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PROJECT PERFORMANCE ASSESSMENT REPORT

BOSNIA & HERZEGOVINA

BUSINESS ENVIRONMENT ADJUSTMENT CREDIT

(IDA 36450)

June 27, 2014

IEG Public Sector Evaluation

Independent Evaluation Group

Currency Equivalents (annual averages)

Currency Unit = Marka

2002	US$1.00	KM 1.24
2007	US$ 1.00	KM 1.24

Abbreviations and Acronyms

BAC	Business Environment Adjustment Credit
BEEPS	Business Environment and Enterprise Performance Surveys
BiH	Bosnia & Herzegovina (State)
BMO	Business Membership Organization
DfID	UK Department for International Development
EBPAC	Enterprise and Bank Privatization Adjustment Credit
EC	European Community
EPA	Economic Partnership Agreement
FBiH	Federation of Bosnia & Herzegovina
FDI	Foreign Direct Investment
FIC	Foreign Investors Council
FILE	Fostering an Investor & Lender-Friendly Legal Environment
FYR	Former Yugoslav Republic
GPS	Global Positioning System
GTZ	Gesellschaft für Technische Zusammenarbeit.
ICIS	Improving Investment Climate and Institutional Strengthening Project
ICR	Implementation Completion and Results report
IEG	Independent Evaluation Group
IEGPS	IEG Public Sector Evaluation
IT	Information Technology
KM	Marka (local currency)
NORAD	Norwegian Agency for Development
OHR	Office of the High Representative for Bosnia and Herzegovina
PDO	Project Development Objective
PFSAC	Public Finance Structural Adjustment Credits
PPAR	Project Performance Assessment Report
PPD	Public-Private Dialogue
PTAC	Privatization Technical Assistance Credit
RS	Republika Srpska
SECO	Swiss Agency for Economic Cooperation
SEE	South Eastern Europe
SIDA	Swedish International Development Agency
SOE	State Owned Enterprise
SOSAC	Social Sector Adjustment Credits
SPIRA	Streamlining Permits and Inspection Regimes Activity
TARA	Tax Administration Reform Assistance
UNCTAD	UN Conference on Trade and Development
USAID	US Agency for International Development
VAT	Value Added Tax

Fiscal Year

Government: January 1 – December 31

Director-General, Independent Evaluation	:	Ms. Caroline Heider
Director, IEG Public Sector Evaluation	:	Mr. Emmanuel Jimenez
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Contents

This report was prepared by Giuseppe Iarossi, and Davis A. Phillips, who assessed the project in October 2012. The report was peer reviewed by Peter Mousley and panel reviewed by Robert Lacey. Yezena Zemene Yimer provided administrative support.

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Figures

Principal Ratings

	ICR*	ICR Review*	PPAR
Outcome	Moderately Satisfactory	Moderately Satisfactory	Moderately Unsatisfactory
Risk to Development Outcome	Moderate	Moderate	Significant
Bank Performance	Satisfactory	Moderately Satisfactory	Moderately Unsatisfactory
Borrower Performance	Moderately Satisfactory	Moderately Unsatisfactory	Unsatisfactory

* The Implementation Completion and Results (ICR) report is a self-evaluation by the responsible Bank department. The ICR Review is an intermediate IEG product that seeks to independently verify the findings of the ICR.

Key Staff Responsible

Project	Task Manager/Leader	Division Chief/ Sector Director	Country Director
Appraisal	Vicki Diane Peterson	Paul J. Siegelbaum	Christiaan J. Poortman
Completion	John Daniel Pollner	Fernando Montes Negret	Jane Armitage

IEG Mission: Improving World Bank Group development results through excellence in independent evaluation.

About this Report

The Independent Evaluation Group assesses the programs and activities of the World Bank for two purposes: first, to ensure the integrity of the Bank's self-evaluation process and to verify that the Bank's work is producing the expected results, and second, to help develop improved directions, policies, and procedures through the dissemination of lessons drawn from experience. As part of this work, IEG annually assesses 20-25 percent of the Bank's lending operations through field work. In selecting operations for assessment, preference is given to those that are innovative, large, or complex; those that are relevant to upcoming studies or country evaluations; those for which Executive Directors or Bank management have requested assessments; and those that are likely to generate important lessons.

To prepare a Project Performance Assessment Report (PPAR), IEG staff examine project files and other documents, visit the borrowing country to discuss the operation with the government, and other in-country stakeholders, and interview Bank staff and other donor agency staff both at headquarters and in local offices as appropriate.

Each PPAR is subject to internal IEG peer review, Panel review, and management approval. Once cleared internally, the PPAR is commented on by the responsible Bank department. The PPAR is also sent to the borrower for review. IEG incorporates both Bank and borrower comments as appropriate, and the borrowers' comments are attached to the document that is sent to the Bank's Board of Executive Directors. After an assessment report has been sent to the Board, it is disclosed to the public.

About the IEG Rating System for Public Sector Evaluations

IEG's use of multiple evaluation methods offers both rigor and a necessary level of flexibility to adapt to lending instrument, project design, or sectoral approach. IEG evaluators all apply the same basic method to arrive at their project ratings. Following is the definition and rating scale used for each evaluation criterion (additional information is available on the IEG website: http://ieg.worldbankgroup.org).

Outcome:The extent to which the operation's major relevant objectives were achieved, or are expected to be achieved, efficiently.The rating has three dimensions: relevance, efficacy, and efficiency. *Relevance* includes relevance of objectives and relevance of design. Relevance of objectives is the extent to which the project's objectives are consistent with the country's current development priorities and with current Bank country and sectoral assistance strategies and corporate goals (expressed in Poverty Reduction Strategy Papers, Country Assistance Strategies, Sector Strategy Papers, Operational Policies). Relevance of design is the extent to which the project's design is consistent with the stated objectives. *Efficacy* is the extent to which the project's objectives were achieved, or are expected to be achieved, taking into account their relative importance.*Efficiency* is the extent to which the project achieved, or is expected to achieve, a return higher than the opportunity cost of capital and benefits at least cost compared to alternatives. The efficiency dimension generally is not applied to adjustment operations.*Possible ratings for Outcome:*Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Risk to Development Outcome:The risk, at the time of evaluation, that development outcomes (or expected outcomes) will not be maintained (or realized). *Possible ratings for Risk to Development Outcome:*High, Significant, Moderate, Negligible to Low, Not Evaluable.

Bank Performance: The extent to which services provided by the Bank ensured quality at entry of the operation and supported effective implementation through appropriate supervision (including ensuring adequate transition arrangements for regular operation of supported activities after loan/credit closing, toward the achievement of development outcomes. The rating has two dimensions: quality at entry and quality of supervision.*Possible ratings for Bank Performance:* Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Borrower Performance: The extent to which the borrower (including the government and implementing agency or agencies) ensured quality of preparation and implementation, and complied with covenants and agreements, toward the achievement of development outcomes. The rating has two dimensions: government performance and implementing agency(ies) performance. *Possible ratings for Borrower Performance:*Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Preface

This is a Project Performance Assessment Report for the Bosnia & Herzegovina (BiH) Business Environment Adjustment Credit (BAC). A mission to BiH took place over the period October 22nd to November 2nd, 2013 to assemble data and information for this report. The report was prepared by Giuseppe Iarossi (Bank) and David A. Phillips (Consultant)

We would like to acknowledge the help of the following Bank staff in supporting this report: Ruvejda Aliefendic, Samra Bajramovic, Paula Genis, Haris Mesinovic, Vicki Peterson, John Pollner, Tarik Sahovic, Margo Thomas, and Yezena Yimer. Jasmin Vajzovic and Magdalena Raosavljevic joined the mission in the field.

We would also like to acknowledge the many Government and Agency Officials in BiH who kindly gave up their time to assist our visit. (See annex B)

Our main sources of information included the following (see also list of references at end):

Following standard IEG procedures, copies of the draft PPAR was sent to government officials and concerned agencies for review and comment. No comments received.

Summary

Objectives and Design

The Business Environment Adjustment Credit (BAC) was approved by the Board in 2002 and finally closed in 2007. Hence it was initiated before the introduction of a new approach to budget support, when they were relabeled as DPLs with OP 8.60 offering new terms for guidance, including changes in the standards for evaluating budget support operations. Today we expect all DPLs to have results frameworks, which was not the case in 2002.

The Presidents Report stated that the operation would: “support the Government's reform program to improve the investment climate and further development of a single economic space to promote domestic and foreign investment and private sector growth”. The objectives of the reform program were to reduce “those administrative and regulatory barriers that would have the most critical near-term impact on the three phases of business development” by:

(i) improving business entry through streamlined and transparent countrywide approach to business registration and licensing and strengthened legal framework and capacity for attracting foreign investment;

(ii) streamlining the environment for business operation by reducing companies' administrative and regulatory compliance costs through rationalization of inspections and regulations, strengthening of judicial and extra-judicial capacity to resolve commercial disputes; improving enforcement of secured transactions; and leveling the playing field for private sector participation in public procurement, and

(iii) facilitating business exit through improved bankruptcy and liquidation systems. Underlying these objectives is the need to strengthen the consultative capacity between the public and private sectors to promote policies and legislation that are business-friendly.

The policy program of the BAC was developed out of the ongoing dialogue between the donor community and the State Government of BiH that followed the Dayton Accords of 1995, and in line with the strategic priorities of the Government. The policy areas addressed were consistent with Government objectives which had also been derived partly from a Bank report (FIAS 2001) on the legal, regulatory and administrative costs to business.

The BAC operation was designed as a two-tranche sector adjustment credit totaling $44.0 million. It was accompanied by a series of parallel donor capacity building technical assistance activities. The tranched design proved difficult to implement in practice because the capacity building conditions could not be fulfilled within the target dates and multiple extensions had to be agreed for release of the second tranche. In this respect the operation had to deal with the triple challenge facing the country, namely: a) post-conflict recovery, b) the transition from a planned to a market economy, and c) a fragmented governance structure created at the Dayton Accords, in particular the division between the two main Governing Entities, the Federation of Bosnia & Herzegovina (FBiH) and Republika Srpska (RS).

Despite the delays in meeting the performance conditions for second tranche release the operation was not restructured, nor were the performance targets amended.

Outputs and Outcomes

By completion the operation had, with the help of donor supported capacity building, implemented a series of specific reforms. In efforts to reduce administrative and regulatory barriers (Objective 1) a business registry was operational, the laws and regulations governing it were effective, and registrations were going ahead under the new system although they had not accelerated; the Foreign Investment Promotion Agency (FIPA) was in operation although its effectiveness was moderate. To streamline the environment for business operation (Objective 2) a collateral registry for movable assets was operating well with the active support of the banks, and registrations were increasing; a centralized business inspection system with state of the art technology was in place and had improved efficiency through a selective and coordinated inspections system; and a compulsory membership in the Chambers of Commerce had been abolished but then the policy reform was partly reversed. To facilitate business exit (Objective 3) a revised bankruptcy law was allowing greater labor mobility but had practical weaknesses. And lastly, to strengthen the consultative capacity for public-private dialogue (Objective 4) private business membership organizations were formed but the Chambers had been reintroduced in the process, which was a policy reversal.

While new institutional capacity was operating effectively in most cases, the longer term outcome varied between the reform initiatives taken. In some cases it was also difficult to measure and/or to attribute to the operation. For example, there has been no evidence of acceleration of business registration over the past five years and performance relative to comparator countries has been moderate. In the case of collateral registration before-after comparisons over time are very positive but inter-country comparisons suggest that the outcome of the reforms in BiH was also about average. The reduction in the cost of inspections to business has been significant but usable country comparators are not available. Other areas have not shown good outcomes. The foreign investment agency was expanded but had not shown evidence of improved performance by project completion. Similarly business exit through the amended bankruptcy law has increased but practical problems arose in its application because opposition to closing State Owned Enterprises (SOEs) had exposed weaknesses in the law.

While the objectives of the operation were relevant the partial fulfillment of outcomes was related to a design based on time-bound performance targets which proved to be inappropriate to the long term requirements of post-crisis economic transition. However, despite the difficulties in delivering results the BAC did play a significant catalytic role in pushing forward key business reforms at a difficult time, a conclusion that is widely supported within the country. On balance, taking account of the implementation delays, the mixed outcomes, the overall catalytic effect, and the contribution of the other agencies responsible for capacity building, the BAC's attributable outcome achievement is rated **moderately unsatisfactory**.

Bank and Borrower Performance

Bank performance: Bank implementation performance was adversely affected largely because of the lengthy period of capacity building needed to fulfill reform objectives in a post-crisis transition economy. This was to some extent aggravated because the capacity building was in the hands of donor agencies rather than being part of the Bank operation and therefore not directly under Bank control. The Bank's project team was nevertheless diligent in the face of a particularly difficult implementation environment. Much effort was made, largely from the local office, to push through the reforms and achieve the targets.

At the same time the problems of implementation led to ten extensions of the second tranche release and hence of the closing date in order to finally fulfill the objectives under the policy conditions. This may have given the impression to the Government that the lending conditions were easily re-negotiable. The lack of adherence to the target dates may have been aggravated by the lack of a fully developed results framework and indicators to guide the implementation of the operation. Intended half-yearly monitoring surveys that might have better highlighted the problems in meeting targets were not carried out. In 2005 a proposal was made to management to restructure the tranche release conditions but it was not adopted. While the President's Report foresaw the risks of implementation delay in practice they were very difficult to mitigate.

The rating for the Bank Performance has to balance a) flaws in design that affected implementation, b) the significant effort to solve implementation problems through close supervision, and c) management's willingness to extend the completion deadlines rather than amend the targets.

The rating for Bank performance is **Moderately Unsatisfactory.**

Borrower Performance: The Government's performance was significantly affected by elections and changes of Administration during the implementation period, which reduced its level of commitment to the project. Combined with this were the following factors: a) the multiple agencies within Government that had responsibility for parts of the project, b) the difficulties of implementing market reforms in a post-conflict environment, and c) the dual Entity responsibility reliant on coordinating committees. The Implementation Status Reports (ISRs) however reported that the Governmental Authorities were at all times making considerable efforts to push forward with implementation, and only once implied a failure to perform, in 2005 when the project rating was reduced to MU. Delays in delivery of legal reforms and new procedures were a direct reflection of the highly fragmented governance structure and frequent opposition of an Entity or Canton to particular regulatory or procedural changes. Taking account of the project from start to completion it is concluded that the Government was not able to satisfactorily fulfill its commitments.

The original coordinators of the BAC were the Ministry of Trade and Economic Reform (in FBIH), and the Ministry of Administration and Local Government (in the RS). However numerous other agencies were also partly responsible for implementation. These included the full hierarchy of Governing bodies and courts, and numerous agencies such as inspectorates, registries, and FIPA. As a result coordination was often ineffective.

Rating for Overall Borrower Performance: **Unsatisfactory**

Risk to Development Outcome

There were a number of risk mitigation mechanisms set out in the Presidents Report that were largely unsuccessful in practice, and hence the risks to the reforms going forward remain essentially the same. Firstly, there remains a *significant risk* of weak support for State level reforms because of political opposition from the Entities, RS and FBiH. Secondly, there is a *moderate risk* of erosion or reversal of previous reforms especially in the light of opposition to some policies. Thirdly, there is a *moderate* risk of the degrading of capacity in the regulatory bodies overseeing systems such as business inspections and the business registry. Fourthly there is a *moderate risk* of erosion of compliance with legal and regulatory processes which may degrade regulatory compliance.

These risks can only be mitigated through responsiveness to technical and organizational problems and close, sensitive and time-intensive, supervision with continuity of expert support. The current support program of the Bank, including the Investment Climate and Institutional Strengthening (ICIS) Project is however proceeding with an awareness of these lessons which is likely to improve the prospects for sustained positive benefits going forward.

The risk rating for the sustainability of Development outcomes is **Significant**.

Lessons

Because of the 'triple challenge' facing BiH in some respects the legacy of the operation is unique and not easily susceptible to generalized lessons. Bearing this in mind, the key lessons are:

- In high risk environments (post crisis, fragmented governance, etc.) an 'early wins' strategy may be required, but should be accompanied by flexibility, early and structured review, and an exit strategy in the event that reforms come off track.
- Formulation of laws in adjustment operations needs to be accompanied by careful attention to addressing implementation constraints, particularly in post-crisis or transition environments, where capacity is particularly weak and the institutional framework is fragmented. Other aspects related to the implementation of the laws needs to be properly addressed in the intervention. In the case of the bankruptcy law for example the legislation needed to be backed up by clearer and more effective enforcement regulations.
- The choice of a quick disbursing instrument was questionable in the light of the medium-term requirements of capacity building. Operations that require intensive on-the-ground capacity assistance are not suitable for pure adjustment-type lending because the adjustment timetable is usually inconsistent with the capacity building timetable. Capacity building projects must be of long duration, especially in a post-conflict situation, to adjust to local conditions and allow sufficient implementation time to build up sustainability. Programmatic lending instruments would be more consistent with these requirements.

- In situations with multiple development partners and significant capacity constraints, effective leadership and coordination, both in Government and development partners, is essential.

Richard Scobey
Acting Director-General
Evaluation

1. Background and Context

Background

1.1 The Business Environment Adjustment Credit (BAC) in Bosnia-Herzegovina was selected for evaluation to help inform the macro evaluation on Investment Climate reforms, as it was considered an example of regulatory reforms conducted in a challenging political environment.

1.2 At the time that the Business Environment Adjustment Credit (BAC) was initiated in 2000-2001, the Federation of Bosnia & Herzegovina (FBIH) was facing the unique triple challenge of: 1) reconstruction after civil war (which ended with the Dayton Accords of 1995), 2) the transformation from a centrally planned to a market economy, and, 3) a highly complex governance structure designed primarily to restore peace. Progress had been made on the rehabilitation of infrastructure and basic institutional development, including the establishment of the central bank, State and Entity treasuries, and issuance of the national currency. Major policy initiatives had been taken including trade and price liberalization, tax reform, social sector and financial market reforms, and privatization. Progress had also been made in removing barriers to the movement of goods and people within the country, and a common, national level customs tariff regime had been introduced. Nevertheless there remained significant needs. These were considered to be:

- Accelerating privatization to eliminate the unfair competition of privileged state-owned firms.
- Strengthening the banking sector to build the capacity of financial intermediaries to support private sector growth.
- Lightening a burdensome tax regime to motivate companies to return from the informal to the formal sector.
- Liberalizing trade, modernizing customs administration and strengthening competition policy to improve the competitive environment for the private sector
- Improving property rights and access to land to help create an active land market.
- Reducing corruption.
- Increasing the independence and capacity of the judiciary.

Context

1.3 At the time when the BAC was appraised, GDP growth was decelerating but remained at 4 to 5 percent per annum, with relatively low inflation. However unemployment was at 37 percent. Even with the reasonable level of cooperation between Government entities at that time fragmented governance (in FBiH and RS) was making decision-making difficult and hampering reform efforts which were required inter alia for integration with the EU. In 2001, according to a World Bank (FIAS) study, major weaknesses remained within the legal framework for setting up and operating businesses in FBIH which encouraged corruption and raised the cost of doing business. The 14-step business registration process took months to complete, discouraging firms from formalizing. There remained a lack of effective regulations and mechanisms for secured lending, such as movable collateral registration, which restricted access to working capital. The court system was deficient and there were long delays in the resolution of commercial disputes. Operating businesses faced numerous inspectorates with often overlapping mandates, leading to excessive administrative costs of compliance. The prospects for recovery therefore depended significantly on accelerated implementation of institutional reforms.

1.4 The BAC was one of a series of World Bank adjustment operations initiated over 1999 to 2001 designed to support the recovery and transformation of the economy at the turn of the decade. These included the Enterprise and Bank Privatization Adjustment Credit (EBPAC), Public Finance Structural Adjustment Credits I and 1I (PFSAC), and two Social Sector Adjustment Credits (SOSAC). These operations were the second stage of post-crisis support following an initial series of emergency credits in 1997-99. The Business Environment Adjustment Credit (BAC) was approved by the Board in 2002 and finally closed in 2007. Hence it was initiated before the introduction of a new approach to budget support, when they were relabeled as DPLs with OP 8.60 offering new terms for guidance, including changes in the standards for evaluating budget support operations.

2. Objectives, Design, and their Relevance

Objectives of the Operation

2.1 The Presidents Report stated that the operation would: "support the Government's reform program to improve the investment climate and further development of a single economic space to promote domestic and foreign investment and private sector growth." Objectives of the reform program were to reduce 'those administrative and regulatory barriers that would have the most critical near-term impact on the three phases of business development' by:

(iv) improving business entry through streamlined and transparent countrywide approach to business registration and licensing and strengthened legal framework and capacity for attracting foreign investment;

(v) streamlining the environment for business operation by reducing companies' administrative and regulatory compliance costs through rationalization of inspections and regulations, strengthening of judicial and extra-judicial capacity to resolve commercial disputes; improving enforcement of secured transactions; and leveling the playing field for private sector participation in public procurement, and

(vi) facilitating business exit through improved bankruptcy and liquidation systems. Underlying these objectives is the need to strengthen the consultative capacity between the public and private sectors to promote policies and legislation that are business-friendly. Underlying these objectives is the need to strengthen the consultative capacity between the public and private sectors to promote policies and legislation that are business-friendly.

2.2 The project development objectives were based on selected findings of the 2001 World Bank (FIAS) study. From interviews with Bank staff, the selected initiatives were those that were considered to be: a) achievable in a relatively short time frame, b) had large potential impact, and c) for which support was readily available. Accordingly, the process was to start with the recommendations that had already been put forward in the FIAS study and discussed with the Government, then to engage stakeholders to further prioritize the identified actions and confirm complementary donor commitments; and, finally to refine the list based on the Bank's strengths in specific areas. The project design also leveraged technical assistance from bilateral donors, which was ongoing or could be mobilized quickly.

2.3 The objectives were translated into specific, measurable, operational objectives through the BAC policy program. The tranche release conditions under the policy program, from the Presidents Report were as follows.

BOARD CONDITIONS

- State Council of Ministers adopted amendments to the Decision on Foundation of Foreign Investment Promotion Agency, satisfactory to the Association, and allocated funding for its operations.
- Entities adopted Foreign Investment Laws, satisfactory to the Association and fully harmonized with the State Law on Policy of Foreign Direct Investment.
- State and Entities established a formal mechanism, satisfactory to the Association, for regular consultation with the private sector to consider their views in the formulation of policies and legislation affecting business.
- Entities formally adopted the concept of common procedures and single database for each of business registration and registration of pledges on movables (i.e., collateral registry).
- Entities adopted Laws on Registered Pledges on Movables, satisfactory to the Association.
- Entities conducted an independent baseline survey of administrative and regulatory costs of business.
- State and Entities drafted an anti-corruption action plan, incorporating public procurement and initiated the public consultation process.
- Entities eliminated the overlapping authorities of the Financial Police and the Revenue (Tax) Administration.
- State adopted the Law on Associations and Foundations of FBIH, satisfactory to the Association, allowing associations to cooperate across FBIH.
- Entities established a working group to draft new harmonized bankruptcy laws. The working group has already produced a draft that is in the process of being finalized.

SECOND TRANCHE CONDITIONS

- FIPA representative offices are staffed and operating in both Entities.
- Pilot of the business registry system embodying common procedures, common forms, and single database has been tested in selected courts across both Entities, and a plan for full implementation, satisfactory to the Association, has been adopted.

- Entities reduce the average number of days to register a business from 80 to 30 days or less in the Federation and from 31 to 23 days or less in the RS, as measured by independent surveys on a semi-annual basis.
- Entities reduce the number of steps required to register an enterprise to 7 or less.
- Pilot of the collateral registry system embodying common procedures, common forms, single database and trained participants (judges, clerks, banks) has been tested in selected courts across both Entities, and a plan for full implementation, satisfactory to the Association, has been adopted.
- Entities have established a business inspection system, satisfactory to the Association, that provides for: the review and rationalization of the mandates of inspectorates operating at Entity and sub-Entity levels; clarification and publication of the mandates of the inspectorates and the inspectors; rational, planned inspection schedules, standard forms and guidelines; amendments to legislation as necessary to implement rationalization of the inspectorates, and regulatory assessment with the goal of appealing obsolete or unnecessary regulations.
- The average number of aggregate on-site inspector days per inspected business per annum for the Market, Labor, Financial Police and Revenue Administration combined will be reduced from 28 days to 15 days or less in the RS and from 18 days to 12 days or less in the Federation.
- Entities adopt amendments to the Laws on Chambers of Commerce, satisfactory to the Association, to eliminate mandatory membership.
- Entities adopt strengthened and harmonized Laws on Bankruptcy and Liquidation, satisfactory to the Association.

Restructuring of Objectives

2.4 There were no amendments to the operational objectives of the BAC. The performance targets were reconsidered mid-way through the operation as a result of a need to extend the operation's closing dates. The extensions, which numbered ten, were due to failure to meet a number of second tranche release conditions. However performance targets were not, in the end, amended. (This is reviewed in more detail in 2.23 and in section 3 of this report).

The Relevance of the Operation's Objectives,

COUNTRY CONDITIONS

2.5 Two surveys of business condition in BiH informed the project's objectives. The Bank (FIAS) study addressed the legal and administrative barriers to business in BiH. It identified three major problems: the absence of an adequate legal and regulatory framework to establish and operate a business; the lack of consistent and transparent business regulations and administrative procedures; and, the lack of effective, efficient, and adequately funded administrative and judicial systems. A second, 2002 baseline study, found that the most serious barriers to business were corruption, tax rates and administration, 'unfair competition' from the informal economy, and access to finance. The study also found, consistent with the World Bank (FIAS) study, that there were difficulties with the registration of a new enterprise, work permits, customs regulations, and labor regulations. However inspections, product and service standards and intellectual property regulations were not found to be key obstacles and in Republika Srpska (RS) firms did not rate the functioning of the judiciary as a serious obstacle. These findings were therefore not entirely consistent with the Bank study in terms of ranking of constraints but they were consistent with the overall reform agenda.

2.6 The BAC operation was selectively based on the findings of the above studies. Its objectives included the removal of key regulatory obstacles and some specific issues of access to finance, labor, and the capacity of the courts. However they were not entirely in line with the key problems facing the business community. The project management described the strategy as one of addressing 'early wins' across a broad spectrum of issues that could be relatively easily delivered rather than a prioritized, integrated reform approach. This resulted in a rather piecemeal approach in some reform areas. However there was ex ante justification for this approach in the difficult, post-conflict environment when it was critical to move the reform process forward rapidly and win support from a fragmented Government. There was not a full Bank ESW backing for this operation – it was put in place following the first round of emergency loans and before much ESW work had been done. Hence the design of the operation was a bit rushed and in hindsight appears to have been weak.

CONSISTENCY WITH GOVERNMENT STRATEGY

2.7 While the operation's 'early wins' approach did not fully address the key business needs its objectives were consistent overall with the Government's plans for improving the business climate, as set out, for example, in the 'Action Plan for Implementation of Business Environment Reforms' adopted by RS and FBiH, which were based on the recommendations of the Bank (FIAS) study. They were also consistent with the Government's Economic Development Strategy for 2000-2004 which included acceleration of privatization, strengthening of the financial sector, and establishment of an enabling environment for domestic and foreign investment.

CONSISTENCY OF THE OBJECTIVES WITH THE CAS AT CLOSURE AND BEYOND.

2.8 The CAS for BiH at the closure of the project stated that while progress had been made in improving the business climate, BiH lagged behind its regional neighbors. There had been progress in improving access to finance, improving the efficiency and effectiveness of the business inspection regime and introducing a new business registration system. But private sector activity was still below regional averages, accounting for about 55 percent of GDP. Doing Business reports showed that BiH's relative ranking on ease of doing business was falling. The key requirements for reforming the business climate included the need to further reduce the time to register a new business; improve accounting standards, rationalize the tax and levy system as it affected businesses, further reducing the regulatory burden on businesses. There was thus significant unfinished business and the BAC overall objectives of strengthening the business climate therefore remained relevant at closure.

2.9 Relevance of Objectives is rated **substantial**.

Relevance of the Operation's Design

2.10 **Design of the Operation**. The operation was configured as a two-tranche adjustment operation for $44 million equivalent. [1] The policy areas addressed by the operation were supported by 10 first tranche conditions followed by 9 second tranche conditions each to be adopted by both FBiH and RS. Thus 38 separate policy and institutional development actions had to be taken overall.

2.11 With the extensive policy program to be carried out in two separate Government Entities the timetable required for disbursements was very short relative to the lengthy institutional development process, especially in a post-crisis, transition economy. A programmatic lending instrument would have allowed a more extended timetable, and permitted a more phased approach to institution building through a relatively light disbursement conditions at each stage. This could have avoided the need for the entire set of conditions to be met simultaneously and the resulting repeated time extensions – which called into question the Bank's determination about its own conditionality (i.e. no exit strategy in the event of failure to comply).

2.12 The capacity to implement the institutional and regulatory reforms was managed through parallel funding by donor agencies. The cooperation of the donors was good but the lack of control of capacity building within the Bank's own operation tended to aggravate the problem of the tight timetable for tranche release, and this was made more difficult by the complex oversight arrangements. (See further 2.21).

2.13 **Clarity and realism of the objectives**. The objectives as set out in 2.1 to 2.3 were operationalized through the policy program as a series of specific goals allowing performance targeting and measurement and in this sense were clear and appropriate. However, with the benefit of hindsight some of the objectives were excessively ambitious within the difficult environment and the timing of their fulfillment was unrealistic.

2.14 **The quality of the explicit or implicit results framework.** There was no formal results framework for this operation. The absence of a framework is due to the fact that in 2002 no framework was required for such operations. Today we expect all DPLs to have results frameworks.

2.15 The lack of a fully developed results framework may have worsened the delays in the release of the second tranche; a more complete framework might have resulted in closer attention being paid to what was practically possible to implement at different times; however, the issue was probably more one of deciding how to effectively manage implementation than the framework of the results as such. The use of specific short-run outcome targets may also have encouraged an excessive focus on hitting numerical targets

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[1] Due to the appreciation of Special Drawing Rights against the dollar over 2001-7 the final disbursement in December 2007 amounted to $51.9 million.

such as days taken for court registration rather than the development of the overall effective registration system.

2.16 **Extent to which exogenous factors were taken into account and mitigated**. Despite the intentions the design of the operation was inadequate to take into account exogenous factors such as the strength of political opposition as a result of the continuing stand-off between FBiH and RS, and the opposition to State level institutions from both entities, in particular RS. This inadequacy was particularly clear given the concomitant complex requirements of economic transition. The latter were reflected in for example the opposition to the bankruptcy law as it affected the redundancy of SOE workers, and the pressures to maintain the role of the State-sponsored Chambers of Commerce. While special coordinating arrangements were put in place under the Coordination Board for Economic Transition and European Integration (see 2.21) this was not adequate to deal with these issues,

2.17 **Rating of Operations Design**. On the basis of the above points the relevance of the operations design was **modest**.

The Design of Monitoring and Evaluation

2.18 As stated, a group of 5 “PDO indicators” with baselines and targets were used as the basis for monitoring the operation. These were (for both FBIH and RS) as follows:

- Reduction of average days for registration;
- Reduction of average onsite inspection days;
- Reduction in number of steps for business registration;
- Increase in investment, particularly foreign investment;
- Creation of a movable pledge/collateral registry available at the nationwide level.

2.19 There were no separate intermediate outcome indicators. The PDO indicators and numerical and qualitative targets based on those indicators were used as the project’s sole monitoring benchmarks. The indicators or targets were not modified during the project. The PDO indicators were supported by a planned system of reports. These consisted of a baseline study, and survey reports intended to be produced at six monthly and three yearly intervals. The fulfillment of targets was supposed to be verified through these surveys, which would also allow better monitoring of the business environment, and help to build capacity for monitoring in the Government. The PDO targets and the baseline values established at the start of the project, drawn from the 2001 FIAS study and 2002 baseline study, were as indicated in Table 2.1

Table 1: PDO targets, baselines and achievement				
Indicator	***Baseline Value***	***Target Value***	***Value At Completion***	***Target Fulfilled***
Reduction of average number of days for registration and startup	FBiH 80	FBiH 30	FBiH 27.0	Yes
	RS 31	RS 23	RS 18.0	
Reduction in number of onsite inspection days	FBiH 18	FBiH 12	FBiH 9.9	Yes
	RS 28	RS 15	RS 7.5	
Reduction in Number of Steps for business registration	Foreign Cos 14-15 Local Cos 12	7	5	Yes
Increase in foreign investment	FDI, 4.3% of GDP	No target	FDI, 13.7% GDP	n/a
Creation of collateral (pledge) registry at national level	No registry except for real estate	None	Frequent use of registry	Yes
Source: Project documents				

2.20 The PDO indicators largely corresponded to the second tranche release policy conditions supported by the operation, covering business entry and business operation (but excluding bankruptcy policy - business exit). Indicator selection was based on those policy reforms that appeared to be the most quantitatively measurable, (business registration, inspection, collateral registration, and increase in foreign investment).

2.21 The M&E system was managed within the operation, assisted by outside agencies. The planned system of six monthly reports, which were to be funded by the cooperating donors, did not go ahead. The baseline study and two monitoring surveys, in 2004 and 2007, were completed by three separate private consulting and survey firms. There was no formal evaluation study conducted for the operation.

The Design of the Implementation arrangements

2.22 The entities responsible for implementing different aspects of the operation are set out in the following organizational framework, based on the President's Report. These included the legislatures, all levels of State, Entity, Regional and Local Government, finance and justice ministries, and courts. Nine separate donor agencies were also listed as having administrative or implementing authority.

Table 2: Organizations Implementing the BAC Operation		
Area Of Program	***Administrative And Donor Responsibility***	***Implementing Authority***
Strengthen FDI legal framework and increase operational capacity of the FIPA	Parliaments State Ministries of Commerce, Economic Relations FIAS, EC	FIPA Governments FIAS, EC
Streamline and Establish Countrywide approach to business registration (including strengthening of commercial courts)	Parliaments Industry Ministries Justice Ministries GTZ, DfID	Regional and Cantonal Courts DfID, IFC
Improve access to capital by protection creditors collateral rights (including strengthening of commercial courts)	Parliaments	Regional/ cantonal courts EBRD, USAID, IFC, SEED
Level the playing field for private sector participation in public tender (incl. law)	Parliaments Treasury Ministries Finance Ministries EC	State, regional and cantonal Government EC
Reduce regulatory compliance burden on business (incl. inspection function, licensing and permits)	Central, Cantonal and Municipal Governments	State, regional and cantonal/ municipal Governments DfID
Involve private sector in formation of public policies and commercial law (establish dialogue and reform of Chamber of Commerce)	Governments, Parliaments	State, regional, Governments FIAS, SEED, GTZ, SIDA
Harmonize and strengthen bankruptcy and liquidation practice (incl. strengthen commercial courts)	Parliaments Justice Ministries GTZ	Regional Governments, regional, cantonal courts GTZ, IFC
Source: Presidents Report Annex 5 p37		

2.23 This complex structure was expected to be managed through a hierarchy of coordinating bodies. A high-level Coordination Board for Economic Transition and European Integration had general oversight responsibility for the BAC while implementation oversight was delegated to the Ministry of Trade and Economic Reform (in FBiH), and the Ministry of Administration and Local Government (in the RS), in coordination with the FBiH and RS Prime Ministers' Office. Implementation in practice was also overseen by a working group of technical experts across the relevant ministries of FBiH and RS using a reform action plan that they had devised, based on the FIAS recommendations. Bilateral donor programs were expected to build capacity through providing experts as needed.

Restructuring of the Operation

2.24 The operation was not restructured. There were no changes to the design, scope, scale, implementation arrangements and funding allocations. In this respect there were also no waivers of conditions despite the four year delay in securing second tranche release and ten separate extensions of the credit.

2.25 From interviews with the Bank project management team and donors the reason for the decisions not to restructure despite the multiple extensions was primarily due to the relatively arduous ongoing policy dialogue with BiH and the desire of the Bank and the donor partners to avoid significant departures from agreed policy programs especially since ongoing capacity building work such as the business registry was geared to levels of progress agreed with the donor.

2.26 In 2005 the formulation of a restructuring plan was in fact proposed by the Bank which would have allowed partial Tranche 2 release by accepting compliance with most of the conditions but retaining a third 'floating' tranche to be released against the final two performance-based conditions (registration and inspection). However the restructuring plan was not adopted because it was itself contingent on the fulfillment of a condition on inspections and because it was decided that any restructuring should be done within the context of the restructuring of the whole series of adjustment operations in BiH.

3. Implementation

Implementation progress

3.1 The key implementation events of the BAC operation are summarized as follows.

Table 3: Implementation Process

Process	***Original Date***	***Actual Date***
Concept Review	12/17/2001	12/17/2001
Appraisal	n/a	02/25/2002
Approval	05/30/2002	05/30/2002
Effectiveness:	08/15/2002	08/15/2002
Restructuring	n/a	
Mid Term Review	n/a	
First Tranche	08/15/2002	08/15/2002
Second Tranche	12/31/2003	12/07/2007
Closing	12/31/2003	12/15/2007

Source: Project documents

3.2 Ten conditions were met for first tranche release in 2002. The second tranche release date of December 2003 was not met and a series of ten extensions were granted, starting with three in 2004 alone, of 1, 2 and 9 months each. The 2004 BAC survey review showed little progress towards the second tranche conditions. In May 2007, a second survey showed that all targets had been attained except for the targets for business registration. A final (tenth) 6-month extension until the end of 2007 was approved in June 2007 so that the fulfillment of the target for registrations could be verified.

3.3 It is notable that the Presidents Report (page 18, para. 54) provided for separate release of the Second Tranche to FBiH and RS. "As the onus is on each Entity to achieve these goals, disbursement of the second tranche will be made independently to each Entity upon fulfillment of its second tranche conditions." The implementation of the operation seems to have set aside this provision which might have accelerated disbursement.

3.4 As stated previously there were serious delays in meeting certain of the second tranche release conditions (for implementation of business registration and for inspections) which required exceptional approvals beyond 2 years extension. With the initial extensions granted in 2004 it was already becoming clear that the timetable for complex legal and regulatory reforms was unrealistic within an environment of fragmented Government, including an election. The one month extensions were interim measures designed to trigger a specific action by the Authorities which would in turn justify a further extension. For example in 2005 such an extension was granted while efforts were made to fulfill the conditions on business inspections which would itself be a condition of restructuring the final tranche into two tranches with revised conditions. The final extension granted in June 2007 allowed 6 months to verify that registration targets had been fulfilled using the new business registry which itself had been affected by a delay in finalizing the IT system. The end-of-project report provided to DfID on the Business Registration capacity building stated reservations about the Bank's approach.

> "The original project timetable was, in hindsight, highly optimistic and the project had to be extended on many occasions. Although some of these extensions were unavoidable, experience shows in some cases they were based on planning assumptions which were still optimistic given the user environment and the authority and capacity of user and project team resources to deliver. Moreover, when extending the project, new deadlines tended to be set in short units (3 months at a time), whereas effort on all sides could have been better spent on achieving and managing success in a more flexible, longer planning period. It is also worth noting that project stakeholders were not always encouraged to prioritize work on this project ahead of other tasks simply because of tight deadlines imposed."

3.5 While one month extensions had reportedly been effective for the previous Enterprise and Bank Privatization Adjustment Credit which was linked to an IMF standby loan, the BAC operation did not have the equivalent leverage. The DfID report implies that the Bank's policy towards time extensions impacted somewhat negatively on the consortium efforts.

Parallel funding support to implementation

3.6 The support of the bilateral donor agencies was key to the implementation of the BAC. Concurrent and follow-up support was provided in a series of capacity building projects which followed on from either the 2001 FIAS study recommendations or were coordinated with the requirements of the BAC operation over the period of its implementation. A summary of support is as follows:

Table 4. Details of Complementary Donor Capacity Building Support

Agency	***Activity Covered***
DfID	Business registration. Legal assistance and development and implementation of IT system 2005 to 2007 Training of court personnel in registration system. 2006 to 2007

USAID	- (PRP) Pledge Registry Project, 2002-4, laws on secured transactions, equipment - (JSDP) Justice Sector Development Project. 2004-8; capacity of High Judicial and Prosecutorial Council, courts, State Ministry of Justice, judicial sector - (FILE) Fostering an Investment and Lender-friendly Environment, 2003-6; project: training of judges, bankruptcy trustees; case management software. -(SPIRA) Streamlining permits and Inspection Resources Assistance project, 2004; Equipment, systems development, software, and training. - (TARA) Tax Administration Reform Assistance project. Unified tax system.
SIDA	Trust fund for supporting Training of Inspectors. Assistance to inspectors from 2003 (for 9 line ministries) in RS and FBIH, including training and equipment.
GTZ	Assisting Justice Ministries in reform and redrafting of bankruptcy law, land registry, and public notary regulations.

Source: IEG Field visit

3.7 Active support from the Office of the High Representative (OHR) of BiH was also important in the preparation of the business registration, bankruptcy and pledge registry laws, and amendments to laws such as that for Chambers of Commerce. The OHR used the device of a 'Bulldozer Committee' during 2000 to 2001 to push through a number of reforms.

3.8 There was a consensus that a good level of cooperation between the Bank team and the donor agencies was achieved in view of the critical post-conflict situation in BiH and the difficulties of a fragmented Governance structure in the country. The principal agencies involved were as follows:

3.9 *DfID* was primarily concerned with Business registration. It developed the linked IT system required in the registration process, and it conducted training of court staff in the use of the system. Because of delays in enacting legislation system development started late and was only rolled out in 2006. Problems occurred because of the tardiness or opposition of some cantons in FBiH to adopting the system. To ensure sustained operation additional 'handholding' would have been helpful. However, by 2007 the system was up and running throughout most of FBiH and RS. Subsequently there was some backtracking as adjustments had to be made; the link between the courts and the tax authorities was not continuous and more recently disputes between RS and FBiH arose over data entry limited the system's capability. Thus, the performance of this component of capacity building was not problem-free but the objectives were largely met after a lengthy delay.

3.10 *USAID* had an extensive complementary involvement in BiH over the period of the BAC operation. This included provision of equipment and training under a Bank Development and training project, the Pledge Registry Project, a project to training judges and bankruptcy trustees, the SPIRA (Streamlining permits and Inspection Resources Assistance) project, a project to provide inspection equipment, and the TARA (Tax Administration Reform Assistance) project. Field interviews suggested that the work on inspections and collateral registration had been very good with some minor difficulties. The collateral registry has been described as a 'revolutionary' innovation in that it considerably speeded up the pledging of security for lending. The inspections IT system has been established as a model of its type.

3.11 *GTZ* played a small role, providing expertise for the preparation of the new Bankruptcy law (as well as the land registry and justice Ministries). It also supplied expertise in product quality and trade to the Chamber of Commerce. In field interviews with members of the judiciary its work on the bankruptcy law was regarded as good but needing additional regulations and procedures to ensure its effective operation.

3.12 *SIDA* provided a Trust Fund managed by the Bank from 2003 for training and equipment to support inspectors in nine line ministries in RS and FBiH, prior to the establishment of the central inspectorates. No report was issued on this input but it provided substantive inputs to inspection programs in the labor and market area.

Major Factors Affecting Implementation

3.13 Key to *the* problems of implementation were the complex governance and legal *arrangements* in BiH. The system established post-Dayton involved a federalist structure *balancing* political and ethnic interests, resulting in a state, two entities, one district (Brcko), ten cantons, and 142 municipalities. The State government is responsible for foreign policy, trade and transport, and monetary policy. The RS and FBiH Entity Governments have the remaining powers outside those of the State.

3.14 The *fragmentation* of authority created challenges to any reform process, especially where a common approach was needed in the complex transition to a market economy. The ICR reports that the two Ministries of Justice faced a considerable legislative burden while the inspections reform alone required the creation of completely new Directorates across 9 ministries in RS and 8 in FBiH. While initially there was some acceptance of the need for a State-based solution, these difficulties could not ultimately be adequately managed by the coordination mechanism, and the Bank's lack of direct control over capacity building made the fulfillment of specific quantitative targets more burdensome.

3.15 One of the features of the implementation period, the so-called Bulldozer Committee, was set up to push through changes. The committee operated for about a year over 2000-2001. While this mechanism was efficient at accelerating decisions it also risked unintended results where the apparent resolution of one issue resulted in the uncovering of others.

3.16 The attempt to harmonize six laws (on inspections, business registration, foreign investment promotion, collateral, chamber of commerce, and bankruptcy) in FBiH and RS faced resistance not only from groups opposing a unified State Government. Two other interests were the residual opponents to market reforms, and a Government bureaucracy concerned to avoid possible job losses associated with the reforms.

Implementation of the M&E framework

3.17 The project's set objectives were the five PDOs, and there was no detailed results matrix.

3.18 The baseline survey of administrative and regulatory costs of doing business in FBIH was conducted in 2002 to identify implementation targets. To verify PDO achievement interim surveys were carried out with donor assistance in 2004 and 2007. The three surveys used the same sampling criteria in order to standardize results. The 2007 survey reported on the progress of business registration and inspection reform actions as these were the two final sets of conditions as yet unfulfilled. The presence of field-based Task Team members meant that the project had relatively close supervision and close coordination with other donors providing the technical assistance necessary for the implementation of the reform program.

3.19 However the six monthly monitoring surveys by the Ministry of Foreign Trade and Economic Relations (MTER) that were supposed to assess reform achievement against targets were not in fact carried out. This was stated to be because of a) lack of progress to report during 2003-5 and, b) lack of funding which had been expected to be provided by the Government. Since specific output targets had to be met the lack of regular monitoring and reporting may have made achievement more difficult, while the lack of funding may be an illustration of the difficulties of coordinating key elements of the broad program.

4. Achievement of the Objectives

Interpretation of the Objectives

4.1 As stated in 2.1 to 2.3, the formal objectives of this project were operationalized using specific quantifiable targets as set out in the tranche release conditions of the policy program. Assessment of ‘achievement of the objectives’ is therefore conducted within the framework of the formal objectives through an assessment of the achievement of the specific targets. Each objective and their accompanying outcomes are assessed in the below sections.

- Objective 1: Reduce administrative and regulatory barriers with the most critical near-term impact on the three phases of business development;
- Objective 2: Streamline the environment for business operation;
- Objective 3: Facilitate business exit. Underlying these objectives is the need to strengthen the consultative capacity between the public and private sectors to promote policies and legislation that are business-friendly.

Note on Attribution and assessment of outcomes

4.2 The outcomes of the BAC actions (as in the case of other adjustment operations) are difficult to directly attribute because of time lags, multiple causation and exogenous factors. The outcomes were partly linked to the Bank policy dialogue and advisory work but also to the capacity building assistance and advisory work provided by the participating donors, as well as to the ongoing action by the various Governmental Authorities. The outcomes have also been affected by global conditions such as the 2008 financial crisis. In the following sections the parallel capacity building by the donors is assessed along with the Bank’s input. To be able to assess the scale of the outcomes that are attributable to the BAC it is also necessary to identify a counterfactual. There is no direct counterfactual for regulatory policy action because it is taken by a unique actor (the Government). However, possible comparators could be the action taken by Governments of countries similar in terms of geography, history and economic transition status. Therefore comparable policy changes in other former republics of Yugoslavia are examined side by side with those of BiH, where available and informative.

Objectives and Outcomes

4.3 The following sections are organized according to the four main objectives. Each objective is assessed by project component and given a rating based on performance. Each component also receives a rating. Both short term and longer term outcomes are assessed. The key policy outcomes of the operation assessed below impact the three phases of business development: (i) business entry, (ii) the business environment, and (iii) business exit. Additionally, strengthening public-private policy dialogue is also addressed.

Objective 1: Reduce administrative and regulatory barriers with the most critical near-term impact on the three phases of business development.

4.4 This entails improving business entry through streamlined and transparent countrywide approach to business registration and licensing and strengthened legal framework and capacity for attracting foreign investment. Project components include business registration reform and reform of the Foreign Investment Promotion Agency (FIPA).

OUTCOMES OF BUSINESS REGISTRATION REFORM

Background: Inputs and Outputs

4.5 The acceleration of the business startup process was one of the two key interventions of the BAC operation. The 2001 Bank (FIAS) study found that the registration procedure was too long, with lack of mechanisms to ensure consistency and control, no data transparency or sharing, and too many, often illogical and unnecessary steps. The BAC conditions required that a pilot of the business registry system was tested in selected courts across RS and FBiH, and a plan for its full implementation adopted. In addition the Entities were to reduce the average number of days to start a business from 80 to 30 days or less in FBiH and from 31 to 23 days or less in the RS and to reduce the number of steps required to register an enterprise to 7 or less, as measured by independent surveys.

4.6 A Statewide framework law on business registration was adopted in 2004. The law went further than the BAC second tranche condition. It mandated a maximum of 5 days for court business registration after all documents were submitted, and limited the number of required steps to seven. The new laws also introduced some simplifications of the verification process. Both FBiH and RS adopted business registration laws on the basis of the State-level framework Law. The process unified registration within a shared registration database.

4.7 By 2008, eight out of ten courts were using the full registration system, the exceptions being Mostar and Central Bosnia cantons. The registration system did not start as quickly in

RS due to a case backlog, and to speed up compliance with the BAC condition the authorities started using the new system before the backlog was cleared. The court in Banja Luka was using the full system by November 2007, although the RS courts had to stop using it later while changes were made to the data links.

Donor Contribution

4.8 DfID provided a grant of about $1.6 million to implement the business registry system. Faced with three systems for registration of legal entities and a spate of fictitious registrations it was decided to address both legal reform and registration process. The team worked on the Framework State law with Members of Parliament in FBiH and RS and on the Entity laws adopted in 2005 and regarded this as an example of positive bipartisan cooperation. The project then focused on designing and procuring software and hardware, and training judges and system administrators in its use. The development of the IT system was completed with some delay at the end of 2006 and the hardware was installed at 16 locations. The installation of software at 3 locations was reportedly completed in January 2007. The project trained 67 officials from 16 courts on how to use the system by April 2007.

4.9 While the targets were ultimately met there remained a number of operating problems, which could perhaps have been solved by longer term support by the donor agency. The RS tax department stated that the new data links were not supported by updated procedures, and duplicated forms still had to be filed in each agency. There was a reluctance to share data between Government entities. Another widely cited problem was failure to fully complete forms or the inconsistent interpretation of forms. A further issue has been the requirement for notary clearance, which is seen widely as costly and superfluous, and from some views an illegitimate amendment to the State law.

4.10 The DfID consultants report concluded that while it was delayed the final achievement was a good example of locally-led development and sustained commitment. However, some interviewees thought that the closure of the project was premature, and there were some differences of opinion as to how far the IT system is workable due to disputes over data entry between RS and FBIH, which might have been avoided with a longer period of outside support.

SHORT TERM OUTCOMES

4.11 Progress was made in registration efficiency compared to the 2002 baseline up to May 2007, as can be seen from the table.

Table 5. Business Registration Reform Progress

	Entity	***Baseline 2002***	***Mid-term 2004***	***May 2007 Survey***	***Dec 2007***
Average days for registration and startup	FBIH	80	63	44	27
	RS	31	30	32	18
Steps required to register business	FBIH	10	7-8	n/a	5
	RS	9	7-8	n/a	5
Number of steps to start	FBIH	15	10-12	n/a	8-10

operations	RS	14	9-11	n/a	8-10
Source: Baseline Study; Midterm monitoring study, BAC survey, Registry data					

4.12 At the end of the project period, between May and December 2007, the total time required to startup a business showed a marked decline. The BAC project used Registry data as the confirming evidence and this showed that by the end of 2007 court registrations were being completed in an average of 8.5 days. The court in Banja Luka was reported as registering new enterprises in three days. These improvements effectively reduced the overall time for business startup to below the target set for the BAC project. The number of steps needed to register a business and to start operations also fell, in line with the new law, which improved on the BAC performance target of 7 steps for registration.

4.13 The recorded reduction in court registration days reduced the overall days needed to start a business as follows:

Table 6. Days Required to Start a Business

	Days to start business May 2007 (PULS Survey)	***Days to start business (December 2007) (Registry data)***
Court Registration	21.0	8.5
Statistics Recording	4.3	4.3
Municipal license	5.8	5.8
Revenue/ Customs Certification	4.8	4.8
Pension/insurance arrangements	3.1	3.1
Total	39.0	26.5
Source: PUSL survey and Business Registrar data		

4.14 Responses from the business community were mixed. The Foreign Investors Council (FIC) claims that first time registrations have been taking 5 to 20 days in court, and re-registrations sometimes longer. It also cites absences by judges, inconsistent judgments and demands for additional documents not required by law. Sometimes repeated requests for additional information are made and suspensions of registration because of unrelated parallel legal action.

4.15 Interviews were held with a sample of ten enterprises in FBiH and RS. In RS there was a consensus that business startup takes longer than the reported level, and that 26 days was the 'best case.' In one case court and tax registration took 28 days but only when the judge was 'chased.' NGO registration can require several months wait because a very small proportion of time in the commercial court is allocated to this category. In other cases small errors in documentation were said to have led to unnecessary rejection of an application. Overall however the enterprise respondents agreed that procedures have speeded up more recently in the courts. It is the other areas, such as tax administration, work permits, customs and VAT that are now regarded as more critical.

4.16 In contrast to the skepticism of the business community, the President of the District Economic Court in RS stated that 80 percent of court registrations are completed in 3 days and 20 percent within 5 days provided all documents are in place. A case backlog in 2009 was caused by the need for enterprises to re-register, but the situation has improved since commercial courts opened in the RS in 2009. RS currently plans to further simplify business registration. An inter-departmental working group was formed in 2012 to evaluate the regulations. Changes will probably include online registration and strengthening of the link between courts and tax administration. The Court President in Sarajevo also emphasized that the business registration initiative had been successful. A very large previous backlog of 3200 cases per 1 economic judge had been reduced to 25 cases. Court time that had previously been as much as a year was reduced potentially to a single day if full documentation was provided.

The extent of accelerated registration in the longer run can be cross-checked with the estimates of the World Bank's Doing Business Reports alongside the reported improvement levels of the BAC.

Table 7. Longer Term Outcome: Business Registration Time

	Government entity	*Base line 2002*	*Mid-term 2004*	*2007 Dec*	*2007*	*2008*	*2009*	*2010*	*2011*	*2012*
Avg. days for registration and startup	FBIH	***80***	***63***	***27***						
	RS	***31***	***30***	***18***						
	DB report		68		63	63	69	69	64	40
Number of steps to start operations	FBIH	***15***	***10-12***	***8-10***						
	RS	***14***	***9-11***	***8-10***						
	DB report		12		12	12	12	12	12	12

Source: World Bank Doing Business report and BAC survey

4.17 The Doing Business reports are not in fact consistent with the reports for the operation. The days and the number of steps required for starting a business over 2007-11 according to the Doing Business reports were significantly greater than those reported for the BAC and unchanged from the high 2004 level in FBiH, with a significant reduction only from 2012. The reason for inconsistency was not ascertained but there are inconsistencies in definition and sample size that might explain it. [2] Otherwise it appears that the improvement in registration as a result of the BAC might have been overestimated. This inconsistency further confirms that while the Doing Business is a convenient tool to quickly measure some regulatory reforms, it has important limitations.[3] Consequently it cannot be viewed as a measure of the quality of the investment climate.

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[2] The Doing Business Report findings are based on smaller samples than either the 2007 survey or the registry records.

[3] See IEG 2008

4.18 A measure of outcome is the rate of new registrations (the rate of business entry). To assess the relative scale of the outcome in BiH it may be compared to similar reforms in a group of comparator economies in South Eastern Europe, who received similar outside assistance.

Table 8. Starting a Business in South Eastern Europe 2007 to 2012

	Change in number of procedures	***Change in number of days required***	***Change in cost (percent of per cap. income)****
Bosnia	no change	minus 41%	minus 64%
S.E. Europe	minus 41%	minus 47%	minus 26%

Source: World Bank Doing Business Reports. * This was not part of the BAC conditions

4.19 The table shows that BiH performed less well than the average of six other countries.[4] This was particularly so in the case of the number of procedures (where BiH had zero improvement) but also in the number of days. All comparator countries improved significantly compared to BiH on time and steps required except for Kosovo. However, BiH showed better performance in terms of the reduced cost of starting a business. The results are ambiguous but Bosnia still remains one of the most difficult locations for starting a business.

LONGER TERM OUTCOME

4.20 In the longer term the outcome and impact of the new system is observable however not so much in the improvement in the registration process but more in the effects it has on actual registrations and startups. The Statistical Office provided the following data.[5]

Table 9. Longer term business registration performance

	2004	***2005***	***2006***	***2007***	***2008***	***2009***	***2010***
Total	30618	33290	36206	38913	41722	43619	45317
Total annual increment	***3127***	***2672***	***2916***	***2707***	***2809***	***1897***	***1698***
Of which							
Manufacturing	4035	4342	4665	4923	5202	5358	5474
Construction	1928	2043	2215	2389	2536	2574	2597
Trade, repairs	9831	10563	11221	11815	12347	12617	12765
Catering	653	692	729	796	848	873	953
Transport,communication	1912	2026	2130	2241	2373	2421	2472
Real estate, other	2510	2761	3039	3325	3651	3930	4149
Social/personal services	4857	5724	6791	7808	8885	9841	10794

*Source:*Federal Statistics Bulletin, various years.

[4] Albania, Serbia, FYR Macedonia, Montenegro, Kosovo and Croatia. These countries are a reasonably close match with BiH in terms of scale, geography, post-conflict problems, and transition from central planning.

[5] Court registry records are also available over 2008 to 2012 but a reclassification on January 1, 2011 distorts the trend in activity.

4.21 The above series, which excludes agriculture, public administration, education and health, shows a downward trend in annual registrations since 2007 when the Registry was launched reflected across all sectors shown. However this was in common with all countries who experienced a sharp drop in business entry during the 2008 financial crisis and the drop was correlated with the severity of the crisis.[6] The effects of the financial crisis make it impractical to trace up to now a longer term outcome in terms of business entry activity attributable to the BAC.

Summary of Business Registration Reform Attribution and Outcome

4.22 The outcomes are attributable to both the BAC's output and the capacity building from DfID. The systems development funded by DfID was an essential complement to the Bank's catalytic role, without which it is probably unlikely that the Government would have been able to implement the new system. Positive outcomes in terms of reduced registration time and cost were achieved but the data on earlier results are ambiguous and the benefits were significantly delayed due to problems in implementation. By 2012, five years after the project closed, a substantial reduction in court registration time had finally been confirmed and the scope for further reduction in startup time is outside the court process. Nevertheless, taking South Eastern Europe as a comparator Bosnia's business registration process improvement was modest. In the longer term the effects of the reforms on actual business registrations are obscured by the economic crisis which reduced the number of annual registrations.

4.23 Taking account of all the above factors the rating of the business registration reforms is **Modest**

OUTCOME OF REFORM OF THE FOREIGN INVESTMENT PROMOTION AGENCY

Background: Inputs and outputs

4.24 The BAC conditions provided that the State should adopt amendments to the decision on Foundation of the Foreign Investment Promotion Agency and allocate funding for its operations; that the Entities should adopt Foreign Investment Laws harmonized with the State Law on Policy of Foreign Direct Investment (FDI), and that FIPA representative offices should be staffed and operating in FBiH and RS.FIPA would need to expand its operations and collaborate closely with State, Entity, Canton and local governments to promote further investment across BH.

4.25 Prior to the launching of the BAC a Promotional Agency had been established in 1996 and a State Law on Policy for Foreign Direct Investment was adopted in 1998, drafted with the assistance of FIAS. However the Agency that was initially established faced difficulties. The amended law on the Foreign Investment Promotion Agency (FIPA) was

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[6] Source: 'Entrepreneurship and the Financial Crisis' Leora Klapper and Inessa Love World Bank 2011

adopted in 2004, establishing FIPA as a State-level agency. Amongst changes was the abolition of the ethnically based system for rotating General Managers, and its replacement with a Board comprising a majority of private sector representatives, with a sustainable financing base.

4.26 The revamped FIPA was initially established on a lean basis in 2002 with a small staff of 7 and a budget of about €0.22 million per annum. Branch offices were successfully set up in Mostar and Banja Luka despite their opposition to a State level initiative. Following the re-launch in 2004 the number of staff employed rose by 2012 to 28 under a director, out of which 22 were in the main office and a small staff in the branch offices. The annual Budget which is funded by the Government stands at a significantly increased €1.6 million according to FIPA data.

4.27 The work of FIPA, reorganized in accordance with the BAC condition, is divided into a) provision of data, information, analysis and advice on business and investment, b) identification of investment opportunities, including startup opportunities, privatizations, and local companies seeking foreign partners, and c) assistance to investors through linking with governmental and non-governmental institutions. FIPA offices, including Sarajevo, Banja Luka and Mostar, are operating with full staffing. The branch offices are used mainly for promotion and preparation for investor visits while the central office deals with the main investment promotional work.

4.28 Under the BAC a baseline foreign investment level was established at 4.3 percent of GDP but there was no actual performance target set. By the end of the project period (2007) the FDI rate rose significantly, as shown in the table.

Table 10. Foreign Investment Achievement

	Baseline 2002	***Target***	***Actual 2007***
Foreign Investment % GDP	4.3%	n/a	13.7%

Source: ICR

4.29 Beyond the BAC conditionality on the FIPA and the review of legislation provided for the 2001 Bank (FIAS) study [7] the Bank's main engagement in this action was providing a review of the new law. The Bank made representations to the Government to ensure that the Board of FIPA remained under private sector control in accordance with its letter of Development Policy.[8]

[7] The policy law was designed to promote foreign direct investment and to protect the rights of foreign investors seeking to establish business enterprises, and established guidelines for related laws and regulations by RS and FBiH entities.

[8] Letter of September 16th 2004 from Country Manager to Parliament objected to the appointment of the Head of the Foreign Trade Chamber as a member of the Board. The Law as currently published retains the Trade Chamber member and thus retains a majority of public sector members.

Donor Contribution

4.30 Assistance was provided initially by IFC (FIAS) and the EU, and latterly at a smaller scale from UNCTAD, USAID and NORAD. Assistance consisted of initial funding of advisory staff, equipment, materials and the design of promotional programs. The Office of the High Representative was instrumental in supporting the State Law.

SHORT TERM OUTCOMES

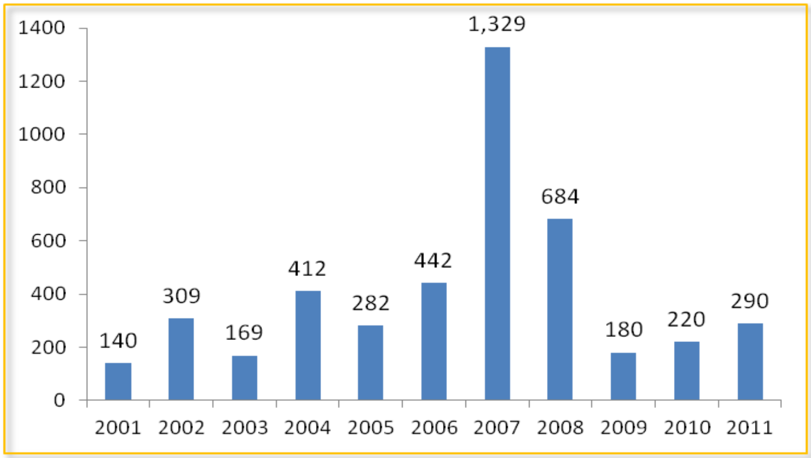
4.31 FIPA management stated that the organization faces challenges caused by: a) poor communication between Government agencies, b) a lack of project proposals due to concerns about the business climate, c) a still excessive number of steps required to start up business, especially at cantonal and municipal level, and d) presence of corruption around existing regulations. Outside stakeholders including the FIC confirmed that, despite its expansion FIPA faces such difficulties because the FBiH and RS Entity Governments are reluctant to fully support a State level Institution even though both Entities adopted the original Law on foreign investment. A number of interviewees also suggested that the agency needed to have a more proactive program to deal with the difficulties faced by investors due to the general business climate.

LONGER TERM OUTCOME

4.32 The longer term outcome is in terms of FIPA's effects on investment, including longer term effects on processing time, and total investment flows.

4.33 There was a considerable increase in foreign investment as a percent of GDP between 2002 and 2007, originating especially from Russia, Austria and Serbia. Even though no causal relationship is implied by the increase in investment and the presence of the upgraded FIPA the increase was consistent with the presence of a professionally established promotional service. However the 2007 investment level was inflated by large deals including the sale of RS Telecom and investment in oil refining and with the 2008 financial crisis it reasserted a much lower long term rate of about 4 percent of GDP, slightly less than the baseline.

Figure 1. Gross Foreign Direct Investment



4.34 Data provided by FIPA on numbers of deals being processed show that there has been a significant increase since 2007 in numbers of transactions characterized by a large number of investments at the minimum capital level but a decline in both total and average value.

Table 11. Long Term Foreign Investment Performance

	2007	*2008*	*2009*	*2010*	*2011*	*2012 8 months*
Total Transactions	1158	1185	945	3769	4992	3162
Avg. time to start business (days)	12-54	12-60	12-60	12-55	12-40	11-37
Avg number of steps to close	9-30/45	9-30/45	9-30/45	8/30-45	8/30-45	8-30/45

Source: Ministry of Foreign Trade & Economic Relations, Doing Business Reports and FIPA

4.35 The transactions and values in the above table are discontinuous between 2009 and 2010 because of a change in the basis of estimate. They show a decline in transactions over 2007 to 2009 followed by a rise in 2010 to 2012. The maximum time required to start a foreign investment operation has fallen while the number of steps has remained the same.

4.36 An alternative overall indicator of the environment for foreign investors in BiH comes from the Doing Business Report on 'protecting investors.'

Table 12. BiH: Performance on Protection of Investors

	2006	*2007*	*2008*	*2009*	*2010*	*2011*	*2012*	*2013*
Over Protection Ranking	..	..	..	..	..	..	98	100
Extent of disclosure (0-10)	3	3	3	3	3	3	3	3
Director liability (0-10)	6	6	6	6	6	6	6	6
Shareholder suits (0-10)	6	6	6	6	6	6	6	6
Investor protection (0-10)	5	5	5	5	5	5	5	5

*Source:*Doing Business Reports, various years

4.37 According to the table over 2006 to 2013 the position of BiH did not improve in terms of these four indicators of investment attractiveness.

4.38 To assess the performance of FDI while controlling for the external factors such as the financial crisis we can examine comparative FDI data for the seven South Eastern Europe economies of the Former Yugoslavia. In this respect, the relative FDI inflows in BiH fell from the 2007 peak when BiH was in third place in the group as a recipient of FDI to sixth place ahead of only FYR Macedonia in 2011. Serbia and FYR Macedonia also experienced a relatively small decline in FDI after 2008 but the decline in BiH was significantly steeper than these two economies. The longer run position of BiH following 2007 has not yet recovered and it remains the second smallest recipient. Even bearing in mind the broader global issues affecting investment, prima facie this is not consistent with the presence of a highly effective investment agency.[9]

Summary of FIPA Reform Attribution and Outcome

4.39 The attributable output of the BAC operation is in terms of the new State law and the push for increase in the capability of FIPA. There is no evidence of an improved outcome – that is in terms of actual FIPA capability. Some respondents felt that FIPA was not operating effectively and FIPA itself cited weak support from RS and FBIH Governments and an adverse business environment as preventing it from achieving success in mobilizing investment. In the longer run the changes in levels of FDI up to 2007 and subsequently are not directly attributable to FIPA, nor indirectly to the BAC operation. However what evidence there is on the value of investment does not suggest a highly effective organization.

4.40 The rating of the FIPA reforms is **modest.**

4.41 The overall rating for Objective 1 on improving the environment for business entry is **modest.**

Objective 2: Streamlining the environment for business operation.

4.42 This comprises reducing companies' administrative and regulatory compliance costs through rationalization of inspections and regulations, strengthening of judicial and extra-judicial capacity to resolve commercial disputes; and, improving enforcement of secured transactions. This objective was implemented through inspection reform, collateral/pledge registry, and reform of the chambers of commerce. Strengthening of the courts was also addressed under objective 1 (i.e. the simplification of the court process for business registration).

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[9]World Investment Report 2012 (UNCTAD)

OUTCOME OF INSPECTION REFORM

Background: Inputs and outputs

4.43 The system of inspections was identified in the FIAS study as an important bottleneck for business operation in FBIH. The BAC conditions required that RS and FBiH establish regulations for a business inspection system that rationalized mandates, procedures and schedules of the inspectorates. They also required that the average number of aggregate on-site inspector days per business per annum for the Market, Labor, Financial Police and Revenue Administration, would be reduced from 28 days to 15 days or less in the RS and from 18 days to 12 days or less in FBiH.

4.44 The Entity Governments adopted inspections laws in 2005 which set up unified Inspections Directorates and they adopted action plans for inspection reform.[10] The laws defined the mandate of the inspectorates and set out inspection schedules and guidelines.[11] The new system became operational in March 2006 in RS and in January 2007 in FBiH. About 26 different inspections from 8 Federal and 9 RS ministries were concentrated into 10 inspection areas under a single Inspections Directorate, including market inspections (prices, safety, intellectual property, consumer protection) and labor inspections (safety at work, labor contracts etc).[12] The Inspectorates report direct to Cabinet, maintaining a degree of independence from Parliament and the Civil Service.

4.45 The targets of the BAC were difficult to implement because of initial opposition from the line ministry inspectorates. While the IT system was established relatively quickly in 8 cantons, Central Bosnia and Mostar were holdouts. From 2009 when it became operational the independence of the inspectorates, especially in the FBiH have also come under pressure from the line ministries who wish to regain control. The FBiH inspectorate has accordingly cut some links with the remainder of the Government service and kept its staff off the Civil Service payroll.

4.46 There was a significant reduction in both numbers of inspection visits and number of days required by the time that the project was closed in December 2007, improving on the targets set out under the BAC, in both FBiH and RS. A 2007 survey [13] found that the average duration of inspections was 7.5 days in RS, and 9.9 days in FBiH. The survey found that the proportions of firms that received inspections, the distribution of the number of inspections, inspectors and days of inspections among the different types of inspectorate were similar in the RS and FBiH. The percent of enterprises inspected in FBiH was reduced from 65 percent

[10]The RS inspectorate employs about 320 staff of which 230 are actual inspectors, of which there are 13 chief inspectors for the main areas of inspection. The BiH inspectorate holds a similar capacity

[11] The Law regarding duration of tax inspection visits states that they should not exceed 10 days for large enterprises and 7 days for all others, and that control should not exceed 15 working days from the date of control inception.

[12]In addition there are included inspections for agriculture – phytosanitary; forestry, veterinary, water, technical – oil/gas, mining, geological, electro-energy, thermal, professions, traffic, surface, and postal.

[13] 2007 enterprise survey was of 302 enterprises. It was conducted by PULS of Sarajevo (now IPSOS).

in 2005 to 25 percent in 2007. The highest number of inspections per annum was conducted by the labor inspectorate, while the revenue administration inspectors stay the longest average time per visit. The achievement under the BAC operation's performance targets were as follows.[14].

Table 13. Inspection: BAC targets and achievements

	Baseline	*Mid-Term 2004*	*Actual 2007*	*Target*
Number of onsite inspection days per enterprise per year	FBiH 18 RS 28	FBiH 12 RS 15	FBiH 9.9 RS 7.5	FBiH 12 RS 15
Source: BiH and RS directorate				

Donor Contribution

4.47 Two outside donors provided the bulk of capacity building support to the BAC. SIDA set up a Trust Fund in 2003 managed by the Bank to support the training of nine line ministry inspectorates, prior to the formation of the inspections directorates. USAID supported the new unified inspectorates. It provided through the SPIRA project programmers to work on software development. It also trained inspectors and hosted conferences (such as 'safety at work'). The Agency provided 85% of the cost of IT system including servers, computers, printers and software and also provided vehicles released from other projects.

SHORT TERM OUTCOMES

4.48 The short term outcomes of this action are assessable in terms of the savings to firms from the more efficient inspection system. These have been estimated as substantial. [15] While the inspections reduced the burden on enterprises the centralized system also allowed other benefits such as crosschecking of records. According to the ICR this allowed illegal workers to be either incorporated into the system or laid off. [16]The Inspectorates quickly proved to be an important means of monitoring the informal economy and increasing tax revenue.

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[14]The data for 2007 are based on 'regular' inspection days. They include income tax inspections but not VAT as it had only just been introduced.

[15] The ICR estimated direct savings from this of KM 10.4 million per annum for companies that were inspected plus saving from reduced frequency of inspections of KM 15.79 million. The economic benefits for the recipient companies, assuming that one employee is designated to deal with an inspection visit, amount to an average of 28 days per annum (page 14-15).

[16] The ICR reports that during the project life the RS inspectorate identified nearly 8% of workers in firms visited as illegal and registered an additional 5,000 workers. The FBiH Pension fund identified 60,000 additional workers resulting in KM 70 million paid to the Fund. About 25,000 unregistered workers, representing about 12% of total formal employment in FBIH, who had been illegally receiving benefits, were de-listed from the unemployment bureaus.

4.49 The Chamber of Commerce in RS considered that the common database was an important improvement provided that it was kept updated. Clarity of rules is allowing less scope for abuse. On-the-spot reports entered in the field and warning notices for compliance rather on-the-spot penalties were a major step forward.

4.50 Ten enterprises were interviewed about inspections in RS and FBIH. Their criticisms were limited mainly to tax inspections [17] where in some financial institutions complex inspections had increased the costs to firms.[18] There was some criticism about the rationality of fines imposed for violations of labor regulations, and about non-standard interpretations of the Law. Market inspections were regarded as most problematic, with complaints about lack of clarity on the jurisdiction of the Entity and Cantonal inspectors. Some respondents thought that the actual inspection days exceeded the officially reported numbers. However overall inspection efficiency was seen to have improved and the time/cost burden on enterprises reduced because of the unified inspections and the common database.

4.51 Since the conclusion of the project both RS and FBIH have introduced web-based inspection systems. In the case of RS a Regulatory Guillotine program was conducted in 2006 to streamline inspections further, and an inspection program was developed for 2007-2009 to systematize procedures. [19] Following the conclusion of the BAC operation a new law in 2010 adopted a standardized inspection procedure and introduced a state-of-the-art Information Management System[20] using a risk-based process. Under this system simultaneous inspections are mandatory and data entry is done in the field. Checklists and procedures for inspections are published on the website and are therefore open for enterprises to inspect. Enterprises are able to file complaints about the system, improving commitment to it. [21]

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[17] A particular complaint was regarding the VAT inspections (which were not covered by the BAC as the system was introduced later). The complexity of VAT rules results in a need for experienced inspectors of which there are too few. In one case the VAT service suspended a rebate while its inspector was said to have 'camped' for several weeks in an exporting company's offices to understand how it did business. BEEPS survey results show a large increase in annual days spent dealing with taxes between 2005 and 2009 most likely due to the introduction of the VAT.

[18]One firm was obliged to rent office space for a tax inspection liaison unit. A firm that had set up a coffee dispenser for its staff was told that it would have to pay the fee applicable to an independently established coffee house. An inspector confiscated items because they were not adequately labeled (but there was not enough space to provide the full label). A firm was fined for incomplete paperwork – it appealed and won its case but has received no remedy. A fish products exporter had to provide to customs 'fish for analysis' even though all relevant inspections had been completed.

[19]www.inspektorat.vladars.net/registar

[20] The system has been demonstrated outside the country – e.g. in Mongolia.

[21]Customers have used the system to lodge complaints, usually against other competing enterprises rather than the inspectors. The RS complaint line had 14,000 complaints over 5 years about failure to follow market and labor standards (e.g. hiring illegal workers).While some corruption is thought still to exist this system is reported to be a major improvement from the previous one.

4.52 The overall improvement is reflected in a BEEPS survey in 2009 where out of a total of 360 enterprises, 288 (80%) found inspections either no obstacle or a minor one. Only 7 percent found them to be a severe obstacle.

4.53 The reason for the success of inspection reforms was a combination of: 1) a high level of interest in the reforms (after initial hesitation) from both BiH and Respublika Serbska (an unusual situation); 2) the expectation that such reforms would potentially boost Government revenues; 3) the change in focus from punitive to supportive; 4) and the interest in the technology and the high caliber technical assistance which promoted it.

LONGER TERM OUTCOMES

4.54 The longer run outcome would be measurable in the reduced cost to enterprises for a given level of compliance with the regulations, leading to higher profits and growth. Data for FBiH since 2007 shows that both the number of inspections and infringements has been reduced which is consistent with a more efficient process. At the same time the percent of violations per inspection has also fallen suggesting that the benefit of a reduction in the time burden on firms has been achieved with the same level or better compliance.

Table 14. Inspections Results for BiH

	2007	***2008***	***2009***	***2010***	***2011***	***2012 1st half***
Border control inspections	134543	138934	122065	118735	111574	5773
Inland control inspections	25063	14476	25907	16486	12586	43168
No of Violation penalties	6687	11476	12524	5366	7301	1720
Change in number of inspections		-3.9%	-3.5%	-8.6%	-8.2%	-21.2%*
Penalties as share of inspections	4.2%	7.5%	8.5%	4.0%	5.9%	3.5%
Value of Penalties (KM million)	4.03	10.07	9.86	4.93	6.97	2.01

Source: BiH directorate

*Annualized

4.55 While the result over the period 2007 to 2009 did not show any clear direction, since 2009 there have been significant reductions in the number of controls at the border and inland, in the number of penalties, and in the number of control decisions issued which suggest that the move towards fewer inspections and a less penal and more advisory control regime has been effective. This is consistent with the objective of reducing burden relative to compliance level.

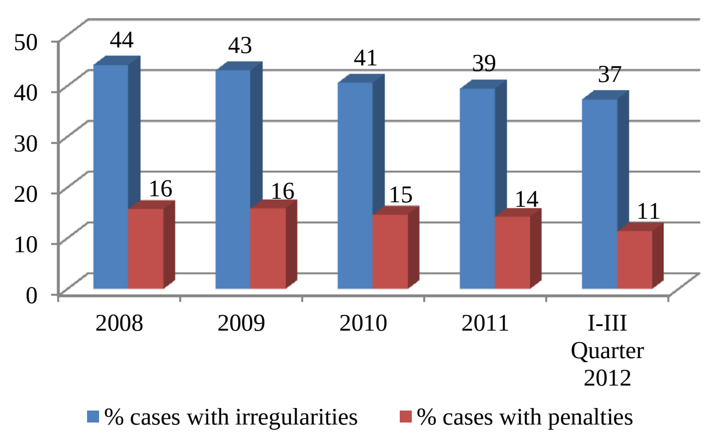
4.56 The RS directorate also provided data for this report on inspections over 2008 to 2012. The source and type of data are not directly comparable with those of FBiH but the direction of change is still instructive.[22]

[22] The inspections Directorate was unable to provide data on average time taken per enterprise per year to compare with the BAC targets This was because inspector time recorded combined time on and off-site.

Table 15. Inspection Results for RS						
	2007	**2008**	**2009**	**2010**	**2011**	**2012 (to Oct)**
No of inspection visits	1121	1353	1668	1415	1508	1351
No of violations reported	113	67	150	262	354	264
Change in number of inspections		20.7%	23.3%	-15.2%	6.6%	-10.4%
Penalties as share of inspections	10.1%	5.0%	9.0%	18.5%	23.5%	19.5%
Total value of fines imposed (000 KM)				224.0	301.0	270.0
Source: RS directorate						

4.57 Unlike FBiH the table shows a slight decrease in inspection visits, but a rise in the number of violations reported. There was a downward trend in the inspections burden through the lower incidence of irregularity and penalty imposition, the latter falling from 16 percent to 11% of inspections. At the same time the data show a slight increase in the average duration of onsite inspections since the introduction of the web-based system in 2010.

Figure 2. Level of Inspection Irregularity



Source: RS directorate

Summary of Inspection Reform Attribution and Outcome

4.58 The reform of the inspections system was the result of capacity building efforts mainly by USAID assisted by the BAC's initiative in regulatory reform and performance targeting. The reforms were of major importance and resulted in requests for a follow-up project (under the ICIS). Beyond the completion of the BAC in 2006 the IFC Regulatory Guillotine followed up with additional regulations and procedures. The longer term outcome, i.e. a reduced cost of inspections for a given level of compliance, leading to higher profits, seems to be occurring but usable data are not available on costs of inspections, only indicative data on time savings. The results from RS are less easy to interpret as they show increased inspection time but reduced irregularities. Despite the lack of usable data the consensus of all interviewees for this report, Government and private, was that the inspection reforms had on balance been positive for business profitability and growth, and the new systems also provided a spinoff benefit in building of local software development expertise.

4.59 The rating of the inspection reforms is **high**.

OUTCOME OF INTRODUCTION OF COLLATERAL/PLEDGE REGISTRY

Background: Inputs and outputs

4.60 The introduction of the Registries was a requirement for the enhancement of secured lending. The BAC conditions required that a Pilot of the collateral registry system and trained participants (judges, clerks, and bank officers) would be tested in selected courts across both FBiH and RS and a plan for full implementation would be adopted.

4.61 Prior to the formalization of legislation on movable collateral the mechanisms used had included guarantors, salary deductions and mortgages. A Law on Secured Lending had been adopted in 2000 and the further need for effective procedures including a pledge registry was identified in the 2001 Bank (FIAS) study. A state-level framework Law on the Pledge Registry was adopted and it became operational in November 2004 under the State Ministry of Justice. There was initial opposition to the State law from RS but this was dropped later when the utility of the pledge mechanism started to become understood. Some respondents held the view that the law, which is currently at State level, should be brought to the RS/FBIH Entity level.

4.62 A unified statewide system of pledge registries now allows secured transactions through centralized information on all collateral posted. Movable assets that can be pledged include equipment, vehicles, livestock, products and materials, intellectual property and accounts receivables. The main users of the system are banks, MFIs, leasing companies, notaries, lawyers, and enterprises entering into contracts with other entities. Pledge certificates are also usable by the Courts to collect on debts in the event that the pledged asset is not available. Registration is renewable each year up to the point at which the underlying obligation to the creditor is fully redeemed. Deregistration occurs once the obligation is fulfilled.

Donor Contribution

4.63 USAID under its Public registry Project installed the system and provided training of judges and registry staff in the use of the registry software. There were minor issues in an otherwise apparently successful project (e.g. capacity building did not initially include the transfer of software codes which would have required significant additional cost). The sustainability and positive benefit of the USAID assistance are shown in the fact that the Ministry of Justice in FBiH has embarked on a two year follow up project to expand the system using its internal USAID-trained staff and its own funds.

SHORT TERM OUTCOMES

4.64 The key short term outcome of the registry project was its effects on cutting the time and cost of borrowing which was regarded as significant (since the costs of establishing loan security through the courts were passed on to the borrower). However it was not possible to obtain quantitative estimates of cost saving.

4.65 To gauge these effects qualitatively interviews were held with a number of Government offices and a major bank.[23] The pledge has been more difficult to enforce in some cases than tangible assets such as real estate and usually both types of assets are required. However the collateral registration system was regarded as providing an effective and important new channel for secured lending, with on-line registration and avoidance of the court process.

4.66 A further short term outcome was the effect on the level and growth of registrations. The number of registrations during the project period following the adoption of the Law, and for the five years since the closure of the project, is as follows.

Table 16. Numbers of Collateral/Pledge Registrations and searches

	2005	***2006***	***2007***	***2008***	***2009***	***2010***	***2011***	***2012 to Sept***
Pledge registrations*	11170	10223	10677	13778	12058	17163	16433	13266
Registry searches	10912	10368	15833	19806	17581	21511	24103	17349

Source: Collateral Registry* One registration may include up to 5 distinct items to be pledged

4.67 By 2012, there were 1,371 active users of the system, and a total of over 106,000 cumulative registrations. Data were not available on the number of de-registrations. The numbers of new pledge registrations and registry searches showed an increase over 2005 to 2012 of 7 to 8% per annum. This rate of growth of new collateral registrations outpaced that of other comparable indicators and suggests a shift to this form of secured lending

LONGER TERM OUTCOME

4.68 The key longer term outcome of the registry system is in terms of its effects on the expansion of secured and total lending. However, no data showing the effect on lending could be provided either by the financial institution interviewed or from sector data on bank lending. The Business Environment and Enterprise Performance Surveys (BEEPS) did not show a rise in use of movable assets as collateral and they showed a slight fall in collateral overall as a percentage of the amount borrowed. The main exception was in the case of the pledging of accounts receivable.

[23]Raiffeisen bank

Table 17. Percent of firms using various collateral		
	2005	***2009***
Land, buildings	63.7%	69.9%
Equipment	35.4	34.4
Accounts Receivable	7.1	12.4
Personal accounts	21.2	14.2
Other	9.7	13.5
Source: BEEPS surveys		

4.69 To gauge the size of the long term secured lending outcome comparator data from the Doing Business reports show public credit registry coverage in South Eastern Europe. Public registry coverage in BiH was zero up to 2009, after which it increased to reach 36 percent of all adults by 2012. The public registry replaced some limited private credit bureau capacity already established. Apart from BiH only Albania and Montenegro are using the public registry route, both slightly behind BiH in terms of expansion of coverage. However progress while positive, is still relatively limited in all three. The other South East European countries (Slovenia, Serbia, FYR Macedonia and Croatia) have emphasized private credit bureaus, and all four have made relatively rapid progress near to or at 100 percent coverage over the past five years.

Summary of Collateral Registry Reform Attribution and Outcome

4.70 The pledge law was a catalyst for an important improvement in secured lending which was component of the improvement of business operation. The BAC had an overarching role in this respect while capacity building by USAID as in other cases was an essential complement to the WB's initiative. The Central Register was the first such system to function across both FBiH and RS and as such was instrumental in encouraging the set up of other State-wide institutions. The benefits of the collateral registry are not yet apparent in the longer term in terms of secured lending but are considered to have been effective in reducing borrowing cost, which would translate into higher profits for borrower and lender. In comparison with other states of South Eastern Europe using public registries BiH has shown good results.

4.71 The rating of the collateral registration reforms is **Substantial**.

OUTCOME OF REFORMS OF CHAMBERS OF COMMERCE

Background: Inputs and outputs

4.72 As part of the support to improve the business operating environment the BAC conditionality required that FBiH and RS adopt amendments to the Laws on Chambers of Commerce to eliminate mandatory membership. The Chambers of Commerce were artifacts of the central planning system of the former Yugoslavia, operating with central, regional and sectoral branches designed to act as an interface between the State and a business community that was mostly under State or collective control.

4.73 The reform of the Chambers was one of the measures taken up by the so-called 'bulldozer committee' run by the Office of the High Representative, and adopted by the BAC. Obligatory membership in the chambers of commerce system was abolished through amendments in 2003 to the FBIH and RS laws on the Chambers of Commerce.

4.74 The purpose of the measure was to reduce the influence of what was regarded as an outdated institution not providing added value to the business sector and to allow voluntary Business Membership Organizations (BMOs) to develop. The amendment was opposed by the Chamber leadership in both RS and FBiH. In discussions in the field the RS Chamber claimed a double standard whereby the new Foreign Trade Chamber was allowed to retain compulsory membership and thereby enhance its position vis-à-vis the Chamber of Commerce. The FBiH Chamber claimed that the freeing of national membership was ineffective because entry membership is at the Cantonal level and has remained compulsory.

Donor Contribution

4.75 Capacity building assistance was not provided in connection with the BAC since the purpose was to weaken the Chambers. This was a cause for complaint by the RS Chamber who nevertheless applied for and received assistance under an EPA program for GTZ to fund training of staff. This diversified the Chamber' services but showed some lack of donor policy coordination.

OUTCOME

4.76 In the RS as a result of outreach efforts membership and fee revenue recovered slightly after 2004 and fees stabilized at about half of their former level. The Chamber diversified, introducing new services such as training in quality standards, and trade seminars, although these are regarded by enterprises interviewed as of only moderate quality. Service revenue increased in relation to membership fees, reaching about 50 percent of the total. The RS Chamber managed to avoid layoffs and expand, bringing in new staff. The FBiH Chamber also tried to diversify into training programs in standards, corporate governance, and product law.

4.77 The FBiH Chamber has been superseded to a large extent by the private voluntary Employers Association that has been given the role of the Government's formal dialogue partner within the FBiH Social and Economic Council (see below). In RS the Chamber remains the formal dialogue partner of the Government within the Council.

4.78 As a result of continuing opposition the RS Chamber re-established compulsory membership in 2009, although fees remain voluntary and payment can only be encouraged through denial of access to services. FBiH is also now contemplating the reintroduction of compulsory membership and the measure has been under Parliamentary consideration for some time. The reintroduction of compulsory membership is a reversal resulting from a less than well-conceived policy change.

Summary of Chamber of Commerce reform attribution and outcome

4.79 The BAC condition was designed to help improve the operating environment for business. It had a direct effect on weakening the position of the Chambers of Commerce vis-à-vis other BMOs, which was its intention. This in turn allowed scope for private BMOs to develop such as the Employers' Associations. However, the measure was not well conceived, partly because it was pushed forward with inadequate forethought by the OHR and was then adopted under the BAC. As a result there has been a partial reversal, though the effects of this reversal are not yet clear.

4.80 The rating of the Chamber of Commerce reforms is **Negligible**

4.81 The overall rating for Objective 2 (improvement of the business operating environment) is **modest**.

Objective 3: Facilitating business exit.

This implies facilitating business exit through improved bankruptcy and liquidation systems.

OUTCOME OF REFORMS OF BANKRUPTCY LAW

Background: Inputs and outputs

4.82 Bankruptcy practice was identified by the 2001 Bank (FIAS) study as a significant, if not major, problem for enterprise development in BiH. The BAC conditions were that entities should establish a working group to draft new harmonized bankruptcy laws and should adopt the strengthened and harmonized Laws on Bankruptcy and Liquidation.

4.83 While the Law in the FBiH was up to date, developed and adopted in 1998 with the assistance of USAID, the system in place in the RS was still based on the laws of the Former Yugoslavia in which bankruptcy orders were issued by judges based on relatively arbitrary assessments of rights to assets. New bankruptcy laws for the FBiH and RS were adopted in 2003 based on a Western (German) model allowing for reorganization and proportional compensation according to rules of priority. The Bank was active in asking for an amendment to the Law in 2004 to facilitate privatization by restricting workers' priority compensation packages.[24].

4.84 The laws were passed amid union protests. This pressure prevented the FBiH authorities putting SOEs into the bankruptcy process whereas RS created a Trust Fund which provided for a notice period (60 days) and sent laid-off workers to employment bureaus. Given the opposition of the trade unions and the complexity of governance the adoption of the bankruptcy and liquidation laws was however a signal achievement. [25]

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[24] Compensation was reduced from an unlimited period to 6-9 months of minimum salary and contributions and mandated a maximum of two months for laying off of workers

[25] Acceptance by the employees was assisted by the Government decision to make back payments of overdue SOE wages at the time that the amended laws were being introduced.

Donors Contribution

4.85 The drafting of the new Bankruptcy law adopted in 2003 was assisted by GTZ (now GIZ) who also provided assistance for regulations on land registration and notaries. The USAID FILE project provided follow-on assistance with training of judges and bankruptcy receivers.

SHORT TERM OUTCOME

4.86 The short term outcome of the new bankruptcy legislation can be identified in terms of the level and growth of bankruptcy cases, and the rate of resolutions under the new system. From 2005 the new bankruptcy filings rose from less than 100 to over 200 per annum in FBIH, and from 121 to over 200 per annum in RS. The number resolved each year has not quite kept pace with the number of new filings, though occasionally exceeding it (in FBIH in 2007 and RS in 2005 and 2008). A jump in unsolved cases has occurred since 2010.

Table 18. Bankruptcy Filings

	Entity	*2005*	*2006*	*2007*	*2008*	*2009*	*2010*	*2011*	*2012 1st half*
Unsolved at start of year	FBIH	188	214	237	230	277	303	315	347
	RS	311	225	261	289	288	289	365	377
New Filings	FBIH	93	105	92	135	188	198	236	91
	RS	121	141	174	164	171	257	217	59
Cases Resolved	FBIH	66	84	95	88	167	183	204	64
	RS	207	105	146	166	170	197	205	46
Resolutions/new filings %	FBiH	71%	80%	103%	65%	89%	92%	86%	70%
	RS	171%	74%	84%	101%	100%	77%	94%	78%

Source: HJPC annual reports for 2005, 2006 and 2007.

4.87 In both FBiH and RS the number of resolutions as a percent of new filings has on average remained below 100% leading to a steady increase in the number of unresolved cases despite the increase in the number of actual resolutions, suggesting that further capacity is required in the RS economic courts and in the economic division of the FBIH courts. This seems to support the2012 Doing Business report (p97) which shows that the time required for the resolution of insolvency has not been reduced (see below). The cost of insolvency procedures as a percentage of the average value of an estate has also remained the same, at 9 percent, and recoveries have averaged a relatively stable 35 percent of asset value.

4.88 While the Law was successfully adopted there have been problems with its practical outcome. In particular, delays by enterprise managers in filing have allowed enterprises to run down to the point where reorganization is no longer a practical option, and wage arrears cannot be paid. The court presidents in both RS and FBIH agreed that the proportion of enterprises that were reorganized was too low.[26] The trustee is regarded as an 'enemy' depriving the workers of rights, and there is a danger of weakening the justice system because of the pressure on politicians to intervene. [27]

4.89 Once in bankruptcy the length of time required for winding up an enterprise has also frequently been significantly extended by out-of-court disputes over claims. The FIC has criticized several aspects of bankruptcy practice. [28] There is a consensus that additional training is needed for bankruptcy judges and receivers, and improved incentives for the judiciary to become involved in the special and difficult problems of enterprise reorganization.

LONGER TERM OUTCOME

4.90 The Doing Business Rankings provide longer term indicators of the progress in the bankruptcy practice.

Table 19. BiH: Bankruptcy Performance Indicators

	2005	***2006***	***2007***	***2008***	***2009***	***2010***	***2011***	***2012***	***2013***
Rank	..	..	..	..	..	..	78	84	83
Time (yrs)	3.3	3.3	3.3	3.3	3.3	3.3	3.3	3.3	3.3
Cost (% of estate)	8	9	9	9	9	9	9	9	9
Recovery rate %	32.7	32.6	34.3	35.5	35.9	35.9	34.7	35.0	35.4

Source: Doing Business Reports: Various Years

4.91 These indicators show that the time required to complete the bankruptcy process has remained at 3.3 years while the cost and recovery rate have also remained about stable over the past few years. To assess these results the table shows BiH results against a comparator set of countries of South Eastern Europe (Albania, Croatia, FYR Macedonia, Serbia and Slovenia).

Table 20. Bankruptcy Process Indicators: Country Comparisons

	Indicator	***2004***	***2013***
BiH	Time (years)	3.3	3.3

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[26] The Court President cited 300 cases of bankruptcy since 2007. Out of these only 25 companies had been reorganized and the remainder had to be closed. There was considered to be a lack of accountability of management to trustees and workers.

[27] Threats have been made against senior members of the judiciary involved in SOE bankruptcy cases.

[28] Among many proposals the FIC wants to strengthen liquidation rules; clarify documents to be submitted to court; obtain a provision to allow titles to be transferred to Financial Institutions. It regards Bankruptcy proceedings as too lengthy; training is inadequate; courts lack resources; receivers are of variable quality and should have stricter entry qualifications; there should be larger penalties for managers who file late. Source: FIC White Book (p66)

	Cost (% assets)	8.0	9.0
	Recovery rate %	32.7	35.4
S.E. Europe	time (years)	2.36	2.22
	Cost (% assets)	13.2	11.8
	Recovery rate %	32.9	38.2
Source: Doing Business Reports			

4.92 Over the last 10 years the average time required in BiH has not improved. It remained the longest compared to the average of six comparator countries where, on the contrary, improvements have been recorded. Bankruptcy cost in BiH has remained low at between 8 and 9 percent of estate value although it has risen recently. The BiH recovery rate has improved over the period but less so than for the comparator countries.

Summary of Bankruptcy Reform Attribution and Outcome

4.93 The BAC intervention acted as a catalyst for the reform and development of the Bankruptcy laws, assisted by complementary capacity building from bilateral donors. Attributable short term outcome was in terms of an increased rate of filings and resolutions but there were unresolved problems associated with the operation of the Law (now being addressed by the follow-up ICIS operation) which suggest that a more sustained approach would have been advisable including further building of judicial capacity to enforce it. There is also a rising backlog of unresolved cases and an increase in cost per case relative to comparator countries. Longer term outcomes have not been positive since system performance has not improved over five years since the end of the project.

4.94 The rating of the bankruptcy reforms is **Modest.**

4.95 **The overall rating for Objective 3 on facilitating business exit is Modest.**

Objective 4: Strengthen the consultative capacity between the public and private sectors.

4.96 This implies improving the policy dialogue for business operation and leveling the playing field for private sector participation in public procurement.

OUTCOME OF REFORM OF PUBLIC PRIVATE POLICY DIALOGUE (PPD)

Background: Inputs and outputs

4.97 Improvement in the policy dialogue was part of the attempt by the BAC to improve the environment for business operation. Prior to the establishment of a formal process, discussions between Government and the private sector occurred irregularly and infrequently, often with the management of the largest and most influential firms, including loss-making state-owned enterprises. The BAC conditionality required that Entity Governments establish a mechanism for regular consultation with the private sector to consider their views in the formulation of policies and legislation affecting business. This involved inter alia replacing the traditional Chamber of Commerce-based process. A formal process was established as a result of the PRSP of 2000, consisting of a Social and Economic

Council in FBiH which was created in 2002 and devolved to Cantonal level. A similar entity had existed in RS since 1997 and was ratified by a Law in 2008.[29] However there is not a State level Council.

SHORT TERM OUTCOME

4.98 As stated previously, contrary to the intent of the BAC, the RS Chamber was retained within the public-private dialogue as formal partner of the Government and Labor bodies, to some extent crowding out the new private Employers Association (founded in 2001). The RS Chamber participates in standing committees on business issues. Parliamentary draft bills are usually sent to the Chamber for comment and in some cases it has managed to get decisions reversed–for example in the case of a water tariff. The Chamber receives advance notices of relevant debates and participates in the preparation of subsidiary legislation.

4.99 The FBiH Chamber by contrast lost part of its authority to the Employers Association (founded in 2002) which now sends delegates to meet with the Government and the Unions. The FBiH Employers Association, which has 90 percent private membership, has been given the right to join the parliamentary working groups and examine draft laws.

4.100 An alternative, informal, channel of dialogue, the Foreign Investors Council, was founded in 2006 with the assistance of USAID. Currently the FIC supports 34 investors with a further 8 expected to become members. It produces a regular policy ‘White Book’ with proposals for policy changes and it has an arrangement with the FBiH Prime Minister’s Office to hold 3 monthly meetings on White Book proposals. It has also arranged visits by the Prime Minister to member companies.

4.101 While formal dialogue mechanisms have been created, interviews with firms suggested that the initial interest in the Social and Economic Councils had weakened because of lack of preparation and structure, ineffective moderators, and lack of a specific agenda. Dialogue has also been limited in some views by reluctance on the Government side to expose itself to the scrutiny of private business or the media whom it fears will look for evidence of malfeasance, whether justified or not.

Summary and Attribution of Action to support policy dialogue

4.102 While the level of dialogue has improved, apart from setting a requirement to setup a mechanism, interviews suggested that The BAC did not itself play a significant role in establishing the Public-Private Sector dialogue and therefore any improvement cannot be attributed to it. The new mechanism was actually set up through the previously formed Economic and Social Councils, the FIC with USAID support, and the IFC through its Regulatory Guillotine process. The overall outcome attributable to the BAC has been less

[29] The Law on the Economic and Social Council (Official Gazette of the Republic of Srpska, no.110/08) was adopted in 2008.

than satisfactory because of the continuing influence of the Chamber in the RS and the apparent lack of material support to the Economic and Social Councils.

4.103 The rating of the PPD registration reforms is **Modest.**

5. Ratings

Outcome

5.1 Based on the aforementioned rankings the overall outcome attributable to the BAC operation is rated **Moderately Unsatisfactory** (MU).

5.2 The operation's objectives were substantially relevant, while the relevance of the design and efficacy were modest. The BAC operation supported the establishment of economic reforms that were consistent with the overall reform agenda. There were three major constraints identified in BiH, namely: (i) absence of an adequate legal and regulatory framework to establish and operate a business; (ii) lack of consistent and transparent business regulations and administrative procedures; and lastly, (iii) lack of effective, efficient, and adequately funded administrative and judicial systems. Progress was achieved through reforms made to business registration, the Foreign Investment Promotion Agency (FIPA), inspections, the collateral/pledge registry, bankruptcy law, and public-private policy dialogue. While objectives were consistent with Government strategy to improve the business climate, the project design allowed for a relatively short timetable for disbursements relative to the capacity development needs of a post-crisis transition economy. There were 38 separate policy and institutional development actions that had to be met. Additionally, the project design focused on the use of specific short-run outcome targets rather than on overall effective systems. At the same time, complex governance and legal arrangements coupled with fragmentation of authority posed challenges during project implementation. While progress was made in achieving targeted outcomes, the project had significant and persistent delays with no amendments to the operational objectives of the BAC. Taking all of this into account, IEG rates the outcome **moderately unsatisfactory**.

6. Risk to Development Outcome

6.1 The President's Report for the BAC listed the main risks as, (i) the complex governance structure of Entities, Cantons, municipalities and cities; (ii) the possible loss of momentum due to elections; and (iii) opposition from both inherited Socialist attitudes and emerging vested interests in the current system. It asserted that these risks were manageable. In the case of registrations it considered the risk minimal because the Cantonal and regional courts would receive equipment and training. Surveys would be conducted to monitor the costs of doing business and guide reform toward release of the second tranche. Furthermore risks would be minimized by donor-funded local economic development initiatives. Finally, the coordinating authority, Coordination Board for Economic Transition and European Integration, would reduce risk by providing continued support for the reform program and the Governments' anti-corruption programs and many of the laws, regulations and structures set up under the operation would mitigate the risk that vested interests may oppose change.

6.2 On the basis of the outcomes that have been spelled out in section 4, these risk mitigation assurances were largely not fulfilled and the risks to the reforms going forward remain largely similar. Firstly, based on local discussions there remains a *significant risk* of weak support for continuing reforms because of political opposition to State level changes. Secondly, there is a *moderate risk* of erosion or reversal of previous reforms especially if opposition (e.g. from Cantonal Governments) is allowed to continue or develop, as occurred in the case of the business registry and the Chambers of Commerce. Thirdly, there is a *moderate* risk of the degrading of capacity in the regulatory bodies overseeing systems such as business inspections and the business register. Fourthly there is a *moderate risk* of erosion of compliance with legal and regulatory processes which may degrade legislation such as the bankruptcy process, and the independence of the inspection system.

6.3 The level of risk to development outcomes when applied to the already marginal outcomes of the BAC, rated MS, would mean that the risk-adjusted expected value of development otucmes could plausibly fall to MU.

6.4 These risks can only be mitigated through responsiveness to technical and organizational problems and close, sensitive and time-intensive, supervision with continuity of expert support. The current support program of the Bank, including the Investment Climate and Institutional Strengthening (ICIS) Project is however proceeding with an awareness of these lessons, which is likely to improve the prospects for sustained positive benefits going forward.

6.5 The risk rating for the sustainability of Development outcomes is **Significant**.

Bank Performance

Quality at Entry

6.6 The strategic relevance of the operation was largely satisfactory and in line with the economic reform objectives.[30] However the realism of the reform targets laid out was flawed because a lengthy period of capacity building would be needed to fulfill reform objectives in a post-crisis transition economy. This was aggravated because the capacity building to implement the critical reforms was in the hands of donor agencies rather than being part of operation.

6.7 The choice of instrument was a two-tranche adjustment operation. The policy areas addressed by the operation were supported by a large number of specific policy conditions, including 18 policy triggers in two Entity Governments for second tranche release. The timetable was very short relative to the capacity development needs, considering the environment and risks of political opposition. The capacity to implement the reforms was also to be managed through parallel funding by donor agencies and the operation involved complex oversight arrangements. The Coordination Board for Economic Transition and

[30] As an adjustment operation it did not have explicit environmental, gender and social development or fiduciary requirements.

European Integration was inadequate to deal with the political opposition that emerged later, as a result of the continuing stand-off between FBiH and RS and their opposition to State level institutions. Considering the unknowns at project entry the analysis of risk and the results framework were insufficient. However, it must be noted that the BAC was designed during a 'window of opportunity' when post-war progressive governments were in office in FBiH and RS who wanted to take ambitious action, and there appeared ex ante to be reasonable grounds for supporting them. The objectives were also supported by sector studies that were used to identify reforms and was consistent with a strategy of going for 'early wins.'

6.8 The rating for QAE is **Moderately Unsatisfactory.**

Quality of Supervision

6.9 A QAG panel in September 2006 assessed the supervision of BAC as Highly Satisfactory overall.[31]This was largely because the Bank's management team was regarded as doing a very effective job in the particularly difficult implementation environment, and the findings of this report concur with that assessment. Much effort was made, largely from the local office, to push through the reforms and achieve the targets. The QAG assessed the focus on Development Effectiveness and Supervision Inputs and Processes as Highly Satisfactory, while Supervision of Fiduciary/Safeguard Aspects and Candor and Quality of ISR dimensions were rated Satisfactory. The QAG cited the timely and proactive problem solving approach with the project being actively supported by Sector and Country management. The QAG panel on the other hand identified a lack of client commitment, and inability to reach consensus between Government entities and stakeholders as underlying causes of persistent delays in implementation of Second Tranche measures.

6.10 However, despite the high rating by QAG it is questionable why the operation received satisfactory performance ratings in every supervision report except for one in March 2005. The second tranche release date of December 2003 was not met and a series of ten extensions were granted, starting with three in 2004 alone, of 1, 2 and 9 months each. The 2004 BAC survey review showed little progress towards the second tranche conditions. In May 2007, a second survey [32] showed that all targets had been attained except for the targets for business registration. A final (tenth) 6-month extension until the end of 2007 was approved in June 2007 so that the fulfillment of the target for registrations could be verified.[33]

Table 21. ISR Ratings of the Operation

Date	*DO Rating*	*IP Rating*
07/01/2002	S	S
12/30/2002	S	S

[31] QAG Quality of Supervision Report 2006

[32] BAC Review, PULS Consultants (now IPSOS), May 2007

[33] The final, tenth, extension notification to the Government was sent in June 2007

06/19/2003	S	S
11/05/2003	S	S
06/17/2004	S	S
12/21/2004	S	S
03/24/2005	MU	MU
10/21/2005	MU	MS
06/27/2006	MU	MS
04/28/2007	MS	MS
12/27/2007	S	S
Source: project documents		

6.11 The final ISR rated the overall outcome as Satisfactory. The ICR rated the operation as Moderately Satisfactory because the cost of the delays weakened what it concluded were otherwise satisfactory outcomes. This cost was however mitigated, it argued, because the delays permitted an institutional learning process which improved the outcomes.

6.12 The reasons given in the ISR for the reduction to an MU rating in March 2005 were as follows:

> While both Governments are achieving progress in attaining the targeted outcomes, these achievements are being done with significant and persistent delays. The team expected both inspection and business registration laws to be adopted by both Parliaments at the beginning of 2005, with inspection and business systems in place and functioning by the end of March 2005. The efforts on establishing these systems are financed by different donors, DfID, USAID and SIDA - and they stand ready to start systems implementation, which is linked to the formal adoption of the legislation. To date, the Federation Government has already adopted both laws, while the RS Government is targeting adoption of the laws by March 25, after which the State Government is planning to apply for further project extension of one month to accommodate Parliamentary proceedings. If the adoption by both Governments does not take place by the end of March, the team recommends providing no further extension of the closing date of the project (ISR/03/24/2005).

6.13 A proposal was made subsequently to restructure targets so that implementation could be completed more easily, but this did not in the end go ahead. While the March 2005 ISR recognized that the delays were becoming a serious issue the problem could have been understood and addressed prior to this. The sense within the project team was that credit was due for progress achieved in a difficult environment. However progress should be gauged against targets rather than against starting points. For this operation the targets were being missed by a wide margin. It would therefore have been justifiable either to put the project into the unsatisfactory category where it would get special attention as a project at risk, or to restructure it through revision of the targets.

6.14 The multiple brief extensions may have given the impression to the Government that the lending conditions were negotiable ex post. The approach to extensions was also not necessarily supported by the cooperating donors. The lack of adherence to the target dates may have been aggravated by the lack of a fully developed results framework and indicators to guide the implementation of the operation. Intended half-yearly monitoring surveys which might have better highlighted the problems in meeting targets were not carried out. In 2005 a proposal was made to management to restructure the tranche release conditions but it was not adopted. While the President's Report foresaw the risks of implementation delay in practice they were very difficult to mitigate despite the close on-the-ground supervision effort by the project team. Thus the high quality supervision effort, noted by the QAG, could not offset the problems of deciding whether targets should be adhered to, dropped or extended.

6.15 Taking the above points of a) flaws in the design of implementation but b) the considerable efforts made on the ground to offset these, the rating for supervision is **Moderately Unsatisfactory.**

Rating for Overall Bank Performance

6.16 The rating for the Bank Performance balances a) some design flaws, b) the significant effort to remedy the issues through close supervision, and c) management's willingness, under pressure, to extend the completion deadlines rather than amend the targets. The rating is **Moderately Unsatisfactory.**

Borrower Performance

GOVERNMENT PERFORMANCE

6.17 The Government's performance was significantly affected by elections and changes of Administration during the implementation of the BAC which reduced its level of commitment to the project. Combined with this disadvantage were the following factors: a) the multiple agencies within Government that had responsibility for parts of the project, b) the difficulties of implementing market reforms in a post-conflict environment, and c) the dual Entity responsibility reliant on coordinating committees. The ISRs however reported that the Governmental Authorities were at all times making considerable efforts to push forward with implementation, and only once implied a failure to perform, in 2005 when the project rating was reduced to MU. Delays in delivery of legal reforms and new procedures were a direct reflection of the highly fragmented governance structure and frequent opposition of an Entity or Canton to particular regulatory or procedural changes. While this serves as an explanation for understandable delays it has to be recognized that in the end the Government was not able to satisfactorily meet its commitments.

6.18 Government performance is rated **Unsatisfactory.**

IMPLEMENTING AGENCY PERFORMANCE

6.19 The original coordinators of the BAC were the Ministry of Trade and Economic Reform (in FBIH), and the Ministry of Administration and Local Government (in the RS). However multiple other agencies were also responsible for implementation. These included the full hierarchy of Governing bodies and courts, and numerous agencies such as inspectorates, registries, and FIPA. As a result coordination was often ineffective. The totality of implementing agencies, duplicated in FBiH and RS, were to be coordinated at the top level by Coordination Board for Economic Transition and European Integration. The coordination of the implementing agencies became more difficult with the take-over of Government by non-reformist political groups.

6.20 Implementation agency performance is rated **unsatisfactory.**

RATING FOR OVERALL BORROWER PERFORMANCE

6.21 Based on the above points the overall rating is **Unsatisfactory**

7. Lessons

Lessons and supporting evidence from the Outcome assessment

7.1 BiH suffered from a triple problem: a) the aftermath of civil conflict including the presence of a constitution imposed to settle a conflict rather than to develop the economy; b) the need to transition from a socialized to a market economy, and c) a highly fragmented Governance structure inconsistent with decisive action at the State level. Taking this into account the main lessons were as follows.

- In high risk environments (post crisis, fragmented governance, etc.) an 'early wins' strategy may be required, but should be accompanied by flexibility, early and structured review, and an exit strategy in the event that reforms come off track.
- Formulation of laws in adjustment operations needs to be accompanied by careful attention to addressing implementation constraints, particularly in post-crisis or transition environments, where capacity is particularly weak and the institutional framework is fragmented. Other aspects related to the implementation of the laws needs to be properly addressed in the intervention. In the case of the bankruptcy law for example the legislation needed to be backed up by clearer and more effective enforcement regulations.
- The choice of lending instrument was questionable. Operations that require intensive on-the-ground capacity building are not suitable for pure adjustment-type lending because the adjustment timetable is usually inconsistent with the capacity building timetable. Capacity building projects must be of long duration, especially in a post-conflict situation, to adjust to local conditions and allow sufficient implementation time to build up sustainability. Programmatic lending instruments would be more consistent with these requirements.
- In situations with multiple development partners and significant capacity constraints, effective leadership and coordination, both in Government and development partners, is essential. As shown in this evaluation effective coordination and implementation was undermined by (a) fragmented development partners, (b) a division of labor, with donors providing essential TA, disjoint from WB assistance, and (c) weak capacity and political ownership.

Developments since the operation closed: how have the lessons been taken into account

7.2 The 2007 CAS (Country Partnership Strategy) found that to a significant extent the obstacles facing the business community in BiH remained in place, with BiH being at the low end of the doing business rankings for the sub-region. This remains largely the case. The BiH Doing Business rankings have lagged behind other countries in the region since the closure of the operation. The 2013 Doing Business Report ranks BiH last within the Balkan region in terms of 'ease of doing business' and 126th overall in the World out of 183 countries. BiH ranks in the lower half of the worldwide Rankings in eight reported areas, the only exceptions being access to credit and dealing with insolvency. Some lack of cooperation between FBiH and RS remains apparent from observation although most recently improvements have finally taken place in some areas such as business registration where data was being withheld by one or other Entity. The need for a long term approach to institutional change has however been clearly recognized through the follow-up operations that have taken off from the work of the BAC and are continuing to push forward on a range of reforms.

7.3 These operations have included The *IFC Sub-national Competitiveness Project*, which focused on further regulatory simplification including improved procedures for obtaining licenses and permits and for FDI. This project took account of lessons of the BAC by a) narrowing down the policy reform agenda and b) ensuring cooperation from stakeholders through advanced support for regulatory changes. The *IFC Investment Climate Project* also focused on regulation, especially with regard to agribusiness and was implemented in close collaboration with the private sector with outreach to all levels of authority in order to secure better vertical coordination. The *Improving Investment Climate and Institutional Strengthening Project* has made further changes in quality inspection, registration and bankruptcy, with greater provision for participation of each state entity and of the Cantons (Central Bosnia and Mostar) that did not cooperate with the BAC program.

7.4 In summary the difficulties of supporting complex institutional change in a political divided country were seriously underestimated in hindsight. However many of the design and process lessons of the BAC have been taken into account, in principle, in the coverage and approach of the new generation of projects in BiH, although risks remain and the business environment remains weak.

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Annex A. Basic Data Sheet

BOSNIA & HERZEGOVINA BUSINESS ENVIRONMENT ADJUSTMENT CREDIT (CREDIT NO. IDA 36450)

Key Project Data (amounts in US$ million)

	Appraisal estimate	Actual or current estimate	Actual as % of appraisal estimate
Total project costs	44.0	51.9	1.18
Loan amount	44.0	51.9	1.18
Cofinancing	-	-	-
Cancellation	-	-	-

Cumulative Estimated and Actual Disbursements

	FY2002	***FY2008***
Appraisal estimate (US$M)	19.0	44.0
Actual (US$M)	20.2	51.9
Actual as % of appraisal	106.3	1.18
Date of final Disbursement: December 7, 2007		

Project Dates

	Original	Actual
Initiating memorandum	12/17/2001	12/17/2001
Negotiations	09/09/2001	02/25/2002
Board approval	12/28/2000	05/30/2002
Signing	06/10/2002	
Effectiveness	05/15/2002	05/15/2002
Closing date	12/31/2003	12/15/2007

Task Team Members

Names	Title	Unit	Responsibility/ Specialty
Lending			
Vicki Krecic Peterson	Task Team Leader	ECSPF	
Ulrich Albert Hewer	Program Manager	ECSPF	
Martin R. Slough	Senior Financial Specialist	ECSPF	
Devesh Chandra Mishra	Lead Procurement Specialist	ECSPS	
Senada Havic		CFABB	
Nermina Sljivo		ECCBA	
Yibin Mu	Senior Financial Economist	CCGCM	
Gwen Swinburn	Consultant	ECSSD	
Michel Zarnowiecki	Consultant	ECS-ECA	
Geeta Batra	Head	IBRT	
Hans Shrader	Program Manager	CFA-IFC	
Supervision			
Vladimir Kreacic	Task Team Leader	ECSPF	
Hormoz Aghdaey	Task Team Leader	ECSPF	
John Pollner	Task Team Leader	ECSPF	
Haris Mesinovic	Consultant	ECSPF	
Tarik Sahovic	PSD Specialist	CICRS	
Lamija Hadzagic	Financial Management Specialist	ECSPS	
Nicholay Chistyakov	Senior Finance Officer	LOAFC	
Jasna Mestnik	Finance Analyst	LOADM	
Damir Leljak	Finance Assistant	LOADM	
Van Vu Nichols	Portfolio Officer	ACTCF	
Svitlana Lewis	Resource Management Officer	ECSPF	
Paula Genis	Operations Officer	ECSPF	

Staff Time and Cost

Stage	Staff Time and Cost (Bank Budget Only)	
	No. of staff weeks	USD Thousands (including travel and consultant costs)
Lending		
FY01	27	107.50
FY02	42	197.16
FY03	3	12.56
FY04		0.00
FY05		0.00
FY06		0.00
FY07		0.00
FY08		0.00
Total:	**72**	**317.22**
Supervision/ICR		
FY01		0.00
FY02		0.00
FY03	7	107.06
FY04	19	138.26
FY05	32	80.06
FY06	27	105.78
FY07	22	95.36
FY08	7	58.61
Total:	**114**	**585.13**

Other Project Data

Borrower/Executing Agency:

Follow-on Operations

Operation	*Credit no.*	*Amount (US$ million)*	*Board date*
Small and Medium Enterprise Access To Finance project(First and Additional)	P111780	70.0 120.0	Dec 2009 April 2012
IFC (ICAS) Sub-national Competitiveness project		2.1	June 2007
Improving Investment Climate and Institutional Strengthening project (Trust Fund).		5.0	April 2011

Annex B. List of Persons Met

Bakic, Samir	Assistance to Minister, Federal Ministry of Finance
Baksic, Alija-Remzo	Director, Association of Employers, FBiH
Bejtovic, Adela	Head Of Cabinet, Sarajevo Municipal Court
Bukvic, Nedim	Program Officer, SIDA
Car, Demo	FBiH Inspections Directorate
Cudic, Bojan	Senior Associate, RS SME Development Agency
Grujic, Felica	Director, FIPA (Council Of Ministers)
Hajric, Mirza	General Director, former FIPA
Idrizovic, Mira	Assistant to President, FBiH Chamber of Economy
Komsic, Julian	Director, PULS (IPSOS) Consulting
Korica, Slavica	Exec Director, Promotion & Analysis, FIPA
Kovacevic, Bojan	Senior Legal Associate, RS SME Development Agency
Krunic, Miroljub	Assistant Minister, FBiH Ministry of Finance
Lacevic, Samir	Banks Association of BiH
Milanovic, Savko	Adviser, RS Inspections Directorate
Milin, Vladimir	Development Specialist, USAID
Milunovic, Igor	Dep. Gen Director, RS Inspectorate
Miovcic, Zdravko	Director, EDA Development Consultants
Misic, Mijo	Executive Secretary, Banks Association
Miskin, Natasa	Program Officer, Embassy of Sweden (former of DfID)
Mutapcic, Demaludin	Notary
Omerovic, Bojana	Executive Director, Foreign Investors Council
Prastalo, Gordana	RS Ministry of Finance
Puskarevic, Vojislav	Director, Raiffeisen Bank
Ristic, Dragica	RS Chamber of Commerce and Industry
Salihovic, Goran	Court President, Sarajevo Municipal Court
Surtov, Boris	RS Inspections Directorate
Tirak, Ibrahim	Director, FBiH Inspectorate
Vranic, Goran	Head of Planning, RS Inspections Directorate

Annex C. Borrower Comments