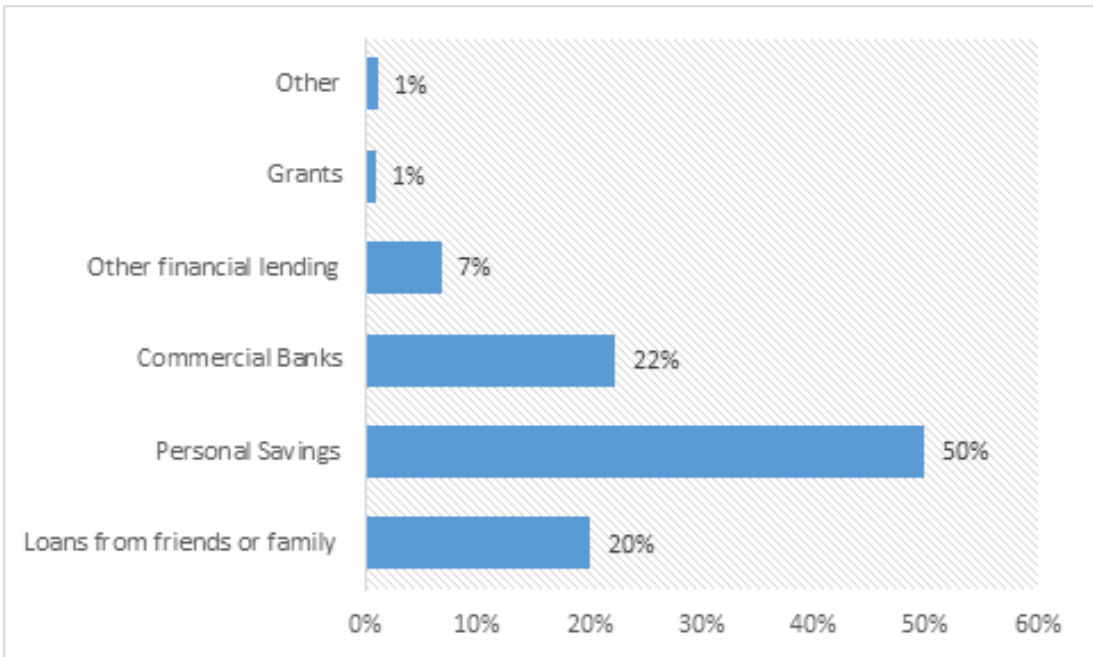


Figure 28 Source of financing for businesses

As the table suggests, personal savings represent the largest source of financing for businesses, followed by commercial banks, friends and family etc. Respondents were also asked about their opinion on the lending conditions from commercial banks and other lending institutions, and about the procedures for obtaining loans.

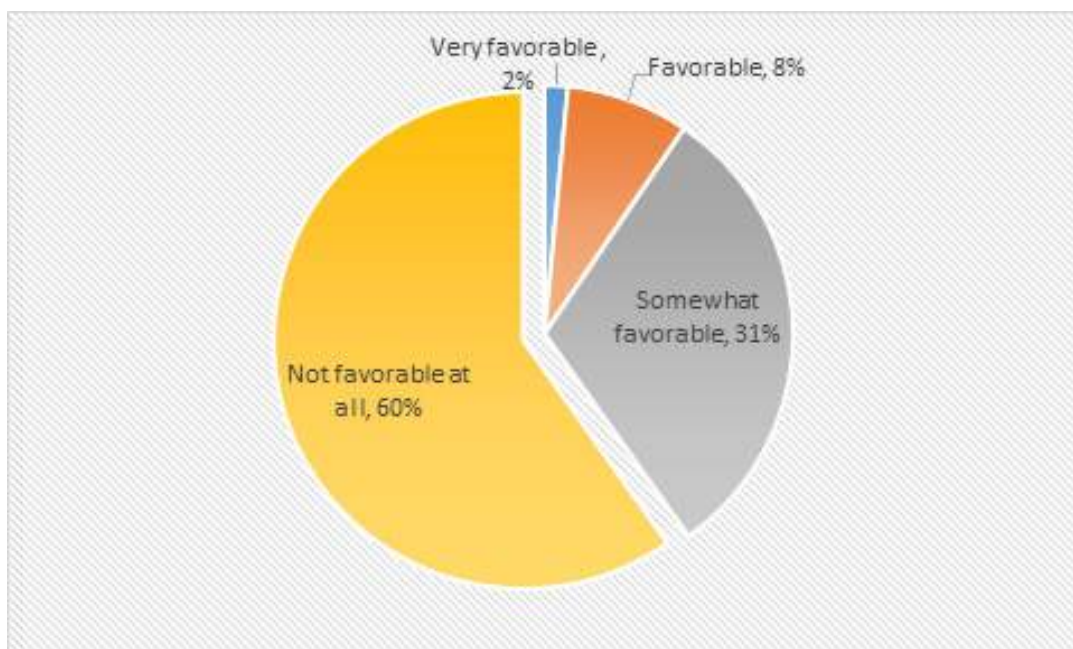


Figure 29 financing terms from financial institutions

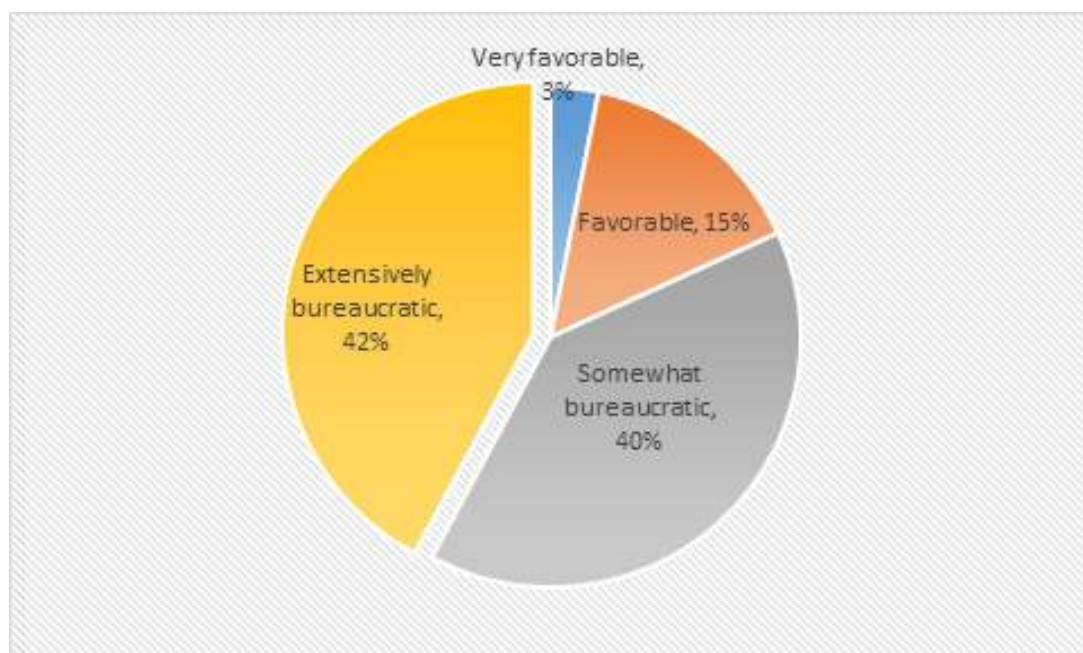


Figure 30 Procedures for getting a loan

Respondent businesses find borrowing terms to be unfavorable, whereas the bureaucratic procedures are extensive. This problem, similar to many other problems and challenges of the doing business environment, is very much related to the weak rule of law, inefficient court system, and ultimately poor contract enforcement, as faulty links in the chain that decrease predictability and increase uncertainty and risk. As a result, this causes extensive documentation requests from banks, as well as a higher risk premium that amounts to a more expensive loan agreement for businesses.

The fact that such a large portion of loans is used for increasing working capital and debt consolidation (47% in total) is worrisome and reflects the difficult state that businesses are currently facing in terms of financial liquidity.

Business Optimism and Good Governance

This final part of the survey concerns the overall outlook for enterprises in Kosovo (self-assessed) for the following years, as well as a comparison with previous years. It should be acknowledged that as pointed out in World Bank’s Doing Business Report, Kosovo has marked major improvements in the business registration phase. Slywka assesses that the business registration procedures have been significantly streamlined, with reduced costs, eliminated requirements and implementation of unified registration sites by KBRA and TAK, and noted that the increased number of registered L.L.Cs is a clear indicator of the positive effects that the reforms in this regard have had. He also mentions the establishment of one stop shops, the Credit Registry Update, elimination of location permit, and further operational improvements to increase efficiency in registrations and reduce registration times for property as positive developments in recent years.

However, in terms of challenges that lie ahead, respondents name unfavorable government policies, access to finance, and economic unpredictability as the three main elements, as depicted below:

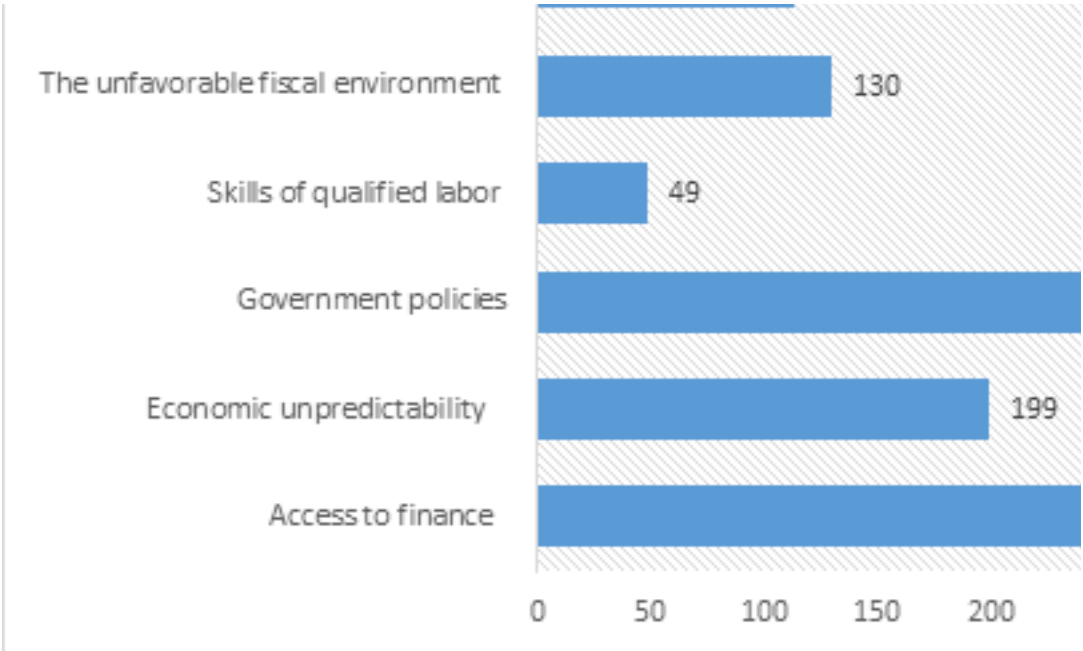


Figure 31 Challenges ahead for SMEs

Business respondents were also asked whether their business is in a better situation currently compared to three years ago or not. Only 5 percent of respondents claim that their situation has improved, while the vast majority of respondents say that there has not been any significant changes. It should be emphasized that only 1% of respondents believe that the state of their business is much better today than it was three years ago. The opinion is more evenly spread with regards to their outlook on the future. And despite the fact that the economic growth and strengthening of the private sector has been listed as the main priority of almost all the political parties in the recent parliamentary elections, only 30% of interviewed businesses are optimistic regarding the future, whereas almost 60% of them are pessimistic about the future developments.

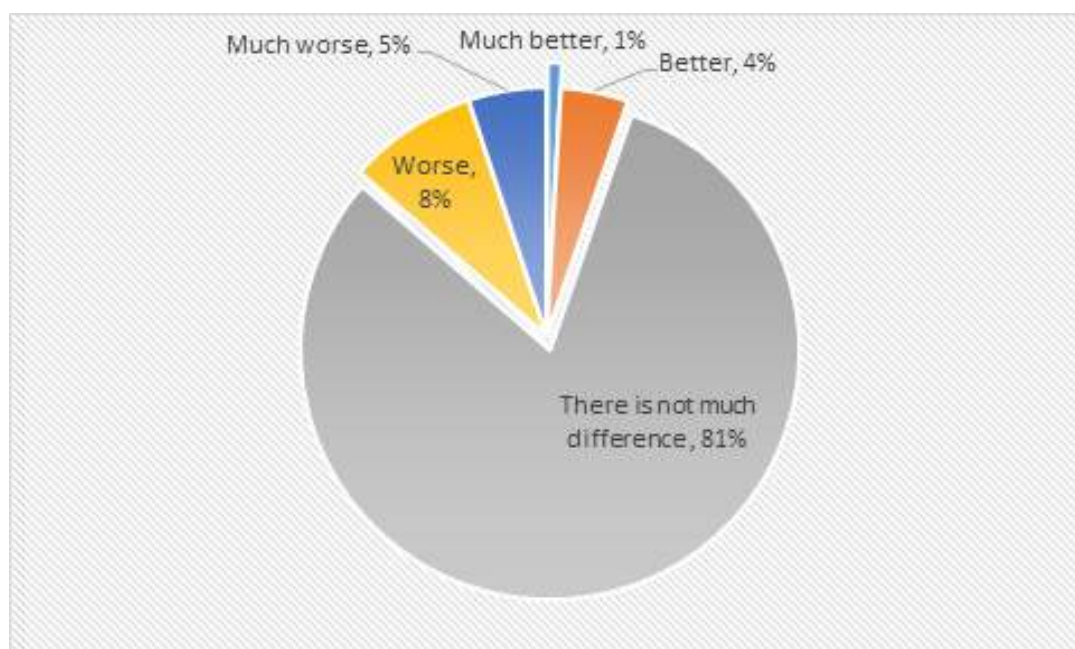


Figure 32 Development of your business in the last three years

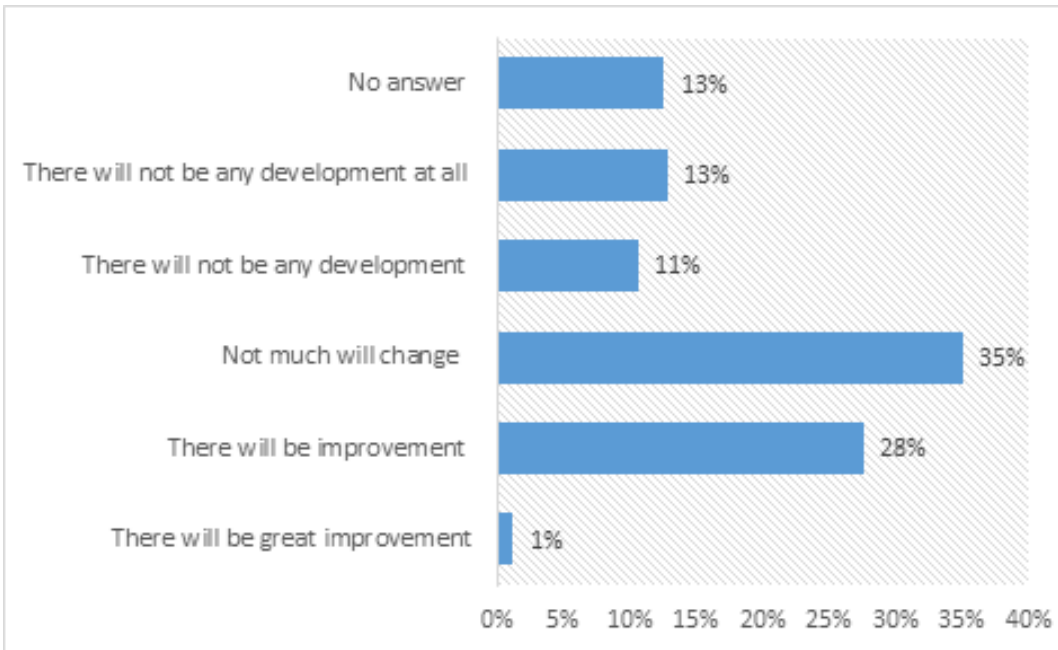


Figure 33 Expectations for the future

In terms of overall policies for Small and Medium Enterprises, only 13% of respondents claim that the conditions for these businesses are favorable and enable growth. The rest claim that the environment on which they operate is a difficult one:

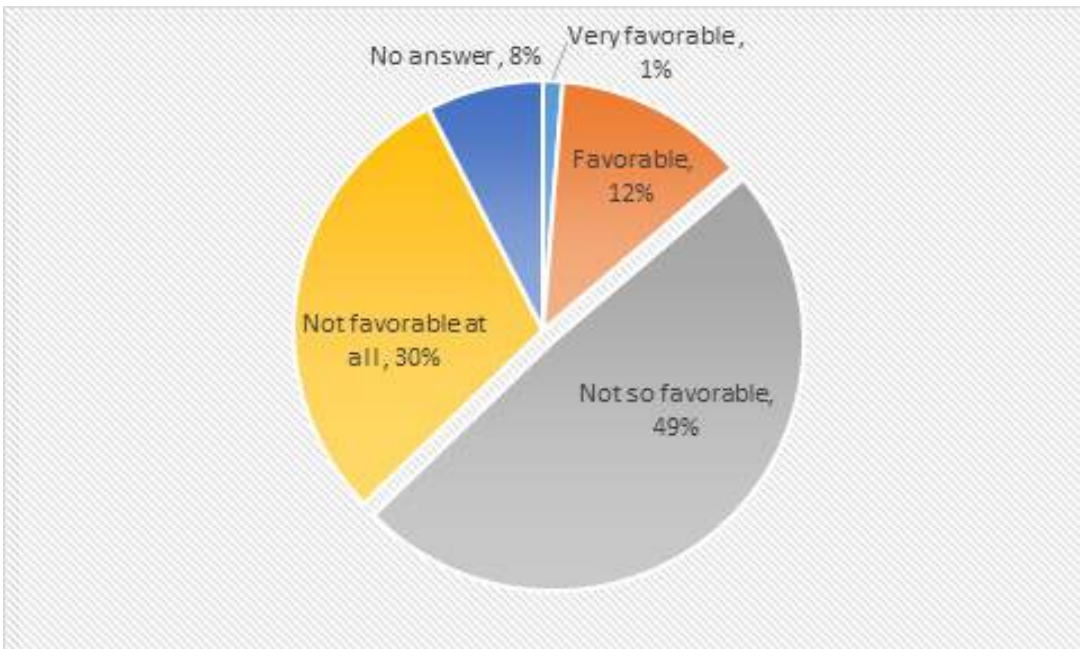


Figure 34 Government's policies towards SMEs

Respondents were also asked to rate 6 ministries based on their public transparency level. It should be noted that according to the respondents Ministry of Infrastructure is ranked as the most transparent ministry, whereas the Ministry of Labor and Social Welfare is the least transparent institution businesses deal with. However it should also be noted that the highest evaluation grade does not go beyond 2.65 in a 1-5 grading scale. The results are summarized below:

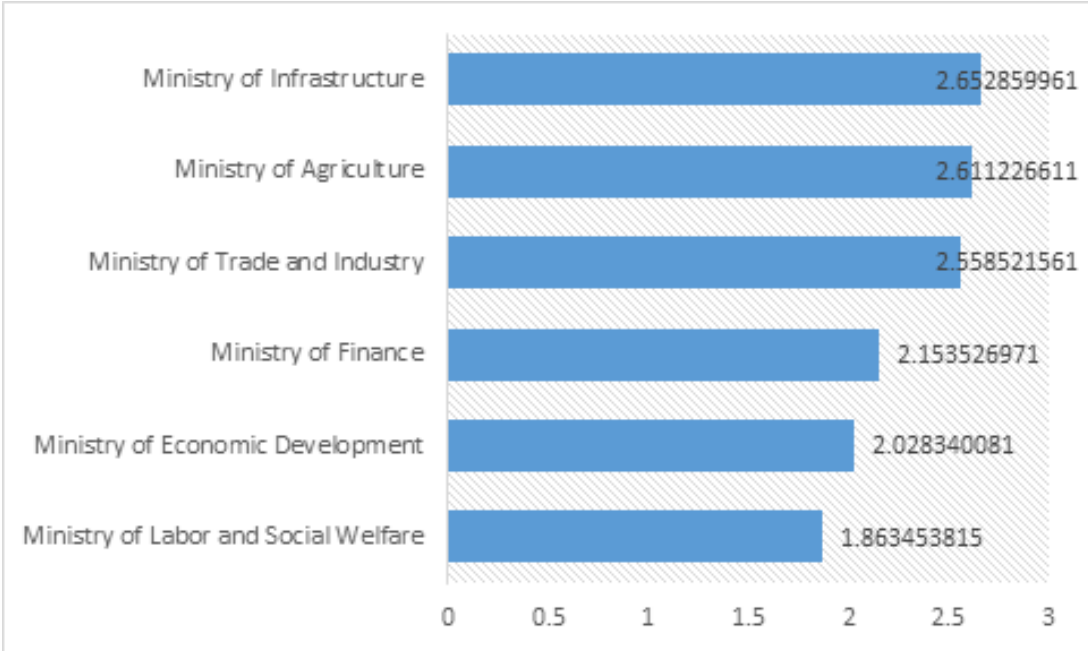


Figure 35 Ministries based on transparency (1- the lowest to 5 - the highest)

In addition, respondents rated the overall performance of the government on six issues, as presented in the following graph:

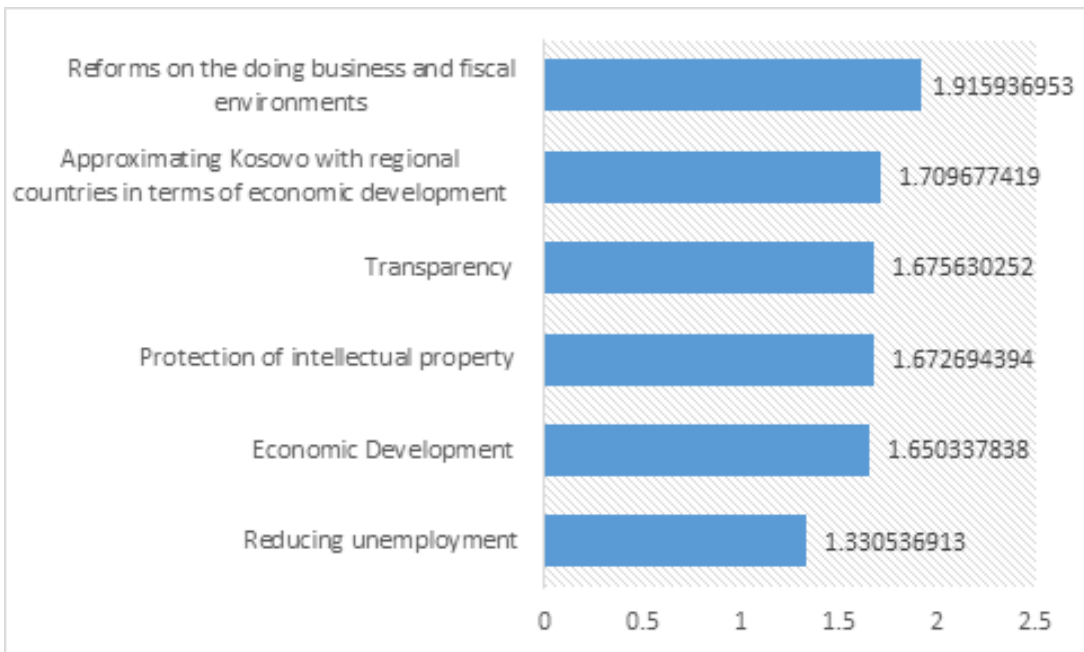


Figure 36 Government's performance (1 - the lowest to 5 - the highest)

Talking about transparency, it should be noted that the ratings for the overall performance of the government is on average graded lower than the six ministries. Another interesting finding is that despite the creation of various public-private consultative councils, not too many respondents believe that the private-public dialogue has improved. To the contrary almost 15% of them believe that it has even deteriorated. However, Haliti emphasizes that councils that have been formed with business associations, such as the Custom-TAK-Business Associations Council, allows these institutions to have access to issues of the private sector on a consolidated manner and to address those issues with a holistic approach of all key stakeholders. With regards to unemployment, which has received the lowest ranking from all elements, Demi shared GAP's analysis of the Employment Strategy – a document of the Government of Kosovo that aims at decreasing unemployment rates in the country, while pointing out that the strategy as a whole does not contain a very thorough analysis of labor market and lacks specific targets and recommendations. As such, the strategy will not serve its purpose of reducing unemployment in Kosovo.

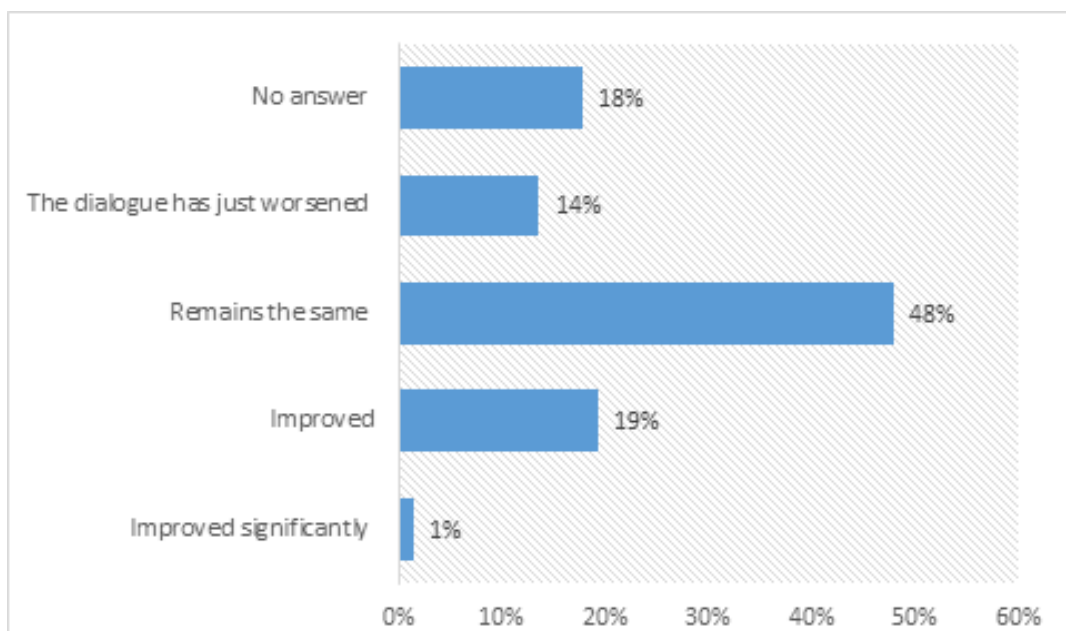


Figure 37 Public Private Dialogue

To end with the section of surveys, respondents were asked their opinion about the policies the government plans to undertake in the future. The responses as to whether they believe that the business environment will improve are relatively spread, as provided below:

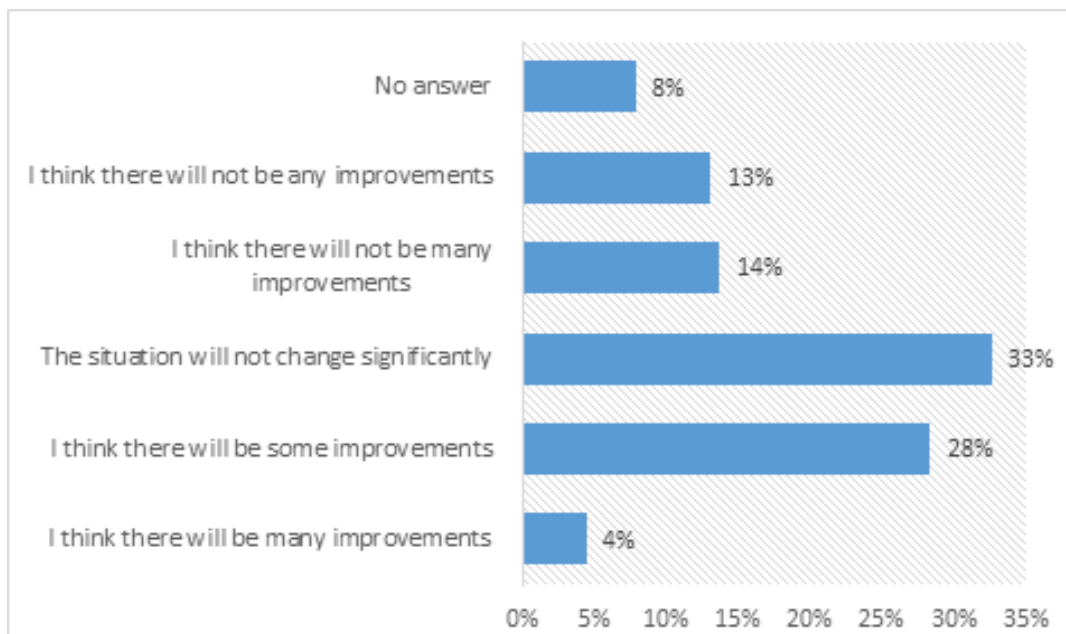


Figure 38 Business Environment in the Future

Recommendations

Fiscal Environment

Because of a large dissatisfaction by businesses with the fiscal environment, the Government, namely the Ministry of Finance should introduce policies that further improve the fiscal environment. This may include **further exemption of goods, particularly raw materials not produced in Kosovo from customs dues**. This would also encourage the development of manufacturing sector, substitution of imports, and a future increase of exports, ultimately improving the trade balance picture. **New fiscal incentives may also include tax breaks depending on the number of jobs to be generated and the size of investments**. This was announced by the Ministry of Finance in May 2014 upon a joint agreement with the three largest business associations in Kosovo, the Kosovo Chamber of Commerce, the Kosovo Business Alliance and the American Chamber of Commerce in Kosovo, but is pending amendment of the Corporate Income Tax Law.

Having in mind that 61% of interviewed businesses believe that tax rates in Kosovo are high, and having in mind that most of the interviewed businesses are micro and small businesses based on the number of their employees, the Government may think in the future **decreasing the tax rates particularly for service providers**, given that two years ago the Ministry of Finance increased the tax rate for this industry from 5% to 9%. In addition, TAK should guarantee an **equal treatment for all economic operators**, as the director of the institution himself emphasized during the interview.

The Tax Administration staff should apply **consistent interpretation of the tax legislation**, having in mind the many concerns expressed by businesses recently, and having in mind the survey results which suggest that around 80% of businesses do not believe that the interpretations by TAK are completely fair. This is particularly important knowing that the appeal mechanisms which are available to businesses, including state courts, do not function efficiently. In cases when the laws are not in line with European Union directives, are unclear or allow for dual interpretation, the Tax Administration of Kosovo and Ministry of Finance should initiate the amendment of the laws in order to **further harmonize them with European directives and practices**. This would further increase tax predictability which is particularly important for foreign investors.

Despite the fact that at the initiative of the Ministry of Finance, and its joint efforts with TAK, Customs, Business Community and civil society, a new working group has been established and a strategy for fighting of informal economy has been drafted, the respective **institutions should increase their practical measures for addressing informal economy**. Part of these efforts is also the bringing under control the two border-crossing points in the northern Kosovo, which were used in the past as gates for smuggling of goods. **Tax Administration should strengthen the mechanisms in which businesses and citizens may report the cases of informal economy**. At the same time, more work should be done in raising the awareness of the society on the importance of having more businesses join the formal economy.

Having in mind that in general, businesses are satisfied with the transparency level of Tax Administration of Kosovo, the institution should continue to maintain and further improve its transparency. This applies for corruption as well. **TAK should undertake further measures to increase the integrity monitoring of its staff by further improving the checks and balance systems, particularly for lower ranking officials and tax inspectors.**

Trade and Customs

Similarly to the recommendation addressed to TAK, **consistent implementation of the legislation is needed** to ensure that all economic operators are treated equally and in accordance with the law. However, another point that needs to be mentioned is that the Custom should **further develop its risk-based approach** upon importation of goods. In this sense, companies that have a good history of declaring and paying custom duties, should not be subject to same restrictions that companies with a bad history have. For example, if a company (or some companies) has misused the authorization for the use of custom warehouses, this should not be an excuse to create barriers in the form of additional criteria for all companies, most of which have conducted their business in a lawful manner. **Also, we believe that this risk based approach should be used also in cases of reevaluation of goods.**

A recent initiative that has been viewed as very positive by all businesses is that the Custom have begun accepting guarantees from insurance companies. This has decreased the cost of doing business in terms of international trade immensely.

However, the Customs and Excise Code requires that the unpaid obligations to customs be covered at all time at a rate of 100% by businesses with a guarantee. We believe that this requirement is excessive, as not all industries have the same risk. **Thus, we recommend to amend the Customs and Excise Code of Kosovo, to allow the director of Custom to decide for the level (coverage) of guarantees required by businesses, based on the risk.**

Another issue that has been brought up by businesses is the unclear specification of goods under the Integrated Tariff of Kosovo (TARIK). **We recommend the Custom to review TARIK and to further specify products in respective categories, in order for companies to have an easier and more accurate declaration procedure.** In doing so, the business associations should also be consulted in order to come with a more comprehensive list.

In order to have a better communication and dialogue between businesses and custom, **we recommend Custom to appoint so called “Industry Officers” within their institutions**, whose role would be to provide advisory services to companies of a particular industry. This would enable businesses to have a more thorough understanding of procedures that are specific to that sector, and would contribute on further improving the public-private dialogue.

Despite the notable reforms that have been made that aim to facilitate procedures in the custom, businesses continue to view these procedures as bureaucratic. Having this in mind, and considering TAK’s experience in this regard, in addition to further continuing the reforms, **we recommend the Custom to make more efforts in informing businesses about their obligations and about procedures.** In this regard, the Consultative Council mentioned above can serve as a good platform for the distribution of information and awareness raising.

Slywka also highlighted that government agencies (including administrative revenue bodies and inspectorates) plan and set revenue targets (even though they lack discretion in implementation and should be collecting all that is due, no less, no more), pointing out that strategic planning issues, such as revenue target setting, can lead to undesirable side effects, including changing the dynamic between agencies and citizens from one that is customer-service focused and compliance seeking, to one of conflict where non-compliance is necessary, and incentivized, in fulfilling those targets. Instead, Mr. Slywka

suggested that administrative bodies should focus on customer / citizen service to encourage public knowledge of requirements and support compliance. **Administrative body operational metrics should be developed and implemented that are (1) with the control of the agency (2) have a customer service / operational efficiency focus and (3) are variables completely within the capacity of the body to control.** Such measures would could strengthen internal management and result in an improved relationship between the state and the people.

Municipal issues

Having in mind that businesses have complained about the implementation and interpretation of municipal regulations, **municipalities should pay more attention to the consistent and uniform implementation of the municipal regulations and applying of fair treatment of all investors, be them local or foreign.**

Despite the fact that there is a general satisfaction with the speed and process of issuing of construction permits, the municipalities throughout Kosovo should work more in further improving and speeding the process of issuing of construction permits. **In cases when the issuing of a permit is subject to existence of municipal spatial plans and city urban plans, the municipalities should finalize the latter as soon as possible, in order for businesses and citizens to be able to exercise this right of theirs.**

When it comes to the municipal tariff rates, the municipalities should reflect on these tariffs and the rates they impose, to reduce the financial burden of local businesses, which are very often seen as a short-term source of revenue collection. **Tariff Rates should not be seen as a source of revenue, but rather as a fee for services that businesses and citizens receive from the Municipality.**

Transparency in the municipal level seems to be a big issue for local businesses with only 5% of them believing that municipalities are very transparent and above 55% of them expressing their dissatisfaction with lack of transparency. **The municipal authorities should make more efforts to pursue some good practices in promoting an open decision-making process, increase people's access to public documents.** All municipalities should be encouraged to follow the example of the local Municipality-Business Community Advisory Council, established by the Municipality of Gjakova, in

which representatives of private sector can provide their input of important matters of local economic development.

Increased transparency and open and frank communication between business community and municipal authorities would also help in further eradication of corruption in the municipal level of governance as well. The survey results suggest that 12% of the interviewed businesses have encountered corruption in the municipalities in which they operate. Given that according to them, the corruption in municipalities occurs when they try to access certain administrative services and civil registry documents, the municipalities should follow the examples of few municipalities throughout Kosovo, including the Municipality of Prishtina to introduce the online application for these documents and services, which would result in a more efficient usage of human capacities and reduce the potential for misuse of authority of municipal civil servants.

Procurement Issues

Despite the fact that AmCham is only one of many organizations that have tackled public procurement, we have seen very few improvements in this regards. Because of this, most of recommendations that were included in our report, Public Procurement in Kosovo: Challenges of the Business Community, still remain the same. The only major development that was noted in this period, that was welcome particularly by the production sector in Kosovo, was the amendment of the Law on Public Procurement to give preference to domestic bidders. As we understood this is a practice that has been implemented in countries in the region for a long time now.

Contracting authorities should carefully consider their options when selecting a contract award criterion. While opting for the lowest price criterion as opposite to the economically most advantageous offer can be easier in terms of evaluating bids, it is not necessarily the adequate criterion to be used in all procurement cases. Some fields, such as health, should require the usage of the economically most advantageous offer criterion in evaluation, due to the importance it has to the overall society and due to the sensitivity of the field. If necessary, contracting authorities should consult experts to make sure the basis of evaluation is transparent and can provide the best possible results. This will increase the probability that companies offering higher quality products/services will win more projects. As a result, in the long run, the budget of

the country will **Technical specifications should necessarily be drafted by experts of the field.** Ministries, agencies, municipalities, and other public institutions that are subject to procurement laws, should budget separate funds for hiring field experts in order to ensure the drafting of technical specification that are truly needed for the project at hand and are in line with best EU practices. This will enable a more transparent process, helping reduce the occurrence of favoritism. Necessary amendments should also be made to the law in power to provide for the hiring of experts in cases when sector-specific expertise is needed in drafting technical specifications. After all, the law on public procurement has been drafted to promote fair competition, and this should be in line with those principles. **Also, contracting authorities should make sure that there are enough funds to cover for the expenses of the project, before announcing the tender and they should avoid the practice of requiring extensive documentation of applying for tenders.**

E-procurement platform should be established. Benefits derived from implementing an electronic platform for public procurement are plenty. E-procurement, will increase transparency, decrease costs, improve efficiency, lower environmental impacts, and increase competition in procurement processes. **Also, much more emphasis and resources should be dedicated to fighting corruption in procurement.**

Rule of Law

The introduction of private bailiffs should play an important role in improving rule of law in Kosovo. The judicial system has had a vast support from donor organizations, particularly from USAID, that have contributed significantly to improving the situation. However, there is still plenty of room for improvement considering the respondents' dissatisfaction with the efficiency, as well as the lack of trust in the institutions.

As a first step, **corruption from judicial institutions must be eradicated**, especially considering that these institutions are themselves entitled to combat this occurrence. A corruption-free judicial system would pave the way for increased efficiency, accountability and independence. The strategy for fighting corruption should be implemented properly.

Another important stride towards a better rule of law is to increase the number of judges, particularly those dealing with economic matters, and to provide additional trainings in the field of economy and business to all judges in the economic department at the basic court in Prishtina. More often than not, business disputes are of a complicated matter, meaning that those people entrusted to solve these disputes should have a very clear knowledge and expertise of the sector. This makes the training component of a crucial importance.

Alternative Dispute Resolution methods should be utilized. Currently there are two alternative dispute resolution centers in Kosovo which are institutionalized: the Permanent Arbitration Tribunal of Kosovo Chamber of Commerce and the Alternative Dispute Resolution Center of American Chamber of Commerce in Kosovo. These centers offer a valuable alternative to businesses in the form of arbitration and mediation. However, **promoting the use of alternative dispute resolution mechanisms (from courts and all stakeholders that make up the judicial system in the country) is recommended,** given that an increased usage of this alternative would decrease the burden from the courts, thus making them more efficient as well.

Moreover, as Slywka suggests, another step forward in improving rule of law is the **further consolidation of all legal acts, including on-going updating of all Administrative Instructions by initiating bodies as well as municipal regulations, in the official gazette** (<http://gzk.rks-gov.net>) that is now functional with USAID's help.

Access to Public Documents

Given that the Law on Access to Public Documents grants the right of access to public documents to all the citizens of Kosovo, all institutions should make all the necessary efforts to implement this legal right and in a reasonable time.

Access to Finance

As stated in the elaboration of this issue in the Access to Finance section, the affordable financing terms are very much dependent on the improved rule of law and contract enforcement, and increased efficiency of the court system and dispute resolution

mechanisms. In order to reduce the level of risk which lending institutions take when funding businesses, another recommendation would **include business improve their financial reporting statements and corporate governance**. A better implementation of the Law of Financial Reporting is also necessary to encourage banks to offer more suitable financing conditions. The next section discusses other means to support SMEs in terms of financing.

In the recent parliamentary election campaign, almost every political party has promoted the idea of a development fund, that would enable private sector companies access to grants and investment funds. As development of these funds would complement the financial industry of the country, **the proposals should necessarily be discussed in a comprehensive manner with all the relevant stakeholders and experts**, in order not to jeopardize the currently sound financial system in Kosovo and also jeopardize the pension savings of the citizens of Kosovo, having in mind that they were thought as initial sources of setting up these funds.

Business Optimism and Good Governance

If we carefully analyze the challenges that businesses, and particularly small and medium sized ones face in Kosovo, namely unfavorable government policies, which adds to the general dissatisfaction of private sector, **the Government institutions and public agencies should address and resolve these permanent concerns of the business community in order to facilitate their growth and development**. A very serious challenge for the businesses remains the high perception of economic unpredictability as a result of frequent amendment of laws, regulations and public strategies for various sectors, inconsistent implementation of laws and regulations and biased interpretation of legislation which very often results in sanctioning of businesses and increasing the uncertainty of business operation. In addition, **improvement of access to finance, further improvement of fiscal environment and reduction of skills gaps, particularly for senior-level positions would enable an accelerated business growth and enable the businesses experience faster development trends, and ultimately lead to a higher economic growth of the country**.

The pessimism of interviewed businesses adds to the importance of government **adopting a comprehensive National Economic Development Strategy**, which despite

the consistent calls of business associations, think tanks and independent experts, was never drafted. The National Council on Economic Development which gathers eleven ministries, representatives of three largest business associations, representatives of National Assembly, Office of the President of Republic and representatives of international organizations, would be a very good venue for the discussion and approval of such strategy. Also, taking into consideration that a large number of respondents does not consider the government policies towards SMEs as favorable, the Economic Development Strategy should focus on these businesses. **The special incentives may include grant and credit guarantee schemes.**

In addition to the aforementioned measures, increased government performance demonstrated through reforms in the doing business environment, increased transparency, protection of IPR, accelerated economic growth, increased private public dialogue, and increased transparency of the respective ministries would only contribute to a better perspective and optimism.

Input/Recommendation Summary Table

FISCAL RELATED ISSUES	No	Issue	Relevant Legislation/ institution	Reference to EC Progress Report 2013	Recommendation
	1	61% of respondent businesses claim taxes in place to be very high	Law on Corporate Income tax; Law on Personal Income tax; Law on Value Added Tax	4.1.4. Customs and taxation	(1) Further exemption of goods, particularly raw materials not produced in Kosovo from customs dues ,(2) introducing fiscal incentives in the form of tax breaks depending on the number of jobs created, (3) decreasing the tax rates particularly for service providers
	2	80% of businesses do not believe that the interpretations by TAK are completely fair and unbiased	Tax Administration of Kosovo Law on Corporate Income tax; Law on Personal Income tax; Law on Value Added Tax	4.1.4. Customs and taxation "Enforcement of tax legislation remains a major challenge."	Consistent interpretation of the tax legislation needs to be installed
	3	Roughly 35% of respondents claim that informality is not addressed properly by institutions	Tax Administration of Kosovo	4.1.4. Customs and taxation "The fight against the informal economy and tax evasion needs to be prioritized and its efficiency significantly increased."	(1) Increase their practical measures for addressing informal economy, (2) Tax Administration should strengthen the mechanisms in which businesses and citizens may report the cases of informal economy, and (3) raising the awareness of the society on the importance of having more businesses join the formal economy.
	4	58% or respondents are not satisfied with the level of transparency in TAK, while 9% claim to have encountered corruption	Tax Administration of Kosovo	4.1.4. Customs and taxation And Fight against corruption	TAK should undertake further measures to increase the integrity monitoring of its staff by further improving the checks and balance systems, particularly for lower ranking officials and tax inspectors.

CUSTOM AND TRADE	5	Businesses complain about unclear and unfair custom procedures that damage their operations	Kosovo Custom	4.1.4. Customs and taxation	(1) consistent implementation of the legislation is, (2) adoption of a risk-based-approach in imports and reevaluation, (3) Kosovo Custom to appoint so called "Industry Officers" within their institutions, whose role would be to provide advisory services to companies of a particular industry
	6	Businesses complain about burdensome and expensive guarantees. Some industries claim that there is no risk at all in their industry so the request for guarantee is unnecessary	Kosovo Custom/ Customs and Excise Code	4.1.4. Customs and taxation	Amend the Customs and Excise Code of Kosovo, to allow the director of Custom to decide for the level (coverage) of guarantees required by businesses, based on the risk.
	7	There are a number of complaints regarding reevaluation and changing of tariff numbers upon imports.	Integrated Tariff of Kosovo	4.1.4. Customs and taxation	Review TARIK and to further specify products in respective categories, in order for companies to have an easier and more accurate declaration procedure.
	8	Businesses feel that there is an increased pressure on them from the Custom to collect more taxes via fines and reevaluations due to budget projections.	Kosovo Custom	4.1.4. Customs and taxation "Kosovo customs collected revenue worth approximately €844 million in 2012. This is 2.2% more than in 2011, but €32 million below projected revenues, partly due to a reduction in imports. In the first six months of 2013..."	Administrative body operational metrics should be developed and implemented that are (1) with the control of the agency (2) have a customer service / operational efficiency focus and (3) are variables completely within the capacity of the body to control.

MUNICIPAL ISSUES	9	Although the situation is improving, there are still challenges for businesses for getting construction permits, particularly when urban or municipal plans for the zone do not exist	Municipalities/ MAPL	2.1 Democracy and the rule of law – Local Government	Municipalities should finalize the municipal spatial plans and city urban plans as soon as possible, in order for businesses and citizens to be able to exercise this right of theirs
	10	50% of respondents believe municipal tax rates to be very high	Municipalities	2.1 Democracy and the rule of law – Local Government	Look at the possibilities for reducing municipal tariff fees. Tariff Rates should not be seen as a source of revenue, but rather as a fee for services that businesses and citizens receive from the Municipality
	11	While 12 percent of respondents say that municipalities are not transparent, there are many complaints about access to public documents in municipalities	Municipalities	2.1 Democracy and the rule of law – Local Government	The municipal authorities should make more efforts to pursue some good practices in promoting an open decision-making process, increase people's access to public documents Increased transparency and open and frank communication between business community and municipal authorities would also help in further eradication of corruption in the municipal level of governance as well.

PROCUREMENT ISSUES	12	This issue was presented as a very problematic one in a previous study conducted by AmCham, titled “Public Procurement in Kosovo: Challenges of the Business Community”	All contracting authorities/ Law on Public Procurement	4.1.6. Public procurement	Contracting authorities should carefully consider their options when selecting a contract award criterion.
	13	There are many complaints about the drafting of technical specifications. Sometimes technical specifications may be drafted to favor specific bidders, but sometime specific bidders are favored accidentally because of lack of expertise of people drafting those specs.	All contracting authorities/ Law on Public Procurement	4.1.6. Public procurement “The capacity of all bodies involved needs to be further improved. It is important to avoid long periods during which key positions are not filled.”	Technical specifications should necessarily be drafted by experts of the field. More trainings should be given to procurement officers
	14	Businesses and business associations have called for the digitalization of process for a long time, in order to reduce costs, fight corruption, increase competition etc.	Law on Public Procurement/ Assembly	4.1.6. Public procurement	E-procurement platform should be established. Also, much more emphasis and resources should be dedicated to fighting corruption in procurement.
	15	The previous AmCham study revealed that businesses are not satisfied with the big number of procurement that are cancelled because of the lack of funds	All contracting authorities	4.1.6. Public procurement “Contract management and planning capacity need to be strengthened. Awareness needs to be raised as regards public procurement procedures and their implementation, and corruption needs to be addressed more effectively by Kosovo authorities.”	Contracting authorities should make sure that there are enough funds to cover for the expenses of the project, before announcing the tender and they should avoid the practice of requiring extensive documentation of applying for tenders.

RULE OF LAW	16	38% from more than 650 businesses think that the judicial system is completely inefficient, which has resulted in a very low trust in the institutions	Judicial System	2.1. Democracy and the rule of law – Judicial System “The Judicial Council has filled 334 out of a total of 404 positions and 125 of the 146 prosecutor positions are filled.”	Increase the number of judges, particularly those dealing with economic matters, and to provide additional trainings in the field of economy and business to all judges in the economic department at the basic court in Prishtina.
	17	See above (high inefficiency)	Judicial System	2.1. Democracy and the rule of law – Judicial System “Court administration as well as case allocation in prosecution offices and courts needs to be improved.”	Alternative Dispute Resolution methods should be utilized. Promoting the use of alternative dispute resolution mechanisms (from courts and all stakeholders that make up the judicial system in the country) is recommended
	18	Due to many stakeholders in the field, and considering the large amendments of laws and issuance of administrative instructions, confusions arise in many fields.	Parliament and Government	2.1. Democracy and the rule of law	Further consolidation of all legal acts, including on-going updating of all Administrative Instructions by initiating bodies as well as municipal regulations, in the official gazette is needed
ACCESS TO CREDIT	19	One of the reasons why banks state that the lending conditions are not very favorable is because of weak financial reporting.	Law on Financial Reporting Standards	3.1. The existence of a functioning market economy - Financial sector development	Businesses should improve their financial reporting statements and corporate governance
	20	More than 60 percent of businesses claim that lending conditions from commercial banks and other financial institutions are not favorable at all	Banks/ Government/ Assembly	3.1. The existence of a functioning market economy - Financial sector development	Ideas proposed by almost every political party about the creation of development funds should necessarily be discussed in a comprehensive manner with all the relevant stakeholders and experts

BUSINESS OPTIMISM & GOVERNANCE				
	21	<p>Business representatives as well as business associations and economy experts have constantly made their voice heard regarding the lack of a national economic development strategy for the country, that would in broad terms define the economic priorities for the future.</p>	<p>Government and Assembly</p>	<p>3. Economic Criteria</p> <p>The new government should necessarily adopt a comprehensive National Economic Development Strategy. The strategy should include issues such as improvement of access to finance, further improvement of fiscal environment and reduction of skills gaps, particularly for senior-level positions would enable an accelerated business growth and enable the businesses experience faster development trends, and ultimately lead to a higher economic growth of the country</p>

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Annex A - Interview Summaries

This section is a summary of the interviews conducted. Parts of these interviews have been incorporated in the previous sections of this study.

Agron Demi – Executive Director, GAP Institute for Advanced Studies

As a representative of the civil society, Agron Demi, Executive Director of one of the most reputable think tanks in Kosovo, Gap Institute for Advanced Studies, has also shared, for the purposes of this study, the work of his institution on the doing business environment, while advocating for improvements in the legislation in power, rule of law, and other key factors.

To begin with, Demi assessed that the doing business environment in the country is not very favorable, due to some key issues that the GAP institute has noted in Kosovo. First, Demi mentions the inability and difficulty of small and medium sized enterprises to have access to finance, as a result of unfavorable financing conditions and extensive documentation requirements.

Secondly, according to him, regardless of the reforms and great amount of work that has been put into law enforcement, the country still suffers from a relatively weak rule of law, which causes for Kosovo's attractiveness in the eyes of potential investors to decrease. Moreover, Demi explicates that corruption remains as much a problem also a way out for businesses to escape and shorten bureaucratic procedures imposed by the government, and recommends for the policymakers' attention to continue to be turned towards the simplification and improvement of such processes.

"Another issue as regards the rule of law, is the legislation itself", Demi added, while asserting that Kosovo lacks a proper consolidation of the laws in power, especially those related to the fiscal environment and foreign investments. However, he explains that in the drafting period of legislation the Institute that he leads is usually invited to provide comments and partake in public hearings, and considers this part to be one of the pillars of improving the legislation and ensuring its application by the citizens.

Finally, Kosovo's labor force that is not as cheap as that in the regional countries and lacks the qualifications required by the market, presents a separate challenge to both the private and public sectors in the country. In this context, Demi shared GAP's analysis of the Employment Strategy – a document of the Government of Kosovo that aims at decreasing unemployment rates in the country, while pointing out that the document as a whole does not contain a very thorough analysis of labor market and lacks specific targets and recommendations. As such, Demi suggested that the Government should become more focused on proper planning and target-setting when drafting policies.

Behxhet Haliti – Director of Tax Administration of Kosovo

As the Director of Tax Administration of Kosovo, Behxhet Haliti provided his insights on the overall fiscal environment in the country, and how reforms related to it have led to a better and more favorable doing business environment, from the moment a business entity is registered at the, now, joint KBRA-TAK electronic system, until the point that entity pays its fiscal obligation to the Administration. According to Haliti, the appropriate and easy to understand tax legislation; TAK's service-oriented culture; and the increased communication with relevant parties, such as business associations, are some of the key factors that have caused for Kosovo's performance in regards to the fiscal environment to improve.

Furthermore, Haliti shared that in the recent years, TAK has undertaken several reforms, which have also been reflected in IMF's last report and World Bank's Doing Business Report, where in the aspect of 'Easiness of Paying Taxes' Kosovo's rank has improved from 47th to 43rd. According to Haliti, throughout this period, TAK has also managed to increase the voluntary tax compliance from 78% in previous years to 87% in 2013, with one of the main reasons being the adoption of a new, electronic based system, which is user-friendly and decreases costs.

In regards to the tax rates for Small and Medium Sized Enterprises in Kosovo, Haliti considers them to be quite favorable and similar to those in the region. In this aspect, the main problems and complains from the taxpayers of the private sector do not seem to lie in the tax rates itself, but the overall level of compliance and the (un)equal treatment of all taxpayers.

Moreover, Haliti admitted that the institution he leads and other relevant actors in this field have not managed to diminish the informal economy, even though, according to him great effort is being put into a new approach with focuses on problem identification and sector segmentation. Further, Haliti explained that while previously TAK used to treat informality on an ad-hoc, case-to-case basis, in the last three years it has created a systematic approach, based on the OECD model, which is mainly directed towards understanding the behavior of the taxpayers.

Finally, attention was also given to the Consultative Council, established in 2013 by the Ministry of Finance, in cooperation with TAK, Kosovo Customs, and the main business associations in the country. The Council was mentioned by Haliti as a body that allows for these institutions to have access to issues of the private sector on a consolidated manner and to address those issues with a holistic approach of all key stakeholders.

Terence Slywka – Partnership for Development

Terence Slywka, Chief of Party of the USAID Partnerships for Development Program shared, throughout the interview, his work on summarizing Kosovo's reforms that are in one way or another related to the doing business environment, while offering recommendations on some key points where the government needs to focus on improving. To begin with, Slywka, assessed the business registration procedures have been significantly streamlined, with reduced costs, eliminated requirements and implementation of unified registration sites by KBRA and TAK, and noted that the increased number of registered L.L.Cs is a clear indicator of the positive effects that the reforms in this regard have had.

Moreover, given that World Bank's Doing Business Report includes only 10 indicators, Slywka has mentioned other significant reforms that have actually improved governance and the economic environment in Kosovo, including, but not limited to, the adoption of the electronic Asycuda system by Kosovo Customs, decentralization of customs services from a single Prishtina office to regional branches for improved access by citizens, the government's investments on infrastructure projects, the increased access to information, introduction of private bailiffs, establishment of one stop shops, consolidation of TAK and KBRA, Credit Registry Update, elimination of location permit, and further operational improvements to increase efficiency in registrations and reduce

registration times for property, and so forth.

As regards construction permits and the Law on Construction, Slywka asserts that a proactive approach from Kosovo Government has led to numerous reforms, including decrease of the permit fee (putting on a cost-recovery basis), the ongoing work towards consolidation of plans and zoning maps and so on.

Slywka also highlighted that government agencies (including administrative revenue bodies and inspectorates) plan and set revenue targets (even though they lack discretion in implementation and should be collecting all that is due, no less, no more), pointing out that strategic planning issues, such as revenue target setting, can lead to undesirable side effects, including changing the dynamic between agencies and citizens from one that is customer-service focused and compliance seeking, to one of conflict where non-compliance is necessary, and incentivized, in fulfilling those targets. Instead, Mr. Slywka suggested that administrative bodies should focus on customer / citizen service to encourage public knowledge of requirements and support compliance. Administrative body operational metrics should be developed and implemented that are (1) with the control of the agency (2) have a customer service / operational efficiency focus and (3) are variables completely within the capacity of the body to control. Such measures would could strengthen internal management and result in an improved relationship between the state and the people.

In terms of addressing informality, Slywka suggested that the government should focus government actions or policy decisions that create disincentives for people to engage in the formal economy and needs to have a holistic approach to solve that issue, with all government officials working towards a joint set of reforms and goals. Market mechanisms provide their own incentives including: property protection, ability to grow, developing a credit history, access to loans/financing, ability to enforce contracts, trade, and other protections under the law. To address informality, the discussion should be why good and inherently honest people are giving up the benefits of the market to assume the risks and limitations of informality. While enforcement plays a role at the margins, to significantly address informality, all administrative actions should be considered as they contribute to the collective burden that is outweighing market benefits.

The Government has undertaken a number of positive steps such as streamlining registration, reforming construction and spatial planning, increasing accessibility of contracts, etc. An initial step towards this, according to him, would be the continued consolidation of all legal acts, including on-going updating of all AIs by initiating bodies as well as municipal regulations, in the official gazette (<http://gzk.rks-gov.net>) that is now functional with USAID's help. Slywka also adds that a better communication should be established within all key stakeholders (from public institutions and private sector) when a law or AI is being either drafted or amended. Again, the Government has made initial steps, with a good example of how MESP has engaged the public in areas such as construction reform AIs and implementation as well as the Law on Spatial Planning.

Finally, Slywka concluded the interview by emphasizing that in order to be successful in improving the doing business environment, first for Kosovo citizens, second for the Diaspora, and third for foreign investors, it should firmly abide by Article 120 of the Constitution, i.e. it "shall be based on the principles of accountability, effectiveness, efficiency and transparency". As Slywka pointed out, economic activity (sometimes referred to as the business environment) is an indivisible part of the society and something in which everyone operates every day whether they are directly engaged in a commercial transaction or experiencing the results of policy, government and commerce, thus to achieve significant improvement and realize the growth potential inherent in Kosovo's citizens, we must focus on establishing the Constitution's stated approach to governing and governance, building on the Kosovo examples where this has already started occurring, but going much farther and broader.



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Publication authors: Arian Zeka, Visar Hapçiu, Nida Krasniqi
Surveys collected by: DC Consulting L.L.C.

For more information:
www.amchamksv.org
www.kfos.org