BUSINESS REGULATIONS: CONSTRAIN OR SAFEGUARD BUSINESS ACTIVITY? (THE IMPORTANCE OF REGULATORY IMPACT ASSESSMENT)

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Abstract

Poor quality of laws and regulations can seriously hamper economic growth and sustainable development. Regulatory costs represent significant obstacles to private sector investment, whereas, an effective regulatory environment improves trade performance. Rules and regulations are under the direct control of policy-makers and policy makers intending to change the experience and behavior of businesses will often start by changing rules and regulations that affect them. Good business regulations enable the private sector to prosper and help businesses to expand their transaction network.

In this context, the regulations seem to safeguard economic activity and facilitate business operations. By other side, if regulations are poorly designed, they can become obstacles to doing business. Business regulations are part of institutional constraints.

The main purpose of this paper is, to offer a comparative analysis of reforms undertaken by different European countries (especially Balkan countries), through an interpreter and descriptive analysis using the data set provided by Doing Business Report (2013) in order to evaluate the position of Albania towards its neighbors. The comparison will cover two sides: what has been done (reforms making it easier to do business) and what must be done in the future. Subsequently, the importance of regulatory reforms describing the main benefits of a reform impact assessment (RIA) process will be in focus of the paper. It is important for governments not only to implement a policy but also to understand and evaluate how well this policy will work.

Keywords: Business Regulations, Regulations, Impact, Assessment

Introduction

The private sector provides an estimated 90% of jobs in developing economies[25]. There will be greater opportunities for all people in those countries where government policies support a dynamic business environment, that enables firms to make an investment, create jobs and increase productivity. A growing body of literature evidence suggests that policy makers that seek to strengthen the private sector need to pay attention not only to macroeconomic factors but also to the quality of lows, regulations and institutional arrangements that frame daily economic life.

Business regulations are part of institutional constraints. The regulations impose necessary costs on firms such as the need to adapt the business to meet regulatory requirements or to pay licensing fees, but often these costs are unnecessarily high because of inefficient administration or poor institutional fit[26] that reduce the business entry and firm growth. Worldwide, 108 economies implemented 201 regulatory reforms in 2011/2012 making it easier to do business as measured by *Doing Business.*

A short literature review on this issue will be provided to show the relevance and national level impact of business regulations and other institutional constraints, followed by the main policies to address these constraints.

1.Literature review: Business regulation as part of Institutional Constraints

Whereas firms need to be regulated and licensed, if the costs they incur in complying with regulation are unnecessarily high, business entry and firm growth will be lower. The literature points to faster growth when countries improve their rank in the World Bank's Doing Business Index, especially if they move from being one of the worst performers to being amongst the best. There is some evidence also of poor licensing and regulation leading to low entry rates of new firms and lower productivity and growth of established firms. However, by itself, the better business regulation may not result in faster economic growth.

1.1 Business regulation and licensing. Why is it relevant?

The regulations impose necessary costs on firms such as the need to adapt the business to meet regulatory requirements or to pay licensing fees, but too often these costs are unnecessarily high because of rent-seeking behavior, inefficient administration, or poor institutional fit (World Bank (2005a)), thereby reducing business entry and firm growth.

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[25] Doing Business 2013

[26] WORLD BANK 2005a. A Better Investment Climate For Everyone. *World Development Report.* Washington DC: The World Bank

National level impact: A large academic literature has followed since Djankov et al. (2002) recorded the number of procedures, time, and cost needed to start a business in 85 countries. This literature uses not only the World Bank's Doing Business Indicators but also other available databases2 to examine the effects of regulatory barriers and business licensing on firms' dynamics. A recent review by Djankov (2009) surveys the literature that links entry regulation on the one hand, and entrepreneurship and productivity, on the other. He concludes that the evidence points to economically large and statistically significant effects between entry rates and productivity growth. Using a large sample of industrial and developing countries, Loayza et al. (2005) examine empirically the overall effect of business regulation on economic growth. They suggest that high levels of regulation are associated with lower growth (which is the case for product and labor market regulation), but that the quality of regulation (i.e. Better institutions) help mitigate, and even eliminate, the adverse impact of regulation on economic growth.

Firm level impact: Klapper et al. (2004) use firm level data from Western and Eastern Europe to show that anti-competitive regulations such as entry barriers lead to slower growth in established firms. More specifically, Besley and Burgess (2004) find that pro-worker regulations across India states are associated with lower output, employment, investment and productivity in manufacturing firms. Using a database of manufacturing firms, Klapper et al. (2006) conclude that regulatory barriers hamper the creation of new firms, discourage the entry of small firms, and affect even older firms, which grow more slowly and to a smaller size.

2. What are SMART business regulations?

As defined by *Doing Business* SMART business regulations, doesn't mean necessarily fewer regulations but regulations that have the following characteristics:

- ✓ STREAMLINED – regulations that accomplish the desired outcome in the most efficient way,
- ✓ MEANINFUL – regulations that have a measurable positive impact in facilitating interactions in the marketplace,
- ✓ ADAPTABLE – regulations that adapt to changes in the environment,
- ✓ RELEVANT – regulations that are proportionate to the problem they are designed to solve,
- ✓ TRANSPARENT – regulations that are clear and accessible to anyone who needs to use them.

3. Comparative analysis on business regulatory reforms during 2011/12

Entrepreneurs around the world face a range of challenges. One of them is inefficient regulation. Furthermore inefficient regulation becomes a challenge for governments as part of policy-makers. This section will offer an overview of business regulation reforms undertaken by Albania and its Balkan neighbors during 2011/12 using the dataset of *Doing Business* report.

Albania made starting a business easier by making the notarization of incorporation documents optional, cutting procedures by 1, time by 1 day and cost by 7% of income per capita. Albania made paying taxes easier for companies by abolishing the vehicle tax and encouraging electronic filing for taxes. By other side regarding the dealing with construction permits, Albania is a "non practice" economy with barriers preventing private builders from legally obtaining a building permit. In this case it is a tide in the ranking.

Bosnia and Herzegovina made it easier to transfer property between companies by computerizing the commercial registry, cutting registration time by 8 days. Bosnia and Herzegovina eased the administrative burden of filing and paying social security contributions by implementing electronic filing and payment systems. Bosnia and Herzegovina made access to credit information more difficult by stopping the private credit bureau's collection of credit information on individuals.

Croatia made paying taxes less costly for companies by reducing the health insurance contribution rate.

Greece reduced the time required to obtain a construction permit by introducing strict time limits for processing permit applications at the municipality. Greece strengthened investor protection by requiring greater immediate and annual disclosure of material related-party transactions. Greece enhanced its insolvency process by abolishing the conciliation procedure and introducing a new rehabilitation proceeding.

Kosovo made starting the business easier by eliminating the minimum capital requirement and business registration fee and streamlining the business registration process. Kosovo strengthened the investor protection by introducing a requirement for shareholder approval of related-party transactions, requiring greater disclosure of such transactions in the annual report and making it easier to sue directors when such transactions are prejudicial. Kosovo made the biggest improvement in the strength of investor protection in the past year.

FYR Macedonia made starting a business easier by simplifying the process of obtaining a company seal. This country has advanced the furthest toward the frontier in regulatory practice in construction permitting since 2005

Montenegro supports the business through reforms in dealing with construction permits and access to credit. Construction permits became less expensive during 2011-2012 by reducing the cost of pre- and post construction procedures. Improvements were made in access to credit information by guaranteeing borrowers' right to inspect their personal data.

Serbia resolved the insolvency process by introducing private bailiffs, reducing the starting prices for the sale of assets, prohibiting appeals, expediting service of process and adopting an electronic registry for injunctions to make public all prohibitions on the disposal of the pledge of movable or immovable property. Serbia also introduced a private bailiff system that made enforcing contracts easier and from the other part made starting a business easier by eliminating the paid-in minimum capital requirement.

Slovenia reforms in business during the years 2011-2012 consist on the areas of protecting investors, paying taxes and resolving insolvency. Regarding these reforms, Slovenia strengthened investor protection through a new law regulating the approval of related-party transactions. The payment of taxes became easier and less costly for companies by implementation of electronic filing and payment of social security contributions. A reduction in the corporate income tax rate has also been noticed. Efforts on resolving the insolvency process have been made by requiring that the debtor offers creditors payment of at least 50% of the claims within 4 years, giving greater power to the creditors' committee in a bankruptcy proceeding. Prohibition of insolvency administrators from allowing relatives to render services associated with the bankruptcy proceeding seems also a contribution in this case. Last, establishing fines for members of management that violate certain obligations or prohibitions supports the strengthening of the insolvency process.

Reform efforts in Southeast Balkan have focused on making it easier to start a new business, protecting investors, paying taxes and resolving insolvency. The table below gives a summary of data regarding the ranking of all the countries mentioned above based on Doing Business 2013 report. There are used different criteria to rank the countries according if there has been a positive, negative or no change in reforms regarding these criteria. The data that has (+) sign beside the number means that, there has been a positive change regarding the regulation reform. The data that have the (-) sign beside the number means that there has been a negative change regarding the regulation reform. The data that have no sign beside the numbers means that there have been no changes in these criteria. As we see from the table Greece, Serbia and Slovenia have undertaken more than 2 positive reforms in business regulations. Albania has made progress in starting a business and paying taxes. A progress has been made but much more remains to be done regarding the improvements in other criteria.

Table 1 Countries Data[27]

Country	Albania	Bosnia & Herzegovina	Croatia	FYR Macedonia	Greece	Kosovo	Montenegro	Serbia	Slovenia
Country Income classification	Lower middle income	Upper middle income	High income	Upper middle income	High income	Lower middle income	Upper middle income	Upper middle income	High income
Ease of doing business (rank)	85	126	84	23	78	98	51	86	35
Starting a business (rank)	62 (+)	162	80	5 (+)	146	126 (+)	58	42 (+)	30
Dealing with construction permits (rank)	185	163	143	65	31 (+)	144	176 (+)	179	61
Getting electricity (rank)	154	158	56	101	59	116	69	76	31
Registering property (rank)	121	93 (+)	104	50	150	76	117	41	83
Getting credit (rank)	23	70 (-)	40	23	83	23	4 (+)	40	104
Protecting investors (rank)	17	100	139	19	117 (+)	100 (+)	32	82	17 (+)
Paying taxes (rank)	160 (+)	128 (+)	42 (+)	24	56	44	81	149	63 (+)
Trading across borders (rank)	79	103	105	76	62	124	42	94	57
Enforcing contracts (rank)	85	120	52	59	87	138	135	103 (+)	56
Resolving insolvency (rank)	66	83	97	60	50 (+)	87	44	103 (+)	42 (+)

4. What must be done? Efforts to implement a RIA system in Albania

The policy-making process in Albania has shown a lot of gaps and policy makers are now committed to strengthening the process of better regulations. Establishment of a Regulatory Impact Assessment (RIA) is a key element in the process of improving capacities to produce qualitative and conductive regulations to businesses. RIA is also a key tool for improving the efficiency and effectiveness of regulatory decision-making. Assessing the potential effects of a new regulatory proposal, RIA gives the evidence to decision makers in terms of the positive and negative impact of the new regulation. This allows the adoption of more efficient regulations and improves the quality of the regulatory environment. RIA also improves the transparency of a regulation.

[27] The table is prepared by author by gathering the data from Doing Business 2013 report.

In the particular case of development policies for Small & Medium Enterprises (SMEs) the impact assessment refers to impact of regulations, programs and projects, especially efforts including loans and guarantees, equity financing, development of an enterprise culture, offering advice, assistance and training for SMEs in the fields of technology and management.

4.1 Short- Term benefits of RIA

- ✓ Improved information about changes in regulations that will be available for the business community and civil society,
- ✓ Reductions in the cost of doing business,
- ✓ Improving the dialogue with the business community and other interested parties,
- ✓ Improving government capacity during the drafting of new legislation.

4.2 Long-Term benefits of RIA

- ✓ Economic growth and more investments in business sector,
- ✓ Consumer welfare, public safety, health and environment protection,
- ✓ Benefits in public sector efficiency, particularly in planning and drafting process,
- ✓ Complying with European law and regulations that will accelerate the process of EU accession.

5. Conclusion

The economies that rank highest on the ease of doing business are not those where there is no regulation, but those where governments have managed to create rules that facilitate interactions in the marketplace without needlessly hindering the development of the private sector.

Economies that rank high on the ease of doing business tend to combine efficient regulatory processes with strong legal institutions that protect property and investors' rights.

Finding the right balance in business regulation can be a challenge. It becomes an even greater challenge in a changing world, where regulations must continually adapt to new realities. Regulations need to adapt to new demands from the market and to changes in technology also.

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