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REGULATORY REFORM IN FIVE WESTERN BALKAN COUNTRIES: EVIDENCE AND PERSPECTIVES

ABSTRACT: *This Paper analyses the importance of regulatory reform for the creation of an effective legal and regulatory system in Western Balkan countries. The authors explore the progress achieved in this reform area, arguing that regulatory reform was mostly partial, focused on specific sectors and areas, and lacked a strategic approach. It was focused on the simplification of existing regulation and the implementation of Regulatory Impact Analysis (RIA).*

The paper concludes that in order to secure the sustainability of the regulatory reform progress, especially in the period of economic crisis, the countries in the

region should apply a strategic approach in this area, focusing on the improvement of the quality of regulations and the reduction of unnecessary administrative burdens that affect business activities and investments. The process of the establishment of a competitive legal and regulatory environment should be strongly correlated with the continuation of the EU harmonization process and with the regional cooperation among the countries in the region.

KEY WORDS: *Regulatory reform, Regulatory impact analysis (RIA), legal and regulatory system, EU integration process, economic crisis*

JEL CLASSIFICATION: K40, L51, P27, P37

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1. ROLE OF REGULATORY REFORM IN THE TRANSITION PROCESS IN SELECTED WESTERN BALKAN COUNTRIES¹

Regulatory reform is a process in which the focus is placed on improving regulatory quality by enhancing the performance, cost-effectiveness, quality and implementation of regulations (OECD, 1997: 6). The principal role of regulations should be to address market failures, which inhibit productive investments and growth (World Bank, 2005: 10).

The role of an effective regulatory regime in promoting economic growth and sustainable development has always been a major concern of researchers and policymakers. There is a number of studies that support the view that efficiency and quality of regulation affect private investment and the economic performance of an economy. Jalilian, Kirkpatrick and Parker (2007) have shown that there is a strong causal link between regulatory quality and economic growth and confirm that the standard of regulation matters for economic performance. Djankov et al. (2002) argue that the quality of institutions and excessive regulation can have a significant negative impact on investment (see also: Kauffman and Kraay, 2002, Olson, Sarna and Swamy, 1998, Busse and Groizard, 2006).

The challenge for governments, however, is not to overreach in correcting these failures. While under-regulation may fail to address social interests or externalities, overregulation can stifle the ability to pursue opportunities, thus curtailing growth (World Bank, 2009a: 71).

Simplification and deregulation has for a long time been the focus of activities in the area of regulatory reform. During the last several decades, regulatory reform has gained in significance and is an important part of the agenda not only of developed countries, but also of developing and transition countries. In developed countries, the regulatory reform process was driven by the need to further promote competitiveness, while in transition countries it was also driven by the need for a substantial change of their legal systems from a socialist legal system to a market economy one.

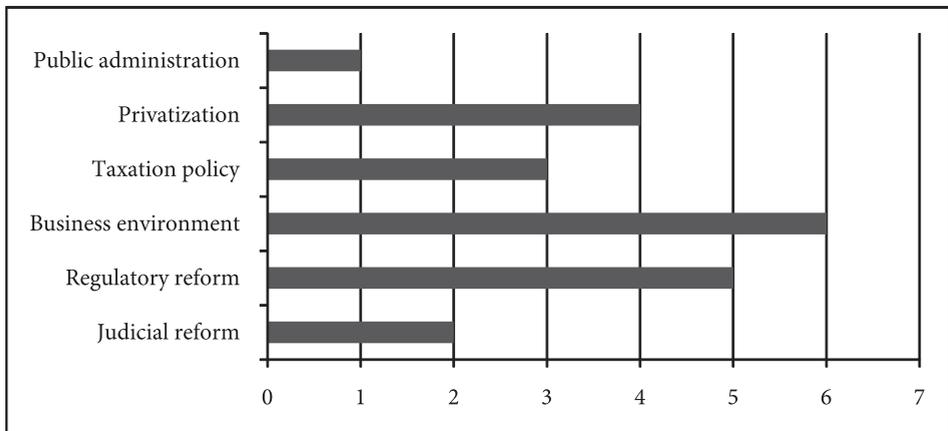
The Western Balkan region has started the transition process to a free market economy with some delays in comparison to the new EU member states, mostly due to political instabilities in the region. However, the reform process has been

¹ This paper covers Albania, Bosnia and Herzegovina, Macedonia, Montenegro and Serbia (hereinafter: Western Balkan countries or Western Balkan Region)

intensified in this decade, with the aim of completing the transition process. Within it, intensive regulatory reforms have been among the key reforms in the countries in the region, due to their importance for the economic performance of their economies.

According to the IFC Survey with high level policy creators and legislators from five Western Balkan countries² (IFC, 2009), regulatory reform has been recognized as one of the major policies on the reform agenda in the previous decade (Figure 1). The survey also shows that this reform has been recognized as one of the three most successful ones (Figure 2).

Figure 1. Mayor policy issues in the last 5-10 years in Western Balkan region

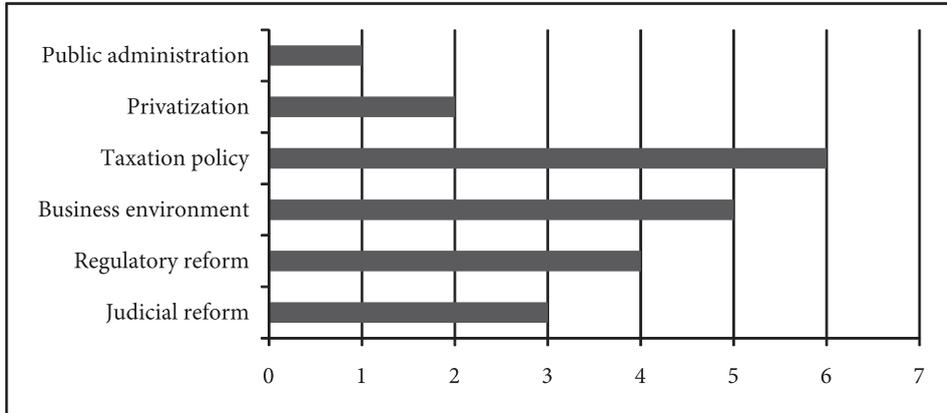


Source: Preliminary results of IFC Survey on Business Enabling Environment policy issues and procedures in Western Balkan Countries (2008)

Note: Values range from 6 as the highest ranked policy to 1 as the lowest ranked policy

² Preliminary results of the IFC Survey on Business Enabling Environment policy issues and procedures in Western Balkan Countries, conducted in 2008 with high level policy creators and legislators from five Western Balkan countries, presented at the 2nd Meeting of the Steering Committee of Regional Network of Policy Makers in South East Europe in Tirana, Albania, December 9–10, 2008

Figure 2. Most successful policy issues in the last 5-10 years in the Western Balkan region



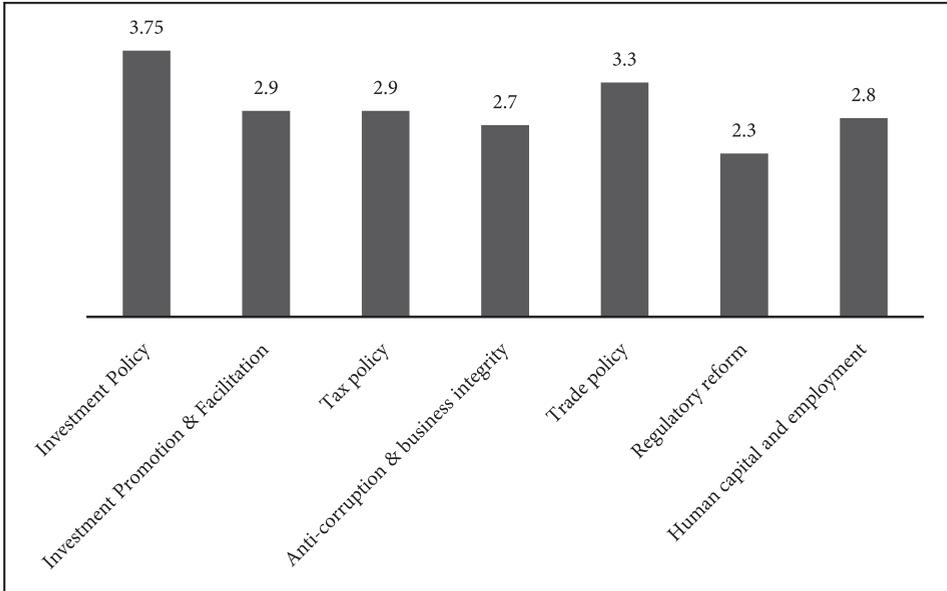
Source: IFC Survey on Business Enabling Environment policy issues and procedures in Western Balkan Countries (2008)

Note: Values range from 6 as the highest ranked policy to 1 as the lowest ranked policy

The OECD Investment Reform Index (IRI) also gives an insight into the progress in several key areas of policy reform, including regulatory reform (OECD, 2007). The IRI 2006 indicated that regulatory reform was the lowest ranked category of reform progress among seven reform areas (Figure 3). The preliminary results of the IRI 2009, which examined certain aspects of regulatory reform, indicate considerable progress over the last three years.

In spite of the achieved progress in this reform area, there is substantial work to be done in the coming years, due to the large scope of this reform and its relation to the EU accession process. According to the IFC Survey (IFC, 2008), regulatory reform is expected to be the most important reform on the reform agenda of the countries in the region in the forthcoming period (Figure 4).

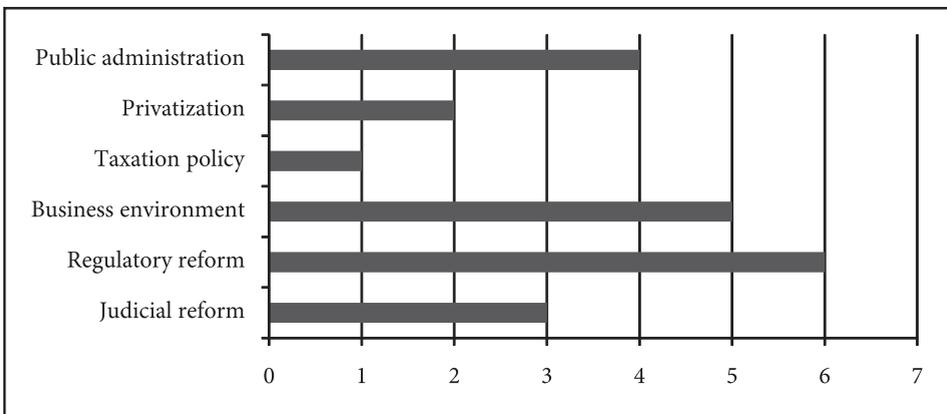
Figure 3: OECD Investment Reform Index 2006 in Western Balkan region



Source: OECD Investment Reform Index 2006.

Note: Each policy dimension is rated on a scale of 1 to 5 (weaker to stronger).

Figure 4: Major policy issues in the coming years in Western Balkan region



Source: IFC Survey on Business Enabling Environment policy issues and procedures in Western Balkan Countries (2008)

Note: Values range from 6 as the highest ranked policy to 1 as the lowest ranked policy

The intensive legislative reform agenda in the Western Balkan countries resulted in the drafting of a significant number of regulations that fulfill market standards. This process has been significantly influenced by: (i) arrangements concluded with the International Monetary Fund and the World Bank; (ii) activities of other international and bilateral organizations and the donor community related to the regulatory reform implementation and (iii) the EU integration process.

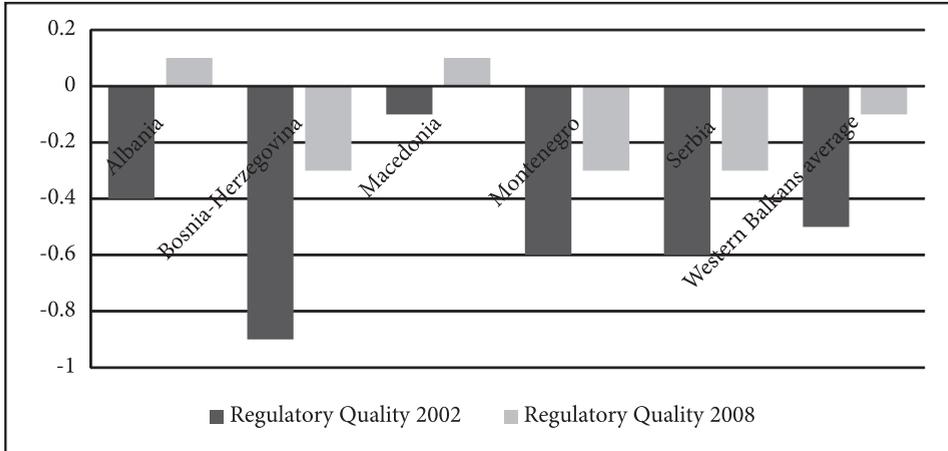
The international community, the World Bank and the IMF in particular, have played an important role in the post-conflict period in the Western Balkan region, with the aim of accelerating the reform process, which would result in the transition of these countries to market economies with better economic growth prospects. In the early period of transition, characterized by an inherited legal system from the period of socialism not in line with market economy standards, these two international financial organizations have initiated the creation of a basic legal foundation for sound economic development. A number of other international and bilateral organizations and donors strongly supported this process, through financial aid and technical assistance.

The EU integration process was the next important step in legislative reform process, which not only significantly accelerated activities in the area of regulatory reform, but also contributed to a more systemic and comprehensive approach in the creation of a new legal system. The national plans for harmonization with the EU Acquis Communautaire represent the basic platform for the implementation of the harmonization process in each country in the region.

As a result of the above mentioned processes, notable improvement in the quality of a number of laws has been achieved (Figure 5), but serious deficiencies remain, including excessive regulation in certain areas, lack of necessary regulation in other areas, lack of capacity for drafting complex legislation within the ministries and other administrative bodies, as well as the low quality of some new laws due to fast drafting and enactment of laws without adequate impact assessment (Penev et al., 2009).

However, a favorable legal and regulatory environment as one of the key segments of an investment climate that is conducive to investment implies the existence not only of high-quality, modern, market oriented laws, but also of an adequate institutional infrastructure, necessary for implementation of laws. Legal implementation itself is a much more serious problem, due to the lack or poor functioning of the institutions necessary for the implementation of laws.

Figure 5: World Bank Governance Indicators



Source: World Bank Governance Indicators Database

Note: The values of indicators range from -2.5 to 2.5, with higher scores corresponding to better outcomes

The improvement of the quality of the regulations has also had an impact on the ease of doing business, through the improvement of the ranking of the Western Balkan countries in the World Bank “Doing Business” project, which measures business regulations and their enforcement in 181 countries, covering ten regulatory areas. The ranking of these countries, however, is still relatively unfavorable, which can be seen through comparison with the ten new EU Member States. Nevertheless, due to the simplification and reduction of administrative burdens and activities undertaken in the previous few years, a progress in their ranking in the Doing Business Report is clearly visible (Table 1).

Table 1. World Bank Doing Business Rankings

Regional average	Ease of Doing Business Rank in 2008 (among 181 countries)	Ease of Doing Business Rank in 2009 (among 181 countries)
Western Balkan countries	101	92
New EU member countries	47	45

Source: World Bank Doing Business database

2. STRATEGIC APPROACH TO REGULATORY REFORM

The regulatory reform agenda is very broad and complex and therefore it is important to have a strategic approach to the synchronization of activities related to simplification, administrative burden reduction and quality control of new legislation. Also, sufficient political support is required to accelerate the realization of such agenda.

The OECD recommendation is that each country should adopt, at the political level, broad programs of regulatory reform that establish clear objectives and frameworks for implementation. (OECD, 1997) The OECD is of the opinion that the adoption of a clear strategy is of such great significance because the states with explicit regulatory strategies achieve faster sustainable development than the countries with no such strategy. The more complete and concrete the principles and the action plan, the more complete and efficient the reforms (OECD, 2002).

The “better regulation” agenda in the EU has gained momentum and high level political support after the adoption of the Lisbon Strategy (European Commission, 2000) and the Mandelkern Group on Better Regulation Final Report of 2001 (European Commission, 2001). The Mandelkern Group Report represents a strategic document, which sets the principal elements of the regulatory reform agenda on the EU as well as member states level. The Mandelkern Report clearly stated the importance of regulation in achieving the aims of public policy, as well as the need to have high-level and cross-governmental political support and appropriate resources, in order to succeed in the implementation of regulatory reform. Since the adoption of the Mandelkern Group Report, significant progress has been achieved in the implementation of regulatory reform. A program of simplification of the existing EU legislation, aimed at reducing administrative burdens, as well as an impact assessment system, have been put in place at the EU level. In order to monitor the results, the European Commission published three annual strategic reviews of better regulation in the European Union, which give an overview of the realization of the agenda in this field.

Although the Mandelkern Report was strictly related to the EU institutions and EU Member States, it has had an impact on the Western Balkan region as well, through the implementation of some segments that are contained in the abovementioned report, such as the simplification of the existing legislation and administrative burden reduction and obligation to perform RIA.

The developing awareness of the importance of a strategic approach to regulatory reform at the EU level, as well as on the level of Member States, which started at the time of issuance of the Mandelkern Report, has affected the practice in the Western Balkan countries, which are all in the process of accession to the EU. However, a strategic approach to regulatory reform is still in its early phase at the level of the governments of the Western Balkan Countries. Most of these countries still do not have a comprehensive government level regulatory reform strategy document which would set the objectives, determine the tools which will be used to achieve such objectives and determine the timeline for the implementation of such tools (Table 2).

Serbia has been implementing segments of regulatory reform since 2002, and these activities led to the adoption of an overall strategic document in 2008. The Regulatory Reform Strategy for the period 2008-2011 sets the objectives to establish a regulatory system which: (i) promotes economic development and social prosperity; (ii) supports national competitiveness, protecting public interest at the same time; (iii) reduces administrative business costs; (iv) accelerates and reduces administrative procedures, and (v) improves the international rating of the Republic of Serbia in terms of business and investment environment quality. This two-pronged Strategy establishes the principles of good regulatory practice and provides for the implementation of a systemic regulatory review of the existing regulations as well as the improvement of the existing RIA system which was formally introduced in Serbia in 2004.

Table 2: Strategic Approach to Better Regulation Agenda in Western Balkan countries

Country	Regulatory reform strategy document	Segments of regulatory reform strategy in other country strategic documents
Albania		x
Bosnia and Herzegovina		x
Macedonia		x
Montenegro		x
Serbia	x	

Even though the other countries in the region have not yet adopted regulatory reform strategy documents, some segments of regulatory reform strategy are covered in their strategic documents and National plans for adopting the Acquis.

In some of these countries, the main focus has been on the regulatory instruments which improve the quality of new regulations, while some of them are more focused on the simplification of the existing legislation or on the decrease of administrative burdens.

Macedonia has elements of the regulatory reform strategy contained in several overall strategy documents, including The Program of the Government 2006–2010, Annual programs of the Government and The National Program for Adoption of the Acquis Communautaire. In the Program of the Government 2006-2010 (GoMk, 2006), the regulation level of the Macedonian economy has been recognized as too broad and unsuitable for a modern and dynamic economy. Therefore, the Government made a decision to implement a two-pronged strategy using tools such as (i) the regulations guillotine, to review the stock of regulations and (ii) the regulatory impact assessment (RIA), to review the flow of regulations.

In Albania, a more strategic approach to regulatory reform started with the adoption of the Government Program for the period 2005-2009 (GoA, 2005) in which special importance was given to: (i) the reduction of administrative barriers and (ii) the improvement of the implementation of laws. The Government has recognized the need to remove administrative barriers and improve the quality of regulations affecting businesses, with the aim of attracting more private investments.

The regulatory activities in Bosnia and Herzegovina have been strongly affected by the international community through the Peace Implementation Council, Office of the High Representative, the European Commission, and resident missions of the World Bank and IMF, in a more or less successful cooperation with the Council of Ministers of Bosnia and Herzegovina, entity governments and Brčko District. Even though Bosnia and Herzegovina has some segments of regulatory strategy at the entity level, the country is still far from the creation of an overall regulatory reform strategy.

In Montenegro, some of the segments of a regulatory reform strategy were contained in the Government's Administration Reform Strategy 2002-2009 (GoM, 2002). One of the key goals of the Administration Reform Strategy was the improvement of the quality of legislation and deregulation of over-regulated areas. This strategy also classified the development of economic regulation as a reform priority, through improving efficiency and independence of the regulatory

bodies' activities and constituting mechanisms for surveying the achieved results within the area of the regulatory bodies' competences.

In view of the developments at the level of the EU as well as of its member states, in particular some of the new EU member states, which have adopted strategic regulatory reform documents, the Western Balkan countries should also move towards a systemic and strategic approach to regulatory reform.

3. SIMPLIFICATION OF THE EXISTING LEGISLATION AND ADMINISTRATIVE BURDENS REDUCTION

Overregulation and unnecessary regulatory and administrative burdens discourage private investment and impair economic growth. To reduce such negative impacts, it is important to keep regulations simple, transparent and enforceable.

The need to simplify existing regulations and eliminate administrative burdens is present in all legal systems, but it is of particular importance for transition countries, due to the intensive legislative activities and changes which are necessary for the creation of new, market oriented legal systems.

At the level of the European Union, simplification and administrative burdens reduction is an important part of the regulatory reform agenda. In 2006 the European Commission proposed to measure administrative costs arising from legislation in the EU and to reduce administrative burdens by 25 percent. This goal was set both for the EU as well as for the member states, and it is to be achieved by 2012 (European Commission, 2006). An Action Program for reducing administrative burdens in the European Union was launched by the Commission in order to achieve the above target. In the Action Plan it is stated that administrative costs are estimated to amount 3.5 percent of GDP in the EU and that achieving the 25 percent reduction target could lead to an increase in the level of the EU GDP of approximately 1.4 percent or 150 billion euro in the medium term (Gelauff and Lejour, 2005). It is also foreseen that the Commission has taken action which will reduce the Acquis by almost 10 percent.

In most Western Balkan countries, a need has been recognized for a comprehensive elimination or replacement of redundant and unnecessary regulation, as an important precondition for the creation of a new legal system in line with market

economy standards, which will influence the creation of an investment friendly environment.

Table 3: Simplification of existing regulations and reduction of administrative burdens in Western Balkan countries

Country		Implemented	In progress	Initiated	None
Albania			x		
Bosnia and Herzegovina	- State level				x
	- BH Federation			x	
	- Republika Srpska	x			
Macedonia		x			
Montenegro					x
Serbia			x		

Aiming to create a favorable legal and regulatory environment, The Program of the Government of Macedonia 2006–2010 has anticipated the implementation of a process of massive deregulation and reform of the regulatory institutions (GoMk, 2006). The reform was comprehensive and included all regulations relevant for the economy. The Government adopted the Decision for Introducing the Regulations guillotine in November 2006 (GoMk, 2006a). The Reform was focused on repealing certain bureaucratic procedures for reducing corruptive actions and enhancing the business climate, encompassing the following groups of regulations: (i) licenses and permits; (ii) administrative fees; (iii) administrative procedures; (iv) agriculture and agribusiness procedures, and (v) abolishing 363 regulations of the period when Macedonia was part of former Yugoslavia. In order to implement the Regulations guillotine program, the Government established an institutional structure comprised of a Coordinative Committee headed by the Deputy Prime Minister of the Government for economic affairs and Committee for Regulatory Reforms, providing political support to the project, and working groups of the ministries and state administrative bodies, which provide for the presence of the operative level of the administration.

The reform has been performed in three phases: (i) drafting a list of regulations and the assessment of the justification of each regulation; (ii) reassessment of the justification of regulations and creating an opinion on amending, annulment, or not amending the regulation, and (iii) introducing a unique electronic register of regulations published on the Government web-site. The first two phases have

been completed, while the establishment of the electronic register of regulations is in its final phase.

Unlike in Macedonia, where the approach was to implement an overall simplification, in Bosnia and Herzegovina the approach is sectoral, mainly focused on the reduction of administrative burdens in the area of licensing and inspections. The process of simplification of existing regulations was initiated in 2006, at the entity level, in Republika Srpska, through the so called “regulations guillotine”, which focused on the inspections system. The goal of the initiation of the guillotine was the removal of unnecessary and inefficient regulations and formalities that were unfavorable and burdened the costs of operation in the Republika Srpska. The Government established an Economic System Regulatory Reform Council, chaired by the Prime Minister in order to: (i) initiate and monitor the economic system reform, (ii) present initiatives and proposals for amendments to the existing laws and pass new laws, other regulations and by-laws, and (iii) give preliminary opinions on draft laws and other draft regulations, which are important for business environment improvement and successful operation and development of companies and entrepreneurship. A Registry of Procedures and Approvals and Inspection Procedures and Control Subjects was established and contains a database of all procedures and approvals, as well as inspection procedures and control subjects. This database was designed to contain all necessary information for individual procedures and approvals, as well as inspection procedures and control subjects.

After the finalization of the regulations guillotine in Republika Srpska, a similar project was envisioned in the Federation of Bosnia and Herzegovina, which will be mainly focused on the application of the guillotine approach to the area of inspections. Such reform has not yet been initiated at the State level in Bosnia and Herzegovina.

In Albania, some segments of this reform are under way and visible progress has already been achieved in the deregulation of the licensing system and business registration. A Regulatory Reform Action Plan endorsed by the Council of Ministers in March 2006, with the aim of guiding implementation of reform actions in the following three years, incorporated elements and segments of the deregulation/reregulation process, such as (i) the improvement of existing legal framework through the removal of administrative barriers to business and (ii) the overall simplification of the regulatory framework affecting business. As a result of the abovementioned activities, the business registration process was completely transformed from a multiple-step process requiring action by courts,

central tax administration, local tax administration and labor administration, to a simultaneous one-stop administrative process, and the reform in the licensing system transferred prior control to post control and introduced the principle of silence is consent, as well as the elimination of all excessive licensing requirements.

Implementation of the regulations guillotine in the period from February 2009 until December 2009 is one of the main components of the Regulatory Reform Strategy of the Republic of Serbia 2008-2011 (GoS, 2008). The main focus of this reform is to reduce administrative costs of operation for businesses by at least 25 percent by 2011. Serbian Government established a Regulatory Review Unit as an expert body which is implementing this reform. The inventory phase was completed and listed approximately 8800 regulations which are in force. In the analysis phase, approximately 2000 regulations that affect the business are being reviewed and analyzed. The business community has the opportunity to actively participate and propose which regulations create unnecessary administrative costs and which regulations should be abolished and amended. In the recommendations phase, the Regulatory Review Unit shall produce a specific set of recommendations containing a list of regulations that shall be abolished and a list of regulations that shall be amended with specific amendments that need to be implemented. It is intended that the recommendations are to be adopted by the Government by 15th December 2009. In the implementation phase, all outdated, unnecessary laws and regulations are to be abolished while all inefficient regulations that create unnecessary costs for businesses are to be amended by 30th June 2010.

Montenegro has not yet introduced a systemic review of the existing legislation. However, intensive activities in the harmonization of the domestic legal system with the *Acquis* have influenced not only the adoption of new legislation, but also changes to existing laws that were not in line with market legal system.

Simplification of the existing regulations, in particular using tools such as the regulations guillotine, is an attractive reform for the political structures which operate in an insufficiently stable political environment such as the Western Balkan region, because this reform can show concrete results in a short period of time. Therefore, in most of the countries in the region, political support was gained for the initiation of this reform. The quality of the implementation of this reform depends not only on the quality of participation of all the stakeholders, but also on continued political support throughout the process.

4. OBLIGATION TO PERFORM REGULATORY IMPACT ANALYSIS (RIA)

Regulatory Impact Analysis (RIA) is becoming widely used as a method of improving the quality of regulatory environment not only in OECD countries, but in a number of other countries as well. It is a tool through which the policy makers can assess in advance the impact of the proposed laws in terms of the potential costs, benefits and risks.

RIA helps to: (i) properly define the problems which would be overcome by adopting the regulation; (ii) perceive the effect of the proposed regulation; (iii) identify alternative options for achieving the desired aim; (iv) assess potential regulatory and deregulatory options; (v) improve transparency through consultation and a debate of all interested parties; (vi) determine whether the benefits justify the costs; (vii) determine whether particular sectors are disproportionately affected; and (viii) ensure that implementation issues are taken into consideration early in the process.

The OECD Reference Checklist for Regulatory Decision-Making contains the principles on regulatory decisions that can be applied at all levels of decision and policy-making in order to improve effectiveness and efficiency of government regulation. (OECD, 1995 and 2005). The Checklist, however, cannot stand alone, but must be applied within a broader regulatory system, including adequate analysis, consultation processes and systematic evaluation of existing regulations.

Activities related to improving the quality of new initiatives in the EU have been carried out since 2002. Since 2002, the Commission has completed over 400 impact assessments, of which 135 in 2008. An Impact Assessment Board, created in 2006, is independent of the policy making departments and represents a central quality control unit at the level of the Commission. In 2008, the IAB requested resubmissions of impact assessments in 32 percent of the cases (European Commission, 2009).

Most of the governments of Western Balkan countries have initiated the implementation of RIA in their legal systems. Serbia is the first country in the region that introduced mandatory RIA in 2004, while Macedonia has introduced the obligation to perform RIA in 2009.

Table 3: Obligation to perform Regulatory Impact Analysis (RIA)

Country		Formally introduced	In progress	None
Albania				x
Bosnia and Herzegovina	- State Level		x	
	- BH Federation			x
	- Republika Srpska		x	
Macedonia*		x		
Montenegro				x
Serbia		x		

* *Obligation to perform RIA in Macedonia is introduced for all laws, except those laws that are in an “urgent” adoption procedure.*

Mandatory RIA was introduced in the Serbian legislative process using as a model the OECD checklist (OECD, 1995). The obligation to perform RIA was introduced in the Serbian legislative system in October 2004, when the Government adopted amendments to the Rules of Operation of the Government. These amendments stated that for each new law, the responsible Ministry will prepare a justification statement containing the answers/analysis to a set of questions – the RIA checklist. The Government established the Council for Regulatory Reform in order to perform quality control of RIA’s prepared by the ministries. When submitted to the Government, the law must be accompanied by the opinion of the Council. If the opinion is negative, the law is referred back to the ministry for adjustments of the RIA.

The obligation to perform RIA was officially introduced into the legislative system of Macedonia in 2008 with amendments to the Rules of Operation of the Government and the implementation of this new mechanism became obligatory from 1st January 2009. RIA is obligatory for all draft laws, with the exception of the laws that are in an “urgent” adoption procedure. As of 1st January 2009, the Sector for Economic and Regulatory Reforms in the General Secretariat has the role to implement RIA at the center of the Government and to review proposed legislation. In each of the ministries, a network of legal and economic officials is in charge of preparing the RIAs. This network of officials became the group of key legal and economic experts assisting ministers and senior officials in preparing policies and regulations.

In Albania, RIA has not yet been officially introduced into the legislative system. However, some elements of RIA (fiscal impact assessment and assessment of

expected social and economic impacts) are carried out as an integral part of the explanatory statement accompanying the draft law. The first serious attempt to introduce RIA as an integral part of the Albanian regulatory reform framework was made in the Government Regulatory Reform Action Plan from March 2006. This document included the development of the Government's capacity to improve the quality of new regulations through Regulatory Impact Assessment. It was envisioned that the responsibility for the preparation of the RIA for new regulations and policies should lie with the relevant ministries and a network of legal and economic officials should be set up in selected line-ministries. The quality control, monitoring and evaluation of the pace and quality of regulatory reform, including the implementation of the RIA system, should be carried out by the Trade Policy Department within the Ministry of Economy. As of today, the action plan has still not been implemented.

The business community in Republika Srpska has recognized that the outcome of the guillotine could be undermined if an *ex ante* review mechanism is not implemented and is now advocating the introduction of RIA (Thomas, 2007) In Republika Srpska, a Regulatory Reform Council was established in order to coordinate and assist Ministries in the performance of RIA. The Council is supported by a small secretariat, established within the Ministry of Economic relations and coordination. The first pilot project of RIA of the Law on Spas was finalized in October 2007. The realization of two additional RIA pilot projects has been initiated and they are meant to be finalized by the end of 2009. In the case of Bosnia and Herzegovina, in 2008, the World Bank/FIAS signed a Memorandum of Understanding with the Ministry of Foreign Trade in order to implement the first RIA pilot project at the state level in Bosnia and Herzegovina. RIA has not yet been implemented in the legal system of the Federation of Bosnia and Herzegovina.

The Development Strategy of Montenegro 2003-2007 and the Administration Reform Strategy in Montenegro 2002-2009 indicated the necessity for proposed regulations to be proportionate, balanced and effective. These Strategies imply a comprehensive public consultation in which all subjects, affected by those regulations, shall participate. In order to achieve greater discipline and monitoring in the regulatory area, the Strategies introduce the following measures: (i) regulatory "check list", (ii) methodology of regulatory analysis, (iii) modeling explicit standards for legislation quality, including initiation of alternative approaches to regulating social relations (economic stimulation, contractual mechanisms, and auto-regulation). The Administration Reform

Strategy provides for introducing the RIA system into the legislative system, by 31st December 2009.

RIA implementation lags behind in the countries in the region with respect to the activities related to the simplification of existing legislation, as RIA implementation not only requires political support, but also resources for training, performing adequate RIAs and the establishment of adequate institutional infrastructure. Investing into a good RIA system does not produce immediate results and is therefore less attractive to the political structures. RIA implementation is in an early phase of implementation in most of the countries in the region and it is necessary to raise the awareness of its significance in order to secure that RIA becomes a stable and integral part of the legislative process.

5. REGIONAL APPROACH TO REGULATORY REFORM

Regional approach to the improvement of the legal and regulatory environment in the Western Balkan region, as a part of the South East European region, has been identified as one of the reform priorities for cooperation among the South East European countries since 2001. This cooperation was supported by the international community, under the OECD Investment Compact for South East Europe.³ The countries in the region have recognized the importance of a regional approach in this important area and signed several ministerial declarations related to this cooperation, under the auspices of the OECD Investment Compact, and created a platform of their common regulatory reform agenda.

Several of the key principles from the Investment Compact ministerial declaration *Attracting investment to South East Europe: Common principles and best practices*, signed in 2002, were related to regulatory reform activities, including (i) transparency of laws and regulations and administrative practices affecting foreign and domestic investment; (ii) coherence and stability of these laws, regulations and administrative practices; (iii) national treatment for foreign investors at both the pre and post establishment stage; and (iv) simplification of administrative procedures needed for the establishment or development of private investment. The main aim of the implementation of these activities has been to contribute to the creation of a favorable climate for both international and regional

³ OECD Investment Compact for South East Europe was, is a regional program launched in 2000, designed to improve the investment climate and to encourage private sector development in South East Europe through the implementation of reforms enhancing domestic and foreign investment.

investment (OECD, 2002a). The importance of bringing the direct investment regulatory framework in line with best international practices and improving the investment climate throughout the region has been recognized. Participating Countries have agreed to intensify the activities related to removing the obstacles to business development, in particular regulations and administrative practices that obstruct or delay investment (OECD, 2003).

In the Investment Compact ministerial declaration *Removing obstacles to FDI in South East Europe*, signed in 2003 it was agreed to take the following key measures over the next year, taking into account the legal situation in each country: (i) to reduce licensing and approval procedures and special registration procedures, including reciprocity requirements for foreign investment, to the level necessary for normal company law registration and (ii) to establish transparent laws, regulations, procedures and practices regarding government procurement with the aim of ensuring full national treatment of foreign investment/investors, (OECD, 2003a). The importance of achieving further significant progress in the areas of regulatory reform was recognized.

The OECD Investment Compact ministerial declaration *Building a New Environment for Private Investment in South East Europe* (OECD, 2004a), signed in 2004, recognised the importance of regulatory reform for the region, and importance of high quality regulatory governance for strengthening the confidence of private investors in the region. Based on a regional study *Regulatory Governance in SEE Countries: Progress and Challenges* (OECD, 2004), countries in the region, supported by the OECD Investment Compact for South East Europe, drafted individual Action Plans for the realization of priorities in the regulatory reform area, whose realization was annually monitored. Visible progress has been achieved across the region with the implementation of these Action Plans. Most of the progress in the region has been achieved in deregulation of existing regulations and in reduction of administrative burdens. Some results were achieved in the area of institution building and implementation of laws, but it was recognized by the countries in the region that this field of reform is still lagging behind the other areas of regulatory reform.

The regional cooperation in the area of regulatory reform has been continued through (i) a Working Group on Regulatory Reform, as one of the four working groups established in 2007 by the South East Europe Investment Committee and (ii) a South East Europe Network of Policy Makers, launched in 2007 with the support of the IFC Advisory Services for Southern Europe.

The work of the Working Group on Regulatory Reform up to date has included the analysis of progress of RIA in the region and the challenges the region faces in its implementation. It also followed the improvement of the quality of economic legislation in the region through the realization of the regional project *Improving the Process of Economic Reform Legislation in Western Balkan countries*.

The South East Europe Network of Policy Makers supports systemic and sustainable improvement of the business environment across the region, including the improvement of the legal and regulatory environment. The network includes high level policy makers and members of parliament from the Western Balkan countries, as well as experts from the region. Its missions include contributing to a better business environment in the Western Balkans through serving government institutions, private sector and professionals in the field of regulatory reform and developing knowledge and capacity in conformity with and oriented toward requirements of stakeholders working in the field of regulatory reform.

Building on the previous regional cooperation activities conducted with the support of the international community, the need for regional cooperation in the area of regulatory reform has been recognized by the parliaments of the countries in the region. After the parliamentary conference held in Belgrade in March 2009, Serbia, Bosnia and Herzegovina, Macedonia and Montenegro signed a regional declaration *The Role of Parliaments in Promoting Competitiveness and Economic Growth by Improving the Business Environment in Western Balkan Economies*, which points to the necessity of regional cooperation with the aim to improve the quality and the implementation of laws on the regional level.

6. REGULATORY REFORM IN A PERIOD OF ECONOMIC AND FINANCIAL CRISIS

The global financial crisis has gone far beyond the financial sector, causing serious repercussions for the “real economy”. All regions of the world have been seriously affected by the crisis and their growth is sharply declining. According to the IMF, this decline for advanced economies is projected to be 3.8 percent, while GDP growth in developing and transition countries is expected to increase to a modest 1.6 percent, which represents a significant slowdown in respect to the previous years (IMF, 2009). Among developing regions, transition countries have been hit the hardest by the global economic and financial crisis, as their growth in the previous period has depended on strong private capital inflows, which will be reduced in the forthcoming period (IMF, 2009). After years of growth of over 6 percent in transition countries, real GDP growth in the region slowed to 4 percent

in 2008 and, according to the World Bank projections, is expected to drop 4.7 percent in 2009, driven by a collapse in capital inflows, a sharp deterioration in the area of trade and contraction in both domestic and external demand (World Bank, 2009). Similar trends have characterized the Western Balkan region. Real GDP in this region expanded by 6.3 percent in 2007, slowed to 4.4 percent in 2008 mostly due to the decline in the real GDP in the fourth quarter of 2008. The continuation of the trend is expected in 2009 and its growth is projected to contract by 5.0 percent in 2009. In 2010, GDP growth is expected to increase to a modest 0.4 percent (IMF, 2009a).

One of the principal sources of the financial crisis is clearly bad regulation. The financial crisis emerged after decades of “deregulation” and regulatory reform, in which developed countries were extensively liberalizing their regulatory environment in order to be more competitive and attract investments. Therefore, the risk is that regulatory activities will now once again shift to re-regulation, excessive and overburdening regulation and that there will be a re-introduction of state control functions, in order to avoid future crises. This could cause a wave of heavy regulation, instead of seeing the shift towards “smart” regulation. This shift would be a big cultural change, which may in particular affect countries in transition, such as Western Balkan Countries. These countries are still on the path to liberalize their legal systems and complete the shift to a market economy, and their legal framework has still not been shaped to ensure a sufficient inflow of investments. At the same time, they are all in the process of harmonizing their legislation with the Acquis. If EU countries and the EU start re-introducing heavy and excessive regulations in order to deal with the financial crisis, in the harmonization process this will be absorbed by the Western Balkan countries and it will add another layer of unnecessary burdens to the already existing ones.

A major challenge for Western Balkan countries is to continue to attract private foreign and domestic investment during the crisis that will stimulate economic activity and growth, particularly attracting those investments that serve long-term development goals and enhance competitiveness (UNCTAD, 2009).

In view of the above, the current crisis reinforces the argument that the aim of regulatory reform should be better, not necessarily fewer, regulations and that the quality of enforcement and broader governance matter greatly for the effectiveness of regulations (World Bank, 2009a).

At the level of the European Union and its member states, it has been recognized that important challenges must be faced in addressing the current economic

and financial situation. The EU Commission stated that better regulation must remain an essential part of the response – regulating where there is a need to do so, in a manner which is as straightforward as possible, based on dialogue with stakeholders, and in a way that keeps burdens on businesses and citizens at the necessary minimum. The Commission has identified the next steps which require continued efforts and the on-going political support of the other European institutions, the Member States, local and regional authorities, and stakeholders (European Commission, 2009).

In the period of crisis, the Western Balkan countries have also recognized the importance and necessity to continue and reinforce regional cooperation, especially in the area of regulatory reform. At the Belgrade parliamentary conference held in March 2009, it was agreed that the parliaments in the region should play an important role in facing the economic crisis and in taking measures necessary to overcome it, bearing in mind the intensive regulatory activities which lay ahead, both at the global and national levels. It has been agreed that, in the period of crisis, it is even more important to promote regulations that are favorable for the development of entrepreneurship and the private sector.

The Declaration points out that the development of a quality legal and regulatory framework shall be one of the most important prerequisites for attracting foreign capital in the countries of the region. The influx of capital is severely reduced in this time of crisis. In that process, the legislative role of the parliaments shall gain in importance, both in terms of the harmonization of domestic legislation with the European Union legislation, as well as adoption of regulations as a measure for overcoming the crisis.

In order to secure the best possible quality of the legal and regulatory framework, it has been noted that in the process of harmonizing national regulations with the EU legislation, the national legislation should be harmonized within itself as well.

The benefits of the regional cooperation are also based on the fact that all the countries in the region are in the process of European integrations, and the harmonization of national legislation with the Acquis will lead to the harmonization of the legislation within the region, thus establishing a harmonized regional legal and regulatory framework, which is an additional advantage for attracting large regional investment.

7. CONCLUSIONS

All of the countries in the region have, over the past several years, initiated reforms in some of the areas related to regulatory reform. In most cases these reforms were partial, focused on specific sectors or areas. Instead of being strategic or proactive, the prevailing approach was mostly ad-hoc or reactive to actual problems and has usually been initiated by the international community and, in particular, the EU accession process. In order to secure the sustainability of the regulatory reform progress, it is of a crucial importance that all the countries of the region apply a strategic approach in this area.

In the current difficult economic circumstances, the improvement of the quality of regulations and the reduction of unnecessary administrative burdens that affect business activities and investments of both foreign and domestic investors in Western Balkan countries are of crucial importance for the creation of a more favorable business and investment environment. In the situation of a crisis, better regulation should not be confused with excessive regulation which would lead to a less competitive regulatory environment. On the contrary, regulatory activities should be focused primarily on securing the so called “smarter” regulations that would support future economic development and growth of the countries in the region.

The continuation of EU harmonization, especially in the field of economic legislation which affects the business environment, should be a main focus of the countries in the region. In parallel to harmonizing their national legislations with the European legislation, the countries in the region are also mutually harmonizing the legislations among themselves, thus creating a harmonized legislative framework at the level of the region.

A risk exists that the international community, including the European Union, will be less involved in the region than in the previous period, because most of the political energy of the European political landscape will be directed towards solving the crisis within the EU. This requires greater political accountability and self-responsibility of political leaders and leaderships in the countries of Western Balkans. This accountability should also be focused on maintaining and raising the level of political support for the regulatory reform agenda, as one of the key reforms which can contribute to the creation of better prospects for regaining economic growth in the region.

The regional approach to the improvement of legal and regulatory environment in the Western Balkan region, which points to the necessity of regional cooperation with the aim to improve the quality and the implementation of laws on the regional level, should be strengthened and continued. The harmonization of national legislation with the Acquis will lead to the harmonization of the legislation within the region as well, thus establishing a harmonized regional legal and regulatory framework. Since the influx of capital is severely reduced in this time of crisis, harmonized regional legal and regulatory framework will be an additional advantage not only for reversing the decrease of investment inflow, but also for attracting large regional investment.

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