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## NATIONAL COUNCIL FOR EUROPEAN INTEGRATION

# THEMATIC ROUND TABLE ON TRADE, INDUSTRY, CUSTOMS, TAXATION, INTERNAL MARKET, COMPETITION, CONSUMER AND HEALTH PROTECTION KOSOVO 2020

## REPORT

May 2013, Pristina

This report has been developed based on a series of meetings conducted by the Thematic Round Table on Trade, Industry, Customs, Taxation, Internal Market, Competition, Consumer and Health Protection. As such, it is part of a set of documents endorsed by the Task Force for European Integration. The work of the Task Force for European Integration and its Thematic Roundtables, including the preparation of this report, has been supported by Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) through the Project “Support to the European Integration Process in Kosovo”. The views, information and arguments do not necessarily reflect the official opinion of the MEI, GIZ or any other stakeholder to every detail.

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## I. INTRODUCTION

This report aims to come up with a diagnosis of the current state of play in the thematic areas covered by the Thematic Roundtable No. 4 (on Trade, Industry, Customs and Taxation, Internal Market, Competition, and Consumer and Health Protection) within the Task Force for European Integration of Kosovo. Based on the structure and the work processes of this Roundtable, this report is divided in five chapters:

- Chapter 1: Trade;
- Chapter 2: Industry and SMEs;
- Chapter 3: Existence of Functioning Market Economy and Capacity to Cope with Market Forces within the Union;
- Chapter 4: Internal Market; and
- Chapter 5: Customs and Taxation.

Aiming to identify the strengths and weakness in each area, within the European integration framework, this report elaborates the issues related to these areas and summarizes the main strengths and weaknesses which are identified as part of the consultation process with the stakeholders involved in the work of this roundtable. As such, it aims to provide an overview of the opinions, views and assessments presented in the meetings and workshops as well as in different reports and other materials produced by Kosovo Government institutions, business associations, civil society organizations, European Union, as well as donor projects and international organizations in Kosovo which operate in the mentioned areas. The data and information contained in the report are based also on the discussion materials on each area that were drafted before each thematic meeting or workshop. The entire content of the report is drafted during the time period between October 2012 and May 2013.

The first chapter, on *Trade*, begins with a general overview on the trends of trade balance of Kosovo, including overall trade statistics on import and export and the structure of goods exported and imported by Kosovo. The second section is focused on geographical orientation of trade of the country, which summarises the actual state of play in relation to trade relations, the arrangements and trends in trade exchanges of Kosovo with other trading partners (divided in three groups: EU, neighbouring countries – as part of CEFTA, and other part of the world). The third section focuses on relevant legal, policy and institutional framework in the area of trade. This section presents a short overview of legislation (including the main EU *Acquis*) and applicable policies in this area, as well the main institutions and coordinating structures in Kosovo which are responsible for this area (including roles and responsibilities of each of them).

The fourth section of this chapter reviews Kosovo's trade regime, with the main focus on tariff policies, trading arrangements as well trade regulation mechanisms, contingency measures respectively, anti-dumping, counter balancing and protection measures. The last two sections of this document discuss the relations among trade and employment on one side and trade and direct foreign investments on the other side. This report concludes with a summary of conclusions, by listing the

main strategic challenges and recommendations for action in the area of trade.

The second chapter, on *Industry and SMEs*, begins with a short overview on this area, focusing on the size of the SME sector and the industry in relation to the economy of the country and its importance as regarding government policies and efforts related to further development of the sector. It continues with an overview of the legal and policy framework of the sector, which is focused on domestic legislation (laws on SME support, business organizations, inspection services, internal trade, foreign investments, technical requirements and assessment of conformity, general safety of products, trade in oil and petroleum products, tourism and touristic services, economic zones and public-private partnership), as well EU *Acquis* applicable on this area.

Furthermore, the second part of the second chapter analyses the policy framework in this area, with the focus on SME Development Strategy for Kosovo 2012-2016, Strategy on Industry 2010 – 2013 and Kosovo Economic Vision Action Plan 2011-2014, as well as broad aspects of relevant policies, respectively legal and regulatory reforms, the so-called ‘regulatory guillotine’ and Regulatory Impact Assessment (RIA). The part on institutional framework and development is focused on three main bodies, which act under the Ministry of Trade and Industry (Kosovo SME Support Agency, Investments Promotion and Department of Industry) and two inter-institutional bodies (Consultative Council on SMEs and Sub-group on Industry as part of the Working Group on Trade Policies). The last part on implementation and application, discusses a number of main issues: access to finance, entrepreneurial and innovation culture, bankruptcy, informal economy, implementation of legislation for SMEs and EU legislation on Small Businesses.

The third chapter, on *Existence of Functioning Market Economy and Capacity to Cope with Market Forces within the Union*, is focused on five particular areas: market entry and market exit, legal system, human and physical capital; sector and enterprise structure and economic integration with EU. The first section of the chapter, on market entry and market exit, is focused on the reforms undertaken to facilitate the entry to and exit from the market, facilitation of doing business and development of private sector, in general, including also on creation of the *de novo* firms, privatization of Socially Owned Enterprises (SOE) and corporatization of Public Enterprises (PE), as well as direct foreign investments. The last two parts of the first section are focused on the legislation framework and development and the relevant institutions for entry and exit from the market. The second part of the fourth chapter, on legal system, focuses on the property rights and their implementation as well as competition, including aspects of institutional framework and development, which are relevant to this specific area.

The third part, on human and physical capital, is divided in two parts, one on human capital and the other on physical capital. The part on human capital focuses on higher and vocational education and training as well as research, and labour market and employment. The part on physical capital focuses on road infrastructure,

railway, telecommunications, electricity and water sector, as well as on natural gas, public heating and waste management. Both parts cover also aspects of institutional framework and institutional development. The fourth section, on sector and enterprise structure, touches upon the general structure and size of enterprises operating in the Kosovo's economy, specifically focusing on services sector, industrial products (mainly metals and raw materials, such as the goods which are most exported) and agriculture, including the main challenges that development of enterprises and economic growth is facing with.

The last section of this chapter, on economic integration with EU, is focused on trade relations between Kosovo and the EU (which are covered in more details in the report on *Trade*). This section also touched upon particular interrelated issues, such as industrial policies (covered in more details in the report on *Industry and SMEs*), internal market (discussed in more details in the report on *Internal Market*) and customs and taxation (covered in more details in the report on *Customs and Taxation*). This report closes with a summary of conclusions, presenting the main challenges and recommendations.

The fourth chapter, on *Internal Market*, is divided into nine main sections (according to areas), respectively: free movement of goods, free movement of workers as well as the right of establishment and the right of providing services across borders, free movement of capital, public procurement, the right of companies, intellectual and industrial rights, competition policies and consumer and health protection. The first section is focused on particular areas of standardization, accreditation, metrology, conformity assessment and market oversight. The second section of the chapter covers access to the labour market and coordination of social security schemes. The third section discusses particular areas of the right of establishment, freedom of service provision across borders, postal services and mutual recognition of professional qualifications.

The fourth section of this chapter focuses on free movement of capital and payments and payments' system.<sup>1</sup> Further, while the fifth section is focused on public procurement as a whole, the sixth section is focused on the right of companies and company accounting and audit. The seventh section discusses the copy rights and related rights, industrial property rights and implementation of the two categories of rights. The eighth section covers specific areas of state effect on competition, antitrust and mergers, state aid and liberalization. The last section is focused on two specific areas: consumer and health protection. In addition, each of the nine sections is divided in three main parts: the first part focuses on legal and policy framework, the second part focuses on institutional framework and institutional development and the last part focuses on implementation. At the end, a summary list of the main challenges and recommendations is provided.

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<sup>1</sup> The specific area on money laundering is covered by the chapter on Internal Affairs, within the report of the Thematic Roundtable No. 2, on Rule of Law.

Chapter five, on *Customs and Taxation*, is divided in two sections: one on customs and the other one on taxation. The section on customs begins with a short overview on the main developments on this area. Furthermore it describes the legal framework and the relevant policies on this area. In the aspect of legal framework, this section provides an overview on domestic legislation framework on customs and excise, integrated border management, customs measures and protection of intellectual property rights, Value Added Tax (VAT) and foreign trade, as well EU *acquis* applicable in this area. As regarding policy framework, we discuss here the Kosovo Customs' Strategic Operational Framework 2012-2014, Kosovo Economic Vision Action Plan 2011-2014 and Kosovo Trade Policies. The second part of this section discusses the responsible institutional framework in the area of customs, mainly Kosovo Customs. This chapter ends with an overview on implementation in the field in respect to customs.

Similarly, the second part of this chapter begins with a short overview on the main developments in the specific area of taxation. As regarding legal framework, the report discusses the laws that regulate indirect and direct taxation that is implemented in Kosovo: Value Added Tax (VAT), excise, income tax, personal income taxation, corporate tax and property tax. As regarding policy framework, it discusses the Kosovo Tax Administration Strategic Plan 2010-2015, Compliance Strategy 2012-2015, as well as the relevant Kosovo Economic Vision Action Plan 2011-2014, Kosovo Trade Policy, SMEs Development Strategy for Kosovo 2012-2016 as well as Government Programme and Action Plan 2010-2012 on Prevention of Informal Economy in Kosovo.

This diagnostic report ends with a list of names of the representatives of different stakeholders involved in the diagnostic process of the state of play in all areas, and a number of annexes"

- Annex 1: List of the main EU *acquis* applicable to the area of trade;
- Annex 2: List of *acquis* applicable to the area of industry and SMEs;
- Annex 3: List of main EU *acquis* applicable to the area of internal market;
- Annex 4: List of the main EU *acquis* applicable to the area of customs;
- Annex 5: List of the main EU *acquis* applicable to the area of taxation;
- Annex 6: List of goods subject to excise and other respective taxes; and
- Annex 7: Additional information in the area of customs.

## Chapter I: Trade

### 1. Overview of Trends in the External Sector in Kosovo

For over a decade, Kosovo has experienced a very large negative trade balance. Exports have been low, whereas imports were much higher (Table 1.1.). Exports of goods and services reached the peak of over €900 million in 2011, accounting for around 20% of GDP. From early 2000, exports have been growing impressively, albeit from a very low base. Increased export presence of Kosovo's goods and services continued later in the last decade, with the highest leap in 2010 of 35% increase in exports. Their participation in GDP over the period rose from 5% in 2007 to 7% in 2011. Similarly, exports of services performed with an upward trend from 10% of GDP in 2007 to 12% in 2011. On the other hand, imports in 2011 have exceeded the €3 billion mark, accounting for over 65% of Kosovo's GDP. Imports have been growing equally rapidly, at a rate of around 20% in the last few years (except in 2009, resulting from the effects of global financial crisis, which was felt also in terms of exports). The average coverage ratio of imports, i.e., exports of goods as a percentage of imports, over the past five years stood at 10.7%. The resulting trade balance is hugely negative, exceeding €2 billion in 2011, or 45% of GDP. What makes matters even worse, the gap is widening continuously (except 2009).

Table 1.1: Main indicators of Kosovo's external position

	2007	2008	2009	2010	2011
Exports of goods and services (current, mil. €)	515,000	575,000	597,591	811,000	931,000
Exports of goods and services (annual percent growth)	-	11.7	3.9	35.7	14.8
Exports of goods and services (percent of GDP)	15.0	15.0	15.0	19.0	20.0
Imports of goods and services (current, mil. €)	1,831,000	2,171,000	2,103,041	2,604,918	3,042,020
Imports of goods and services (annual percent growth)	-	18.6	-3.1	23.9	16.8
Imports of goods and services (percent of GDP)	54.0	56.0	54.0	62.0	66.0
Trade balance (current, mil. €)	-1,316,000	-1,596,000	-1,505,450	-1,793,918	-2,111,020
Trade balance (annual percent growth)		21.3	-5.7	19.2	17.7
Trade balance (percent of GDP)	-38.6	-41.4	-38.5	-42.6	-45.5

Source: World Development Indicators (<http://data.worldbank.org>, accessed on 8 September 2012)

The aggregate trade situation, however, conceals a significant difference between trade in goods and trade in services. In the goods sector, the persisting negative balance of trade has recently reached around €1.7 billion (see Figure 1.1). In contrast, the services sector has been performing reasonably well. As Figure 1.2 shows, Kosovo has experienced a positive trade balance in services since 2006. However, the surplus in services

dropped substantially as a result of increase in imports of construction services (high-way linking Kosovo with Albania) starting in 2010.<sup>2</sup>

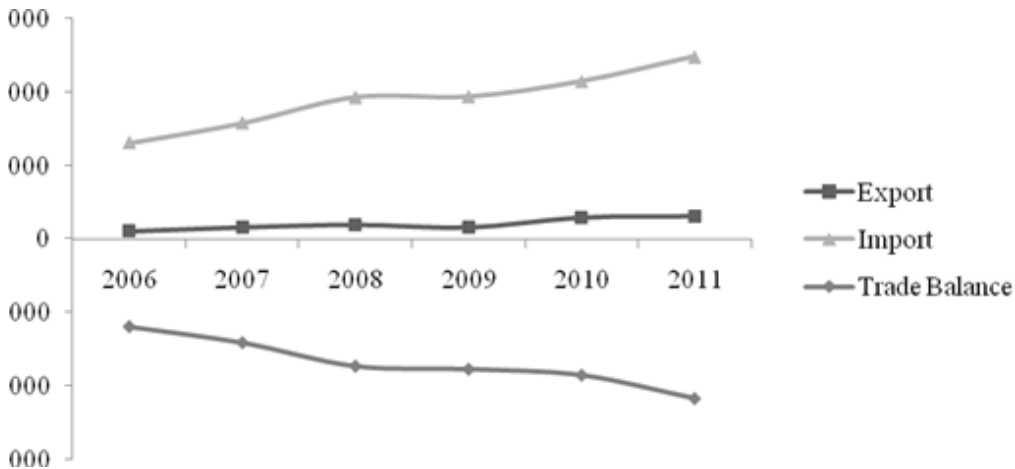


Figure 1.1: Exports and imports of goods in Kosovo (mil. €)

Source: Central Bank of Kosovo (2012)

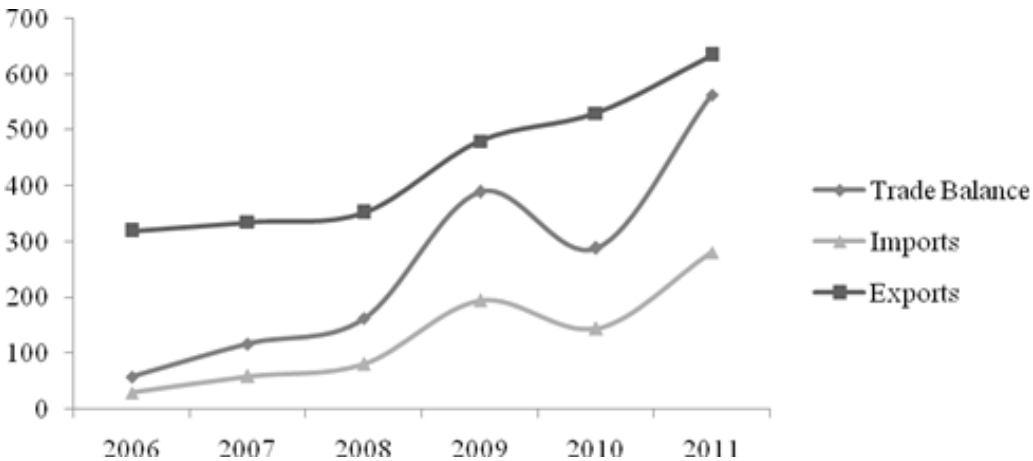


Figure 1.2: Exports and imports of services in Kosovo (mil. €)

Source: Central Bank of Kosovo (2012)

<sup>2</sup> Central Bank of Kosovo (2012), Monthly Statistical Bulletin No. 128, <http://www.bqk-kos.org/?cid=2,129> (accessed on 27 September 2012).

The Kosovo Statistics Agency (2012) reports that industrial goods dominate the structure of trade exchange in Kosovo. Base metals were the most exported industrial product in 2011, comprising over 60% of total exported goods, a significant increase from 2006, when it made around 45% of the total. Base metals are followed by the category of mineral products, the second largest Kosovo exported commodity, with around 13% of the total. Food and related crop-based products are the third largest exported group of products, with over 8% of the total exports, followed by machinery, appliances, and electrical equipment (4.8% of the total), plastic and rubber (3.9%), and textiles and garment (3.7%).<sup>3</sup>

For a number of years food and related products have dominated the structure of imports (currently this category of goods is in the second place, with 12% of the total), while in recent years mineral products have become the major imported commodity, with 21.6% of the total. The third imported category is machinery, appliances, and electrical equipment, with 11% of the total. The increase in imported minerals, on the one hand, and machinery, appliances, and electrical equipment, on the other hand, indicates that Kosovo is steadily building its manufacturing base.

Apart from trade in industrial goods, another important category of trade in goods is that of agricultural products. Although considered potentially as a sector with significant comparative advantage<sup>4</sup>, Kosovo agricultural producers have managed to exports only around €25 million in 2011, as compared to €266 imported. The situation has been more or less the same during the whole last decade; however the widest gap between exports and imports in agricultural products has been accounted in 2011. The category of prepared foodstuff, beverages, and tobacco products and that of vegetable products comprise the largest amount of agriculture exports. They are mostly exported to Albania, Macedonia, Serbia and Germany. Regarding the imports of agricultural products, Kosovo mostly imports prepared foodstuffs, beverages and tobacco, followed by vegetable products, and live animals and animal products.

On a final note, as Central Bank of Kosovo reports there are indications that the transport, travel services, IT and construction sectors have been quite active in serving export markets. However, the biggest influence on the service export figure relates to sales of services to foreign firms and persons residing in Kosovo, that is, the so-called virtual exports. While trade in services gives positive signals, one should take the numbers with caution as the data on services are being updated and streamlined.<sup>5</sup>

<sup>3</sup> Kosovo Agency of Statistics (2012), External Trade Statistics, [http://esk.rks-gov.net/ENG/publikimet/cat\\_view/10-economic-statistics/14-external-trade-statistics](http://esk.rks-gov.net/ENG/publikimet/cat_view/10-economic-statistics/14-external-trade-statistics) (accessed on 15 September 2012).

<sup>4</sup> It is estimated that out of a total surface area of 1.1 million hectares in Kosovo, approximately 588,000 or slightly more than half is agricultural land with fertile, nutrient-rich soils. About 90% of agricultural land is dedicated to livestock activities such as pastures, meadows, forage crops and some fodder crops for animals. The remaining area is used for grain production, vineyards, potatoes, fruit and vegetables.

<sup>5</sup> Central Bank of Kosovo (2012), Monthly Statistical Bulletin No. 128, <http://www.bqk-kos.org/?cid=2,129> (accessed on 27 September 2012)

## 2. Geographical Orientation of Kosovo's Trade

Data show that Kosovo mainly trades with two groups of countries, namely European Union countries plus Switzerland and the neighbouring countries. As Table 1.2 shows, in 2011 the major EU trading partners were Italy and Germany; Italy was the greatest importer of Kosovo's goods, followed by Germany. Instead, Germany is the largest EU exporter in Kosovo, followed by Italy. Regarding the regional partners, due to the infrastructure revamp on the both sides of the border, Albania is becoming an increasingly important destination for Kosovo's products. In a short time, Albania has become the most favourable export destination for goods from Kosovo. Two other important regional destinations are Macedonia and Serbia. The latter countries, together with Germany, are the largest importers in Kosovo. However, in the recent years other countries such as China, Turkey, and India are increasingly becoming important trade partners for Kosovo. With all these countries Kosovo has a significant negative trade balance in goods.<sup>6</sup>

Table 1.2 Kosovo's major goods' export and import partners in 2011<sup>7</sup>

	Exports		Imports		Trade balance (mil. €)
	Value (mil. €)	%	Value (mil. €)	%	
Italy	83,924	26.3	159,444	6.4	-75,519
Albania	34,566	10.8	96,400	3.9	-61,834
Macedonia	30,949	9.7	365,961	14.7	-335,011
China	28,268	8.9	170,285	6.8	-142,017
Germany	24,144	7.6	293,441	11.8	-269,297
Switzerland	17,611	5.5	22,194	0.9	-4,583
Turkey	7,831	2.5	184,452	7.4	-176,621
Serbia	7,198	2.3	254,917	10.2	-247,718

Source: Kosovo Agency of Statistics (2012)

Next, we discuss the mechanisms that govern trade relations with the three sets of countries and other related features.

### 2.1. Trade Relations with the EU

In 2000, through the EC Regulation No. 2007/2000, the European Union (EU) enacted Autonomous Trade Measures (ATMs) for the Western Balkan region, including Kosovo. Almost all products were covered, excluding wines, sugar, calf meat and certain fish products that were subject to specific tariffs. As ATMs are of temporary nature, measures were cancelled at the end of 2010, only to resume in January 2012. The cancellation

<sup>6</sup> Unfortunately, disaggregated data on service exports are not available.

<sup>7</sup> Kosovo Agency of Statistics (2012), External Trade Statistics, [http://esk.rks-gov.net/ENG/publikimet/cat\\_view/10-economic-statistics/14-external-trade-statistics](http://esk.rks-gov.net/ENG/publikimet/cat_view/10-economic-statistics/14-external-trade-statistics) (accessed on 15 September 2012).

affected primarily Kosovo's producers, as other countries in the region had already had signed Free Trade Agreements (FTA) with the EU. These FTAs were signed as a part of the Stabilisation and Association Process (SAP), which is designed to guide the reforms of South Eastern European (SEE) candidate and potential countries that are in the process of acceding to the EU. Due to the unresolved political status, Kosovo was left outside of the process. Instead of SAP, a different mechanism was devised to track Kosovo road to the EU, in the form of Stabilization and Association Tracking Mechanism and later as a Stabilization and Association Process Dialogue.

Recently, the EU is sending signals that it is ready to engage in FTA negotiation with Kosovo. So far, the steps taken on the EU side aimed at assessing Kosovo's preparedness to negotiate and implement a trade agreement, and identified the measures Kosovo needs to take to ensure future progress. Indeed, Kosovo has made significant progress to start the negotiations of free trade agreement with the EU. Progress Report clearly indicates the improvement of the position of Kosovo in the area of free movement of goods, including quality infrastructure, industrial property rights and trade policies.

### 2.1.1. Trade Exchange with the EU

With around 45% of export demand in 2011, and around 40% of total imports, the EU is the major trade partner of Kosovo (see Table 1.3). On average, since 2007 Kosovo's exports to the EU have increased by 36%, whereas imports by around 12%. The increase in exports have been rapid; in 2007 and 2008 the increase in exports was 70% and 82%, respectively, compared to the previous year. However, the impact of the financial crisis caused a sudden drop, and exports to the EU did not pick up until 2010. With regards to imports, the year-on-year increase has been slowing steadily. Despite some positive indications regarding the export performance, the negative trade balance of Kosovo with the EU has been widening constantly, reaching over €800 million in 2011.

Table 1.3: Kosovo's trade with the EU

	Exports		Imports		Trade balance (mil. €) a)
	Value (mil. €) a)	%	Value (mil. €) a)	%	
2006	42,300	38.2	454,300	34.8	-412,000
2007	69,300	42.0	572,900	36.3	-503,600
2008	94,000	47.4	702,000	36.4	-608,000
2009	71,300	43.1	755,000	39.0	-683,700
2010	131,500	44.7	821,300	38.3	-689,800
2011	136,400	43.6	941,700	38.0	-805,300

Source: Central Bank of Kosovo (2012)

Note: a) Figures are rounded.

As reported by the Kosovo Agency of Statistics (2012), apart from Italy and Germany (discussed earlier), Kosovo trades also with other EU member states, such as Slovenia, Austria, and Belgium, with an equal share of around 4% in total Kosovo's exports to the EU. Other significant import partners are Greece (11% of total EU imports), Slovenia (7% of total EU imports), and Bulgaria (around 5% of total EU imports).

With regards to trade composition, Eurostat data (2012) show that Kosovo exports to the EU mainly goods for further processing, whereas it imports from the EU mainly machinery and equipment (see Table 1.4).<sup>8</sup>

Table 1.4: Trade composition of exports to and imports from the EU

Description		Value (mil. €) <sup>a)</sup>	%
Exports			
	Manufactured goods classified chiefly by material	100,000	73.1
	Crude materials, inedible, except fuels	25,000	18.5
	Machinery and transport equipment	4,000	2.7
	Miscellaneous manufactured articles	3,000	1.9
	Food and live animals	2,000	1.5
	Beverages and tobacco	2,000	1.2
Imports			
	Machinery and transport equipment	192,000	28.5
	Manufactured goods classified chiefly by material	111,000	16.5
	Food and live animals	93,000	13.8
	Chemicals and related products	86,000	12.8
	Miscellaneous manufactured articles	66,000	9.9
	Mineral fuels, lubricants and related materials	56,000	8.3
	Beverages and tobacco	44,000	6.6

Source: Eurostat (2012)

Note: <sup>a)</sup> We do want to make the reader aware that there are certain discrepancies between the Kosovo's official data on external sector and the EU individual country statistics produced by Eurostat.

<sup>b)</sup> Figures are rounded.

As Table 1.4 shows, over 90% of exported goods (around 40% of total exports) to the EU are base metals and other mineral commodities. This includes over €85 million of steel rods, unprocessed metal and related products exported mainly to Italy and Germany in 2011. In addition, a percentage of exports were sold in the form of unprocessed hides and skins and textile. Only a small fraction of exports are finished manufacturing products, that is, machinery and transport equipment (around 2% of total EU exports, or less than 1% in total Kosovo's exports).

<sup>8</sup> See [http://trade.ec.europa.eu/doclib/docs/2011/january/tradoc\\_147309.pdf](http://trade.ec.europa.eu/doclib/docs/2011/january/tradoc_147309.pdf) (Accessed on: September 15, 2012).

On the other hand, as pointed out earlier, machinery and transport equipment dominates the import structure from the EU. These are mainly in the form of passenger vehicles and vehicles for transport of goods, totalling at over €90 million. Petroleum and related products constitute another important category of commodities imported from the EU, in this case from Italy (over €50 million). Tobacco imports from Germany reached €33 million in 2011. Other imported commodities from the EU include wood products, chemicals, pharmaceuticals, and others.

## 2.2. Trade Relations with the Neighbouring Countries

Trade relations within the region of Western Balkans are governed by the Central European Free Trade Agreement (CEFTA). CEFTA is a fairly deep integration mechanism, as it covers means of expanding trade in goods and services through elimination of barriers to trade between the signatory parties. In addition, it aims to fostering investment through means of fair, stable and predictable rules. Furthermore, it provides protection of intellectual property rights, in accordance with international best practices. Additionally, it harmonizes provisions on modern trade policy issues, such as competition rules and state aid. It also includes clear and effective procedures for settling disputes. Last but not least, the Agreement is meant to provide a framework for the signatory parties to prepare for EU accession.

For Kosovo, CEFTA did not live up its expectations; barriers and other obstructions from other parties still persist. The most notable example was the blockage of Kosovo's goods by Serbia and Bosnia and Herzegovina after Kosovo introduced new customs stamps following the declaration of independence, in February 2008. Kosovo undertook reciprocal measures against these two countries by blocking Serbian goods entering Kosovo and imposing pre-CEFTA customs duties on Bosnian goods. Eventually, the issue was resolved in September 2011. Less significant 'incidents' between Kosovo and other signatory parties within CEFTA involve Macedonia, in the case of export of grain, Albania, in the case of potato and animal feed pallets, and other cases.

Table 1.5: Kosovo's trade with neighbouring countries

	Exports		Imports		Trade balance (mil. €) a)
	Value (mil. €)a)	%	Value (mil. €) a)	%	
2006	51,700	46.7	536,300	41.1	-484,600
2007	65,100	39.4	579,600	36.8	-514,500
2008	61,500	31.0	717,800	37.2	-656,300
2009	53,500	32.4	692,500	35.8	-639,000
2010	70,900	24.1	799,000	37.3	-728,100
2011	82,400	26.4	899,500	36.3	-817,100

Source: Central Bank of Kosovo (2012)

Note: a) Figures are rounded.

As Table 1.5 shows, the relative importance of neighbouring markets for Kosovan products is decreasing steadily. While in 2006, 46.7% of total exports were sold in CEFTA markets, in 2011 this figure fell down to 26.4%. Also with regards to imports, the decline is evident, but it is not as significant as in the case of exports. Partially, this can be explained with the problems Kosovo's businesses face when trading with neighbouring countries (discussed above). Another explanation could be the fact that in the last few years the targeted markets of Kosovo's producers have been expanding; products made in Kosovo have reached the distant markets of China and India (to be discussed later).

As we pointed out earlier, Macedonia and Serbia, followed by Albania, are the most important trade partners in the region. In 2011, these three countries have sold goods in Kosovo worth around €630 million, relative to around €73 million exported to these countries. Macedonia and Serbia have been holding a dominant position in the Kosovo's markets since 1999. In the case of the former, prior to the signing of CEFTA agreement, Kosovo has endorsed an agreement signed by former Yugoslavia and Macedonia virtually exempting Macedonian goods from duties. In the latter case, until 2008 trade between Kosovo and Serbia has been considered as a domestic trade. In the case of Albania, the erection of the road infrastructure has enabled greater trade exchange between Kosovo and Albania.

While in 2006 Kosovo exported goods worth over €12 million, in 2011 this figure almost trebled to €35 million. The rate of increase of Albanian exports to Kosovo was even higher: they increased by five times during the same period of time, from over €18 million to €96 million. In coming years, the exchange between Kosovo and Albania will potentially increase further as a result of cultural ties, further planned improvements in the infrastructure (mainly in the Kosovo side), streamlining of administrative procedures, greater flow of knowledge and technology, and other factors. In addition to the market potential, the importance of Albania lies in the access to sea it provides for Kosovo's goods. Access to sea creates huge potentials for the development of Kosovo.

Kosovo exports base metals and other mineral goods to Macedonia and Albania. Another significant category of products exported to Albania is that of steel rods, grain and flour, and agricultural products. Cement is the main product exported to Serbia. With regards to imports, Macedonia leads with petroleum and petroleum-related products, which amounted to around €200 million in 2011. Albania, among others, exports to Kosovo construction material (mainly cement) and agricultural products, whereas Serbia exports construction material (brick and clay), beverages, grain and flour, etc.

### **2.3. Trade Relations with the Rest of the World**

In December 2008, Kosovo was designated as a beneficiary country under the U.S. Generalized System of Preferences (GSP) programme. This programme provides duty-free access for up to 4,800 products. Under this programme, a wide range of Kosovo products are eligible for duty-free access to the United States. Kosovo enjoys also the Norway's GSP programme. 64 low-income countries have duty and quota free market access for

all goods to Norway. Also, Japan has expressed readiness to offer GSP programme for Kosovo and the process is still ongoing, almost nearing finalization.

However, the volume of trade with these countries is rather insignificant. Apart from Switzerland, recently Kosovo has been strengthening ties with Turkey and the distant markets of China and India. The share of exports to these countries has doubled since 2006, from 15.2% to 30% in 2011 (an increase of 5.5 times). Imports, in relative terms have remained constant (around 25% since 2006), although in value terms almost have doubled. Trade balance with this group of countries remains negative and increasing constantly (see Table 1.6).

Table 1.6: Kosovo's trade with the rest of the world

	Exports		Imports		Trade balance (mil. €) <sup>a)</sup>
	Value (mil. €)a)	%	Value (mil. €) a)	%	
2006	16,800	15.2	315,300	24.1	-298,500
2007	30,700	18.6	423,700	26.9	-393,000
2008	43,000	21.7	508,400	26.4	-465,400
2009	40,500	24.5	488,000	25.2	-447,500
2010	91,600	31.2	524,600	24.5	-433,000
2011	93,700	30.0	638,100	25.7	544,400

Source: Central Bank of Kosovo (2012)

Note: <sup>a)</sup> Figures are rounded.

With a value totalling €184 million in 2011, Turkey is Kosovo's fourth largest importer. Kosovo imports from Turkey a wide variety of goods, including electrical equipment, textile, garment, food products, and others. Kosovo has managed to export around €7 million, mainly textiles, rubber, and base metals. Base metals and related products were the major commodity exported to China (around €24 million). On the other hand, China exported to Kosovo shoes, furniture, plastics, and other products worth approximately €170 million. Trade gap between Kosovo and Switzerland is more balanced compared to that with China and Turkey. Kosovo's exports to this country in 2011 were worth around €17 million, whereas imports exceeded €20 million. Goods exported to Switzerland were base metals, whereas those imported included rubber, pharmaceuticals, and furniture.

### 3. Legal, Policy and Institutional Framework in the Area of Trade

This section focuses on the legal and institutional framework relevant for the area of trade. It begins with an overview outlining major EU *acquis* acts and provisions applying to this area (at the level of both the treaty and other acts adopted by EU institutions). Next, it briefly analyzes the main Kosovo's domestic legal acts applying in this area. Lastly, it focuses on the main Kosovo's institutions in charge of implementing

the trade-related legal and policy framework, as well as other relevant stakeholders involved.

### **3.1. Domestic Legal Framework in the Area of Trade**

Kosovo is in the process of developing its domestic EU-compliant trade legislation. In 2011, Kosovo has adopted new Law on External Trade, a main law setting out principles to govern external trade relations of Kosovo. Last year Kosovo has completed the legal infrastructure on trade remedies/contingency measures. However, the Law on Anti-dumping and Countervailing Measures is not yet fully in line with international best practices and it will be amended. Hereunder is presented a brief summary of relevant domestic legislation in the area of trade.<sup>9</sup> In general, there is a continuous work on reforming domestic laws and regulations on international trade.

#### **3.1.1. Law on External Trade**

The purpose of the Law 2011/04-L-048 on External Trade is to define the general rules for the exercise of external trade between physical and legal persons residing within the territory of Kosovo and those residing abroad. The Law is based on WTO principles and agreements, as well as EC Directives, CEFTA provisions, and other international best practices. The Law has been drafted during 2011, and entered into force in October 2011. It replaced the Law No. 2002/6 on External Trade Activity of 2002.

#### **3.1.2. Customs and Excise Code**

The Customs and Excise Code (2008/03-L-109) sets out the legal framework for trade and customs administration, and as such is a highly important mechanism for revenue collection (fiscal administration), facilitating trade, and attracting investment into the country. The Code is in full conformity with the European Union Customs Code of 1992. This is a fundamental point, since closer association with the EU is a priority for Kosovo, and closer association will require and will, in any event, be facilitated through harmonization of Kosovo's domestic laws with the EU legislation. There are plans to amend the Law to comply with EU 2008 customs blueprint, or later versions of the EU Customs blueprint.

#### **3.1.3. Legislation on Contingency Measures**

Two laws have been adopted to provide the framework for applying three contingency measures: Law No. 2010/03-L-097 on Anti-Dumping and Countervailing Measures and Law No. 2011/04-L-047 on Safeguard Measures on Imports. These measures are of utmost importance to tackle illegal business practices of importers or when there is a

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<sup>9</sup> The summary is mainly based on the EU Progress Report 2011, PPMA Report (2010) "Review of the KWosovo's Legal Framework on Foreign Trade" and other relevant studies on this area.

sudden surge of imports that harms domestic industries.

As stipulated therein, the purpose of the Law on Anti-Dumping and Countervailing Measures is to provide the legal basis for the imposition of anti-dumping measures against dumped imports and countervailing measures against subsidized imports in a manner that complies with the rules and requirements of the European Union and the World Trade Organization. The Law is in line with international best practices with regards to the initiation, the size of the duty, and timeframe of the duty. However, the Law incorporates complex EU procedures and institutions that are not appropriate for Kosovo; therefore its amendment has been included in the 2012 Government Legislative Programme and transferred to the 2013 programme. The current Law refers to the EU institutions for implementing the Law. In addition, the Law creates a six member Commission in charge of investigating antidumping cases and recommending actions. This Commission, according to BEEP analysis, since its enactment, has proved unworkable. In a two-year time, a very small number of cases have been investigated and no case has been initiated. In the revised Law, administrative responsibility will be vested with the Trade Department.<sup>10</sup>

The Law on Safeguard Measures on Imports sets out the principles and procedures relating to application of safeguard measures in cases when a product is imported in Kosovo in large quantities that it causes injury or threat of serious injury to domestic producers of like or identical goods. This law is considered to be in full accordance with the WTO and the EU agreements and directives, and CEFTA provisions, except regarding the timeframe of application of the law. The WTO Agreements on Safeguards establishes that safeguards should be applied initially for four years, and if the review establishes that the injury to domestic industries from the sudden increase of imports still persists, measures can be extended for a final four years. The Law on Safeguard Measures on Imports establishes a single-time horizon of eight years for applying safeguards measures. This is contrary also to CEFTA provisions, which are even more restrictive. Signatory countries have committed themselves to applying safeguards for a year, and if the injury persists, extend for another year following one year of break.

### **3.1.4. Legislation on Quality Infrastructure**

The EU Progress Reports of 2009 and 2010 acknowledge that Kosovo has achieved some progress in terms of approximation with European standards in terms of quality infrastructure relevant for the area of trade, namely in those of accreditation, standardisation and metrology. The progress has been related, inter alia, to the legislation adopted in these three areas. The activities of the quality infrastructure mechanisms in Kosovo are based on the following laws: Law 2009/03-L-144 on Standardisation; Law 2010/03-L-203 on Metrology; Law 2004/28 on Precious Metal Products; and Law 2005/02-L43 on Accreditation, and its subsequent revision Law no. 2011/04-L-007.

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<sup>10</sup> See BEEP (2010), Review of the Kosovo Legal Framework for External Trade.

Another important ingredient of the quality infrastructure in Kosovo is the Department of Industry (see discussion below), especially the entity on quality infrastructure. The latter is in charge with promulgating technical regulations. The activities of the latter rely on the Law 04/L-078 on General Safety of Products and the Law 04/L-039 on Technical Requirements for Products and Conformity Assessment.

### **3.2. EU Acquis Relevant for the Area of Trade**

As stipulated by the Treaty on the Functioning of the European Union<sup>11</sup> (Article 3.1.), core issues for the area of trade, namely customs union, competition rules necessary for the functioning of the internal market and common commercial policy, are under the Union's exclusive competence. On the other hand, it (Article 2.3.) stipulates that Member States are in charge of coordinating their economic and employment policies within arrangements established by this Treaty and determined by the Union. The Treaty further defines the customs union as the area wherein all customs duties on imports and exports and charges having equivalent effect between Member States, including customs duties of a fiscal nature, are prohibited (Article 30), and common customs tariff in their relations with third countries are in place, with the customs union covering all trade in goods (Article 28). Such prohibitions apply to quantitative restrictions on imports and exports (Articles 34 and 35), yet this does not preclude prohibitions or restrictions on imports, exports or goods in transit justified on grounds of public morality, public policy or public security; the protection of health and life of humans, animals or plants; national treasures possessing artistic, historic or archaeological value; or of industrial and commercial property. Such prohibitions or restrictions shall not, however, constitute a means of arbitrary discrimination or a disguised restriction on trade between Member States (Art. 36).

Moreover, in order to ensure implementation and compliance with these principles, the Union is in charge of adopting measures establishing or ensuring functioning of the internal market as an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured (Article 26, para. 1 and 2). The internal market also extends to agriculture, fisheries and trade in agricultural products (Article 38.1.). Lastly, the Treaty establishes the EU's common commercial policy, which is based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, foreign direct investment, the achievement of uniformity in measures of liberalisation, export policy and trade protection measures, such as those to be taken in the event of dumping or subsidies (Article 207.1.).

In addition, specific areas related applicable to trade (covered in more details in the relevant specific areas under this Thematic Roundtable) are those in the areas of Customs Union and free movement of goods, freedom of movement for workers, right of estab-

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<sup>11</sup> Consolidated Version of the Treaty on the Functioning of the European Union, Article 3, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2010:083:FULL:EN:PDF> (pp. 83/51).

lishment and freedom to provide services, free movement of capital (the latter under the heading of economic and monetary policy and free movement of capital), competition policy, taxation, as well as industrial policy and internal market (*including the legislation on quality infrastructure, namely standardisation, accreditation, metrology, conformity assessment and market surveillance, and that regulating the areas of industrial and intellectual property rights*), and, lastly, law relating to undertakings.

More specifically, major acts in the area of Customs Union and free movement of goods<sup>12</sup>, subdivided into general ones and those on statistics. On the other hand, the most important acts in the area of competition<sup>13</sup> are those on competition principles. Lastly, the category of Restrictive practices includes two main *acquis* acts, namely Council Regulation (EC) No. 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty; and Commission Decisions implementing the principles deriving from various cases relating to proceedings pursuant to Article 81 of the EC Treaty and Article 53 of the EEA Agreement. It also includes *acquis* acts implementing the case law, which are subdivided into three subcategories: prohibited agreements, authorised agreements, exemptions and negative clearances and supervision procedures (the latter including the High Authority's Decision. No 1-65 of 3 February 1965 concerning notification of decisions on information to be obtained from or checks to be made on associations of undertakings for purposes of application of Article 65 of the Treaty). Other specific subcategories under the area of competition policy include *restrictive practices, dominant positions, concentrations, application of the rules of competition to public undertakings, state aids and other subsidies, intra-Community dumping practices, obligations of undertakings, and national trading monopolies*. (See Annex 1 for a list of acts relevant for the area of trade.)

### 3.3. Kosovo's Institutional Framework on Trade

A detailed mapping of the existing institutional environment on trade has been done by the 2009 UNDP report "A Needs Assessment for Kosovo's Trade Related Institutions". The report discusses the main institutional mechanisms related to trade in Kosovo. It distinguishes between the leader in trade issues, i.e. Ministry of Trade and Industry and the leadership, i.e. all other trade-related institutions. The study highlights two main handicaps of institutional framework on trade in Kosovo: first, the lack of human and technical capacities to design, implement, assess, and fine-tune trade policy; and, the virtual non-existent coordination of institutions and policies in the area of trade.

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<sup>12</sup> EUR-Lex: Customs Union and free movement of goods, <http://eur-lex.europa.eu/en/prep/latest/chap02.htm>.

<sup>13</sup> EUR-Lex: Competition Policy, <http://eur-lex.europa.eu/en/legis/latest/chap08.htm>.

### 3.3.1. Ministry of Trade and Industry

The mandate of the Ministry of Trade and Industry pertains to creating an environment conducive to promoting the development of the private sector, specifically through the development of SME sector and attraction of Foreign Direct Investments. In addition, MTI is the main institutional player in trade-related issues. Activities of MTI, among others, pertain to quality infrastructure, IPR issues, tourism, coordinating EU activities as relate to the mandate of MTI, market inspectorate, petroleum sector, state reserves, and other. Some of these entities are discussed briefly below.

As pointed out, MTI's main activity is trade. A number of the MTI entities are, in one or another way, related to trade. Trade is an important driver of economic growth. Kosovo has designed policies and erected institutions aiming at facilitating the trading process, including the design of trade policies, implementation, coordination, and fine-tuning of the policy. At the core of all these processes stands the Department of Trade within MTI. This department is responsible for the development and implementation of the trade policies in Kosovo. This department consists of three units: Trade Policy Unit, Trade Agreements Unit and Market Protection Unit. Out of the three units, the latter is more active unit and faces most challenges, and because of its nature the work takes a longer time and asks for complete and accurate data, especially when it comes to market analysis. On the other hand, collection of qualitative data requires capacity building of the Statistics Agency of Kosovo and better cooperation with the latter. It is important to point out that Trade Department oversees the major consultative process on trade policy (see discussion below).

In seeking to expand international trade, it is virtually impossible to underestimate the importance of adopting and implementing international practices in the areas of metrology, accreditation, standardization and certification, and technical regulations, as these provide a vital link to global trade, market access, and export competitiveness and contribute to consumer protection and confidence in product safety, quality, and health, and protection of the environment. Under MTI operate five entities with a mandate to cover abovementioned issues: Kosovo Standardization Agency, Metrology Department, Accreditation Directorate, Department of Industry, and Market Inspectorate. With regards to the Department of Industry, quality infrastructure pertains to the one set of activities performed under the umbrella of this entity, the other being the design of industrial policies and other policies to gear up the industrial sector in Kosovo.

Last but not least, the Investment Promotion Agency of Kosovo operates under the auspices of the MTI. IPAK is responsible for a number of investment and export promotion activities (see also later discussion on investment portion of IPAK). With regards to exports, IPAK is in charge of conducting activities to promote the exporting activities of Kosovo producers, supporting identification of export opportunities, providing support to enterprises and business associations related to exporting activities, and providing information on regulatory framework both within and outside Kosovo.

Besides Kosovo Trade Policy, an important instrument available to MTI and other stake-

holders directly involved in the area trade is also the International Trade Guide. This guide, developed with the support of USAID Program for Improvement of Business Environment, is a resource that provides business information on transit, import and export of goods, and on customs and non-customs procedures and duties. The guide is organized in matrix form (part of requirements) and with explanations in narrative form (in the part of procedures).

### **3.3.2. Other Trade-related Institutions**

Trade-related institutions and stakeholders outside the MTI are numerous, starting from the Prime Minister's office, donors, agencies and departments within other Ministries, business community, think tanks, and other relevant institutional mechanisms. All these rather diverse stakeholders deal with the issues of trade policy making, some more directly and some rather remotely. Within the Government of Kosovo, except MTI there are a number of institutions whose activities partially are related to the trade. These are the Ministry of Finance (including Kosovo Customs and Kosovo Tax Administration), Ministry of Agriculture, Forestry and Rural Development, Kosovo Statistical Agency, Food and Veterinary Agency, Central Bank of Kosovo, Ministry of Foreign Affairs and the Ministry of European Integration.

The Ministry of Finance consists of the three important mechanisms in the process of trade policy: Kosovo Tax Administration, Kosovo Customs, and the Macroeconomic Department. The Kosovo Tax Administration is important as any action taken with regards to trade will have potential implications is the Government revenues or spending. Furthermore, KTA plays an important role in terms of collecting and processing data on trade. In this context, the Department of Trade requires data on the number of businesses paying taxes and that actually operate, which is a key element to ensure reliability of data in this area. Currently, Department of Trade uses data produced by the Agency for Registration of Businesses in Kosovo, but the latter is not completely reliable, since it still lacks a complete system on business dissolution and bankruptcy. Therefore, in order to ensure access for the Department of Trade to the KTA data, it is necessary to establish the appropriate legal and procedural basis, perhaps through a memorandum of cooperation.

In addition, Kosovo Customs is an implementing mechanism and a major source of raw data on foreign sector. Regarding the latter, at the end of 2012 it has been signed a memorandum of cooperation with the Department of Trade, which will grant the latter with access to the Automatic System of Customs Data (ASYCUDA), which will significantly facilitate data collection and consequently improve the quality of data in the area of trade.

Finally in terms of MF, the key is the Department of Macro-Economic Policies, which performs a prior and post implementation evaluation of a certain policy to the Government revenues.

The Ministry of Agriculture is another important actor, especially in terms of sectoral issues of trade policies. Moreover, the Kosovo Statistical Agency is also a key actor since it is compiling comprehensive statistical data on the foreign sector in the context of trade.

Another important institution in this area, in particular with regard to statistical data, is the Central Bank of Kosovo (CBK), which covers statistics in the area of services. In this context, a useful resource is the Database on Services, which is managed by CBK and contains data on exports and imports of services (which includes 120 occupations in the service sector). The use of such a database is required by the standards of the World Trade Organization (WTO) and is used by EU countries and CEFTA. However, there is still no legal and procedural basis that will enable MTI to access this database.

Regarding the role of the Food and Veterinary Agency in facilitating trade, this mainly relates to the inspection of imported food. Significant progress in this regard includes elimination of unnecessary permits, licenses and certificates, establishing procedures for veterinary and phytosanitary inspections (including an SOP and a manual), training of border inspectors, improvement of the IT infrastructure (specifically assessing its compatibility with the risk management module of 'ASYCUDA World', and the design of border inspection points. These achievements are result of the USAID Program for Improvement of Business Environment support.

Furthermore, cooperation of MTI with business community is fairly regular. Regarding the former group, there is a direct communication with the major business associations in Kosovo, namely the Kosovo Chamber of Commerce, Kosovo Business Alliance, and the American Chamber of Commerce. The communication covers exchange of information, joint conferences and workshops, etc. In addition, the MTI has established links with other smaller groupings representing the business community. KCC as the largest business association consists of 15,000 members, and membership in it is voluntary. It represents the various economic sectors in consultation with government institutions (including employers within the Economic and Social Council). It also contributes to economic development and business support services directly through education and training, lobbying (through 30 sectoral associations), investment promotion (via B2B [business to business], trade missions, fairs, and Foreign Investors Club). KCC has also signed agreements with over 35 business associations in the region and beyond.

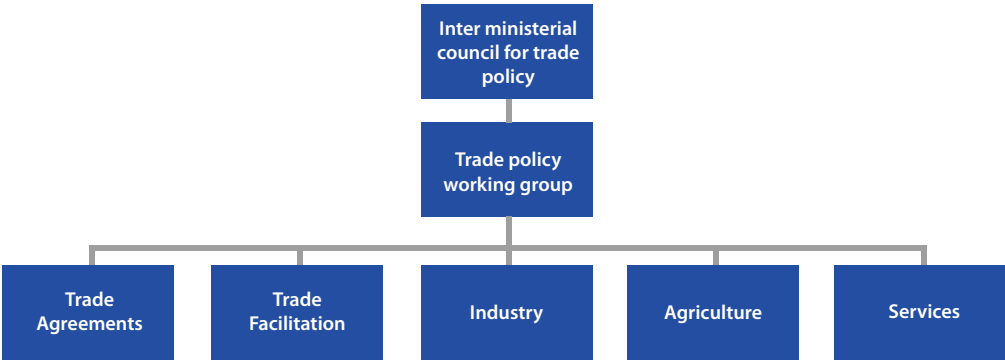
Another set of stakeholders involved in the process of trade policy-making is the donor community. Donors have been a crucial factor in the institutional development of the post-war Kosovo. Donors such as USAID, EC, World Bank, GIZ, etc., have been providing continuous support to the MTI and other relevant institutions on trade-related issues.

Other stakeholders related to trade concern civil society, universities, other independent bodies (committees within the parliament, Central Bank, etc.), trade unions, etc.

### 3.3.3. Coordinating Trade-related Bodies

Coordination of trade-related institutions is one of the important factors in the trade policy process. The Trade Policy of Kosovo, adopted in 2009, acknowledges that coordination between trade-related institutions in Kosovo is virtually missing. Hence, in 2010 the Government of Kosovo established the Inter-Ministerial Council for Trade Policy, a political-level body that brings together Ministers from trade-related ministries, such as: Ministry of Trade and Industry, Ministry of Finance, Ministry of European Integration, Ministry of Agriculture, Ministry of Infrastructure, and Ministry of Foreign Affairs (see chart below). The main task of the Council is to ensure political support, coordination and approval of key issues related to foreign trade.

Chart 1.1: Trade coordination mechanism in Kosovo



The Inter-Ministerial Council for Trade Policy has established a technical-level group, the so-called Trade Policy Working Group (TPWG), a mechanism that brings together technocrats from various government institutions, businesses, civil society, donors, etc. The main function of this group is to coordinate all activities conducted in the context of the trade policy or policies related to trade development. TPWG has established five specific subgroups, as presented in the chart above: sub-group on trade agreements, trade facilitation, and three sectoral sub-groups. Already, these subgroups are active, especially the sectoral ones and the sub-group on trade facilitation. Most recently, the subgroup on trade agreements has commenced, and it will be in charge to run FTA negotiations with Turkey. It is likely that the same sub-group will play a major negotiating role when FTA negotiations with the EU begin. All these coordination mechanisms have been sanctioned in the 2011 Law on External Trade.

Since its establishment until October 2012 the NCTP met only twice, the WGTP every three months, and more frequently subgroups (as needed). It is therefore necessary to increase the efficiency of operation and decision making of these structures, since meetings are not prepared appropriately in advance (including the preparation of the parties involved, meetings are too long and fail to produce tangible and clear results). So,

perhaps it is necessary to conduct a comprehensive and systematic assessment of their needs. Further, based on this and the activities arising from the Trade Policy and the SAA process, to clarify their functions in terms of concrete products they should issue and concrete results should achieve. All these should be translated into concrete activities, integrated within the annual work plans.

Another important issue is to address the overlap of functions of these structures and the National Council for Economic Development (NCED). While, trade structures are responsible for ensuring the functioning of the whole policy cycle, specifically in the area of trade, NCED has a role in the development of consultations between all stakeholders in the country responsible for the strategic aspects of economic development and economic policy in general. Last but not least, the government institutions estimate that it is required to improve participation and business community contribution to these coordination structures (in particular at the level of sub-groups and in matters related to the CEFTA Agreement).

## **4. Trade Regime in Kosovo**

### **4.1. Tariff Policy**

Kosovo has established a single tariff rate of 10% *ad valorem* on all imports, except those from CEFTA member countries which are exempt from customs tariffs, and specific groups of products, which are duty free from all other countries. The latter include, for instance, artificial fertilizers, medical equipment, and goods for humanitarian purposes. In some later stages the list of exempted products has been extended, to cover for some specific machinery and raw materials.

In Kosovo, commodities such as tobacco, coffee, alcoholic and non-alcoholic drinks, wine, beer, fuel and related products, vehicles, etc. are charged with excise tax. The excise is applied also for the same categories of goods that are produced within Kosovo. The rate is set as a specific tariff. For the purpose of stimulating the domestic production the excise is not paid for mazut in the cases when it is used as a raw material.

According to the Central Bank of Kosovo, government revenues from import tariffs currently amounts to less than 10% of all government revenue. Kosovo relies heavily on the tax revenues collected from the border. Based on data over the years 2007-2011, the total revenues have continued to grow at an annual average of about 10%. Revenues collected at the border during this period rose by an annual average of 11.7% or about 55% compared with 2007. In 2011 alone, these revenues went up for 18% compared to 2010. Revenues collected internally during the same period rose by an annual average of 8.5%, or about 36.1% compared to 2007.<sup>14</sup> Revenues from customs during this period rose by an annual average of about 13% or around 55% compared to 2007 in nominal

<sup>14</sup> Kosovo's Answers to the EC Questionnaire on the Preparation of the Feasibility Study for a Stabilisation and Association Agreement p. 104, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

terms. Only during 2011, these revenues increased by 18% compared to 2010.<sup>15</sup>

A recent BEEP report,<sup>16</sup> among a number of policy options, argues that Kosovo's current tariff structure should be reviewed and changes to tariffs should be made based upon economic analysis, stakeholder input and a determination of national interests. The study argues that agricultural produce and infant industries that can become internationally competitive should be supported with an appropriate tariff level. These steps would potentially cause loss of government revenues; therefore a formula needs to be found to keep the government revenues intact, whereas the various tariff bands applied should keep the average tax rate at the same level. To address this, MTI is working on developing an approach for progressive reduction of tariffs (including compiling a list of sensitive goods to be protected).

## **4.2. Non-tariff Instruments**

Kosovo currently applies no quantitative restrictions. The same can be said about price restrictions. However, Kosovo applies technical regulations and standards (e.g., sanitary and phyto-sanitary rules and technical standards). For instance, import certification (licensing) policies and procedures are applied to certain products (meat, dairy products, etc.) and on the importation of live animals and some animal by-products.

In addition, for a number of years Kosovo has been striving to develop quality infrastructure.<sup>17</sup> As pointed out, Laws on Technical Regulations and Products Standards, Conformity Assessment and Mutual Recognition are in force, but the enforcement of these laws requires substantial additional efforts. The Kosovo Standardization Agency is working effectively to adopt international voluntary standards. Up to 4,000 of them have been adopted so far, and the agency plans to adopt 2,000 per year. The Government of Kosovo intends to put more efforts in building a total quality infrastructure to ensure implementation and enforcement of these laws and to provide assurance of compelling public policy needs related to the protection of human health and safety and protection of the environment.

Labelling requirements are in place obliging that information in Albanian are provided to consumers on both imported and domestically produced goods. Trademark and other intellectual property protections exist in law, but are not adequately enforced.

Trade inhibiting effects potentially may have practices and procedures applied by Kosovo Customs. The first one concerns Customs Classification Procedures. Kosovo Customs applies the principles and practices of the WTO Agreement on Customs Valuation, and in accordance with the provisions of the Central European Free Trade Agreement. Im-

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<sup>15</sup> Ibid.

<sup>16</sup> Trade Policy of Kosovo 2012: An Update.

<sup>17</sup> On the quality infrastructure mechanisms in Kosovo see Tsorbatzoglou, G. and Wheatley, R. (2010), Quality Infrastructure Feasibility Study, a report commissioned by the European Commission, Kosovo; and, BEEP (2011) Report on Metrology, Standards and Conformity Assessment Tools to Facilitate Trade.

ports of goods, which originate in the European Union and in CEFTA countries, make up approximately 80% of all imports into Kosovo; over 98% of import transactions with these blocks of countries are accepted under WTO Customs Valuation Method 1 – in other words, the declared transaction (invoice) value is accepted on 98% of these import transactions.

For the remaining 2% of these import transactions, the declared import value is not deemed acceptable by Customs, and WTO Valuation Methods 2 to 6 are applied in the WTO-specified sequence. In addition, there are no difficulties with regards to the Customs Classification Procedures. Kosovo Customs applies the “Harmonized Commodity Description and Coding System” (the “HS”). Finally, customs clearance procedures follow best international practices. As data from Customs authorities show, nearly 80% of import transactions are cleared by Kosovo Customs within two hours of lodgement of a goods declaration. Cases involving longer customs clearance time result from inadequate or incorrect data entered on goods declarations (15% of import cases) and disputes over customs valuation of imports (5%). All export transactions are cleared by Kosovo Customs within 30 minutes of lodgement of a goods declaration.

Another area related to non-tariff policies is that of competition. According to estimates of the Kosovo Competition Authority, the main challenges include insufficient institutional capacity, low level of promotion and competition incentive in the market (and often are taken measures that have contributed to the strengthening of monopoly, through policies relating to licensing, authorizations, metrology and market inspection), insufficient degree of the Competition Authority’s recommendations implementation, and the inefficient use of authority as a policy instrument to increase the reliability of businesses and citizens in economic governance.

### **4.3. Trade Agreements**

As discussed earlier, the level of trade openness of Kosovo is rather high. This has resulted from a range of mechanisms that govern Kosovo’s trade with its main trade partners. As explained, Kosovo has specific trade arrangements with its two major trading blocks, namely the EU and neighbouring countries. Trade with the EU is regulated by the Autonomous Trade Measures (ATM) that were established in 2000, and which were restored in early 2011, after a one year break, in 2010. Based on the European Commission study on Kosovo, 2009, during 2010 preparations were made for the signing of a Free Trade Agreement (FTA) with the EU. However, after the publication of the Feasibility Study, in October 2012, it was decided to integrate these preparations within the preparations for the signing of the Stabilization and Association Agreement (SAA), respectively the chapter on trade. In this context, the study on the impact of this SAA chapter in Kosovo’s economy has been concluded, a study that is one of the short-term benchmarks deriving from the Feasibility Study for commencement of the SAA negotiations.

Trade with neighbouring countries is conducted under rules and provisions outlined in

the CEFTA agreement. As it has been stated earlier, CEFTA resonates to a deep integration mechanism as it covers an extensive list of issues in addition to trade liberalisation. With other countries, Kosovo has signed GSP with the US and Norway, and it is likely that the same agreement will be reached with the Japan. Currently there are ongoing FTA negotiations with Turkey.

The next step for Kosovo is multilateral integration, or the full integration into the global trade system. In other words, membership in the World Trade Organization (WTO) is one of the goals of the Government of Kosovo. An assessment of the options Kosovo has in accessing WTO and the potential benefits it has from it have been provided by BEEP “Support of WTO Observer Status for Kosovo”. The study argues that WTO membership would benefit Kosovo by allowing it to take part in the discussion and determination of various trade issues of concern. However, there are a number of constraints for Kosovo to join the international organization, namely the fact that some WTO members have not recognized Kosovo. Membership in this organization requires consensus among all member states regarding acceptance of the new member.<sup>18</sup>

Kosovo is currently weighing up the membership options. One feasible option remains applying for membership as a customs territory, to avoid political frictions. Another consideration is whether to apply for observer status and later on for a full membership. The BEEP report supports the idea of immediate application for observer’s status. WTO observers have the right to observe formal meetings of the General Council and subsidiary bodies, including accession working parties. They also have access to the main WTO document series and may request technical assistance in relation to the operation of the WTO system and accessions. Observers may be invited to speak at meetings after members have spoken, but they cannot participate in decision-making.

Against this backdrop, one should acknowledge the wide-ranging constraints WTO membership puts on the policy space of developing countries, such as Kosovo. Therefore, future steps towards WTO membership should take into consideration this constraining factor.

#### 4.4. Contingency Measures

Kosovo has also been working on completing the infrastructure on contingency measures. As discussed above, the three contingency mechanisms are in place although the Law on Antidumping and Countervailing Measures has been included in the 2012 legislative agenda for amendment. Currently, MTI is finalizing the standard operating procedures for contingency measures based on the best international practices. *Trade Policy of Kosovo 2012: an Update* provides an extensive account of contingency measures as applied in Kosovo, including a discussion of WTO and CEFTA rules and procedures on contingency measures. The report recommends that contingency measures should be

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<sup>18</sup> A briefing note on the advantages and disadvantages of the application for WTO observer status by Kosovo; prepared by BEEP (2011) for the Minister of MTI (2011).

employed when appropriate to address CEFTA trade problems. A summary is provided below.

#### **4.4.1. Antidumping**

Antidumping measures are authorized under WTO rules and regulations (Agreement on Anti-Dumping or the Agreement on Implementation of GATT, 1994, Article VI). CEFTA also authorizes the signatory countries the use of antidumping duties in accordance with WTO procedures (CEFTA Annex 1, Art. 22). The Law adopted in Kosovo relies on these principles but enforcement mechanisms make it unworkable (see earlier discussion). The WTO sets forth principles and procedures for the imposition of anti-dumping measures. “Dumping” is defined as products of one country being introduced into the commerce of another country at less than the “normal value” of the products. Specifically, dumping occurs when the export price of the product exported from one country to another is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country.

The Agreement specifies that in order to impose anti-dumping duties, authorities have to demonstrate that there has been a material injury, threat of material injury, or material “retardation” or holding back of the establishment of the domestic industry. In addition, authorities must establish that there is a causal link between dumped imports and injury to domestic industry. Antidumping duties cannot exceed the anti-dumping margin. With regards to the timeframe, duties have to be terminated in a five-year time, with possibility of extension if the injury to the domestic industry persists. Since complex antidumping investigations can take more than a year before conclusion, the Agreement envisages the imposition of provisional measures (up to nine months) before imposing definitive antidumping measures.

As regards to the implementation of anti-dumping measures, according to some stakeholders from the business community, there was a failure to comply with procedures and legal and procedural provisions. According to them, these violations (specifically when setting these measures to Building bricks imported from Serbia) have to do with criteria to assess the imported goods price in relation to the prices of the same goods sold in the market of Kosovo, informing and consulting businesses and assessing the damage caused by these measures to the local businesses. Another drawback mentioned by representatives of the business community is the lack of transparency.

Therefore, during the implementation of such measures in the future, it is necessary to address these shortcomings by focusing on capacity building of institutions responsible and proactive and systematic inclusion of the business community in consultations during the development and implementation of legislation and policies. As highlighted above, in particular the first requires capacity building of the Department of Trade on market research and policy analysis, improving the exchange of statistical data, and improving the quality of the horizontal structures in the area of trade. In this regard, we also need to improve the transparency of institutional structures established to take de-

cisions on specific cases. Finally, the information improvement and the capacity building of business associations to participate effectively in the development and implementation of legislation and policies are required. This includes improvements in terms of expertise, information collection, market research and consultation mechanisms within them, and should affect all sectors of the economy and issues related to the functioning of businesses represented by these associations.

#### **4.4.2. Countervailing Measures**

Known also as anti-subsidy duty, pursuant to the WTO and CEFTA Agreements, countervailing duties are special duties levied for the purpose of offsetting any subsidy specifically granted to a manufacturer or exporter of goods when imports of those goods injure a domestic industry in the country of importation. Subsidies are defined generally as a financial contribution by a government that confers a benefit. Export subsidies (subsidies granted based on export performance or use of domestic content) are *per se* illegal. Other subsidies are actionable based upon their injurious effects. This includes Agricultural subsidies unless they in the “green box” as defined by the WTO Agreement on Agriculture.

For a number of years, there here have been calls from the business community in Kosovo to tackle unfair trade practices causing injury by, among others, Macedonian, Slovenian, Serbian, and Hungarian exporters as a result of subsidies granted by their respective governments. If their claims are substantiated, the unfair practices of Slovenian and Hungarian producers could be simply counteracted by increasing the MFN import duties for the agricultural products concerned. However, this approach would not work for the Macedonian and Serbian producers. By being a part of CEFTA, the Government of Kosovo has committed to keep import duties bound to zero. In this case, Kosovo has to resort to countervailing duty to counteract the injury to domestic producers caused by subsidized imports.

Within WTO rules, there is a two-track approach to addressing prohibited and actionable subsidies. First, the multilateral track takes the dispute through negotiation and if that is not successful, the WTO dispute settlement mechanism; and, second, the unilateral track relies on an individual WTO member launching an investigation to determine whether subsidized exports are causing injury to domestic industry. The CEFTA agreement is fully in line with WTO rules and procedures pertaining to countervailing duties.

##### **4.4.2.1. Safeguards**

Kosovo has recently adopted a safeguards legislation (the Law on Safeguard Measures on Imports, Law No. 04/L-047) that implements the WTO and CEFTA safeguard provisions. Safeguard procedures permit a country to restrict imports temporarily in situations where increased imports of a product have caused serious injury, or are threatening serious injury, to producers of the product in the importing country. The WTO's Safeguards Agreement sets forth procedures to be followed by WTO members before

increased tariffs, quotas or other import restrictions can be applied. In principle, safeguard measures have to be applied to the imports from all countries exporting the goods at stake. However, quotas can be allotted between supplying countries, and developing country exports can in some circumstances be excluded. In general, safeguard measures should not exceed 4 years although this may be extended for up to 8 years. In addition, restrictions should be progressively liberalized after the first year.

CEFTA Annex 1 Article 23(1) confirms the right of CEFTA members to take safeguard actions in accordance with the WTO Safeguards Agreement. However, in contrast to the WTO Agreement, Annex 1 Article 23(2) permits the use of bilateral safeguard measures. Article 23 applies specifically to agricultural imports and requires immediate consultations and also permits the imposition of “appropriate measures” pending a negotiated solution. Article 24(5) restricts bilateral safeguard measures under 23(2) to “an increase in the corresponding rate of duty applicable under this Agreement. The resulting rate of duty shall not exceed the lesser of: (a) the MFN applied rate of duty in effect at the time the action was taken, or (b) the MFN applied rate of duty in effect on the day immediately preceding the date of entry into force of this Agreement.”

It appears that the provisions of Article 24(5) limiting bilateral safeguard measures to an increase in the corresponding MFN rate of duty in effect at the time or the MFN rate of duty in effect immediately preceding the date of entry into force of CEFTA could be read as limiting safeguard measures imposed by Kosovo to the imposition of a 10% duty.

## **5. Trade and Employment**

Generally, the literature supports the view that trade is directly linked to economic growth and prosperity. First and foremost, trade enables full and efficient utilisation of nation's resources. Next, by expanding size of the market, trade makes possible division of labour and economies of scale. Moreover, exports are a transmission channel of skills, ideas, and technology. Competition enhancing effects of trade are also acknowledged. Exports are known to contribute to poverty reduction; exports of goods and services are believed to increase incomes for poor people, government revenue, opportunities for employment, including high paid jobs abroad, particularly for women and young job seekers.

Job creation and poverty reduction are critical for Kosovo, the expansion of country's international trade one of the priorities. According to the 2009 Labour Force Survey, unemployment remains extremely high, at 45.4%, although the unknowns regarding the informal sector conceal the real picture. To what extent export activity has maintained or generated new jobs in Kosovo remains unknown. No research has been conducted to identify the real effects of the trade on employment.

As a general principle, promotion of employment through exports requires that policy measures be concentrated on increasing the level of competitiveness of labour intensive activities. However, no definite answer can be given on the relationship between trade

and employment in Kosovo, and other related issues, without a well-informed analysis.

### 5.1. Trade and Foreign Direct Investments

Developing countries are actively seeking ways to attract FDI as a means of acquiring capital and technology and providing employment and export opportunities. There are a number of countries in the region that have been successful in increasing the levels of competitiveness of domestic industries through FDI. An earlier case is Hungary, and lately Serbia has been following the same path. Foreign multinationals are a source of capital, technology, and technical and managerial know-how. In addition, the evidence shows that multinationals produce spillovers for the entire economy, notably for domestic producers.

The data show that Kosovo still remains unattractive destination for foreign companies (for the recent data, see CBK, 2012). However, Kosovo has undertaken a number of policy measures to attract foreign investors. Kosovo has a fairly modern legislation protecting foreign investors, it has signed mutual investment protection agreements, expanded markets through trade liberalisation, and it has been striving to improve the overall business environment to attract foreign investors. With regards to the latter, Kosovo has been reducing red tape and other bureaucratic processes, easing the process of business registry, reducing time and costs of international transactions, adopting the ‘umbrella concept’ for permits, which aims to eliminate up to 50% of existing licenses until 2014, and other reforms.<sup>19</sup>

As pointed out earlier, the role of promoting Kosovo to foreign investors has been vested with the Investment Promotion Agency of Kosovo, which operates under the auspices of the MTI. The workload of IPAK is formally shared between investment promotion and export promotion, although the former takes priority. The mandate of IPAK covers: the support for the conduct of regulatory changes to create a favourable investment climate in Kosovo; supporting activities to promote Kosovo as an attractive investment location; providing information and consultancy to investors in order to overcome any barriers that they may face in the process of investment.

According to the business community estimates, there is a consistency in the institutions’ policies affecting promotion of FDI, as demonstrated by the application of anti-dumping measures for construction materials and potatoes, and temporary measures for cement. In this context, it is estimated that in addition to the EU and regional market, it is necessary to better utilize the General System of Preferences with the U.S. in order to increase foreign direct investments, particularly in agriculture and food industry. Also it is important to work on a more realistic and positive presentation of business environ-

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<sup>19</sup> Kosovo’s Answers to the EC Questionnaire on the Preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 121, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

ment in the country in front of the potential foreign investors (such as, e.g. about 29% growth of private sector in years 2009 to 2011, the operation of 30 businesses with a turnover of over € 5 million per year, etc.). Finally, it also needs an improved public-private dialogue for particular economic sectors with priority to trading in Kosovo, including e.g. policies such as the customs duties exemption of raw materials.

### **Summary of key Challenges Identified in the Area of Trade**

This report provides a detailed account of the major developments in trade in goods and services in Kosovo. Initially, it describes the basic indicators related to trade. Next, it discusses the institutional environment for trade, first, by reviewing the legislation, and, second, the institutions involved with governing trade-related affairs and coordination among the major stakeholders in trade. Further, the study discusses the major elements of the trade regime in Kosovo. Finally, a brief account on the relationship between trade and employment and trade and FDI is provided.

Based on the arguments provided, the next section outlines the main challenges facing stakeholders in Kosovo to lift the export sector to higher levels of international competition.

Looking at the international trade statistics for Kosovo, one can observe some striking developments:

- First is the widening trade deficit for goods, although exports have been growing at an impressive rate.
- Second, data reveal a lack of diversification and the predominance of low value added goods (e.g., metals and minerals, scrap) in the export structure.
- Third, although the trade surplus in exports of services is persisting, it may not continue for long as, on the one hand, the international donor presence is declining steadily, and on the other hand, services in Kosovo are becoming gradually becoming more attractive for foreign suppliers (for instance, construction sector).

In terms of legal framework in the area of trade, as identified in the 2011 EU Progress Report, approximation with the EU *acquis* still remains a challenge. Primarily, this concerns the quality infrastructure mechanisms. In addition there are calls for modernisation of customs legislation, and completion of contingency measures framework.

- With regards to the former, some progress has taken place in the legal framework, albeit further progress is necessary in the approximation of product specific legislation.
- With regards to the latter, the Report states that Kosovo's customs legislation is largely in line with the EU Customs Code, although there are calls for fur-

ther modernisation of the Customs legislation, mainly to provide for additional trade facilitation mechanisms and to make it fully compliant with new EU customs legislation.

- Furthermore, legislation on the contingency measures is not fully compliant with the WTO agreements and the EU directives. With regards to the latter, finalizing WTO compliant standard operating procedures, a specific requirement within CEFTA, remains an issue to be dealt with by Kosovo's authorities.
- In general, as with other legislation in Kosovo, issues with implementation and enforcement of some trade-related laws remain an issue of concern.

The two official documents of trade policy (as endorsed by Kosovo's institutions in 2004 and 2009, respectively) call for measures to increase the economy's competitiveness by further liberalizing trade, coordinating mechanisms on trade, tackling sectoral issues to increase domestic competitiveness, and erecting trade remedies mechanisms to counter-act illegal actions by neighbouring countries.

- However, these proposals seem rather disjointed, i.e. without a common thread. In addition, a large number of policy directions provided in these documents have not been implemented.
- The EU Progress Report argues that ad hoc policies generate increased economic uncertainty.
- Furthermore, according to the business community, other challenges include non-preferential economical policies for businesses, non-tariff barriers to exports (e.g. additional documentation requested from businesses), lack of fiscal incentives for business development, high interest and taxes (which affect many businesses extinct), and the lack of incentive policies (e.g. direct subsidies to agriculture, and subsidies to bank interest).

Furthermore, the major constraint to formal trade-related institutions remains the lack of sufficient technical and human capacities. This has been acknowledged in a number of studies conducted recently.

- Regarding the Department of Trade within MTI, the most difficult challenges are in the area of market protection.
- Another challenge in terms of the institutional building are insufficient capacities to study the impact of the implementation of the SAA part on trade to the economy of Kosovo (starting from the study in question that is part of the short term criteria deriving from the feasibility study, but also other similar studies that will be required in future during the SAA negotiations and its implementation).
- Regarding the business community involvement in the development of legislation and policies, the challenge remains the fact that the government institu-

tions do not take seriously enough into account needs, interests, proposals and recommendations of the business community in the development and implementation of legislation and policies, starting from the improved transparency. On the other hand, the lack of sufficient capacities of the business community associations to contribute sufficiently and effectively to the development of legislation and policies relevant to the area of trade also poses an obstacle.

- In addition, although coordinating mechanisms for the area of trade have been put in place, they are still not fully functional. In this regard, something that hampers their operation is uncertainties about the results and products that should derive from their work, and planning their work (at least annually). Further, issues with organisation of the meetings, representation, the speed of acting upon the issues brought forward by business community, pose a serious challenge to their functionality.
- Lack of adequate capacities of the business community associations to contribute satisfactorily and effectively to the functioning of the trade coordinating structures.
- At a strategic level, there is an overlap in responsibilities and functions of the Inter-Ministerial Committee for Trade Policies and the National Council for Economic Development.

One of the pressing issues on trade is related to the availability and the quality of data.

- The EU Progress Report warns that economic statistics remained weak, hampering a comprehensive assessment of the economic situation.
- In this context, trade analyses, a prerequisite for evidence-based decision making, is virtually inexistent in Kosovo.
- No policies or policy actions are assessed on ex-ante and ex post basis, which would enable policymakers to fine-tune trade-enhancing prescriptions on a regular basis.
- More specifically, the lack of sufficient cooperation at the technical level between institutions that possess relevant statistical data for the area of trade. (Mainly between MTI, the Statistical Agency of Kosovo, Kosovo Customs, Kosovo Tax Administration and Central Bank of Kosovo). In this context, there is no legal or procedural basis that would regulate access to, and exchange, integration and processing of statistical data that is in possession of each of these institutions.

There are many challenges regarding the implementation of legislation and policies in the area of trade. On the one hand, according to the business community, challenges include and relate to:

- Increased customs bases upon importation of goods;

- Non-implementation of CEFTA Agreement;
- Unfair competition (including 'hidden' subsidies);
- Lack of effective market surveillance;
- Implementation of anti-dumping measures and other protective measures in the form of ad hoc and based on individual businesses, rather than a broad approach, based on industry and economic sectors
- Legal infrastructure and very poor efficiency of courts;
- Law enforcement problems (in particular corruption and smuggling);
- Informality and fiscal evasion;
- Lack of good communication and support of municipal administration;
- On the other hand, the government institutions emphasize as challenge the insufficient awareness of businesses on trade legislation and policies, especially on requirements deriving from the approximation with European Standards and free trade with countries in the region.

Another challenge has to do with identification of the Kosovo economy sectors having competitive advantages.

## Chapter II: Industry and SMEs

### 1. General Overview

#### 1.1. Enterprise, SMEs and Business Environment

SMEs constitute the backbone of Kosovo's economy. They contribute to economic growth, employment, improvement of trade balance and generate biggest part of the state budget. According to the data of the Kosovo Business Registration Agency (KBRA), by the end of 2011 SMEs (including micro enterprises) constituted around 99.97% of all businesses operating in the country (for more details, see Table 2.1 below).

Table 2.1: Statistics on enterprises according to their size (2007 – 2011)<sup>20</sup>

	2007		2008		2009		2010		2011	
	No.	%	No.	%	No.	%	No.	%	No.	%
Micro enterprises	6,744	96.79	8,242	97.50	9,798	97.48	9,420	98.00	9,919	98.40
Small enterprises	178	2.55	160	1.89	215	2.14	165	1.72	139	1.38
Medium enterprises	40	0.57	43	0.51	31	0.31	21	0.22	19	0.19
Subtotal SMEs	6,962	99.91	8,445	99.91	10,044	99.93	9,606	99.94	10,077	99.97
Large enterprises	6	0.09	8	0.09	7	0.07	6	0.06	3	0.03
TOTAL	6,968	100%	8,453	100%	10,051	100%	9,612	100%	10,080	100%

Source: Kosovo Business Registration Agency

As the table shows, from 2007 to 2011, the number of SMEs grew at a rate of around 20% each year, while the overall increase during these five years was around 35%, yet there is no data available on the number of SMEs that were closed and went bankrupt. Based on the ownership type, the following categories of companies operate in Kosovo: individual businesses, general partnerships, limited partnerships, limited liability companies, share-holding companies, foreign companies, socially-owned-enterprises, publicly-owned enterprises, agriculture cooperatives, and other companies under the jurisdiction of the PAK (see table no. 2.2.).

<sup>20</sup> Ibid, p. 152.

Table 2.2: Statistics on number of companies based on ownership

Ownership type	Number of companies	Percentage
Individual businesses	105,623	88.82%
General partnerships	3,731	3.14%
Limited partnerships	92	0.08%
Limited liability companies (LLC)	8,340	7.01%
Share-holding companies	398	0.33%
Foreign companies	597	0.50%
Socially owned enterprises	22	0.02%
Publicly owned enterprises	12	0.01%
Agricultural cooperatives	76	0.06%
Companies	33	0.03%
Total	118,924	100%

Source: Business Registration Agency in Kosovo (November 2012)

The fact that over 88% of the companies are individual businesses shows that Kosovo needs to stimulate creation of more sophisticated forms of businesses.

On the other hand, KBRA data indicate that by the end of 2011 SMEs participated in employment with 232,411 employees, or about 63% of the total number of people employed by enterprises (Table no. 2.3.), yet there is no data available on the number of people employed by SMEs each year. According to the European Commission data, more than 90% of the enterprises employ less than four people.<sup>21</sup> Moreover, it is estimated that all enterprises produced 47.6% of the total amount of country's exports in 2011, and according to the 2010 data of the Tax Administration of Kosovo, SMEs participated with 43.3% in country's GDP.<sup>22</sup> On the other hand, it is estimated that given the number of new entrants to the labour market every year, Kosovo needs a real economic growth of at least 7%.<sup>23</sup>

<sup>21</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

<sup>22</sup> Kosovo's Answers to the EC Questionnaire on the Preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 251, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

<sup>23</sup> SME Development Strategy for Kosovo 2012–2016, p. 6, [http://www.smesupport.biz/cms/images/stories/key-documents/190711\\_sme\\_development\\_strategy\\_for\\_kosovo\\_en.pdf](http://www.smesupport.biz/cms/images/stories/key-documents/190711_sme_development_strategy_for_kosovo_en.pdf).

Table 2.3: Number of people employed by enterprises in December 2011<sup>24</sup>

Categories of SMEs	Number of enterprises	Number of employees
Micro enterprises (1 – 9 employees)	109,798	185,123
Small enterprises (10 – 49 employees)	1,508	24,877
Medium enterprises (50 – 249 employees)	224	22,411
<b>Subtotal SMEs</b>	<b>11,530</b>	<b>232,411</b>
Large enterprises (more than 250 employees)	60	137,096
<b>TOTAL</b>	<b>111,590</b>	<b>369,507</b>

Source: Kosovo Business Registration Agency (input for the Feasibility Study)

A basic comparison of the data provided in the end of 2011 with those provided in September 2012 (Table 2.4. below) indicate that there was virtually no change in the number of people employed by SMEs (an increase for only 6 employees), whereas the number of people employed by large enterprises seem to have dropped for 81,438 (from 137,096 down to 55,658). In relative terms, in end-2011 SMEs have employed around 63% of all people employed in all enterprises (with all the rest employed in large enterprises), while in September 2012 the share of those employed in SMEs rose to 81% (with the rest of 19% employed in large enterprises).

Another very problematic challenge remains the high discrepancy between the data of the BRAK about the number of registered businesses and those of the Kosovo Tax Administration about the number of businesses that pay taxes on regular bases. According to the latter, there were only about 40,000 businesses at the end of 2012. Based on the data of the business community (Kosovo Business Alliance), at least 60% out of the overall number of businesses registered with the KBRA are not active, since at least 1,000 of them close their activities annually (the report says that 6,000 new ones get opened). According to them, active companies should be considered the ones that pay taxes at least once a year. Therefore, a companies' bankruptcy system (including the legal and procedural bases as well as institutional and executive capacities of the judiciary for application) should be functionalised as soon as possible and it should be simple, quick, and without administrative or similar obligations.

On the other hand, the associations of business community should facilitate the application of measures for enhancing the capacities and capabilities of companies for application of the bankruptcy procedures and for operation in line with legal and procedural standards. In addition, this also shows that there is an urgent need for a significant improvement of the coordination between the KBRA, KTA, Market Inspectorate and Municipalities, as well as with the business community associations in order to make sure that work is being done continuously and systematically on the ground for identification of the businesses that do not operate anymore and those that operate illegally as well as to harmonise the data bases. According to the MTI, they have started to work on

<sup>24</sup> Ibid, p. 13.

the integration of their data bases in the second half of 2012.

Table 2.4: Statistics on the number of people employed by enterprises in 2012

Size of enterprises	Number of enterprises		Number of employees	
	No.	%	No.	%
Micro enterprises (1 – 9 employees)	109,800	98.4	185,129	64 %
Small enterprises (10 – 49 employees)	1,508	1.4	24,877	9 %
Medium enterprises (50 – 249 employees)	224	0.2	22,411	8 %
Subtotal SMEs	11,532	99.99%	232,417	81 %
Large enterprises (more than 250 employees)	58	0.1	55,658	19
TOTAL	11,590	100%	288,075	100%

Source: Kosovo Business Registration Agency

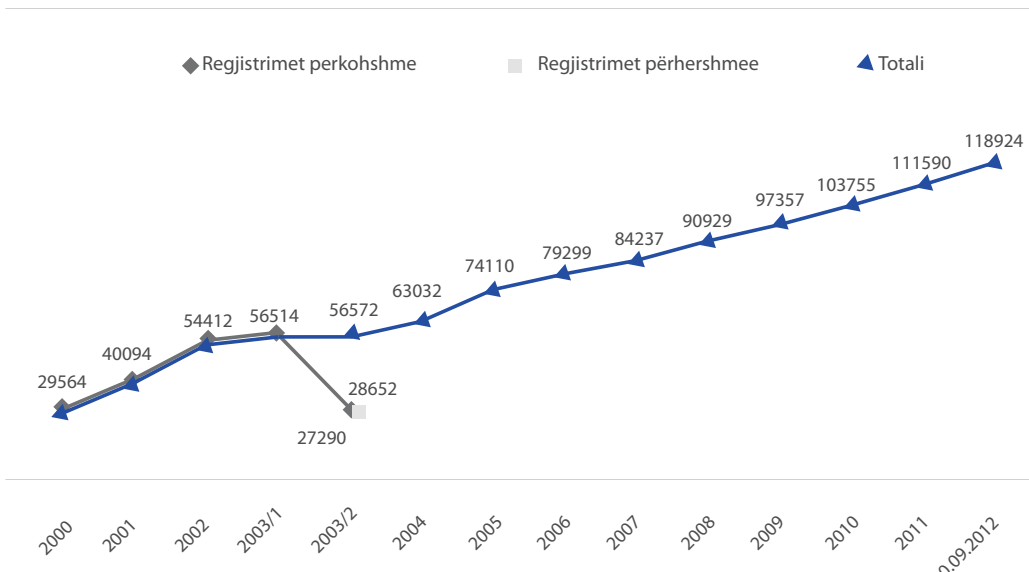
Given the size of the SME sector relative to country's economy, the Government of Kosovo recognizes the importance of SMEs to country's economic development, which is also demonstrated by adoption of the SME Development Strategy. Kosovo is also a member of the Small Business Act for Europe. However, a number of challenges need to be addressed. The discrepancy of data identified above shows that the data are not yet fully reliable. First of all, this shows that the process and methodology of data collection and processing used by the KBRA is standardized and regulated. Secondly, this methodology should be streamlined among those used by other relevant institutions (such as the Kosovo Agency of Statistics, Central Bank of Kosovo, Ministry of Labour and Social Welfare, etc.) so that the data collected and processed be comparable. This would enable unified interpretation of trends of SME development and their contribution to employment, GPD, exports and imports, state budget, and to economic development, in general (including various aspects related to foreign direct investments).

When discussing about SMEs, it shall not be forgotten that implementation of the Small Business Act for Europe as well as SMEs Development Strategy, are the major challenges. Implementation of both these important documents addresses all the challenges mentioned above. In order to implement these two documents, institutional coordination and efforts at central and local level need to be in place.

Thirdly, the whole process and methodology of data collection and processing should be more transparent, as this is fundamental to independent assessment of all such aspects of SME development, while the timing of their publication be standardized. Fourthly, this process needs to be improved substantially in terms of quality (including in terms of relation with aspects of education and vocational qualifications), with a view to enabling an easy comparison between the various sectors of SME activity. This would further enable easier identification of comparative advantages of business sectors and better utilisation of such qualitative data in developing policies and instruments for SME support and private sector development.

Moreover, the whole system of data collection needs to allow for a more accurate and objective analysis of the size of grey economy, which is, in turn, key to effectively fighting informal economy. This is because, according to the EU, informal economy in Kosovo is considered to be large and one that is fuelled by weaknesses in tax and expenditure policies and in law enforcement, including in the fight against corruption and organised crime, and as such, reduces the tax base and the efficiency of economic policies. Ultimately, addressing such gaps would contribute to establishing stable, transparent and predictable conditions for foreign investors and thus meeting SAA obligations.<sup>25</sup>

Chart 2.1: Trend of business registration in Kosovo in 2000 – 2012 period



Source: Kosovo Business Registry Agency

In addition to improving regulatory environment and infrastructure and an “[...] increased use of research and innovation policy [...]”<sup>26</sup>, efforts at a ‘micro’ level need to be focused on improving management skills of enterprises. Furthermore, according to the last EU assessment, the lack of information about SMEs is the main obstacle for their development, while the support for new businesses is undeveloped. In addition, the system for classification of companies should be improved even further.<sup>27</sup> On the other hand, difficulties in relation to legal enforcement of contracts, unreliable electricity

<sup>25</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

<sup>26</sup> Kosovo 2005 Progress Report, p. 44, [http://ec.europa.eu/enlargement/archives/pdf/key\\_documents/2005/package/sec\\_1423\\_final\\_progress\\_report\\_ks\\_en.pdf](http://ec.europa.eu/enlargement/archives/pdf/key_documents/2005/package/sec_1423_final_progress_report_ks_en.pdf).

<sup>27</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

supply and limited and expensive access to finance<sup>28</sup> still constitute serious structural impediments to SME and private sector development.

## **1.2. Industry and Industrial/Competitiveness Policy**

Traditionally, Kosovan industry was characterized by the production of metals and metallic products, plastics and rubber-products as well as chemicals. Covering only 30% of the demand of the local markets, food production is well below its potential, and therefore its increase could also help boost primary agricultural production. Kosovo has an enviable endowment of natural resources. At 14.7 million tons, Kosovo possesses the world's fifth-largest proven reserves of lignite. This mineral is of outstanding importance for the country, representing in the long term one of the important factors for the generation of power.<sup>29</sup> Mining industry in Kosovo has both a longstanding history and an important potential for future exploitation; there are estimates that Kosovo's grounds bear at least €13.5 billion worth of mineral resources. Kosovo's mines yield lead and zinc, and especially lignite, the latter serving as Kosovo's main source of electrical energy.

In order to be able to address in a very comprehensive way all issues related with industry sector the Ministry of Trade and Industry has adopted a strategy in 2009, which was not endorsed by the Government of Kosovo. There has been some progress in the area of enterprise and industrial policy, particularly as regards policy development in favour of SMEs. However, efforts to develop industrial policy and policy in strategically important manufacturing sectors need to be intensified.

As far as industry is concerned, the business community assesses that a challenge that should be addressed with priority is the lack of sufficient institutional capacities for situation assessment in the industry sector. The best assessment of the current situation is of crucial importance for development of more quality policies, including identification of priority industrial sectors that have competitive advantages, as well as concrete measures of public policies for helping the development of industry. The challenge with institutional capacities is also related to policies that are about industry and SMEs, particularly in the areas of trade, quality infrastructure, fiscal policies, education and professional training programs in line with the labour market demands.

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<sup>28</sup> Ibid.

<sup>29</sup> Invest on Kosovo, ECIKS, pp. 13-14, [http://www.eciks.org/english/publications/InvestinginKosovo\\_2011\\_Web.pdf](http://www.eciks.org/english/publications/InvestinginKosovo_2011_Web.pdf).

## 2. Legal and Policy Framework in the Area of Industry and SMEs

### 2.1. Domestic Legal Framework on SMEs

This section provides an overview of the domestic legal framework relevant for the area of enterprise, SMEs and business environment, focusing on laws governing support to SMEs, business organisations, inspection services, internal trade and foreign investments.

*The Law No. 03/L-031 on Support to SMEs*<sup>30</sup>, adopted in 2008, aims to regulate government policies and measures on classification, as well as promotion of creation and development of SMEs. It establishes three categories of enterprises (based only on the number of employees): micro enterprises (up to 9 employees), small (10 – 49 employees); and medium enterprises (50 – 249 employees). However, according to the latest assessment by the EU, the classification of enterprises needs to be further improved.<sup>31</sup> It also further clarifies responsibilities of the SME Support Agency of Kosovo (SMESAK) within the Ministry of Trade and Industry, putting it in charge of supporting SMEs through various mechanisms: legal and policy development; access to finance and other direct support programmes and schemes; private sector investment; eliminating and reducing barriers to business doing and SME development and opening up market opportunities for SMEs; entrepreneur training and consultation; business incubators, business and industrial parks; establishing flexible rules governing employer-employee relations; facilitating communication between SMEs, with larger enterprises and other relevant private consultants, trainers and professionals, with a view to enhancing capacities and expertise of SMEs; and information sharing. The framework of promotion of SMES involves the following activities: encouragement full use of business incubators, development of an effective system for management of data, establishment of business parks in small cities, as well as analyzing their functioning and providing recommendations.<sup>32</sup>

The *Law No. 04/L-006 on Business Organisations* specifies the types of business organisations through which business activity may be conducted in Kosovo. It also establishes the registration requirements for each type of business organisation, lists the legal provisions applicable to each type of business organisation with respect to its legal capacity and structure, as well as their rights and obligations as legal entities, of owners, managers, directors, legal representatives and third parties. It also establishes the legal provisions aimed at promoting and facilitating orderly and efficient creation, opera-

<sup>30</sup> Law No. 03/L-031 amending the Law No. 02/L-5 on Supporting the Small and Medium Enterprises, Article 3, [http://www.kuvendikosoves.org/common/docs/ligjet/2008\\_03-L-031\\_en.pdf](http://www.kuvendikosoves.org/common/docs/ligjet/2008_03-L-031_en.pdf).

<sup>31</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

<sup>32</sup> Kosovo 2010 European Partnership Action Plan, pp. 37–38, [http://www.mei-ks.net/repository/docs/EPAP\\_2010\\_final.pdf](http://www.mei-ks.net/repository/docs/EPAP_2010_final.pdf).

tion and dissolution of such business organisations. Similarly to common practices in EU countries, this law stipulates that the following five categories of businesses can be registered in Kosovo: (1) individual person enterprises (i.e. individual entrepreneurs)<sup>33</sup>, (2) general partnerships<sup>34</sup>, (3) limited liability companies, (4) limited partnerships and (5) joint stock companies. It also allows for registration a branch of a foreign company. Compared to previous provisions, registration procedures have been simplified under this law: registration is free of charge for start-up businesses, while the requirement of seed capital for LLCs is eliminated and that for JSCs is reduced from €25,000 down to €10,000.<sup>35</sup>

The *Law No. 03/L-181 on Market Inspectorate and Inspective Supervision* determines the inspective supervisory functions and operations and authorisations of market inspectors, who are in charge of implementing and enforcing legal provisions on inspection supervision. This law is considered to be in line with the Regulation no. 765/2008/EC. It reforms the Central Market Inspectorate into an executive body of the Ministry of Trade and Industry operating independently, with its separate budget allocation, and accountable to the Permanent Secretary of MTI. Accordingly, the Inspectorate is managed independently by the Chief Inspector, who is responsible for organizing and coordinating its work, setting -up its structure and methods to carry out market inspection, through the annual work programme of the Inspectorate.<sup>36</sup>

The *Law No. 04/L-00 on Internal Trade* regulates requirements for carrying out internal market trade (including wholesale and retail sale), auction, mediation in trade, restrictive practices, as well as protection measures for carrying out trade activity, supervisory measures, and administrative and punitive measures against illegal competition in the context of internal market. Compared to previous provisions, this version of the law has reduced the administrative burden for business doing by eliminating a number of work permits and sanitary inspection permits. Specifically speaking, six (6) licenses are eliminated for construction companies, which are: licenses for construction, design, revision, oversight licenses, technical acceptance license and lab license.<sup>37</sup>

The *Law on Foreign Investments* is designed to protecting, promoting and encouraging foreign investment in Kosovo by providing foreign investors with a set of fundamental and enforceable legal rights and guarantees, with e view to ensuring that they and

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<sup>33</sup> "A personal business enterprise is established by the operation of a business by a sole proprietor who is a natural person engaged in commerce" (Law on Business Organisations, <http://www.assembly-kosova.org/common/docs/ligjet/Law%20on%20amend%20law%20on%20business%20organisations.pdf>).

<sup>34</sup> "A general partnership comes into existence either through registration or by operation of law." (Ibid).

<sup>35</sup> Kosovo's Answers to the EC Questionnaire on the Preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 148, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

<sup>36</sup> Ibid, p. 174.

<sup>37</sup> Ibid, p. 150.

their investments are protected and treated with fairness and respect, in strict accordance with the rule of law and widely accepted international standards and practices. It focuses on non-discriminatory treatment of foreign investors.<sup>38</sup> This law is under the amendment procedure, with the changes proposed being aimed to improving business environment, with the aim of attracting and protecting foreign investors.<sup>39</sup>

As far as the area of SMEs is concerned, there is a general consensus between the governmental stakeholders and the business community that the legal framework is complete, particularly following the reforms of the last two years, as a result of which Kosovo was ranked higher in the World Bank's doing business report. However, a remaining challenge is the access of SMEs to finances, which needs to be addressed through the application of concrete measures and mechanisms within the governmental policies on relevant areas. In a more specific level, the EU Feasibility Study Report assesses that Kosovo should complete its legislation the policies on enterprises.<sup>40</sup>

## 2.2. Domestic Legal Framework on Industry

This section provides an overview of the legal framework relevant for the area of industry in Kosovo, namely laws governing trade of petroleum and petroleum products, tourism and touristic services, and economic zones.

The *Law on Technical Requirements and Assessment of Conformity* regulates the manner of prescribing the technical requirements for products, procedures of conformity assessment with the prescribed requirements and extraction of regulations by the competent Ministries. The provisions of this Law that apply to certain products or product groups regulate at least one of the following elements: (1) technical requirements which products that are being placed on the market or in use have to comply with; (2) rights and obligations of economic entities that place products on the market or in use; (3) conformity assessment procedures; (4) rights and obligations of bodies conducting procedures of conformity assessment of products with the technical requirements. As far as the implementation area is concerned this law regulates the market surveillance and the validity of conformity documents issued abroad.

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<sup>38</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 35, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

<sup>39</sup> Doing Business 2013: Smarter Regulations for Small and Medium-Size Enterprises, Banka Botërore, <http://doingbusiness.org/reports/global-reports/doing-business-2013>. This index averages the country's percentile rankings on 10 topics, made up of a variety of indicators, giving equal weight to each topic. The rankings for all economies are benchmarked to June 2012.

<sup>40</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

The *Law on General Product Safety* regulates general safety of products placed on the market. It applies to all products, which according to the law are considered products, unless the safety of a given product is regulated by any other provision of the applicable law. If the special law or the provisions governing application of that law regulate the safety a given product, then this Law shall apply only when the risks or types or risks for that product have not been anticipated by that special law or by the provisions resulting from that law.

Pursuant to the *Law on Trade of Petroleum and Petroleum Products*, the MTI Licensing Office is in charge of issuing licenses, following application, submission of the required documents and fee payment. The license is issued for each activity and storage, respectively for each sale station point separately, and it has a validity of 2 years. Licensing procedures for entities exercising tobacco trading activities are defined by AI o.04/2012, pursuant to article 17 of Law No.04/L-041 on Production, Collection, Processing and Trading of Tobacco. A commission formed by the MTI General Secretary decides on issuance, continuation, refusal, and abrogation of licenses. License validity is 5 years, with possibility of extension.

Licensing for activities of touristic agencies is regulated by AI No.12/2010, pursuant to *Law on Tourism and Touristic Services*. The licensing commission, formed by the MTI General Secretary, decides on issuance, continuation, refusal, and abrogation of licenses. It has a three year mandate. License for exercise of the activities by the agencies is valid for three years.<sup>41</sup>

The *Law on Economic Zones* is intended to ensure new investments, industrial and production activities for export, facilitate the entry of goods and capitals, apply the advanced technology, create new jobs and benefit from opportunities for foreign investments and financing and trade exchanges. It also governs the establishment, functioning, management and oversight of economic zones, stipulating the rights and obligations of developers, users/operators and other subjects that exercise activities related to economic zones, types of activities carried out in economic zones, and ways of moving goods through them, as well as fiscal easing predicted under them. The Ministry of Trade and Industry has initiated amending of this law, with the aim of easing the process of creation of the new economic zones, business parks, industrial parks and innovation centres. Such amendments will also reflect the relevant institutional setup.

In 2011, the Government of Kosovo took substantive steps to further open Kosovo to foreign investment through the passage of the *Law, No. 04 L-045 on Public-Private Partnership (PPP)*. The new PPP Law has been harmonized with the EU *Acquis*. The law creates separate definitions for Concession and PPP, meaning that deals can be structured more flexibly. A provision for unsolicited proposals has been removed, ensuring a competitive bidding process. Limits on the length of projects have also been removed.

<sup>41</sup> Kosovo's Answers to the EC Questionnaire on the Preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 149, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

### 2.2.1. Overview of the EU Acquis Applicable in the Area of Industry and SMEs

As in every other area in the framework of EU integration, the area of industry and SMEs is also regulated by a number of primary and secondary EU *acquis* acts. This legislation consists of two broad categories: principles enshrined in the treaties and specific provisions contained in the rest of EU *Acquis* acts issued by EU Institutions, namely EU agreements with third countries, regulations, directives and decisions (legally binding instruments), as well as recommendations and opinions (which do not have a legally binding effect).

As far as *principles enshrined in the Treaty on the Functioning of the European Union (Lisbon Treaty)* are concerned, it stipulates that the Union shall have competence to carry out actions to support, coordinate or supplement the actions of the Member States in, inter alia, the areas of industry and tourism.<sup>42</sup> Furthermore, the Treaty obliges the Union and its Member States to ensure existence of conditions necessary for industrial competitiveness. More specifically, in accordance with a system of open and competitive markets, actions of any member state in the area of industry and SMEs shall be aimed at:

- Speeding up the adjustment of industry to structural changes;
- Encouraging an environment favourable to initiative and to the development of undertakings, particularly SMEs, throughout the Union market;
- Encouraging an environment favourable to cooperation between undertakings;
- Fostering better exploitation of the industrial potential and policies of innovation, research and technological development.<sup>43</sup>

In addition, Member States are obliged to consult each other, in liaison with the Commission and, where necessary, coordinate their action. At the same time, the EC may take any useful initiative to promote coordination in this area, in particular initiatives aiming at the establishment of guidelines and indicators, the organisation of exchange of best practice, and the preparation of the necessary elements for periodic monitoring and evaluation.<sup>44</sup>

Another underlying principle enshrined in the Lisbon Treaty is that of strengthening the scientific and technological basis by achieving a European research area in which researchers, scientific knowledge and technology circulate freely, and encouraging it to become more competitive, including in its industry, while promoting all the research activities deemed necessary by virtue of other Chapters of the Treaties. This is aimed to be achieved also by encouraging SMEs in their research and technological development activities of high quality and by supporting their efforts to cooperate with one another with a view to enabling them to exploit the internal market potential to the full, in particular through opening-up of national public contracts, the definition of common

<sup>42</sup> Treaty on European Union and the Treaty on the Functioning of the European Union, Article 6, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2010:083:FULL:EN:PDF>.

<sup>43</sup> Ibid, Article 173.

<sup>44</sup> Ibid, Article 173.

standards and the removal of legal and fiscal obstacles to that cooperation.<sup>45</sup>

At the level of specific provisions, based on the structure of chapters, the area of industry and SMEs is covered by Chapter 20, on *Enterprise and Industrial Policy*<sup>46</sup> (see Annex 1 for a list of acts relevant for the area of industry and SMEs).

When it comes to the area of industry and SMEs in Kosovo, the domestic legislation at least makes reference to the relevant EU *Acquis*. However the question is to what extent the EU *acquis* is transposed into domestic legislation. This brings us to another point, namely that, formally speaking, Kosovan legislation in this area is in line with the EU standards, through reference made to the EU *acquis*, but in reality the institutions in charge, mainly the Ministry of Trade and Industry, need to do more in terms of effectively transposing EU *acquis* into national legislation, as well as ensuring compliance with it, implementation and enforcement.

On the other hand, the section on policy framework focuses mainly on the SME Development and Industry Strategies, but also on certain sections of other policy documents tackling the area of industry and SMEs.

### 2.3. Policy Framework in the Area of Industry and SMEs

In the context of EU accession, the practice is that enterprise policy is developed in an integrated manner, with the involvement of other ministries. The ministry in charge of drafting the National Development Plan consults the Ministry in charge of SMEs and industrial policies. In a more advanced stage of accession, the ministry in charge of SMEs and industrial policies participates in the preparation of projects that could be funded by pre-structural funds instruments. Lastly, there should be a co-ordinating structure, also including representatives of the business community, in charge of simplifying and improving the business environment.<sup>47</sup>

This section mainly focuses on the SME Development Strategy, but it also briefly discusses specific sections of other strategies that are relevant to SME and private sector development.

The *SME Development Strategy for Kosovo 2012 – 2016 (with vision to 2020)*, adopted in July 2011, is firmly based on the two main pillars of EU's SME strategic framework: the Small Business Act (SBA) for Europe, which Kosovo has committed itself to implement, and the EU Competitiveness and Innovation framework Programme (CIP), which Kosovo aspires to become part of in the near future.

<sup>45</sup> Ibid, Article 179.

<sup>46</sup> EUR-Lex: Industrial Policy and Internal Market, <http://eur-lex.europa.eu/en/consleg/latest/chap13.htm>.

<sup>47</sup> Guide to the Main Administrative Structures required for Implementation of the Acquis (2005), p. 66, [http://ec.europa.eu/enlargement/pdf/enlargement\\_process/accesion\\_process/how\\_does\\_a\\_country\\_join\\_the\\_eu/negotiations\\_croatia\\_turkey/adminstructures\\_version\\_may05\\_35\\_ch\\_public\\_en.pdf](http://ec.europa.eu/enlargement/pdf/enlargement_process/accesion_process/how_does_a_country_join_the_eu/negotiations_croatia_turkey/adminstructures_version_may05_35_ch_public_en.pdf).

As a sectoral document setting out the policy framework of the Government of Kosovo on SMEs, this strategy consists of measures (divided into three levels: strategic goals, goals and strategic objectives) needed to be undertaken in order to further advance reforms towards a dynamic SME sector and generate new jobs. Its vision being “*globally competitive Kosovo SMEs*”, the mission set out by this strategy is the following: “*Improvement of the business environment and entrepreneurship culture with the aim of the creation and rapid growth of sustainable SMEs*”. At the level of strategic goals, the SME Development Strategy aims at strengthening the legal and regulatory framework; improving SMEs’ access to finance; promoting and developing entrepreneurial culture; strengthening domestic and international competitiveness of SMEs; improving dialogue between private and public sectors and with civil society; strengthening SME support institutions; and improving the position of female entrepreneurs, youngsters, minorities, specific groups and support for entrepreneurs in disadvantaged zones.

When it comes to strengthening the legal and regulatory framework, it aims to achieve this by simplifying this framework, improving inter-ministerial support for implementation of this strategy, improving functioning of the Regulatory Impact Assessment (RIA), significantly increasing the number of SMEs entering the formal sector, improving the easiness of starting and closing businesses, as well as implementing the Small Business Act (SBA) for Europe. Improvement of SMEs’ access to finance is aimed to be achieved by developing, expanding and promoting a range of financial instruments for SMEs, attracting funds from diaspora, providing training to SMEs on access to finance, and increasing the level of fiscalisation. This strategy aims to promote and develop entrepreneurial culture by strengthening this culture itself, promoting and increasing co-operation between schools and businesses, and stimulating creativity and innovation. Competitiveness of SMEs is aimed to be achieved through development of SMEs’ technical, innovative and management skills (in line with the EU Information and Communications Technology Support Programme – ICT-SP), introduction of international standards and quality management systems, developing and ‘import substitution’ plan to support SMEs’ competitiveness in the domestic market, identification of priority sectors for SME support, establishing a Business Innovation Centre, and facilitating access of SMEs to regional and other foreign markets.

Under improving dialogue between the public and private sectors and with civil society, this strategy aims to raise SMEs’ awareness on economic development, support the EU Integration Working Group on Economy and Trade, as well as by improving the advocacy process and responsiveness of institutions towards SMEs. When it comes to strengthening SME support institutions, this strategy sets out to target the SME Support Agency, Regional Development Agencies, Municipal Business Centres, economic zones, business parks and business incubators, as well as business consultants and business service providers. The last strategic goal targets specific groups of people active in the SME sector, such as women, youngsters, people with special needs, minorities and people living in disadvantaged areas.

A key obstacle to implementation of the SME Development Strategy so far has been lack

of an implementation plan. On the other hand, its implementation requires that sufficient budget is allocated and capacities of relevant authorities are further strengthened.<sup>48</sup> Moreover, although it should serve as a referring document for all relevant authorities in dealing with the area of SMEs, the lack of involvement of other institutions but MTI in developing it might pose another set of challenges in implementing it. Therefore, an action plan would also help towards a clearer division of responsibilities among various stakeholders relevant for the area.

With more than half of SMEs in the country engaged in trade, yet only fewer than 10% of them engaged in production (mainly in food, drinks and tobacco industries)<sup>49</sup>, this vision and mission are clearly too ambitious to be achieved within five years, particularly given Kosovo's huge trade deficit (the latter, due to both the weak structure of its exports and an underdeveloped industrial sector). Therefore, the SME Development Strategy needs to be better linked with the Trade Policy and the Industry Strategy, and vice-versa, while the two latter also need to be accompanied by action plans that would more clearly set out measures to implement them. Another challenge in terms of implementation is that this strategy establishes a rather limited number of policy instruments, particularly when it comes to direct support to SME development and growth. While aiming to consolidate and establish a sound private sector legislative and regulatory framework and to improve access of SMEs to information on laws and regulations, it states that introduction of streamlined regulatory procedures will contribute to fighting informal economy by encouraging SMEs to register, as "This should afford SMEs greater opportunities to access sources of credit and financing and commercial dispute resolution, while contributing to overall market-based economic development and robust job creation" in the sector.<sup>50</sup>

In order to enable effective support to SME development and easing business doing in an uncompetitive and red tape heavy environment, a right balance between further legislating, in one hand, and rationalizing and streamlining the existing legislation in favour of easing business doing, on the other, is necessary. There also need to be clear objectives on what specific issues will be regulated by additional legislation and how that will contribute to SME and private sector development. The same is needed in relation to improved access to information. As far as it can be observed from the current situation analysis section of the strategy, this is chiefly due to limited baseline information and knowledge on the issues and needs of SMEs and private sector, in general. This is particularly the case when it comes to information on specific business sectors, since this section of the strategy contains very little information on the situation and needs of such sectors. Moreover, more involvement of and consultations with the business community in policy development is needed, whereas there need to be more clarity on

<sup>48</sup> Kosovo 2010 Progress Report, pp. 39-40, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2010/package/ks\\_rapport\\_2010\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2010/package/ks_rapport_2010_en.pdf).

<sup>49</sup> SME Development Strategy for Kosovo 2012-2016, p. 18, [http://www.smesupport.biz/cms/images/stories/key-documents/190711\\_sme\\_development\\_strategy\\_for\\_kosovo\\_en.pdf](http://www.smesupport.biz/cms/images/stories/key-documents/190711_sme_development_strategy_for_kosovo_en.pdf).

<sup>50</sup> Ibid, p. 20.

what policy measures, of a strategic nature, could be undertaken in order to genuinely improve access of SMEs to finances and contract enforcement.

A *Private Sector Development Strategy* was prepared in 2008 but was not approved by the Kosovo Government. It refers to SME Development as one of its components, but there is no reference to an action/implementation plan.

In addition to strengthening the SME Support Agency and the Investment Promotion Agency<sup>51</sup> (planned to be merged into one within the current year), other aspects to be addressed include better embedding of development of Free Economic Zones in the overall Government economic development policies.<sup>52</sup> Enhanced use of business incubators and business parks in supporting SME and private sector development, as well as continuously assessing and evaluating their functioning, with a view to providing recommendations, as also needed, but also development of an effective data management system.<sup>53</sup> A wider and more important need is carrying out strategic assessments on the specific sectors of business activity with competitive advantages and in need for restructuring.<sup>54</sup> Related to this, competitiveness of the specific sectors within the private sector also needs to be assessed<sup>55</sup> continuously, with a view to using proper policies and incentives in support of balanced development of a number of competitive sectors, such as, for instance, by addressing the existing imbalance between manufacturing and service sectors.<sup>56</sup>

On informal economy and supporting investment, while an updated action plan to address the informal economy and to remove administrative barriers to investment is in place and export guarantee funds have been established<sup>57</sup>, and many barriers to business doing have been removed, there is little or no comprehensive evaluation on what impact such action plans have so far had in economic development, particularly on alleviating the high unemployment rate that has already become chronic. In general, there is a consensus among various stakeholders that Kosovo has so far managed to attract a small amount of foreign direct investment, only around 8.5% of GDP, mainly concentrated in the services and financial sectors (with much less potential to improve trade balance and

<sup>51</sup> Council Decision of 18 February 2008 on the principles, priorities and conditions contained in the European Partnership with Kosovo, [http://eur-lex.europa.eu/smartapi/cgi/sga\\_doc?smartapi!celexplus!prod!DocNumber&lg=en&type\\_doc=Decision&an\\_doc=2008&nu\\_doc=213](http://eur-lex.europa.eu/smartapi/cgi/sga_doc?smartapi!celexplus!prod!DocNumber&lg=en&type_doc=Decision&an_doc=2008&nu_doc=213).

<sup>52</sup> Stabilisation and Association Process Dialogue (SAPD): Conclusions of the 2012 Subcommittee Meeting on Trade, Industry, SMEs, Customs and Taxation, Ministry of European Integration, July 2012, Prishtina.

<sup>53</sup> Kosovo 2010 European Partnership Action Plan, pp. 37–38, [http://www.mei-ks.net/repository/docs/EPAP\\_2010\\_final.pdf](http://www.mei-ks.net/repository/docs/EPAP_2010_final.pdf).

<sup>54</sup> European Commission Enlargement Strategy and Main Challenges 2007–2008, pp. 44–45, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2007/nov/strategy\\_paper\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2007/nov/strategy_paper_en.pdf).

<sup>55</sup> Kosovo 2010 European Partnership Action Plan, p. 33, [http://www.mei-ks.net/repository/docs/EPAP\\_2010\\_final.pdf](http://www.mei-ks.net/repository/docs/EPAP_2010_final.pdf).

<sup>56</sup> Stabilisation and Association Process Dialogue (SAPD): Conclusions of the 2012 Subcommittee Meeting on Trade, Industry, SMEs, Customs and Taxation, Ministry of European Integration, July 2012, Prishtina.

<sup>57</sup> European Commission Enlargement Strategy and Main Challenges 2007–2008, p. 23, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2007/nov/strategy\\_paper\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2007/nov/strategy_paper_en.pdf).

generate jobs, compared to other sectors, such as, for instance, manufacturing). This is also because, in order to meet its obligations within the framework of the SAA, Kosovo has still to establish stable, transparent and predictable conditions for foreign investors.<sup>58</sup> Furthermore, development of an innovation strategy started in March 2012.<sup>59</sup>

The *Kosovo Economic Vision 2011 – 2014 Action Plan*, which highlights the main economic development priorities and sectors, aims, among others, to improve investment environment and support the private sector. This is aimed to be achieved by amending and completing the essential legislation that create conditions to attract investment and removal of excessive administrative barriers, with a view to facilitating operation of the private sector and thus contributing to economic growth. This entails comprehensive reforms to eliminate 50% of the excessive license and permit requirements. Another aspect in terms of developing this sector is intensifying activities for attracting foreign investments and integration in the international financial institutions.<sup>60</sup>

When it comes to the *legal and regulatory reform*, although judged to be satisfactory and in line with the EU legislation, the current level of development of the legal and policy framework in Kosovo, as well as its implementation, still seems to fall short in terms of creating a supportive environment for SME growth. Therefore, the Ministry of Trade and Industry has recognized that more efforts, at all levels of government, are needed to remove barriers to business investment, growth, and job creation, and that simplifying administration is a key to promoting development of the SME sector. These efforts constitute the core elements and thus play a prominent role in the new development concept for the SME Development Strategy for Kosovo. The challenge is to build on and integrate the regulatory reform components of the various initiatives under way relating to investment, as well as the legal and competitiveness reforms and investment promotion policies, while also focusing in meeting requirements in the framework of EU accession.

It is worth pointing out that when it comes to the start up of new businesses, the Government has made some progress. The business registration system has been linked with that of the Tax Administration and Customs, which enables businesses to obtain the fiscal number, VAT Certificate or the import-export certificate (in the case of small importers) in parallel to the registration process. In other words, businesses now can be registered with a single procedure in one place, or “One Stop Shop”. This is a very im-

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<sup>58</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

<sup>59</sup> Kosovo's Answers to the EC Questionnaire on the Preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 246, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

<sup>60</sup> Ibid, p. 134.

portant step in improving the legal and regulatory business environment in Kosovo. In addition, the Government of Kosovo has initiated the process of drafting two additional laws, a law on licence and permit system and one on inspection. The former will consolidate the regulatory framework on licensing and permits, and will improve the business climate by eliminating administrative barriers and reducing costs to business doing. It will also address some of the remarks of the World Bank *Doing Business Report*, i.e. dealing with construction permits. On the other hand, the latter will establish the legal framework governing inspections activities, also allowing internal market inspections to use ex officio authority.

Establishing the so-called '*regulatory guillotine*' is also part of reforms that are necessary in the context of legal and regulatory environment. It is a tool for rapidly reviewing a large number of regulations and eliminating those that are no longer needed without the need for lengthy and costly actions on each of them. Regulatory guillotine is a systematic and transparent approach to reviewing, eliminating, and streamlining business regulations, also adapting techniques used in other countries in transition to carry out rapid deregulation. As such, it provides a quick fix to the most critical problems of unneeded and inefficient regulation and creates an opportunity to build a permanent system for quality control of new business regulations, with a view to avoiding reoccurrence of the same problems (the so-called '*creeping reregulation*'). It is designed to reduce the costs of reform within a legal environment that is already overburdened by the need of difficult structural reforms.

The regulatory guillotine is based on the view that the regulatory problem facing businesses is systemic, and that isolated and marginal reforms must be supplemented by broad-scale and systematic reforms that extend across the public sector. It is expressly designed to:

- Reverse incentives in the reform process and thereby overcome some of the barriers that have slowed or blocked broad-based regulatory reforms in the past. These barriers include high administrative costs, intense insider resistance to change, and lack of planning on how to sustain change in the future;
- Create a sustainable process for future quality control and legal security, mainly by establishing a quality checklist and review process and by creating a comprehensive and central regulatory registry with positive security; and
- Create the institutional infrastructure needed to ensure continuous and effective implementation of regulatory reform, including establishment of mechanisms for inter-ministerial coordination and cooperation, strengthening the engines of reform, and building core capacities for regulatory analysis.

*Regulatory Impact Assessment (RIA)* can contribute to economic efficiency by highlighting aspects of regulation which limit consumer choice and the level of competition in an economy. It helps to identify potential burdens on business and ensure that they are kept to a minimum, and also serves to identify potentially anti-competitive or protectionist regulations prior to enactment of such regulations. By including consultation with a wide range of stakeholders, it also provides an opportunity for those potential-

ly affected by regulations to draw attention to unforeseen consequences that may not previously have been considered. Other positive aspects RIA brings about include increased efficiency and effectiveness of the public service, improved quality of policy advice given to ministers by promoting increased use of evidence (empirical data) in policy-making, reducing costs by allowing more extensive analysis of alternative options for achieving policy objectives. Last but not least, it contributes to achieving six principles of better regulation: necessity, proportionality, consistency, effectiveness, transparency and accountability. These principles should always be taken into account when evaluating different options and deciding whether a particular regulatory option should be pursued. The only assessment done so far is for the budgetary implications of the proposal, whereas the whole RIA process has not been used so far because of the lack of capacities of the Ministry of Trade and Industry.

In the area of industry, the *Industry Strategy 2010 – 2013*, adopted in 2010, contains a number of priorities, which will be reflected in the MTI sector strategy planned (which is expected to be completed in June 2012 and will cover the five-year period 2012 – 2017). It is intended to address, in a very comprehensive way, all issues related with industry sector, and contains the following main priorities: improving the legal framework in accordance with the new approach guidelines, promoting industrial development and increase the role of industry in GDP creation, increasing competitiveness of manufacturing enterprises and promotion of investment in industry. However, efforts to develop industrial policy and policy in strategically important manufacturing sectors need to be intensified.

The *SME Development Strategy 2012 – 2016* provides for strengthening of SME competitiveness in domestic and international markets. In addition, the Industry Strategy 2010 – 2013 contains a number of priorities, which will be reflected in the MTI sector strategy (expected to be adopted soon, covering the five-year period 2012 – 2017). These priorities are the following: improving the legal framework in accordance with the new approach guidelines, promoting industrial development and increase the role of industry in GDP creation, increasing competitiveness of manufacturing enterprises and promotion of investment in industry.<sup>61</sup> Development of an innovation strategy has started in March 2012.<sup>62</sup>

As far the framework of policies in general is concerned, the business community assesses that an important challenge for development of industry is the lack of an economic development master plan, and instead priorities are fragmented in separate strategies of different institutions. In addition, the EU Feasibility Study Report assesses that the lack of comprehensive easily accessible and updated information on SMEs is an important obstacle for the SMEs that operate in Kosovo. Last, but not least important, the EU assesses that Kosovo should work on further harmonisation of the support measures for

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<sup>61</sup> Ibid, p. 247.

<sup>62</sup> Ibid.

the SMEs through the Small Businesses Act for Europe.<sup>63</sup>

### 3. Institutional Framework and Development in the Area of Industry and SMEs

In the context of EU accession, the practice in the area of industry and SMEs is that the central body responsible for the formulation and co-ordination of policies is usually the ministry in charge of economic affairs or that of industry (and trade). In most countries, line ministries that are responsible for managing specific industrial branches are part in the policy-making process. For instance, foodstuff and wood processing fall under the competence of the Ministry of Agriculture, chemicals under that of the Ministry of Environment and pharmaceuticals under the Ministry of Health. Implementing agencies include those in charge of privatisation, competition, FDI and export promotion, SMEs, as well as chambers of commerce, business associations (horizontal and sectoral), regional development agencies and business support centres (including Euro Info Centres).<sup>64</sup>

In Kosovo, in the context of Government institutions, the main stakeholder in charge of the area of SMEs and private sector development is the Ministry of Trade and Industry, namely the SME Support Agency and Investment Promotion Agency.

Whereas the law formally establishing the *SME Support Agency* (Law on Support to SMEs) was for the first time adopted in September 2005, the agency started operating as of December 2006. The main role of the agency is advisory service and information, serving as a 'one-stop-shop' for all investors. This agency also aims to reduce the number of SMEs for which access to financial resources is an obstacle to their growth and development. In order to achieve this, this agency works in four directions:

- Formulation of proposals for improving SMEs access to financing, including alternative means that are viable (both financial and non-financial);
- Design and implementation of innovative SME financing instruments and capacity building for intermediaries (through the Credit Guarantee Scheme for SMEs);
- Creation of working groups to improve quality and access to professional advice, support and training on finances, and
- Developing programmes to establish credit for innovative business initiatives.<sup>65</sup>

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<sup>63</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

<sup>64</sup> Guide to the Main Administrative Structures required for Implementation of the Acquis (2005), pp. 66–67, [http://ec.europa.eu/enlargement/pdf/enlargement\\_process/accesion\\_process/how\\_does\\_a\\_country\\_join\\_the\\_eu/negotiations\\_croatia\\_turkey/adminstructures\\_version\\_may05\\_35\\_ch\\_public\\_en.pdf](http://ec.europa.eu/enlargement/pdf/enlargement_process/accesion_process/how_does_a_country_join_the_eu/negotiations_croatia_turkey/adminstructures_version_may05_35_ch_public_en.pdf).

<sup>65</sup> Kosovo's Answers to the EC Questionnaire on the Preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 254, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

The SME Support Agency continued to participate actively in regional initiatives. On July 2011 is signed the establishment act of Association for Development of Kosovan SMEs with SMEs Association for South-eastern Europe.<sup>66</sup> This is an important step towards bringing SME sector in Kosovo in a wider competitive environment. It has also initiated the process of membership into the Observatory of European SMEs<sup>67</sup> and the European Enterprise Network.<sup>68</sup> The SME Support Agency is the main institution responsible for implementing the SME Development Strategy, with an allocation of € 1.3 million and € 30 million from the donor community.<sup>69</sup>

The *Investment Promotion Agency of Kosovo (IPAK)* is in charge of supporting foreign investments (including promotion of exports) in Kosovo. It carries out this through a wide range of support programmes. The 2005 Law on Foreign Investments vests IPAK with the following responsibilities:

- Assisting foreign investors in ensuring observance of their rights, guarantees and privileges established by this law in relation to the establishment, implementation, operation and liquidation of an investment in Kosovo;
- Advising public authorities regarding their obligations and other matters relating to foreign investment;
- Receiving, on behalf of Kosovo, the consents of foreign investors to arbitration;
- Providing policy recommendations to the Government of Kosovo for the purpose of promoting the creation of a favourable investment climate in the country;
- Improving the perception of Kosovo as an attractive place for investment (through targeted advertising campaigns and public relations events, such as exhibitions, investor forums and seminars), and providing information to and liaising with public media;
- Supporting initiatives that seek to improve the quality of the investment climate through, inter alia, market surveys, feasibility studies and research, and participating in relevant governmental and non-governmental working groups and task forces;

<sup>66</sup> Input to the Progress Report (May–September 2011), Ministry of European Integration, 2011, Prishtina.

<sup>67</sup> The Observatory of European SMEs was established by the Commission in December 1992 in order to improve the monitoring of the economic performance of small and medium sized enterprises (SMEs) in Europe. Its task was to provide information on SMEs to policy-makers, researchers, economists and SMEs themselves. The last edition was published in 2007. **Since 2008 the Observatory of European SMEs has been replaced by the SME Performance Review (for more, visit <http://ec.europa.eu/enterprise/policies/sme/facts-figures-analysis/sme-observatory>).**

<sup>68</sup> The Enterprise Europe Network is a key instrument in the EU's strategy to boost growth and jobs. Bringing together close to 600 business support organizations from more than 50 countries, we help small companies seize the unparalleled business opportunities in the EU Single Market (for more, visit <http://een.ec.europa.eu>).

<sup>69</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

- Providing information and advisory services to investors for the purpose of facilitating investment decisions, establishment of businesses and of business contracts; and
- Promoting Kosovo's exports by, inter alia, researching and identifying export opportunities, marketing local products in activities abroad, providing technical assistance to exporting business organizations, and collecting, processing and distributing export-related information inside and outside of Kosovo.<sup>70</sup>

The Ministry of Trade and Industry has initiated the process of amending the Law on Support to SMEs. The new draft law is expected to be called a Law on the establishment of an agency for the development and promotion of the private sector, and will bring under the same umbrella SME Support Agency and Investment Promotion Agency of Kosovo. Currently, IPAK needs to strengthen its cooperation with local governments and the SME Support Agency in order to achieve a better coordination of activities<sup>71</sup>

The *Consultative Council for SMEs* was established in 2001 and it serves serving as a forum for discussion, consultation and advancement of issues that preoccupy the SME sector. The Council is chaired by the Minister of Trade and Industry and consists of 26 members representing governmental and non-governmental stakeholders, business community (Kosovo Chamber of Commerce), as well as universities and donors). The Council meets four times a year.<sup>72</sup> Its role needs to be strengthened in order to serve as an instrument for public-private and inter-ministerial cooperation, and thus to be able to influence the design and delivery of SME policies.<sup>73</sup>

In addition, an *Industry Subgroup* operates within the Trade Policy Working Group, where the following other stakeholders are represented: Ministry of Trade and Industry (Departments of Industry and Trade), Ministry of Finance, Ministry of Foreign Affairs, Ministry of European Integration, Customs, Food and Veterinary Agency, Tax Administration of Kosovo, Kosovo Chamber of Commerce, Business Alliance of Kosovo, Kosovo Chamber of Advocates, Association of Exporters, business representatives and relevant donors (UNDP, USAID, WB and EUO/EC). This subgroup operates since March 2011, and meets every three months. It has so far had the following main achievements:

Approval of Standard Operating Procedures, which define the scope of the subgroup as follows:

<sup>70</sup> Law on Foreign Investment, Article 20, [http://www.assembly-kosova.org/common/docs/lig-jet/2005\\_02-L33\\_en.pdf](http://www.assembly-kosova.org/common/docs/lig-jet/2005_02-L33_en.pdf)

<sup>71</sup> Stabilisation and Association Process Dialogue (SAPD): Conclusions of the 2011 Subcommittee Meeting on Trade, Industry, SMEs, Customs and Taxation, p. 9, [http://eeas.europa.eu/delegations/kosovo/documents/eu\\_kosovo/sapd\\_trade\\_conclusions\\_final\\_en.pdf](http://eeas.europa.eu/delegations/kosovo/documents/eu_kosovo/sapd_trade_conclusions_final_en.pdf).

<sup>72</sup> Kosovo 2007 Progress Report, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2007/nov/kosovo\\_progress\\_reports\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2007/nov/kosovo_progress_reports_en.pdf).

<sup>73</sup> Council Decision of 18 February 2008 on the principles, priorities and conditions contained in the European Partnership with Kosovo, [http://eur-lex.europa.eu/smartapi/cgi/sga\\_doc?smartapi!celexplus!prod!DocNumber&lg=en&type\\_doc=Decision&an\\_doc=2008&nu\\_doc=213](http://eur-lex.europa.eu/smartapi/cgi/sga_doc?smartapi!celexplus!prod!DocNumber&lg=en&type_doc=Decision&an_doc=2008&nu_doc=213).

- Reform of doing business and harmonization of legislation with EU directives on industrial products;
- Reform in the construction sector in Kosovo, and
- Reform the system of regulation in the market economy.

Signing of a Memorandum of Cooperation with the Kosovo Chamber of Commerce (in May 2011) on organization of fairs and workshops in specific sectors of industrial products.<sup>74</sup>

In July 2011, the establishment act of Association for Development of Kosovan SMEs with SMEs Association for South-eastern Europe was signed.<sup>75</sup>

Although MTI, as the main institution in charge of the area of industry and SMEs, has made significant progress in increasing its capacities and developing the legal and policy framework, ensuring better policy development and implementation requires that overall coordination and cooperation among the relevant stakeholders (such as SME and Investment Promotion Agencies, chambers of commerce, banking association, courts, regional development agencies, etc.) be further enhanced.<sup>76</sup> This also requires enhanced institutional capacities of the SME Support Agency, which remain limited.<sup>77</sup> On the other hand, although an entrepreneurship learning strategy was adopted in 2008 and its implementation started in 2009, in accordance with the European Charter for Small Enterprises (including through teacher training and curriculum reform), increased efforts are needed to establish structured cooperation and engagement of local businesses with schools.<sup>78</sup>

The MTI *Department of Industry* is in charge of institutionally supporting the establishment of a favourable environment for a sustainable development of the industrial sector in order to be more competitive in the local, regional and wider market. It is designed to achieve this through development of industrial legislation, in conformity with EU Directives and the World Trade Organisation principles and practices, as well as through development of industrial development policies on the effective use of natural and human resources, with a view to increasing domestic production and exports.

<sup>74</sup> Kosovo's Answers to the EC Questionnaire on the Preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 152, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

<sup>75</sup> Input to the Progress Report (May–September 2011), Ministry of European Integration, 2011, Prishtina.

<sup>76</sup> Kosovo 2011 Progress Report, pp. 42–43, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2011/package/ks\\_rapport\\_2011\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2011/package/ks_rapport_2011_en.pdf).

<sup>77</sup> Kosovo 2010 Progress Report, pp. 39–40, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2010/package/ks\\_rapport\\_2010\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2010/package/ks_rapport_2010_en.pdf).

<sup>78</sup> Kosovo 2009 Progress Report, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2009/ks\\_rapport\\_2009\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2009/ks_rapport_2009_en.pdf).

- *Public-Private Dialogue*

Regular quarterly meetings of the Business Consultative Council continued to take place until last year. Due to the fact that the previous format didn't serve effectively needs of public private sector dialogue the Ministry of Trade and Industry now is in a search to find and establish a better format that will practically will make Public Private Sector dialogue much more effective. This is also foreseen to be regulated with the new draft Law on the Establishment of the Agency for the Development and Promotion of Private Sector.

Making the public sector of Kosovo responsive to the needs of SMEs requires a healthy and productive dialogue between the two, but civil society sector acts as an intermediary, and often the initiator, of this dialogue. The overall mindset needed is that economic development of Kosovo is everybody's business. Many assessment reports on Kosovo continue to point out that further efforts are needed to enhance communication, cooperation, and coordination among and between all stakeholders (i.e. public sector, private sector, and civil society).

Building a tradition of dialogue and learning how to negotiate compromises, is one of the best ways for the Government of Kosovo to learn about and react to the private sector's problems and adjust its policies to ensure the sector's growth and development. Dialogue is also a way for Kosovo firms foster a good business climate to help their operations.

The participation of entrepreneurs, employees, civil society and citizens (i.e. consumers) in designing public policy is critical if the Government of Kosovo is to improve transparency, and the quality and effectiveness of its policies. It will thereby consolidate its legitimacy.<sup>79</sup>

Some of the main potential benefits of PPSD include: facilitating investment climate reforms by supporting champions of reform; creating momentum; and, accelerating the reform process. Taking the current situation into consideration, we recommend the following activities: Raise awareness of the role of SMEs in Kosovo's economic development and improve the advocacy process.

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<sup>79</sup> Public-Private Dialogue, DFID, WB, IFC, OECD, [www.publicprivatedialogue.org](http://www.publicprivatedialogue.org).

#### 4. Implementation and Enforcement in the Area of Industry and SMEs

Due to an unfavourable business environment and insufficiency of creative entrepreneurial culture, Kosovo still lacks fast growing innovative firms, which are the main contributors to job creation in Western developed economies. Above 50% of all SMEs are operating in the trade sector, which is characterized by low and unproductive investments. On the other hand, according to the data published by Kosovo institutions, net FDI inflows are estimated to have reached € 394.6 million (8.6% of GDP) in 2011, slightly higher than € 365.8 million in 2010. To date, some 2,000 companies of foreign or mixed ownership have invested in Kosovo.<sup>80</sup>

The construction sector has enjoyed an increase of FDI in Kosovo, followed by the real estate sector. Participation of manufacturing sector in total FDI has declined compared to last year. Financial sector participation in total investment has been on average about 12% of total FDI in 2011. Origin of foreign investment is mainly from EU countries. Slovenia, Germany, and Great Britain are the lead countries of FDI investments in Kosovo.<sup>81</sup> However, the imbalance between manufacturing and service sector remains a critical issue<sup>82</sup> that should be addressed within the framework of implementation of the SME Development Strategy.

At the level of regulatory framework, the time needed for completing the registration of a company with limited liability and joint stock company at Kosovo Business Registration Agency (KBRA) is 3 days. On the other hand, KBRA does not yet apply bankruptcy procedures, but provides ceasing of operations services.<sup>83</sup> Particularly important is the online database of businesses, which requires removal from it of all businesses which are not functional.<sup>84</sup>

According to the EU Feasibility Study report, the cost of the compliance of enterprises with the laws and regulations in force remains high, the support measures for new companies are undeveloped, while incubators are still in the pilot phase and the application of the voucher scheme was cancelled in 2011. Last but not least, the EU recommends

<sup>80</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 35, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

<sup>81</sup> Kosovo's Answers to the EC Questionnaire on the Preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 108, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

<sup>82</sup> Stabilisation and Association Process Dialogue (SAPD): Conclusions of the 2012 Subcommittee Meeting on Trade, Industry, SMEs, Customs and Taxation, Ministry of European Integration, July 2012, Prishtina.

<sup>83</sup> Kosovo's Answers to the EC Questionnaire on the Preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 150, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

<sup>84</sup> Kosovo 2012 European Partnership Action Plan, pp. 20-21, [http://www.mei-ks.net/repository/docs/European\\_Partnership\\_Action\\_Plan\\_2012.pdf](http://www.mei-ks.net/repository/docs/European_Partnership_Action_Plan_2012.pdf).

establishment of a fund for supporting of SMEs and entrepreneurship.<sup>85</sup> These and other challenges identified by the EU have been reflected in the Action Plan on Negotiation of the Stabilisation-Association Agreement, approved by the Government of Kosovo at the end of 2012, but their successful application requires a significant increase of the amount of the budgetary funds allocated for this sort of schemes as well as support for the development of SMEs and industry in general. On the other hand, based on a training needs analysis for SMEs – conducted by the EU SME Project, which included 109 SMEs operating throughout Kosovo – the most urgent identified needs are related to marketing and sales, quality management systems, promotion of export, as well as management and supervision of production.

- *Access to Finance*

The banking sector is considered as one of the success stories, as it has experienced substantial and qualitative growth. According to the Central Bank of Kosovo, assets of the banking sector amounted to €2.5 billion by December 2010, which represents an annual increase of 11.4%. The value of total banking sector loans amounted to €1.5 billion, an annual growth of 13.2%. Loans to the trade sector dominate commercial lending with 50.8% of total loans to enterprises, while loans to manufacturing enterprises represented 12.3% and to construction businesses 10.6%.

Nevertheless the access to finance is a concern for firms in the SEE region. In a 2012 OECD survey of high growth SMEs, access to finance was highlighted as a very important barrier, second only to corruption.<sup>86</sup> Therefore it is imperative that SMEs receive the support of the banks. It is also clear why all the banks focus on SME as their target customers, although only representing 17% of the companies based on the number of employees. To judge a business by the number of its employees is but one measure, and just as relevant are its turnover, profit, and assets. However one of the main problems related with the access to finance for the SMEs is that all the banks, leasing companies, and Crimson lend, see SMEs as a key segment to target. However, none of the banks uses the same definition for a SME. The international banks mainly use the parameters dictated by their parent banks. The local banks have lower thresholds, reflecting their smaller capital and lack of ability to lend to larger businesses.<sup>87</sup>

Despite being perceived as a success story, Kosovar entrepreneurs continuously complain about the high interest rate. On the other hand, the banking sector regardless of the growth of value of loans still has substantial liquidity. Most of Kosovo bank's profit is earned from deposit banking. There is little incentive for banks to lend to SMEs. Measures to improve SMEs access to finance should include a reform of the Cadastral

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<sup>85</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

<sup>86</sup> OECD - EDIF Reform Prioritization, Prishtina, 17 October 2012.

<sup>87</sup> Access to Finance report, prepared by EU SME Project, September 2012.

system, Collateral and credit registration system, the enforceability of debts against the collateral. Additional efforts should be undertaken to develop a fully functional capital market in Kosovo. The legal and court systems, along with the defects in the Cadastral Registers (80% of Prishtina apartments are not legalized) are added problems.<sup>88</sup>

It is a general perception that SMEs are not fully aware of the range of financial options available in the market, therefore action should be taken in order to inform SMEs about the responsibilities of borrowing and repaying loans, and the relative costs of borrowing in the formal and informal sector.

One of the ways to improve SMEs access to finance is by attracting Diaspora funds for investments in Kosovo. Besides remittances directed toward subsidizing personal consumption for people living in Kosovo, the Diaspora is engaged in the privatization process and has directly invested in Kosovo. However there could be additional financial incentives to encourage further Diaspora investments and business partnerships

Within the Western Balkans Investment Framework, the EC encourages partners from International financial Institutions (IFIs) to support new forms of SME financing, in particular equity, venture capital and guarantee mechanisms. The Commission will co-finance a Western Balkan SME platform, which aims to improve access to finance for SMEs through guarantees and venture capital.<sup>89</sup>

To sum up, the main challenges as for as the access of SMEs to finances include limited access options, lack of well-thought proposals by SMEs, high interest rates, lack of the interest of the bank system to give longer-term loans and to lower the interest rates for enterprises in exchange with improvement of the governance of corporations (more precisely, regular auditing).

- *Entrepreneurial Culture and Innovation*

One of the main preconditions for business development is to strengthen the entrepreneurial culture.<sup>90</sup> Based on the current situation in Kosovo this goal will be achieved by: extending entrepreneurship curriculum in Primary Schools, VETs, High Schools and Higher Education Institutions; promoting success stories of enterprises implementing entrepreneurship programmes for young people, women and minorities; promoting and recognizing the most successful enterprises; and encouraging and increasing business networking. This will build upon, and align with, current and proposed donor interventions.

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<sup>88</sup> Ibid.

<sup>89</sup> European Commission Enlargement Strategy and Main Challenges 2011-2012, p. 10, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2011/package/strategy\\_paper\\_2011\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2011/package/strategy_paper_2011_en.pdf).

<sup>90</sup> SME Development Strategy for Kosovo 2012-2016, p. 6, [http://www.smesupport.biz/cms/images/stories/key-documents/190711\\_sme\\_development\\_strategy\\_for\\_kosovo\\_en.pdf](http://www.smesupport.biz/cms/images/stories/key-documents/190711_sme_development_strategy_for_kosovo_en.pdf).

Creativity and innovation are increasingly needed for businesses to gain and sustain competitive advantage. There is generally shortage of ideas on what kinds of businesses to start.

Most new businesses are 'me-too' business, because of this lack of ideas generation, innovation and creativity. This Goal within the SME Development Strategy will serve to develop training schemes introducing creativity and innovation to SME owners and managers, and potential new entrepreneurs. In a further move towards EU candidate status Kosovo will begin to implement the EU Entrepreneurship and Innovation Programme (EIP).

- *Bankruptcy*

The 2004 Law on Liquidation and Reorganisation of Legal Persons in Bankruptcy has apparently not been implemented also because the MTI has not adopted any bylaws implementing it. The law provides that a creditor can submit a bankruptcy petition to a court if (a) the debtor has failed to pay a debt that is at least 60 days overdue; or (b) the total amount of the overdue debt exceeds EUR 5,000. A debtor can initiate bankruptcy proceedings under the same conditions. There are also advertisement requirements. The failure of the directors and officers to initiate proceedings when this is necessary can lead to personal liability vis-à-vis the creditors. Public and socially-owned enterprises are not subject to this Law.

From the perspective of World Bank Doing Business Report for 2012 Kosovo is ranked in the 87 place out of 185 economies in the world.<sup>91</sup>

Having said this, the Ministry of Trade and Industry should immediately adopt bylaws deriving from the Law on Liquidation and Reorganisation of Legal Persons in Bankruptcy. Implementation of this law is important also from the perspective of Small Business Act.<sup>92</sup>

This basically consists on carrying out reforms that will facilitate starting a new business for those entrepreneurs who have previously declared bankruptcy. This means that the entrepreneurs who underwent through non-fraudulent bankruptcy can receive loans and support from institutions in less than one year. Deregistration from the insolvency register is automatic.

- *SMEs and the Informal Sector*

The informal economy prevents genuine competition and increases the relative costs

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<sup>91</sup> Doing Business 2013: Smarter Regulations for Small and Medium-Size Enterprises, World Bank, <http://doingbusiness.org/reports/global-reports/doing-business-2013>. This index measures the average of ranking of a country in 10 subjects, which consist of a variety of indicators, giving the same weight to each subject. Assessment of rankings for all economies covers the period until June 2012.

<sup>92</sup> Small Business Act, OECD, Indicator II.

of enterprises operating in the formal sector. Informal labour contracts and systematic evasion of social security contributions weakens worker protection and reduces their social benefits. It has a negative impact on budget and the entire infrastructure of society due to falling revenues and a subsequent reduction in the provision of proper public services.

An updated action plan to address the informal economy and to remove administrative barriers to investment is in place. Export guarantee funds have been established. An updated action plan to remove administrative barriers to investment is in place. However, further progress is needed on tackling the informal economy and improving the business environment.<sup>93</sup>

According to the report on the Government Programme for Prevention of the Informal Economy in Kosovo 2010 - 2012, the estimated size of the informal economy ranges from 39% to 50% of GDP.

Bringing more SMEs into the formal sector is one of the challenges in the context of implementing the SME Development Strategy. Informality weakens the trust between SMEs and the financial institutions and reduces SMEs' access to credit and ability to make use of formal mechanisms for disputes resolution. It also discourages foreign investment.

It is recommended to analyze both enforcement and encouragement to attract the informal sector towards the formal economy and tackle the factors that discourage SMEs from fully registering employees, activities, turnover and profits towards the respective authorities.

With the support of the *EU SME* project, the SME Support Agency has drafted the SME Development Strategy implementation plan, but it is not yet adopted. Nevertheless, one can observe that a number of activities foreseen thereby, which fall under the remit of the SME Support Agency, are already under implementation, such as reforms of the legal and regulatory framework, Small Business Days, and SBA Indicators. This draft-plan also contains objectively verifiable indicators. Other Government agencies were also actively involved in the drafting process. The SMESAK will review this plan on annual basis

- *Implementation of Legislation on SMEs*

Like in many other policy areas also in the area of SMEs one of the main challenges is the implementation of legislation. Legislation is not being fully implemented and the courts are burdened with a backlog of cases. Both businesses and potential investors require a stable and predictable legal environment in which to operate. When it comes to the legal

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<sup>93</sup> European Commission Enlargement Strategy and Main Challenges 2007–2008, pp. 53–54, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2007/nov/strategy\\_paper\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2007/nov/strategy_paper_en.pdf).

enforcement of contracts it is worth mentioning that Law Arbitration that was adopted in 2008 has now been enacted and AmCham and Kosovo Chamber of Commerce have been authorized to establish an Alternative Dispute Resolution (ADR) Centre to handle arbitration and mediation proceedings.

The right to proceed to arbitration must be included in any contract, and the arbitrators ruling be binding on both parties. Mediation is a less formal process but it is to be hoped that the outcome will be accepted by both parties.

- *Implementation of Small Business Act (SBA)*

In the area of private sector development, the policy coordination by the EU with the Western Balkans and Turkey is guided by the provisions of the EU's Small Business Act. This coordination, based on regular evaluations against established EU benchmarks, has resulted in the emergence of well-tested recommendations reflecting the national particularities of the enlargement countries. The Commission proposes that the results of the Small Business Act be used as a reference tool for future Small and Medium Enterprises (SME) -related activities in the region.<sup>94</sup>

The SBA is key framework policy document for SME development in Europe, which establishes 10 principles for development of SMEs:

- Encourage entrepreneurship culture;
- Reformation of bankruptcy system;
- Reduction of administrative obligations for SMEs,
- E-government and 'One-Stop Shops';
- Increase of access to public procurement;
- Access of SMEs to finances;
- Facilitate accesses of SMEs to opportunities offered by market alone;
- Improvement of capabilities of SMEs and utilisation of different forms of innovation;
- Providing support for SMEs to transfer business challenges into opportunities; and
- Encourage SMEs to benefit from development of trade in third countries.

As such, it is meant to guide private sector development by facilitating policy coordination in Western Balkans and Turkey. This coordination is based on regular evaluations against established EU benchmarks, leading to targeted recommendations, based on particularities of each enlargement country. The Commission proposes that the results of the SBA be used as a reference tool for future SME-related activities in the region.<sup>95</sup> Kosovo is following EU guidelines and the EU secondary legislation in the sector of SME already since 2002. Kosovo has committed itself to implementing the key principles of

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<sup>94</sup> European Commission Enlargement Strategy and Main Challenges 2011-2012, p. 10, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2011/package/strategy\\_paper\\_2011\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2011/package/strategy_paper_2011_en.pdf).

<sup>95</sup> Ibid.

the EU Small Business Act.

Since 2006, when the MTI SME Support Agency was established, Kosovo was included officially in the EU SME Charter process for the Western Balkans, which was based on the EU SME Charter of 2000. The success of the EU SME Charter has led to the SBA in 2009 which firmly based SME policy into the centre of economic and administrative decision making of the European Union and it is a major achievement for the EU and the SMEs in Europe. Kosovo's ability to implement it is hindered by budgetary and administrative constraints.

Therefore, the SME Support Agency is also in charge of coordination of all government activities related to implementation of SBA criteria.<sup>96</sup> Although Government has undertaken a number of measures to improve its ranking on the implementation of SBA indicators nevertheless there are still issues that need to be addressed in a better way. SME Strategy has addressed the issue related with the implementation of SBA Act. It should be noted that SBA Act indicators are responsibility of different government institutions and not only of the Ministry of Trade and Industry. Therefore, more efforts are needed for implementation the SBA indicators.

- *Small Business Days*

The SME Support Agency organizes the so-called Small Business Days. Activities undertaken during these days are in line with 'European SME Week'<sup>97</sup> and they take place almost at the same time like all other European countries. Currently Kosovo is not part of the European SME Week. Before it becomes a member into this forum, Kosovo should join EU Competitiveness and Innovation Program.<sup>98</sup>

It is crucial that the Ministry of Trade and Industry starts preparing a comprehensive analysis about the EU Community Programme on Competitiveness and Innovation. This analysis shall identify problems it is facing and will face when it comes to the access on this programme.

On *industry*, according to the latest assessment of the EU, Kosovo has not yet made use of the full potential of the benefits granted through the EU preferential trade regime and has a substantial trade deficit in industrial goods. To take full advantage of an SAA, Kosovo needs to undertake structural change towards higher added value in export

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<sup>96</sup> There are 10 SBA Principles and 144 indicators that derive from these 10 principles.

<sup>97</sup> Coordinated by the European Commission, this campaign **promotes enterprise across Europe**, in line with the Small Business Act for Europe.

<sup>98</sup> EU Competitiveness and Innovation Programme will change its name as Programme for the Competitiveness of enterprises and SMEs (COSME) 2014-2020 (for more, visit <http://ec.europa.eu/cip/cosme>).

goods, especially in intra-industry trade with EU companies.<sup>99</sup>

Similarly to that of SMEs, the area of industry also faces difficulties as regards legal enforcement of contracts, unreliable electricity supply and limited and expensive access to finance. Coordination and cooperation among relevant stakeholders (public authorities, chambers of commerce, banking association, courts, regional development agencies, etc.) also needs to be further improved, an implementation plan for the industry strategy to be adopted, adequate budget allocated and the responsible authorities need to be strengthened. Tourism is considered a potential to contribute to economic growth, but investment in the infrastructure is required. In general, Kosovo needs to develop policies aimed at promoting industrial revitalisation, modernisation and restructuring.<sup>100</sup>

### **Summary of key Challenges Identified in the Area of Industry and SMEs**

This report presents a detailed assessment of the developments in the area of industry and SMEs in Kosovo. It discusses at the beginning the legal base, then policies and institutional development framework, and the last part analyses the practical implementation aspects. The current situation is briefly presented throughout the report, with a special focus of the most important challenges of this area. In line with the findings and the presented arguments, this part summarises the main challenges and recommendations for addressing them. Challenges and recommendations are presented in an organised manner within the main aspects of the development of this area, such as: investment climate, (doing) business environment, access to finances, bankruptcy, development and application of policies on SMEs, gathering and processing of statistical data, implementation of legislation, informal economy, legal and regulatory reforms, assessment of regulatory impact, industrial policy, public-private dialogue, and EU programmes.

#### **Investment climate:**

- The investment climate provides the basic framework for all investors of home as well as foreign companies to ensure that their investments are protected and are made in a stable and reliable environment. Given that Kosovo businesses face with lack of markets, no doubt, an important challenge is the lack of a favourable investment climate. A favourable investment climate implies financially open markets (free and fast transfer of funds), rule of law, available capabilities, economic predictability, available infrastructure, internal markets, and particularly efficient labour market.<sup>101</sup>

<sup>99</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 21, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

<sup>100</sup> Ibid, pp. 36-37.

<sup>101</sup> Competitiveness of the wood-, metal-, ICT- and non-wood forest products sectors in Kosovo An orientation for future sector support, German Development Cooperation (GIZ Kosovo), 2011, Prishtina.

#### Business environment:

- No stable, transparent, and predictable conditions for investors have been created yet in Kosovo. In this context, there are still legal flaws in regard to the creation of conditions for investments and promotion of opportunities for investments and facilitation of doing business. In addition, there is still room for making the administrative and similar obligations easier as far as operation of enterprises is concerned.

#### Access to finance:

- As far as access to finances is concerned, the main challenges are related to the cadastral system reforms, loan registration system, and implementation of debts against collateral. In addition, another challenge remains non-development of the capital market. Thirdly, the attraction of funds from the diaspora for development of SMEs remains limited and there is no additional financial stimulation for encouraging further diaspora investments and business partnerships with them.

#### Bankruptcy:

- Kosovo has not established yet a complete and functional enterprise bankruptcy system, which includes legal and procedural base, infrastructure and institutional capacities (of the executive and judiciary), as well as capabilities of businesses to implement and act in line with bankruptcy standards, requirements, and procedures. In essence, bankruptcy implies the possibility for a quick closure of enterprises that need to bankrupt without too many obligations, as well as application of the reforms that would facilitate the start of a new business for the entrepreneurs that have declared bankruptcy before. This includes support through loans and other incentives for the entrepreneurs that undergo a genuine bankruptcy (not a fake one) as quickly as possible.

#### Improvement of policies on SMEs and their implementation:

- As stressed above, the development of better policies for modernisation, restructuring and strengthening of SMEs and their application remain a challenge. A medium-term strategy for development of SMEs was approved in 2012, but there is no action plan for its application yet.

#### Collection and processing of statistical data:

- Another problematic challenge remains the stressed discrepancy of data in the area of SMEs, as well as insufficient cooperation and coordination between the relevant institutions and with the business community.

#### Legislation application:

- The application of the primary and secondary legislation in the area of SMEs

remains a challenge as well.

#### Informal economy:

- A more difficult remains transfer of the informal economy to formal economy, including addressing of the factors that discourage SMEs to register fully their employees, activities, circulation, and profit at the respective authorities.

#### Legal and regulatory reforms:

- Another challenge is building of reformed regulatory components of different initiatives related to the European integrations, investments, legal and competitiveness reforms, as well as policies on promotion of investments and further legal and regulatory reform, aiming at further improvement of the business environment.

#### Regulatory Impact Assessment (RIA):

- In addition to the regulatory guillotine, there is also no Regulatory Impact Mechanism (RIM). The RMI can contribute to economic efficiency by stressing the regulation aspects, which limit consumer's selection and level of competitiveness in an economy.

#### Industrial policies:

- As stated above, Kosovo lacks adequate industrial development policies, which would contribute to the activation of economic growth resources, particularly to the production sector. In the post-industrial era, a combination of Information and Communication Technology with value added services would boost economic growth. That would take at least a decade or would require considerable investments in strengthening quality education and business environment. A priority should be given to re-industrialisation so that it does not turn against the services sector and competitive sectors in agriculture.

#### Public-private dialogue:

- In Kosovo, there is also no functional dialogue between the public institutions and the private sector in all the aspects of the development of industry and SMEs. This dialogue is crucial for enabling governmental institutions to react on time and adequately for addressing the problems and for adapting its policies in the interest of growth and development of SMEs.

#### EU programs:

- Kosovo is not yet part of the EU Programme for Competitiveness of Enterprises and Small and Medium Enterprises (COSME) 2014 – 2020.



## Chapter III: Existence of Functioning Market Economy and Capacity to cope with Market Forces Within the Union

### 1. Market Entry and Exit

Among a number of core reforms countries of the socialist block had to undertake in order to make a transition to a fully-fledged market economy was the economic liberalisation. The meaning of the economic liberalisation is threefold: first, it means loosening or elimination of government restrictions on domestic transactions, prices, and markets; second, it covers external transactions and the free exchange of domestic currency for foreign, or the so-called currency convertibility; and, finally it consists of free entry of firms into domestic markets.

With a view to facilitating doing business and making it financially cheaper, as well as in order to integrate the informal businesses into the formal market, Kosovo has made important steps in this segment of reforms, including by reducing legal and regulatory burden and barriers. It has also liberalized the market and prices, except in energy sector and some other services. In addition, it has almost fully liberalized international transactions. Nowadays, the average applied tariff rate is 4.8% across all products.<sup>102</sup> Kosovo does not apply non-tariff measures that would significantly impede foreign trade. It has adopted some licensing requirements for certain products as well as labelling requirements. Lastly, Kosovo has introduced policies and measures to promote private sector development. Kosovo has been undertaking steps to create the necessary conditions for the entry of firms into the market, especially *de novo* micro, small, and medium enterprises.

In addition, Kosovo has undertaken a program of privatisation of former Socially Owned Enterprises and corporatisation of Publicly Owned Enterprises. Furthermore, as the third ingredient of private sector development, Kosovo has been creating necessary conditions to attract foreign capital, or Foreign Direct Investments (FDI). In what follows, this report reflects on the recent development concerning the market entry processes in Kosovo; that is, creating of new businesses, privatisation process, and the inflow of FDI. We conclude the section with a discussion of the firms' market exit.

- *Creation of **de novo** firms*

With regards to the establishment of the new firms, policymakers in Kosovo have been concentrated on improving business climate and easing the process of business registry. The process of business registration has been simplified and facilitated, the number of required documents for exporting and importing has been reduced, and a number of licences have been abolished.

In addition, these and other legal reforms through the last amendments to the Law on Businesses Organizations, in order to facilitate the market entry, it also improves

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<sup>102</sup> Based on calculations of the Department of Trade, Ministry of Trade and Industry.

the protection of investors. These include increase of the requirements for declaration of conflict of interest, publication of annual financial overviews and the possibility of shareholders to law suit and to receive compensation. There are important legal reforms which facilitate market entry, including those in the area of construction. The new Law on Construction, which entered into force in July 2012, sets cadastral fees based on cost recovery, then a risk management approach in terms of administration, and provides that failure to reply means construction permit compliance, and also establishes a code of construction (through a legal act of the Ministry of Environment and Spatial Planning), which, among other things, sets technical standards for construction safety.

In financial sector, the Law on Banks, Micro Financial Institutions and Non-Banking Financial Institutions has advanced the legal base in many directions. It includes additional provisions for corporate governance of banks, administration of problematic banks and exit strategies. In addition, with the aim to improve the governance of banks and micro financial institutions, it sets out requirements for the criteria of the “fit and proper” principle for electing members of board of directors and senior management levels, their composition structure, requirement for declaration of conflict of interest, undertaking the administrative measures in cases of noncompliance with the regulations and laws into force towards institutions and individuals (shareholders, directors and senior managers). Finally, it provides new restrictions on concentrations of credit exposures and exposures to related parties of banks and consolidated supervision of banking groups.

With the support of the World Bank, 25 one-stop-shops have been established in different municipalities. The business registration certificate, fiscal number and VAT certificate will be issued on the spot. The business registration process has been simplified by removing the provision requiring the deposit of the minimum start-up capital (€ 5,000) for limited liability companies and by reducing start-up capital for joint stock companies from € 25,000 to € 10,000. These simplifications will facilitate business start-ups, and reduce the time to start a business. The legal framework and the practices are non-discriminatory. These and other reforms of the business environment helped Kosovo in climbing the ranking in the World Bank Doing Business classification by 28 places, from 128 in 2012 to 98 in 2013. The improvement in the “Starting a Business” indicator was the second largest contributor, following improvements in the “Protecting Investors” indicator. In the former indicator, Kosovo moved up for 44 places, whereas in the later jump was even higher, or 76 places.

As regards facilitation of the entry of new companies into the market, the main challenge remains the high interest rates and high risk of access to credit. In this context, there are numerous structural challenges related to improving the level of support to banking sector in the real market. This requires analysis of supply and demand for bank loans. Further, it should also focus on improving corporate governance, starting from increased reliability of financial statements of companies.

- *Privatisation of SOEs and corporatisation of POEs*

The process of privatisation of socially-owned enterprises in Kosovo begun in 2002, initially conducted by the Kosovo Trust Agency, operating under UNMIK Pillar IV. Following the Declaration of Independence in 2008, the KTA was converted into the Privatisation Agency of Kosovo. The modes of privatisation consisted of special spin-off (which imposed specific requirements on the investor in terms of investment, employment, etc.), regular spin-off (imposed no requirements on the investor), and liquidation. So far, in total some 306 socially-owned enterprises have been privatized fully or partially. The Agency has accumulated significant proceeds from the process, which have been ring-fenced to satisfy potential claims by creditors and workers. However, Kosovo is lagging in terms of large-scale privatisation. Kosovo has so far only privatized its distribution network. The tender has been completed for the Electricity Distribution and Supply Company in June 2012. The process of privatizing post telecom has been dragged for some time; however it is due to be finalized in 2013.

In addition, the Government has entered into or is considering long-term public-private partnerships (PPPs) as a way to attract private investments and develop the infrastructure. In 2010, a 20-year contract was awarded to an international consortium to operate the Pristina airport. Large privatisations and PPPs have the potential to attract investments and improve efficiency. They should however be managed carefully to limit government exposure to future liabilities and provide the right incentives for improved business and operational performance of the companies.

- *Foreign Direct Investments*

Foreign Direct Investments are an important ingredient to the development of the private sector. Conventionally, FDI are viewed as a source of capital and equipment, but at the same time a channel of knowledge transfer, managerial know-how and a route to access international trade networks. The emerging private sector in Kosovo, as well as in other transition countries, virtually lacks all these sources. Hence, FDI are necessary for the overall development of Kosovo.

FDI in Kosovo have been fairly low in the post-war period (see CBK, 2012). However, Kosovo has undertaken a number of policy measures to attract foreign investors. Kosovo has a fairly modern legislation protecting foreign investors, it has signed mutual investment protection agreements, expanded markets through trade liberalisation, and it has been striving to improve the overall business environment to attract foreign investors. With regards to the latter, Kosovo has been reducing red tape and other bureaucratic processes, easing the process of business registry, reducing time and costs of international transactions, adopting the 'umbrella concept' for permits, which aims to eliminate up to 50% of existing licenses until 2014, and other reforms. As pointed out, these and other related reforms have moved Kosovo in the WBDB "Protecting Investors" indicator by 76 places.

- *Market Exit*

The *Bankruptcy Law* governs the process of exiting the market. A bankruptcy law that provides for both liquidation and reorganization of problematic firms is an important tool for market economies. It provides failing firms with an orderly means of exit. It sources ailing but potentially viable firms to restructure. And, bankruptcy shifts control over financially distressed firms to their creditors before all the assets have been misused or dissipated, and it gives creditors the information and power to direct the use of the remaining assets to recover debts.

Kosovo Business Registry Agency does not have bankruptcy procedures. However, the Agency provides services for ceasing of operations. Procedures and documents necessary for the cessation of corporations are as follows:

- Completion of the D form;
- Liquidation announcement in 1/2 page in daily newspapers, in three languages;
- Certification from Tax Administration for business cessation;
- Certification by the Commercial Court;
- Original Business Certificate;
- Copy of owner ID, or passport (in cases of foreign owner/s);
- Corporate Liquidation Decision;
- Decision for appointing liquidator; and
- Capital assets report.

In the period 2007 - 2011 the total number of companies who ceased their operations is 5,822. From January 2012 until May 2012, a total of 337 companies have ceased operations.

In the financial sector, due to specifics and high sensitivity (this sector is among the most regulated sectors in all countries of the world), exit from the market is regulated specifically by respective laws on financial institutions. Law on Banks, Micro Financial Institutions and Non-banking Financial Institutions, adopted in April 2012, regulates the relevant issues, such as taking under administration or control of banks, their recapitalization, mergers, sales and restructuring and form of liquidation. This law is based on international best practices, taking into account the importance of addressing these issues in order to create conditions for more effective protection of depositors, as one of the key mandates of the CBK. As regarding pension funds and insurance companies, their exit from the market is also regulated by relevant laws. Law on Kosovo Pension Funds approved in April 2012, regulates the issue of exit from the market of supplementary pension funds (Pillar III). For insurance companies, this issue is currently governed by Regulation 2001/25 Chapter X, until the General Insurance Law is finalized, which will include the issue of liquidation of insurance companies and the rights and benefits of policyholders in such cases.

## 1.1. Legal and Policy Framework

The legislation pertaining to the firms' market entry and exit, privatisation, and foreign investments in Kosovo is completed. The shortcomings of the legislation covering these areas have been tackled through constant amendments. The core law covering the entry and exit of new firms in the market is the *Law No. 02/L-123 on Business Organisations*. The aim of the law is twofold. Firstly, it provides for, promotes and facilitates the efficient creation registration, operation and dissolution of the usual and customary types of business organizations. Secondly, it aims at bringing the regulation of business organizations in Kosovo into compliance with good market-oriented practices, as well as the basic mandatory requirements of the European Union. The Law has been amended a number of times mainly to incorporate provisions that cover business registry process. In addition to this law, a number of by-laws, which, among others, cover for the operation of Kosovo Business Registry Agency, also apply.

Apart from the Law on Business Organisations, market entry and exit in Kosovo is covered by additional legislation, such as Law on Internal Trade, Law on Trade of Petroleum and Petroleum Products in Kosovo, and Law on Production, Collection, Processing and Trading of Tobacco.

The *Law No. 04/L-005 on Internal Trade*, adopted in June 2011, has eliminated work permits and sanitary inspection permits. Six licenses are eliminated for construction companies, such as licenses for construction, design, revision, oversight licenses, technical acceptance license and lab license.

The process of privatisation of SOEs and corporatization of POEs are governed by two laws: Law on Privatisation Agency of Kosovo and Law on Publicly Owned Enterprises.

The *Law No. 04/L-034 on Privatization Agency of Kosovo* regulates the establishment of PAK and the entire process of privatisation in Kosovo. The 2011 EC Progress Report on Kosovo acknowledges that the new legislative framework on privatization is expected to speed up the liquidation process.

The *Law No. 2008/03-L087 on Publicity Owned Enterprises* and its subsequent amendment of 2012 establish a legal framework governing the exercise of ownership rights in publicly owned enterprises. In addition, the Law provides for the corporate governance of publicly owned enterprises in accordance with internationally recognized principles of corporate governance for publicly owned enterprises. Finally, the Law establishes effective reporting and accountability arrangements to facilitate appropriate oversight of the activities of publicly owned enterprises.

The *Law No. 02/L-33 on Foreign Investments* promotes and encourages foreign investment in Kosovo by providing foreign investors with a set of legal rights and guarantees that ensure protection and fair treatment for foreign investments, in strict accordance with the rule of law and widely accepted international standards and practice. The law is currently being amended to provide further guarantees and incentives for foreign investors.

Apart from certain bankruptcy provisions contained in the Law on Business Organizations (see Article 229 on corporate liquidation decision, decision for appointing liquidator, and capital assets report) the bankruptcy procedures in Kosovo are covered also by the *Law No. 2003/04 on Liquidation and Reorganization of Legal Persons in Bankruptcy*. This law sets out the conditions and procedures for the liquidation or reorganization of legal persons in bankruptcy, and determines the rights and duties of the parties participating or affected by such proceedings.

## 1.2. Institutional Framework and Development

Until recently, the only entity for business registry was the *Kosovo Business Registry Agency* (KBRA), operating within the Ministry of Trade and Industry. As pointed out earlier, with the support of the World Bank, so far 25 *Municipal Business Registry Centres* have been opened across Kosovo. This step is expected to significantly speed-up and ease the process of business registry. In addition, these offices serve as a one-stop-shop centres, where, in addition to obtaining business registry numbers, other necessary procedures to start a business (for instance, obtaining a fiscal number) can also be completed.

The *Privatization Agency of Kosovo* inherits Kosovo Trust Agency, which was dissolved the Declaration of Independence in 2008. The Agency has the authority to sell, transfer and/or liquidate socially owned enterprises and their assets.

The role of promoting Kosovo to foreign investors has been vested with *the Investment Promotion Agency of Kosovo* (IPAK), which operates within the MTI. The workload of IPAK is formally shared between investment promotion and export promotion, although the former takes priority. The mandate of IPAK covers: the support for the conduct of regulatory changes to create a favourable investment climate in Kosovo; supporting activities to promote Kosovo as an attractive investment location; providing information and consultancy to investors in order to overcome any barriers that they may face in the process of investment.

In the financial sector, *the Central Bank of the Republic of Kosovo* is responsible for licensing, regulation and supervision of all financial institutions, according to the principles of market economy, open to free competition and equal conditions for all participants, be them domestic or foreign participants. These competencies include the implementation of the criteria for licensing of new players in the financial sector, which are: capital, adequacy of the owners and senior management, the criteria “fit and proper”, sustainability and financial capacity, achievable business plans, and organizational structure that allows effective supervision of the institution.

According to the Kosovo bankruptcy law, *Municipal Courts* handle bankruptcy procedures for all companies, except SOEs.

*Market Inspectorate* is responsible to inspect private economic operators, based on the

laws and regulations into force (about 15 laws and 30 bylaws), in particular with regard to internal trade, consumer protection, general safety of products (of toys, electrical equipments, machinery, construction products, etc.), trade in oil and petroleum products, metrology, precious metal work, safety construction products, tobacco, tourism and touristic services, crafts, etc.

As regarding improving the governance and institutional capacity to enter into and exit from the market, it is also necessary to continue implementing measures to facilitate the business environment, including through e-governance and harmonization of databases of relevant institutions at the both levels.

## **2. Legal System**

Law in market economies defines the rules of the game and gives individuals the rights and tools to enforce them. The rule of law requires good laws, institutions to enforce them, and demand for those laws. First of all, drafting good laws is of fundamental importance, as the failure to pass good laws imposes costs that go beyond the mistakes in individual laws, and may even affect the integrity of the legal system itself. Laws passed with major inconsistencies and uncertainties, or with a scope for abuse, simply deepen the mistrust in the system. Second, strong and competent institutions are required to enforce the rule of law (more on this later). Finally, the rule of law can prevail and persist if there is a demand for good laws.

Individuals and companies have strong economic incentives to claim their legal rights. In addition, banks and other creditors, for example, will not take seriously their new rights under collateral, debt collection, and bankruptcy laws unless convinced that state bailouts are unavailable. They have to see that aggressive debt collection is necessary for survival. Similarly, when managers require a law-abiding reputation to purchase supplies or raise capital, they will think twice about violating the sanctity of contract or abusing minority shareholders. Market-oriented incentives therefore complement market-oriented laws and institutions.

Rule of law is a prerequisite for private sector development. Economic-related legislation in has at least four functions: defining and protecting property rights; setting rules for exchanging those rights; establishing rules for entry into and exit out of productive activities; and promoting competition by overseeing market structure and behaviour and correcting market failures. So far we have discussed the rules pertaining to the exchange of property right (that is, in the context of privatisation process) and the firm entry and exit processes. In what follow, we will concentrate on the mechanisms of protecting property rights, competition and avoiding market failures.

### **2.1. Property Rights and Contract Enforcement**

Property rights extend from full ownership through partial use rights (such as leaseholds and easements) to rights contingent on specific events (such as inheritance rights

and collateral rights to debtors' property). Countless types of property are defined and protected, from real estate and movable property to new ideas and inventions. Contracts are intrinsically linked with property rights as they provide the means to exchange these rights. With this, contracts serve to the development and prosperity of a nation as they provide a decentralized way of allocating resources to their best uses.

The EU, through the EC Progress Reports for Kosovo, has been stressing constantly that the legal system continued to suffer from poor accessibility and efficiency. In this context, it has been highlighting the need for improving mechanisms to protect property rights and enforce contracts. According to the main document that oversees the progress of current and future EU candidate countries, the weak rule of law in Kosovo and uncertainty over property rights remained major impediments to sustainable economic development. In addition, weak enforceability of contracts remained one of the main concerns of companies and investors in Kosovo. EC further argues that the difficult and costly legal enforcement of contracts continued to hamper seriously the business environment. It is also one of the factors explaining the relatively high interest rates charged by commercial banks to the private sector.

## **2.2. Competition**

Ensuring fair competition in the market is a means of progress. Competition can be promoted through reduction of tariffs and the removal of other non-tariff barriers. Furthermore, these steps should be complemented by regulation of natural monopolies and by antimonopoly legislation, in order to ensure efficiency and protect the public from the abuse of monopoly power in the market.

With a view to ensuring the development of a sound market economy by prohibiting acts that restrict, suppress or distort competition, Kosovo has adopted the *Law No. 2004/36 on Competition*. Specifically, the Law prohibits practices that directly or indirectly fix purchase or selling; limit or control production, as well as market, technical development or investment; limit, divide or share a market or one or more sources of supply; and conclude contracts subject to acceptance by the other party of one or more supplementary obligations that have no connection with the subject of such contracts.

As in the case of property rights or contracts, the issue of enforceability of Competition Law in Kosovo remains a major challenge. This relates mainly to the lack of human and technical capacities of the Kosovo Competition Authority. The 2011 EC Progress Report highlights the need for strengthening administrative capacities of this Authority, including training its staff in order to be able to perform adequately the tasks assigned.

## **2.3. Institutional Framework and Development**

Laws are only as good as the institutions that enforce them. So, which institutions are most critical in his context? First are good laws and effective means for their enforcement. Based on these, rules of the game are established and applied, but they also en-

able lower transaction costs, increased commercial certainty, creation of incentives for efficiency, as well as controlling crime and corruption, so that businesses can focus on productive activities.

There is a wide array of law enforcement institutions with a role of critical importance. Primarily, there are competent and reliable *courts* and specialized *enforcement agencies* that provide the foundation on which all enforcement activity, either formal or informal, ultimately depend. Formal legal systems place *judges, prosecutors, arbitrators, court functionaries* and *private legal professionals* in the role of primary interpreters and enforcers of laws. Equally important are those who produce and distribute information and monitor market participants: such ‘watchdog’ institutions and stakeholders include *accounting firms, credit rating services, securities regulators, investigators*, and other elements of *civil society*, including a *free press*.

The major issue facing Kosovo is upgrading its institutions, including law enforcement mechanisms. The EC Progress Reports have constantly stressed that *courts* and law enforcement mechanisms have been performing poorly, particularly when it comes to market-related law enforcement aspects. They still remain short in terms of human and technical capacities. The same goes for institutions in charge of defining or protecting property in Kosovo (for instance, *Kosovo Property Agency, Cadastral Agency and Offices in Municipalities*, etc.); protection of intellectual and industrial property (*Industrial Property Office, Copyright and Related Rights Office* and *Kosovo Customs*); and competition (*Kosovo Competition Authority*). In addition, they are also considered to be facing the problem of corruption. On the other hand, it is also considered that ‘watch-dog’ mechanisms and civil society, including media, have so far largely failed to deliver in post-war Kosovo, in this context. Furthermore, piracy is widespread.

### 3. Human and Physical Capital

#### 3.1. Human Capital

The literature views labour productivity as a critical factor for sustainable economic growth. Labour productivity depends on workers’ knowledge, skills, motivation, and health. Therefore relieving extreme poverty, maintaining human capital, and adapting it to the needs of a market system are supportive to growth, as well as social justice and political sustainability. Crucial in this respect is developing a high quality education system, formal and informal, respectively. The primary purpose of the education system is to impart knowledge and skills and, just as important, to transmit certain values. The experience of the last twenty years of transition shows that achieving the primary objective involves a number of subsidiary ones: equitable access to education and training; producing the types of educational activities that empower individuals economically, socially, and politically for the societies in which they live (external efficiency); running schools and other institutions as efficiently as possible (internal efficiency); and financing education in ways that are both fair and efficient.

Developing human capital in Kosovo remains an enormous challenge. Policy-makers have been tackling the issue through wide array of education, skills upgrading, and employment generation policies. Kosovo has a comprehensive medium-term Education Strategy, encompassing all education subsectors. The legislation on higher education is in place and requires higher education institutions (and programmes) to undergo external evaluation by the *Kosovo Accreditation Agency* (KAA). A number of programmes do not meet KAA quality standards. The *Ministry of Education, Science and Technology* and the *Ministry of Labour and Social Welfare* have put emphasis on vocational education and training (VET) as means to promote skills development, employability and economic development in Kosovo.

The main challenges are the lack of scientifically qualified personnel, the low number of PhD students, insufficient laboratory equipment and inadequate technical know-how. The research community in Kosovo remains rather isolated vis-à-vis the international scientific community.

A number of policy documents target the grave need of developing human capital in Kosovo. *Kosovo Economic Vision 2011 – 2014 Action Plan* highlights the need for developing human capital. It outlines mechanisms that aim at increasing the quality of human capital with the objective of providing a higher quality workforce in the labour market. In this regard, the Plan emphasizes education and professional development in terms of development of human capital in all sectors.

The *Employment Strategy 2010 – 2012* is one of the main Government employment policy documents. It outlines three policy directions regarding developing a skills base and increasing employment:

- Improving the investment climate and lowering the costs of doing business with the aim of increasing the pace of job creation by encouraging firm entry and expansion in more value added activities;
- Promoting a strong skills base and higher rates of human capital development through the formal education and vocational training systems; and
- Improving the functioning of the labour market through better labour market institutions, policies and regulations.

In order to achieve a quick run improvement in labor market conditions, the Government undertook short run measures to address the urgent need for more jobs through expand the public investment and public works programmes while pursuing medium and long-term objectives for a more sustainable job-creating path.

The *MLSW Sectorial Strategy 2009 – 2013* sets further objectives regarding employment policy and match of the labour market supply and demand. The two employment-related objectives are outlined below:

- Increase of employment rate and strengthening of vocational training, according to labour market demands; and

- Improvement of cooperation with other countries (EU members and non-EU members) on increasing opportunities for employing Kosovo labour force.

In order to meet the first objective, the Ministry of Labour and Social Welfare aims to increase the labour market services' efficiency and effectiveness, improve information, intermediation and vocational training, physical infrastructure and information technology, review and modification of current vocational training curricula and development of new ones and increasing the vocational training capacities, VTC professional and management staff training, reduction of unemployment of youth, women and long-term unemployed, reviewing and expanding of active labour market policies' measures for employment protection of such categories, social dialogue balance, etc.

Under the second objective the MLSW aims to strengthen implementation of EU standards and cooperation on improving technical, financial and human capacities, through technical twinning agreements that would assist the cooperation process, as well as development of policies, legislation and improvement of partnerships for attracting investments and funding job creation projects, by providing support to private sector through establishment of joint companies.

### **3.2. Physical Capital**

It has been evidenced that the physical capital affects industry and firm level productivity. Kosovo has made important steps in building necessary infrastructure conducive to business operations. However, much more needs to be done in upgrading physical infrastructure to the competitive levels. In what follows is a snapshot of the state of the physical infrastructure in Kosovo.

- ***Road infrastructure***

The Government of Kosovo has embarked on a massive program of public investments aiming at modernizing road infrastructure in Kosovo. Work is underway to link with the Albanian Durrës – Vërmicë highway, which gives Kosovo faster access to the sea through the Port of Durrës. This highway, planned to end at the Kosovo – Serbia Merdare border crossing point, will form part of the European E851 route. Once the Kosovo part of the project is completed, the motorway will link the seaport of Durrës with the Pan-European Corridor X. Other road infrastructure projects link central Kosovo with the northern and north-western part of it. Next year will see Kosovo embarking on another major infrastructure project, linking together its central and southern part, and further with Macedonia. As in the case of the highway to Merdare, all these projects aim at connecting Kosovo to the regional and wider road networks.

- ***Railway infrastructure***

Railway infrastructure in Kosovo is in a poor state. The network stretches in length of 333,451 km of open railway line. The Railways of Kosovo through Leshak and Podujevë in the north and east respectively are connected to Serbia, whereas through Hani i Elezit

in the south to Macedonia.

Currently, a part of the line (Prishtina to Podujevo and to the border with Serbia, as well as the south-western line from Xërxë in Prizren) is not operational due to great damages and the high cost of rehabilitation. The other lines are functional, but their level is not satisfactory due to the enormous need for investments. Currently, the safety signals are installed only at the railway stations in line 10 (Leshak – Mitrovicë – Hani i Elezit), whilst all other lines do not have this equipment. The conditions of the railway stations are still not at a desirable level despite repair work carried out on yearly basis. Mobile equipment and the machinery for the maintenance of the railway infrastructure are very old and of low quality and these require daily repairs which have a high cost.

The key priority of INFRAKOS is railway line 10 which connects Kosovo with Serbia and Macedonia, and through which the majority of railway transport is carried out. The feasibility study conducted in 2010 has stressed the need for major investments for the modernization of this railway line. The main areas of railway infrastructure, which requires investments, are as follows:

- Rehabilitation of railway line 10 for the projected speed 100 km/h to 120 km/h (a project calculated to cost circa €174 million);
  - Purchase of the necessary machinery to maintain the railway infrastructure (a project calculated to cost circa €3 million); and
  - Complete rehabilitation of other railway lines, including safety signals, telecommunications and energy equipment (a project in the amount of circa €200 million).
- *Telecommunications Infrastructure*
  - *Landline telephony*

There are three licensed operators that provide landline telephony service:

- PTK is the only enterprise that provides fixed access and calls through the public switched telephone network (PSTN). In the last decade, this operator built its network by focusing mainly on the NGN network, the connection of all urban centres with a high capacity network (optic fibre) and the digitalization of the central network. Whereas the access network is mainly based on the copper cables;
  - IPKO Telecommunications L.L.C provides landline telephony services through the cable network and covers almost the majority of urban centres of Kosovo. This infrastructure is based on the hybrid approach, i.e. the connection to the client's location is combined starting with optic cable, coaxial and finally, following the CPE installation, the client is equipped with copper cable or in certain cases with IP telephones;
  - KONET is the third operator, which does not provide landline telephony service, but only services of rented lines.
- *Mobile telephony*

Currently there are two licensed mobile operators in Kosovo (Standard GSM 900/1800). Coverage has reached around 99% of the population and 88% of the territory. The number of base transceiver stations is around 721. The technology used is EDGE, which, in addition to voice, MMS and SMS cell phone services, also enables the provision of internet services.

- *Internet services*

Internet access is provided by 37 licensed enterprises, 5 of which have direct access to international gateways and provide access to the internet network to smaller ISPs which operate in different regions of Kosovo.

The internet connection for user through the cable modem is the prevalent technology, with 98,000 users. Internet access to ADSL technology was, by the end of 2011, 36,500 users, out of which 94% are individual users and the remainder 6% are business users. The data show an increase among users of internet through ADSL, which compared to 2010, is 7.34%.

Wireless technology mainly dominates the rural areas and unlicensed frequency broadband of 2.5 GHz and 5 GHz are used. These services are provided by small internet providers and the average speed is 256 kbps.

A considerable number of broadband connections are provided by the operators through the coaxial cable – copper line. The main technology continues to be cable modem with 67.6%, whilst 27.7% of internet users use the ADSL technology. The main internet provide with coaxial cable are IPKO and Kujtesa whereas PTK – TiK is the only operator that provides internet access to the end users through the ADLS technology.

The investments by the telecommunications service operator for 2011 reach the amount of €38,266,377.33 and this is a considerable increase compared to year 2010 when investments reached the amount of €30,777,237.11.

- *Electricity distribution network infrastructure*

The distribution network includes 110/x kV and lower, substations, as well as the 35kV lines and lower.

Rehabilitation of the network covers the replacement of lines and poles of 0.4 kV and 10 kV and transformers 10/0.4 kV. The specific needs for investments are based on the network condition and the level of performance in relation to the voltage and load, including the replacement of the conductor section, insulation to support operations at 20 kV level, expansion of the 10 kV network and increasing the capacities of transformers in TS 10/0.4 kV. These investments would improve the consistency of supply, voltage performance, and reduce the technical losses.

- *Transmission network infrastructure*

The data on the quality of the basic infrastructure of our transmission system are as follows:

Physical Transmission Infrastructure:

- Transmission capacity -  $K_i=1550$  MW;
- Foreseen overload during peak hours for 2012 -  $N_p=1190$  MW;
- Security margin (network capacity back up for N criteria) -  $K_r=360$  MW;
- Fulfilment of the N-1 criteria - ~ 90% of cases;
- Interconnection capacity NTC - ~1700 MW;
- Transformative capacity without distributive transformers -  $K_{trans}=3150$  MW;
- Transformative capacity with distributive transformers  $110/x - K_{trans}=4970$  MW

Infrastructure for secure operation of the transmission system:

SCADA/EMS systems (Supervisory Control and Data Acquisition/Energy Management System);

Telecommunication System (OPGW);

Remote Metering System.

Areas in which investments are needed:

Increasing the transmission capacities:

For interconnection lines Line 400 kV Kosovo – Albania;  
Line 400 kV Kosovo – Macedonia.

Increasing the transmission and transformative capacities:

At the level of local consumption – increasing the capacities for the distributive level in order to support an increase in consumption;

Infrastructure for Load Frequency Control – with Albania.

- *Natural gas sector*

In Kosovo there is an underground natural gas network constructed in the 1970s. The network was operational until 1988, supplying Ferronikel, Trepça, Llamkos and the former military barracks in Prishtina, the Prishtina Central Heating District – TERMOKOS, and some industrial facilities. The gas supply was based on the process of gasification of the lignite within the former Electro-Economy Company of Kosovo, now KEK. The operating pressure of this gas pipeline was 25 bars, with an annual capacity of 480 mil-

lion Nm<sup>3</sup>.

The gas pipeline is seriously damaged in some parts and is out of order. This was a conclusion by ESTAP I study. There are thought of erecting a new pipeline as a part of the project of the road between Prishtina and Skopje. However, to this day no study was conducted which would show whether it is feasible and the costs of building a gas network in Kosovo.

- *Central Heating Distribution Systems*

The sector of the central heating is composed of four sections which supply heating to the urban areas of the municipalities of Prishtinë, Gjakovë, Mitrovicë and Zvečan. The central heating covers only around 5% of the general demand for heating in Kosovo.

The primary network of distribution is the Central Enterprise Termokos, Prishtina, in the length of 63 km, with an installed capacity of 2x7 MW in the districts, 2x7MW installed capacity at the Prishtina Hospital (reserve) and 1x4MW installed capacity in the central heating itself for own needs and 2x0.8 MW installed capacity in Fushe Kosove (out of order). The general capacity is: 135.6 MW. An integral part of the distribution system is the pump station and heat exchange, with 323 substations (312 active), which are also separation points between the primary and secondary networks.

The primary source for the generation of thermal energy is industrial fuel oil. The primary distribution network in Gjakova is extended in the length of 23.5 km with a heating capacity of 38 MW. 275 active substations are an integral part of this network. The primary source for the generation of thermal energy is industrial fuel oil.

The central heating system in Mitrovica contains a separate network: the distribution network of Central Enterprise Termomit, Mitrovica, and the distribution network in 160 Zvečan. According to the Heating Strategy of the Republic of Kosovo 2011-2018, the Termomit heating district supplies 160 consumers in the household sector in a heated area of 8500m<sup>2</sup>. The total length of the distribution network is 6 km with an installed capacity of 1x83 MW. The central heating system in Zvečan has a rather smaller distribution network, in the length of 0.8 km.

- *Water sector infrastructure*

This infrastructure is in a relatively good state, but it requires additional investments to ensure and manage water, and water supply network in order to provide 24 hour water supply, as the majority of regions do not have stable supply. There is no treatment of sewage water, although a pilot project was initiated in Skenderaj with the funding of the European Commission.

- *Public sector infrastructure of waste management*

Non-hazard solid municipal waste services are relatively good in the areas where the

service is provided and the work is carried out based on the licenses issued by the Water and Waste Regulatory Office. The operating infrastructure is relatively good, however, they lack funds for updating the machinery.

- *Permanent sanitary landfills infrastructure*

Four permanent sanitary landfills were constructed with EU funding in four regional centres. Their infrastructure is now degraded to a great extent; the public operators of waste collection pay only a part of the debt from the received invoices. Additional investments are required to preserve and render functional the same landfills; on the contrary their prospect is not bright.

### 3.3. Legal and Policy Framework

Kosovo has adopted a number of laws relevant to this area, mainly pertaining to the mandate of the Ministry of Education, Science and Technology, including laws on all levels of education, governance of the education system, and research activity. These laws include the following:

- Law on Higher Education in the Republic Kosovo;
- Law on Pre-University Education in the Republic of Kosovo;
- Law on Scientific Research Activity;
- Law on Inspection of Education in Kosovo;
- Law on Vocational Education and Training;
- Law for Adult Education and Training;
- Law on Preschool Education;
- Law on Publishing School Textbooks, Educational Teaching Resources, Reading Materials and Pedagogical Documentation;
- Law on Education in the Municipalities;
- Law on Final Exam and State Matura Exam; and
- Law on National Qualifications.

The 2011 EC Progress Report argues that the implementation of the legislative framework needs to be enhanced through improved coordination between central and local levels and by allocating more resources.

The Ministry of Labour and Social Welfare has been also mandated with improving human capacities in Kosovo, as well as dealing with employment/unemployment issues. The main piece of legislation in this regard is the *Law no. 03/L -212 on Labour*. This law aims at regulating the rights and obligations deriving from employment relationship, defined as an agreement or contractual arrangement between an employer and an employee for the performance of specified functions or tasks by the employee under the supervision of the employer in return for an agreed remuneration, normally in the form of money. The EC Progress Report 2011 claims that the adoption of the Labour Law has strengthened the legal framework. The cost of implementing it may not be sustainable. Its implementation requires close monitoring, notably to pay attention to a possible in-

creased vulnerability of women on the labour market, due to the newly-provided extended maternity leave.

There is additional legislation mainly under the mandate of the MLSW, namely:

- Law on Organizing Trade Union in Kosovo;
- Law on Social Economic Council;
- Law on Strikes;
- Law on Material Support for Families of Children with Permanent Disability

With regards to developing a physical capital, the Ministry of Infrastructure plays a crucial role. The legislation within its mandate includes the following main laws:

- Law on Railways;
- Law on Road Transport;
- Law on Transportation of Hazardous Goods;
- Law on Roads;
- Law on Road Traffic Safety; and
- Law on Civil Aviation.

Obviously, this is not an exhaustive list of legislation covering physical capital in Kosovo. A specific legislation for instance covers areas of telecommunication, IT, water, waste, and other physical capital related components.

### 3.4. Institutional Framework and Development

As indicated earlier, a number of institutions, mainly governmental, play a role in regulating the area of human and physical capital. Just to mention few within the Government of Kosovo: MEST, MLSW, and MI. The mandate of the *Ministry of Education, Science and Technology* pertains to the activities related to pre-university education, higher education, vocational education, and science and technology. In this context, the *National Qualification Authority* and the *Kosovo Accreditation Agency* operate as independent bodies. The former is a mechanisms that deals with informal education, and aims at improving access to employment and further learning by ensuring that qualifications are relevant to employment and learning, and meet the needs of learners, the economy and education and training institutions. The latter, establishes quality assurance mechanisms in the public and private higher education institutions in Kosovo.

The *MLSW* engages, among others, in developing employment and social welfare legislation and policies and implementing them, specifically on: further labour relations; employment policies; social protection; setting standards for occupational safety and protection at work; developing and overseeing programs for professional training for unemployed; promoting and encouraging social dialogue between the social partners; providing financial assistance from the allocated funds for families and individuals in need; administering and supporting the development of a social insurance system, including pensions and unemployment benefits.

The *Ministry of Infrastructure* is responsible for all modes of transport, infrastructure, telecommunication, etc. Based on the Law on Civil Aviation, recently *Civil Aviation Authority* of the Republic of Kosovo has been established. CAAK operates as an independent civil aviation regulatory agency responsible for the regulation of civil aviation safety and the economic regulation of airports and air navigation services in Kosovo.

As with the rest of institutions in Kosovo, physical and human-related institutions in Kosovo require further improvements in human and technical capacities. The issue of quality of institutions in Kosovo, and lack thereof, has been acknowledged by numerous studies and reports, including EC Progress Report.

#### 4. Sectoral and Enterprise Structure

The table below shows that Kosovo's enterprise sector remains dominated by small and micro-enterprises. About 99.7% of the enterprises employ less than 50 people, contributing about 60% of the overall turnover in the economy. The overwhelming majority of firms have less than or equal to 9 employees. Enterprises tend to be very small and mostly family-run. There is vigorous business creation, but most companies do not achieve significant growth. The percentage of small and medium sized firms is proportionately falling since 2009. Medium and large firms are virtually inexistent. This is a handicap for the economy of Kosovo, as larger firms are better endowed financially and in terms of human resources. Better-endowed large firms are frequently the source of innovation. In addition, large firms are usually main exporters in the country. Moreover, large firms absorb a significant share of demand for smaller firms. Hence, the literature has acknowledged that an optimal composition of the enterprise sector is vital for long-term growth prospects of a country. Given the current distribution within the enterprise sector, Kosovo is far from reaching some optimal mix of large and small firms.

Table 3.1: Size distribution of enterprises in Kosovo (2009 – 2011, in percentage)

Categories of enterprises	2009	2010	2011
Micro enterprises (1 – 9 employees)	97.48%	98.00%	98.40%
Small enterprises (10 – 49 employees)	2.14%	1.72%	1.38%
Medium enterprises (50 – 249 employees)	0.31%	0.22%	0.19%
Large enterprises (more than 250 employees)	0.07%	0.06%	0.03%
TOTAL	100%	100%	100%

Source: Kosovo Business Registry Agency (2012)

The official data show that the enterprise sector has created a significant number of jobs (see table 3.2. below). However, these data should be taken with a caveat for a number of reasons. First, the total number of enterprises may not be accurate, as the database is not regularly updated by KBRA as to remove companies that cease their activity. In addition, data on unemployment are underreported. The informal sector remains large, and it is fuelled by weaknesses in tax and expenditure policies and in law enforcement,

including the fight against corruption and organized crime. It reduces the tax base and the efficiency of economic policies.

Table 3.2: Total number of enterprises and employment in 2011

Categories of enterprises	Number of enterprises	Number of employees
Micro enterprises (1 – 9 employees)	109,798	185,123
Small enterprises (10 – 49 employees)	1,508	24,877
Medium enterprises (50 – 249 employees)	224	22,411
Large enterprises (more than 250 employees)	60	137,096
TOTAL	111,590	369,507

Source: Kosovo Business Registry Agency (2012)

The next table shows the structure of enterprises according to the type of activity. The economic structure is highly concentrated on the retail sector, with about half of all enterprises operating in this area. In total, services are the key component of Kosovo's private sector. The share of services in the economy has been stable in the last years, at approximately 60%.

Table 3.3: Number of registered businesses by activity (2009 – 2011)

Timeframe	Agriculture, hunting and forestry	Fishing	Mineral and mining	Processing industry	Electricity, water and gas supply	Construction	Retail and wholesale trade	Hotels and restaurants	Other
2009	159	2	34	700	18	659	2,892	805	1,764
2010	188	3	59	731	23	681	2,940	872	1,884
2011	325	3	44	770	18	633	2,974	812	2,051

Source: Kosovo Business Registry Agency (2012)

Overall, Kosovo is a net exporter of services. This is the only sector, where Kosovo has a positive trade balance. The export of services represents approximately 10% of GDP, while imports account for approximately 7.5% of GDP. The positive balance mainly reflects increased revenues from the communication and travel services. However, the major contributor in service sector exports remains the so-called 'virtual export', or the consumption of expatriates and Kosovar diaspora. Service exports have an important potential for faster economic growth. During the next three years, exports of services are expected to grow by 6.5% in real terms. Travel services, which mainly depend on visits of diaspora in Kosovo, are expected to be the main contributors to this growth.

Industrial goods are also important in the economy, although the industrial base of Kosovo almost disappeared following years of neglect and mismanagement. However, with

the process of privatisation some industrial activities have resumed, and the revival of the industry is slow but steady. This is shown especially in the export data for minerals. A significant proportion of Kosovo's total exports (61%) are primary products such as raw materials or goods with a low level of processing and relatively low value added, essentially base metals. Consequently, the overall performance of the country's exports remains sensitive to developments in external demand. Mineral products represent the second largest category, with over 12% of total exports. Manufactured exports mainly consist of machinery, plastic and leather. Imports are generally of a higher processing stage, either intermediate or consumer goods. In 2011, Kosovo's imports exceeded € 2.1 billion, with an annual increase of almost 15%. The structure of Kosovo imports is stable. The largest category is mineral products (mostly fuel and ceramic products). Industrial goods, machinery and equipment represent about 11% of total imports, or about 28% of total imports from the EU.

Agriculture is another important sector in Kosovo. Agriculture and fishing has a share of about 17% in the total value added in the economy. It is the main source of income for the majority of the population. The sector has further growth potential, both in terms of production and trade. Kosovo is a net importer of agricultural products. Import of agricultural products (food and beverages, live animals and vegetables) amounts to almost 22% of all imports, however, it is less than 8% of all exports.

The main agricultural exports are beverages, spirits and vinegar (wine, edible vegetables and vegetable and fruit preparations). The most important imports of agricultural products in terms of value are beverages, spirits and vinegar, edible meat, dairy products, pastries and milk preparation. Kosovo's main trading partners are the EU, Albania, Serbia, Macedonia and Turkey. For all agricultural and food categories, a negative trade balance prevails. Kosovo faces a large agriculture trade deficit. With the EU alone, this deficit amounted to €138 million in 2011.

Organic agriculture is at an early stage of development. The produce has to be certified in Albania and Macedonia.

However, the enterprise sector faces enormous challenges. Obstacles to private sector development are numerous, ranging from a weak rule of law, corruption and unfair competition to unstable electricity supply, unskilled labour force as well as difficult and costly access to finance. Access to and the cost of finance remained problematic, mainly due to the high risks in the economy. As pointed out earlier, Government of Kosovo has been taking steps to improve business climate, which will inevitably affect firm prospects. With regards to energy supply, the government is considering long-term power purchase agreements of up to 20 years between the new generation company and the distribution and supply company. In a similar vein, it is contemplating recommending a possible multi-annual ban on new entrants to the market for mobile telephone service-providers. Measures such as these would hinder competition.

## 4.1. Legal and Policy Framework

Legal framework required for developing enterprise sector in Kosovo pertains mainly to the framework required for improving business environment in Kosovo. It pertains to the legislation on business organisations, taxation, labour, product standards and safety, financial sector, property rights, and other, something that has been discussed throughout this section. Hence, there is no need to engage in a further discussion relating to this point.<sup>103</sup>

## 4.2. Institutional Framework and Development

As in the case of legal and policy network, the institutional framework required to ease the business environment has been discussed widely, and it includes different MTI entities, particularly the *SME Support Agency*, *Kosovo Business Registry Agency*, and the *Investment Promotion Agency of Kosovo*. It is important to note that SME Agency's primary focus is on development of the private sector in Kosovo by creating better conditions for small and medium enterprises. In addition, KBRA is an entity whose primary responsibility is the business registration process. The Agency has undertaken some reforms of business registration procedures reducing to a single day the time required to register a new business. As pointed out earlier, Kosovo Government has decentralized the process of business registry by establishing 25 one-stop-shop centres around Kosovo.<sup>104</sup>

Other important institutions in this respect are Ministry of Finance entities, such as the *Tax Administration of Kosovo* and *Kosovo Customs*. The former's mission is to ensure fair and uniform application and enforcement of tax laws in order to collect revenues for the government budget in an efficient and cost-effective manner. Tax Administration plays a significant role in improving business climate in Kosovo. This institution is in charge of issuing two compulsory documents required for starting a business, that is, the fiscal number and the VAT number.<sup>105</sup> The MTI and MF have been working on reducing the number of documents required to register a business, and to squeeze documents needed into only one, that is, Tax Identification Number. This is still work in progress.

## 5. Economic Integration with the EU<sup>106</sup>

Kosovo's relations with the EU in this regard are governed by Autonomous Trade Measures (ATMs), in place until 2015, with no quantitative restrictions or duties. The only

<sup>103</sup> A detailed overview on the legal framework in this area, including the relevant EU Acquis, is provided in the chapter on Industry and SMEs.

<sup>104</sup> A detailed overview on the institutional framework in this area is provided in the chapter on Industry and SMEs.

<sup>105</sup> These institutions are covered in more detail in the chapters on Trade (above) and on Customs and Taxation (below).

<sup>106</sup> Trade relations with the EU are discussed in the chapter above, on Trade, including the discussion on the legislation and necessary institutional arrangements. Hence, the following section is rather brief.

exceptions are veal, wine, sugar and certain fishery products, which are subject to tariff quotas. However, the EU has enacted these measures unilaterally. Hence a flat 10% custom tariff is applied on goods imported from the EU into Kosovo, with some goods enjoying duty-free access, such as pharmaceutical products, certain agricultural products and livestock, fertilisers, and others.

Kosovo's trade balance marked by a high trade deficit, which exceeded €2 billion in 2011 (45% of GDP). The EU is by far Kosovo's most important trading partner, accounting for nearly half of its external trade. With around 45 percent of export demand in 2011, and around 40 percent of total imports, the EU is the major trade partner of Kosovo. On average, since 2007 Kosovo's exports to the EU have increased by 36 percent, whereas imports by around 12 percent. With regards to imports, the year-on-year increase has been slowing steadily. Despite some positive indications regarding the export performance, the negative trade balance of Kosovo with the EU has been widening constantly, reaching over €800 million in 2011. The data on the structure of trade exchanges with the EU show that Kosovo exports to the EU mainly goods for further processing, whereas it imports from the EU mainly machinery and equipment.

There has been significant progress towards a Free Trade Agreement between Kosovo and the EU since the initiation of this process in 2010, which will further establish necessary conditions for the expansion of trade between Kosovo and the EU block. As a first step, the EC sent a questionnaire to Kosovo Government, aimed at examining the current situation of several institutions involved in trade-related matters (including MTI and its bodies, Kosovo Customs, public procurement agencies, Kosovo Statistics Agency, etc.). As a follow-up to the questionnaire, EC sent a fact-finding mission in July 2010.

This mission evaluated Kosovo's readiness to negotiate and implement such an agreement and identified measures to be undertaken in order to further advance towards it. Kosovo has made significant progress towards starting negotiations for this agreement. In its 2011 Progress Report on Kosovo, the EU clearly acknowledged improvement of Kosovo's position in the area of free movement of goods, including quality infrastructure, industrial property rights and trade policy.

Following publication by the EC of the Feasibility Study Report on Kosovo, in October 2012, it was decided that instead of a stand-alone FTA, there will be the classical free trade section within the SAA framework. Under an SAA, ensuring free movement of goods is one of the main objectives. The parties establish gradually a free trade area, within a transitional period to be determined during the negotiations. This free trade area would have to be in conformity with relevant WTO provisions. Kosovo would commit not to establish quantitative restrictions or measures having an equivalent effect, to progressively dismantle its respective customs duties and equivalent measures on almost all trade with the EU. It would commit to prevent practices discriminating directly or indirectly against EU producers. The EU autonomous trade measures already contain a standstill clause making them conditional on the beneficiaries not introducing new import duties and measures having equivalent effect in trade with the EU. This

would become a contractual obligation under an SAA. The customs authorities in Kosovo would need to be able to enforce and safeguard these demanding trade regimes.

In the area of financial services, further liberalization of the insurance market, in particular the removal of border tariffs is necessary, however the inability of Kosovo to gain membership to UN “Green Card” System remains an obstacle in this regard.

Generally, a key prerequisite for economic integration with the EU is the economic development, which for Kosovo it means fast economic growth. A challenge for Kosovo remains the fact that fast economic growth requires macroeconomic stability, investment in health and education, effective institutions and governance, appropriate environment for private businesses, and a satisfactory level of FDI.

### **5.1. Legal and Policy Framework**

For countries entering FTA arrangements with the Union, including Kosovo, it is important to emphasise that the Treaty on the Functioning of the European Union establishes the EU’s common commercial policy, which is based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, foreign direct investment, the achievement of uniformity in measures of liberalisation, export policy and trade protection measures, such as those to be taken in the event of dumping or subsidies (Article 207.1.).

In addition, specific areas applicable to trade are those in the areas of Customs Union and free movement of goods, freedom of movement for workers, right of establishment and freedom to provide services, free movement of capital (the latter under the heading of economic and monetary policy and free movement of capital), competition policy, taxation, as well as industrial policy and internal market (including the legislation on quality infrastructure, namely standardisation, accreditation, metrology, conformity assessment and market surveillance, and that regulating the areas of industrial and intellectual property rights), and, lastly, law relating to undertakings.<sup>107</sup>

### **5.2. Institutional Framework and Development**

The main institutional mechanism in Kosovo with regards to the EU integration is the Ministry of European Integration. MEI’s mandate is the transformation process and the reforms in path towards the European Union. MEI leads and coordinates the harmonization of policies and laws, as well as the dialogue between Kosovo and the EU. However, the trade issues remain with the Ministry of Trade and Industry. Hence, joint teams are being prepared for the forthcoming SAA, especially its free trade segment.

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<sup>107</sup> Major acts in the area of Customs Union and Free Movement of Goods are covered in the chapter on Internal Market.

In this framework, a study on the impact of the SAA part on trade is included, which is focused on *ex post* analysis on the sensitivity for trade, *ex ante* analysis on the impact of trade liberalization, and to improve the competitiveness of the economy . This study was completed in April 2013 and is expected to serve as a key document to guide preparations for negotiating of SAA part on trade. The part on the sensitivity for trade includes a list of sensitive products, based on the criteria of trade balance, import and export dynamics, as well as education, employment and social welfare.

The analysis on the impact of trade liberalization is mainly based on econometric analysis, focusing on the importance of price flexibility and on the creation and 'deviation' of markets, in the context of improving the trade balance. The last component, the one for improving the competitiveness of the economy focuses on employment, productivity and competitiveness, SMEs, FDI and on institutional and governance aspects. In this context, the main directions for the future work include institutional capacity building, linkage of trade dimensions, productivity of the domestic market, employment and data, then the FTAs, government revenues and fiscal reforms, export promotion and setting Kosovo negotiating priorities.

### **Summary of key Challenges Identified in the Area of Existence of Functional Market Economy and Capacity to Cope with Market Forces within the Union**

Challenges Kosovo is facing regarding the establishment of functioning of the market economy and the ability to cope with market forces within the Union are vast. In what follows, the report summarizes some of the main challenges in this area.

- One of the main challenges facing Kosovo is the limited institutional capacities, human and technical, respectively. A number of areas have been identified by the EC progress Report in the context of creating functional market economy, such as competition, IPR, energy efficiency, environment, food safety, employment and social policies, public health policy, etc.). In this context, a better utilization of existing resources is required, than increasing the capabilities of the existing resources, hiring of new people, and through a short and long-term external assistance from the donor sector.
- Governance continues to face with serious challenges, particularly with the higher levels of corruption and bureaucracy. With regards to corruption, it is considered that it undermines the rule of law, impacts negatively on the business environment and national budgets and affects citizens' everyday life in areas such as healthcare and education.
- In addition, Kosovo faces challenges in terms of approximation of national legislation with the parts of EU *acquis* dealing with the establishment of a functioning market economy and the capacity to cope with the market forces within the Union. More specifically, in the main areas where there are pressing challenges such as in the areas of free movement of goods, competition, IPR, etc.
- Another aspect that faces with even more pressing challenges is that of enforcement mechanisms. In this regard, the efficiency of courts and other stakeholders

relating to the legal system in Kosovo, remain problematic.

- In the context of World Bank assessment on business environment, Kosovo institutions have managed to reduce the documentation requirements, time and cost for business registration and international transactions, then access to finance, investor protection, etc. However, the conditions for operation of businesses need further attention, including creating better opportunities for a new business environment and attraction of foreign investments.
- Kosovo lags behind as regarding well educated and trained labour force. This affects the competitiveness of the domestic economy. In this regard, the quality of education in Kosovo does not respond to market needs. Furthermore, there are lacking policies and insufficient funding for lifelong learning. Implementation of the legal framework and coordination between central and local level on these issues also remains a challenge.

As pointed out, Kosovo is on the verge of entering into negotiations for an SAA. In this regard, there are a series of reforms that require attention in the context of a functioning market economy, more specifically in the following areas:

- Alignment with EU standards regarding the recognition of professional qualifications and the right of companies, including accounting, auditing and corporate governance.
- Implementation of structural reforms in agriculture, in particular as regards the harmonization of veterinary, sanitary and phytosanitary regulations with EU standards, in order to support the increase of exports by meeting the international requirements for standards of products. Improving the collection and processing of data also presents a challenge, since there is a big difference between the EU and Kosovo's trade data with agricultural commodities
- Establishment of a legal framework in line with EU standards on free movement of capital and payments system also presents a specific area which requires special focus in the near future, in terms of preparation for the negotiation of the SAA. This is needed in particular to ensure better protection of investors and FDIs in Kosovo, which, in turn, is key to the development of domestic economy.
- In addition, and in relation to this, the specific area of industrial property rights also needs to be addressed with priority, which is needed to ensure the protection of companies from the EU market in a comparable and equivalent degree to protection of domestic companies.
- As regarding quality infrastructure, the major challenges relate to aligning domestic legislation with the *acquis*, adoption of European standards and institutional capacity building to ensure the implementation of legislation.
- In respect to acceleration of reforms and economic integration into European structures, challenges remain in the aspect of development and implementation of economic policies based on the market, including the capacity to collect and process information on the performance and macroeconomic forecasts, and formulation of economic policies and instruments to implement them.

## Chapter IV: Internal Market

### 1. General Overview

#### 1.1. Free Movement of Goods

The economic freedoms established by the EC Treaty have led to a successful integration of the markets of the EU member states into one single/internal market.<sup>108</sup> The importance of the latter relies on the reasoning that “an integrated borderless market is the best way to enhance the competitiveness of the European economy”.<sup>109</sup> Accordingly, the EU economic criteria for accession<sup>110</sup> require that producers are competitive enough to cope with the market pressure within the internal market.

To this point, an EU harmonized national quality infrastructure is a crucial factor in ensuring free movement of goods between member states of the EU.<sup>111</sup> Generally recognized tools which are used for development of competitive market products, and promoting economic growth are: metrology, accreditation, standardization, conformity assessment, and market surveillance. In essence, the importance of these tools relies on the end product offered to the consumer, as to their quality or quantity.<sup>112</sup>

Consequently, the harmonization of Kosovo legislation with EU legislation in this area is a fundamental point in order to be able to compete and be part of the internal market in the future. Additionally, the development and strengthening of administrative capacities in order to be able to enforce this legislation is a must.<sup>113</sup> The compliance with the above is a governmental responsibility; while the institution with main responsibilities in the area of free movement of goods is the Ministry of Trade and Industry (hereinafter MTI). The following paragraphs will present the achievements and analyse the potential shortcomings within the legal framework and policies, institutional framework, and enforcement.

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<sup>108</sup> Free Movement of Goods, Guide to the application of Treaty provisions governing the free movement of goods, Prepared and drafted by Directorate C, Regulatory Policy, of the Enterprise and Industry DG, p. 8, [http://ec.europa.eu/enterprise/policies/single-market-goods/files/goods/docs/art34-36/new\\_guide\\_en.pdf](http://ec.europa.eu/enterprise/policies/single-market-goods/files/goods/docs/art34-36/new_guide_en.pdf).

<sup>109</sup> Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee, The Internal Market for Goods: a cornerstone of Europe’s competitiveness, 2007, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2007:0035:FIN:en:PDF>.

<sup>110</sup> Copenhagen European Council, Presidency Conclusions, 1993, [http://www.europarl.europa.eu/enlargement/ec/pdf/cop\\_en.pdf](http://www.europarl.europa.eu/enlargement/ec/pdf/cop_en.pdf)

<sup>111</sup> Harnessing Quality for Global Competitiveness in Eastern Europe and Central Asia, Jean-Louis Racine, 2011, p. 302.

<sup>112</sup> Ibid. see generally.

<sup>113</sup> Kosovo 2011 Progress Report, pp. 32-33, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2011/package/ks\\_rapport\\_2011\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2011/package/ks_rapport_2011_en.pdf).

## 1.2. Free Movement of Workers

Free movement of workers is one of the four fundamental freedoms of the EU law. Article 45 of the Lisbon Treaty stipulates that the “freedom of movement for workers shall be secured within the Union”, and it should particularly be ensured that “freedom of movement shall entail the abolition of any discrimination based on nationality between workers of the Member States as regards employment, remuneration and other conditions of work and employment”. One of the central issues arising out of this TFEU article has been the definition of “worker”, and it has been concluded that the community law specifically grants protection to workers, who were nationals of the EU member states, an interpretation which has also found ground by the European Court of Justice.<sup>114</sup> Nevertheless, the above does not concern the Kosovan legislation, as the country is not an EU member state; thus any person seeking work permit in Kosovo will be considered a foreign worker.

On a different aspect, the Regulation 1612/68 (EEC) is the key regulation with respect to anti-discriminatory treatment of workers within EU, in comparison to national workers. The main idea behind this regulation is the Social Advantages. This highly debated term within Article 7 of the Regulation “... should be understood to mean all those advantages which, whether or not linked to a contract of employment, are generally granted to national workers because of their objective status as workers...”<sup>115</sup>

## 1.3. Right to Establishment and Freedom to Provide Cross-Border Services

The freedom of establishment is foreseen in Article 49 of the Lisbon Treaty, whereas paragraph two of this article defines this freedom as the “... right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms ...”

On the other hand, any restrictions on freedom to provide services are prohibited in respect of nationals of Member States who are established in a Member State other than that of the person for whom the services are intended<sup>116</sup>, and a services are considered those that “... are normally provided for remuneration, in so far as they are not governed by the provisions relating to freedom of movement for goods, capital and persons...”<sup>117</sup> The main objective of the Services Directive is the removal of legal and administrative barriers to trade in services sector.

Lastly, the Mutual Recognition of Professional Qualifications and Postal Services are

<sup>114</sup> EU Law, Text, Cases, and Materials, 4th Edition, Paul Craig & Grainne De Burca, 2007, p. 747.

<sup>115</sup> Regulation 1612/68 (EEC), [http://ec.europa.eu/employment\\_social/soc-prot/schemes/regulations/161268\\_en.htm](http://ec.europa.eu/employment_social/soc-prot/schemes/regulations/161268_en.htm).

<sup>116</sup> Treaty on the Functioning of the European Union, Article 56, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2010:083:0047:0200:en:PDF>.

<sup>117</sup> *ibid.* Art. 57.

adopted as a means to facilitate the efficiency of the freedom of establishment and the freedom to provide services.

#### **1.4. Free Movement of Capital**

Free movement of capital is one the four fundamental freedoms proclaimed by the Treaty on the Functioning of the European Union. The idea behind the promotion of this freedom is easy accessibility of financial markets, through abolition of restrictions. For this reason, Article 63(1) of the TFEU lays down the general principle of this freedom by stipulating that “...all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited.” This article differs in comparison to the other freedoms because it is not only granted to the member states, but it also confers rights to third countries. The simple reason behind the facilitation of financial market entry to companies coming from third member states to invest within EU is the mutual financial interest of all stakeholders (companies, governments, and individuals).

Council Directive 88/361/EEC for the implementation of [ex] Article 67 of the Treaty is one of the few secondary legislation acts, considering the freedoms direct effect nature. However, the latter is particularly important considering the definition it provides for capital movement. Based on this Directive, the following form part of this definition:

- Foreign direct investment
- Real estate investment or real estate purchases
- Securities investments
- Granting of loans and credits
- Other operations with financial institutions.<sup>118</sup>

Aside from the first paragraph of Article 63, the second paragraph deals with payments, and what this article proclaims is that “... all restrictions on payments between Member States and between Member States and third countries shall be prohibited”. Thus, just as noted by the European Court of Justice, this freedom is there “to allow individuals to discharge obligations on transnational payments without restrictions”.<sup>119</sup>

The importance of this freedom is also underlined by the direct effect nature of Article 63, which directly confers rights on individuals to rely on them before national courts.

#### **1.5. Public Procurement**

The markets which include states or government bodies as stakeholders have long been the focus of EU law with the objective of removing barriers to trade. Bovis gives a rath-

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<sup>118</sup> Nomenclature of the Capital Movements Referred to in Article 1 of the Directive, [http://ec.europa.eu/internal\\_market/capital/docs/nomenclature\\_en.pdf](http://ec.europa.eu/internal_market/capital/docs/nomenclature_en.pdf).

<sup>119</sup> European Union Law: Cases and Material, Damian Chalmers, Gareth Davies, and Giorgio Monti, p. 726.

er clear rationale behind public procurement rules in the EU: “EU public procurement rules exist in order to introduce a discipline of regulation in the relevant markets, and in particular, to ensure that the undertakings from across the single market and beyond have the opportunity to compete for public contracts by removing legal and administrative barriers to participation in cross-border tenders, for ensuring equal treatments, and by abolishing any scope of discriminatory purchasing through enhanced levels of transparency and accountability”.<sup>120</sup>

The TFEU prohibits all discriminatory measures imposed by member states to other member states, and these rules apply to all public procurement measures and all types of government contracts.<sup>121</sup>

There are two main pieces of subsidiary legislation, namely two directives that form the basis of the EU legislation in this area. Initially, it is the Directive 2004/18/EC on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts,<sup>122</sup> which has been amended seven times;<sup>123</sup> followed by the Directive 2004/17/EC coordinating the procurement procedures of entities operating in the sectors of water, energy, transport and postal services.<sup>124</sup> The Public Sector Directive 2004/18 promotes two principles when awarding contracts: equal treatment of economic operators and transparency.

## 1.6. Company Law

The importance of company law, including accounting and auditing of companies, is one of the key elements of the European single market. The reasoning behind this ranking is indeed the economic interest of the EU, which can be achieved through ensuring a sound internal market in the area of company law, accounting and auditing for companies. Therefore, an internal market means the abolition of barriers imposed to companies, particularly to companies which aim to engage in cross-border activities.

In this regard, the main objectives set by the European Commission to reach this overall goal include “providing equivalent protection for shareholders and other parties concerned with companies, ensuring freedom of establishment for companies throughout

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<sup>120</sup> EU Public Procurement Law, by Christopher Bovis, 2012, p. 2.

<sup>121</sup> See generally EU Public Procurement Law, p.53, <http://www.nottingham.ac.uk/pprg/documentsarchive/asialinkmaterials/eupublicprocurementlawintroduction.pdf>.

<sup>122</sup> Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts, <http://www.procurement.ie/sites/default/files/Directive%202004-18-EC.pdf>.

<sup>123</sup> For amendments, see [http://europa.eu/legislation\\_summaries/internal\\_market/businesses/public\\_procurement/l22009\\_en.htm#amendingact](http://europa.eu/legislation_summaries/internal_market/businesses/public_procurement/l22009_en.htm#amendingact).

<sup>124</sup> Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts, <http://www.procurement.ie/sites/default/files/Directive%202004-18-EC.pdf>.

the EU, fostering efficiency and competitiveness of business, promoting cross-border co-operation between companies in different Member States, and stimulating discussions between Member States on the modernization of company law and corporate governance".<sup>125</sup> This area has been under constant reform, also focusing on harmonization in issues of mergers and divisions, as well as on protection of shareholders interests, audits and annual accounts.<sup>126</sup>

In general terms, a future Stabilization and Association Agreement with the European Union would most potentially require no less favourable treatment of EU companies than that accorded to domestic companies, as well as treatment no less favourable than that accorded to domestic companies and branches or to any subsidiary and branch of any third country company, once they are established.<sup>127</sup>

In order to complete the legal framework in the area of company law, it is essential to have rules of company accounting and auditing in place. The importance of these two processes lies on the transparency and disclosure duty of the company's financial reporting. With currently ongoing harmonization process of this area in the EU, there are two main EU directives to be found: the Fourth Directive, on annual accounts of certain types of companies, and the Seventh Directive, on consolidated accounts.

### **1.7. Intellectual and Industrial Property Law**

The basic legal provisions in the EU in the area of intellectual property rights are provided for in Articles 118, 207 and 345 of the Lisbon Treaty. In this respect, Articles 108 and 207 establish the legal basis for the definition and protection of intellectual property rights within the EU and other harmonization efforts in this area.

The area of intellectual property rights, which aims at creating a functional environment for the prevention of unauthorized exploitation of creations (and distinctive signs) of others is quite complex.<sup>128</sup> For this reason, the legislation which regulates this area is divided into three main groups: copyright and related rights, industrial property rights, and legislation on enforcement of intellectual and industrial property rights.

In this regard, intellectual and industrial property rights include copyright and related rights, patents, trademarks, industrial design and geographic indications. Given the

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<sup>125</sup> European Commission-The EU Single Market: Company Law and Corporate Governance, [http://ec.europa.eu/internal\\_market/company/index\\_en.htm](http://ec.europa.eu/internal_market/company/index_en.htm).

<sup>126</sup> European Commission-The EU Single Market: Directives and other official acts, [http://ec.europa.eu/internal\\_market/company/official/index\\_en.htm#directives](http://ec.europa.eu/internal_market/company/official/index_en.htm#directives).

<sup>127</sup> or more details on requirements set for Albania, see Stabilisation and Association Agreement between the European Communities and their Member States, of the one part, and the Republic of Albania, of the other part, [http://ec.europa.eu/enlargement/pdf/albania/st08164.06\\_en.pdf](http://ec.europa.eu/enlargement/pdf/albania/st08164.06_en.pdf).

<sup>128</sup> On intellectual property and its benefits, see European Commission-Trade topics: Intellectual property, [http://ec.europa.eu/trade/creating-opportunities/trade-topics/intellectual-property/index\\_en.htm](http://ec.europa.eu/trade/creating-opportunities/trade-topics/intellectual-property/index_en.htm).

aforementioned, Kosovo's legislation must limit exploitation of such rights so as to ensure that their use does not conflict with principles of free movement of goods. Moreover, domestic legal provisions should make sure that, within the Kosovo market, EU citizens and companies from the EU internal market are treated equally as other persons from countries outside the EU (in line with bilateral agreements) in terms of recognition and protection of intellectual and industrial property rights.

### **1.8. Competition Policy**

One of the key concepts of the competition theory is based on the principle that "rules of fair competition are aimed at protecting competition, with a view to increasing customer welfare."<sup>129</sup> Therefore, free and fair competition must be aimed at the consumer as the final target.

Based on the EU legislation, competition law includes several main components: agreements between corporations, cartels, state aid and market liberalization. Furthermore, prohibition of agreements and rules on cartels essentially require economic operators to act independently of their competitors, unless their merging is based on the basis of research and development of new products (based on and in accordance with specific rules set). The risk of permitting cooperation between competitors lies in uniform pricing, limited production and market allocation.<sup>130</sup> In this regard, the Lisbon Treaty (Articles 101 and 102) sets out rules for protection of competition. Article 101 prohibits agreements, decisions and other practices between companies that are aimed at restricting competition, and Article 102 prohibits abuse of dominant position by companies.

While the aforementioned provisions relate to economic operators, provisions related to state aid control target governments of member states. These rules, namely prohibitions set forth by the provisions of the Lisbon Treaty (Articles 107, 108 and 109) are designed to prohibit those types of governmental aid that might limit or obstruct competition.

The importance of this area in the EU is demonstrated by the fact that, apart from the European Commission, which's task is to enforce these provisions, the member states are obliged to fully enforce these provisions through competition committees or authorities. Moreover, cooperation between central and local institutions is important. While there are two major stakeholders in the EU involved in protection of competition, the European Commission and state competition protection committees, state aid is an exclusive competence of the European Commission, which is the only body entitled to permit state aid.

In terms of obligations of the potential candidate countries, protection of competition also represents one of the major priorities. For instance, the Stabilisation-Association

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<sup>129</sup> Competition Law, Richard Whish, p. 1 (6th Edition. Oxford University Press 2009).

<sup>130</sup> For more details see European Commission–Competition: Cartels–overview, [http://ec.europa.eu/competition/cartels/overview/index\\_en.html](http://ec.europa.eu/competition/cartels/overview/index_en.html).

Agreement with Albania defines competition as a domain that needs to be addressed in the first stage of association.<sup>131</sup>

Therefore, considering the aforementioned, Kosovo must establish the main rules on protection of competition and on state aid, and ensure their full implementation.

### 1.9. Consumer and Health Protection

Consumer protection represents one of the areas of interest for the EU. Consumer safeguards are provided for by Article 169 of the Lisbon Treaty. In essence, provisions of this Article stipulate that, in order to promote consumer interests and ensure a high level of protection thereof, the EU must contribute to the protection of consumer health, safety and economic interests, as well as to promoting consumers' right to information, education and organisation with a view to protecting their interests.

As far as the subsidiary legislation is concerned, the Consumer Rights Directive is considered as the main one among a number of directives.<sup>132</sup> The primary aim of this Directive is to promote a balance between maximum consumer protection and competitiveness of companies.<sup>133</sup>

This area is closely related to the functioning of all other components of internal market, including market supervision and ensuing fair competition. Each of them also sets out consumer protection as a key functional element.

With the conclusion of the Stabilisation and Association Agreement, the EU will require ensuring active consumer protection, in compliance with the EU legislation, as well as full harmonization of the domestic legislation with the *acquis* and effective consumer protection, with a view to improving quality and safety standards of products, as well as monitoring by relevant authorities and ensuring consumers access to courts in cases of disputes.

In addition to consumer rights, another area of primary importance is public health, which's protection is provided for in Article 168 of the Lisbon Treaty. Though public health polices mainly remain an exclusive competence of member states, the EU has a role in supporting and complementing member state actions in this area. Accordingly, in

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<sup>131</sup> Stabilization and Association Agreement between the European Communities and their Member States, of the one part, and the Republic of Albania, of the other part, Article 70(3), [http://ec.europa.eu/enlargement/pdf/albania/st08164.06\\_en.pdf](http://ec.europa.eu/enlargement/pdf/albania/st08164.06_en.pdf).

<sup>132</sup> Directive 2011/83/EU on consumer rights, amending Council Directive 93/13/EEC and Directive 1999/44/EC and repealing Council Directive 85/577/EEC and Directive 97/7/EC, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:304:FULL:EN:PDF>.

<sup>133</sup> European Commission-Justice: The Directive on Consumer Rights, [http://ec.europa.eu/justice/consumer-marketing/rights-contracts/directive/index\\_en.htm](http://ec.europa.eu/justice/consumer-marketing/rights-contracts/directive/index_en.htm).

this period, public health in the EU is managed based on the so-called *joint competence*.<sup>134</sup>

In general, components of public health protection in the EU are divided into two main groups: threats to health (e.g. contagious diseases) and health determinants (tobacco, alcohol, mental illnesses, etc.).

## 2. Legal and Policy Framework in the Area of Internal Market

### 2.1. Domestic Legal Framework

#### 2.1.1. Free Movement of Goods

This section provides an overview and an analysis of the legal framework relevant for the area of free movement of goods, mainly the laws on standardization, accreditation, metrology, technical requirements for products and conformity assessment, and on inspectorate and inspective supervision.

- *Standardization*

The new *Law*, No. 03/L-144, *on Standardization* is the framework law setting out procedures, and the development of every activity related to standardization at the national level.<sup>135</sup> The scope of this law applies to standards that are recognized, drafted, adopted, and approved in the area of economy, metrology and industry at the national level; however, it excludes the area of telecommunications and of different specifications for intern needs.<sup>136</sup> The main objectives of this law include the increase of products safety level, the promotion of quality of products, and consequently reaching the level of abolishing the technical barriers to trade.<sup>137</sup>

Although a formal assessment in terms of the law being in compliance with EU *acquis* has not been conducted yet, it is reported that the standardization law incorporates the two main EU directives in this area, namely the Directive 98/34/E laying down the procedure for the provision of information in the area of technical standards and regulations and the Directive 2006/96/EC. A general assessment of the legislative framework and the existing standards would potentially identify the shortcomings of the current legislation, as well as it would identify the conflicting and inapplicable Kosovo standards.

Generally, one of the main handicaps of the law in terms of its implementation seems to

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<sup>134</sup> Stabilization and Association Agreement between the European Communities and their Member States, on one hand, and the Republic of Albania, on the other, Article 76, [http://ec.europa.eu/enlargement/pdf/albania/st08164.06\\_en.pdf](http://ec.europa.eu/enlargement/pdf/albania/st08164.06_en.pdf).

<sup>135</sup> Law on Standardization, Art. 1.

<sup>136</sup> Ibid, Art. 2.

<sup>137</sup> Ibid, Art. 5.

be its voluntary nature of implementation.<sup>138</sup> Considering that this is also the approach of EU *acquis*, the main burden in terms of its implementation is upon promotional capacities. In this regard, the rational is - the stronger the consensus in the drafting and approving phase, the larger the extent of implementing the law, namely the standards.<sup>139</sup> (See discussion at pp.10-11)

- **Accreditation**

The *Law* No. 03/L-069 *on Accreditation* which has been amended and supplemented by the *Law* No. 04/L-007 lays down the rules on the establishment of the Kosovo Accreditation Directorate, as well as the rules for functioning of the accreditation system of the competent conformity assessment body.<sup>140</sup> One of the main principles of this law, as set in Article 3 is the compliance with European and international rules and procedures. The Law on Accreditation embraces the Regulation 765/2008,<sup>141</sup> particularly the provisions contained in Articles 4 to 14.<sup>142</sup>

Evidently, a well-established and functional conformity assessment system, which includes testing and calibration laboratories, certification, and inspection bodies should be assessed as the main indicator of the proper implementation and functioning of the current legislation on accreditation.<sup>143</sup>

- **Metrology**

The *Law*, No. 03/L-203, *on Metrology* is amended by the *Law* No. 04/L-124 in 2012. The law operates with the objective of regulating the system of measuring units, state etalons, conformity assessment procedures of measuring instruments, metrological requirements for pre-packaged products, authorizations in the area of metrology, and metrological supervision. Furthermore, it sets out responsibilities of the Directorate of Metrology of Kosovo. The information provided in the 2011 Progress Report<sup>144</sup> emphasizes that the compatibility of legislation with *acquis* in this area has not been assessed; however, compared to the old law,<sup>145</sup> the current law is clearly more aligned with the relevant EU *acquis*. This is the case particularly with regards to enabling the adoption of

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<sup>138</sup> See 9, Art. 1(1) & Art. 7(1).

<sup>139</sup> A Strategic vision for European Standards, p. 11, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0311:FIN:EN:PDF>.

<sup>140</sup> Law on Accreditation, Art. 1

<sup>141</sup> Regulation 765/2008 of the European Parliament and Council setting out the requirements for accreditation and market surveillance relating to the marketing of products and repealing Regulation (EEC) No 339/93, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2008:218:0030:0047:en:PDF>.

<sup>142</sup> Law No. 04/L-007 amending the Law No. 03/L-069 on Accreditation, Art. 5.

<sup>143</sup> Progress in Policy Reforms to Improve the Investment Climate in Southeast Europe, Investment Reform Index 2006 OECD, p. 136.

<sup>144</sup> Kosovo 2011 Progress Report, p. 33, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2011/package/ks\\_rapport\\_2011\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2011/package/ks_rapport_2011_en.pdf).

<sup>145</sup> Old Law on Metrology (No. 02/L-34).

two separate new approach directives: Directive 2009/23/EC<sup>146</sup> and Directive 2004/22/EC.<sup>147</sup> On the other hand, although it has been reported that a number of administrative instructions have been adopted, the completion of implementing secondary legislation might be considered a concern.<sup>148</sup>

The *Law*, No. 2004/28, *on Precious Metals*, is another body of legislation which is of relevance in the metrology area. This law regulates the adjustment of production and selling of precious metal products in compliance with International Standards ISO 9202, through which it intends to protect the market from precious metals incompliant with the latter.

- *Conformity Assessment*

The *Law*, No. 04/L-039, *on Technical Requirements for Products and Conformity Assessment* has been adopted in 2011.<sup>149</sup> As it has been reported in the 2011 Progress Report, the old law has been repealed so that the new law would comply with the 2008 horizontal *acquis* on marketing of products.<sup>150</sup> Article 1 of this Law regulates “the manner of prescribing the technical requirements for products, procedures of conformity assessment with the prescribed requirements and extraction of regulations by the competent Ministries”, and further it sets its scope of application to the area of market surveillance.<sup>151</sup> The main EU regulations, the Regulation 765/2008/EC, 768/2008/EC, General Product Safety Directive and General Product Safety Regulation have been considered when the law was drafted. However, the fact that the EU legislation in this area faces constant changes, particularly as to the directives which relate to technical regulations, implies the constant burden of national bodies to be regularly involved in development in this area. The current legislation is not centralized and it involves all competent ministries which need to authorize assessment bodies in their respective area.

- *Market Surveillance*

The *Law* No. 03/L-181 *on Inspectorate and Inspective Supervision* which has been adopted in 2010 sets the principles, structural organization, the competences and procedures of inspection supervision of the market in the territory of Republic of Kosovo.<sup>152</sup>

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<sup>146</sup> Directive 2009/23/EC on Non-automatic weighing instruments (NAWI), <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:122:0006:0027:EN:PDF>.

<sup>147</sup> Directive 2004/22/EC on Measuring instruments (MID), <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2004:135:0001:0080:EN:PDF>.

<sup>148</sup> There are no reliable data on the number of these administrative instructions.

<sup>149</sup> Art. 38: “With the entry into force of this Law, the Law No.02/L-20 On Technical Requirements for Products and Conformity Assessment and the Law No.03/L-092 Amending and Supplementing the Law Nr.02/L-20 On Technical requirements for Products and Conformity Assessment are repealed.”

<sup>150</sup> Kosovo 2011 Progress Report, p. 30, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2011/package/ks\\_rapport\\_2011\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2011/package/ks_rapport_2011_en.pdf)

<sup>151</sup> Law on Technical Requirements for Products and Conformity Assessment, Art. 2.

<sup>152</sup> Law on Inspectorate and Inspective Supervision, Art. 1.

Although its compatibility with EU legislation has not been fully assessed, it is in line with the Regulation No. 765/2008/EC of the European Parliament and the Council.<sup>153</sup>

In terms of harmonization of legislation, another attempt to further reform the market surveillance area is in the agenda, while the Draft Law on Amending and Supplementing the Law No. 03/L-181 on Market Inspectorate and Inspective supervision is open for public discussion. According to this draft, the remarks of the European Commission which were addressed in the Feasibility Study for SAA, i.e. the cooperation of market inspectorate with customs, will be regulated through a special law.<sup>154</sup>

- *Old Approach vs. New and Global Approach Legislation*

In the area of free movement of goods, it is essential to properly address the distinction of the so-called “new and global” approach legislation as opposed to the “old approach”. The Council Resolution of 7 May 1985 on a new approach to technical harmonization and standards has laid down the differences. In general terms, the “new approach” harmonization sets the essential requirements which must be met in order for a product to be put in a market, conversely to the “old approach” where technical specifications had to be met, allowing no flexibility to the manufacturers.<sup>155</sup>

In general, the impression is that the adoption of new approach legislation is fairly slow. To date, there is no full assessment of the compatibility of the legislation in the area of free movement of goods with *acquis*, meaning that there is no definite answer as to how far have the institutions in charge adopted the new approach directives.

However, as an illustration, the following have adopted the new approach (see the annex for a list of EU new approach legislation): e.g. the Law on Metrology seems to have enabled the adoption of two new approach directives, the Directive 2009/23/EC on Non-automatic weighing instruments (NAWI), and the Directive 2004/22/EC, Measuring instruments (MID); two, other bodies of legislation have adopted new approach directives, namely, the Regulation No. 07/ 2012 on Electromagnetic Compatibility (EMC) which is in line with the Directive 2004/108/EC on Electromagnetic Compatibility, and the Rulebook. No.02/2012 on Electrical Equipment Designed for Use within Certain Voltage Limits which is in accordance with Directive 2006/95/EEC; the Law on Technical Requirements for Products and Conformity Assessment is in line with the Regulation 765/2008 on New Legislative Framework (NLF) etc.

As pointed out earlier, the adoption of new approach legislation and European stan-

<sup>153</sup> Kosovo Progress Report 2011 used the terms takes account of (Kosovo 2011 Progress Report, p. 33, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2011/package/ks\\_rapport\\_2011\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2011/package/ks_rapport_2011_en.pdf)).

<sup>154</sup> Draft-law on amending the Law No. 03/L-181 on Market Inspectorate and Inspective Supervision, Art. 8(3).

<sup>155</sup> For a detailed comparison see Guidance: The “New Approach”, <http://www.cen.eu/boss/supporting/guidance%20documents/gd009%20-%20guidance%20on%20the%20new%20approach/Pages/default.aspx>.

dards is of utmost importance. The rationale behind prioritizing the latter by the bodies involved in free movement of goods is the acceleration of reducing existing technical barriers to trade.

### 2.1.2. Free Movement of Workers

This section provides an overview of the domestic legal framework relevant for the area of free movement of workers, mainly the law on foreigners, labour, granting work and employment permit to foreign citizens, and on anti-discrimination.

- *Access to Labour Market*

Generally, one of the main concerns which is generally raised in the area of free movement of workers is discrimination, namely the anti-discrimination policy. The **Law No. 2004/3 Anti-discrimination** is used as the legal basis for anti-discrimination for foreign citizens, although the extension of its scope of application to foreigners can only be implied – because according to Article 1 the equality of treatment is extended to the citizens of Kosovo.

Furthermore, the Law No. 04/L-069 on Foreigners recognizes the right of foreigners to seek employment in Kosovo, upon receiving a work permit, and according to the provisions of the Law No. 03/L-136 on Granting Permit for Work and Employment of Foreign Citizens (see below).

The **Law**, No. 03/L-212, *on Labour* which has been adopted in 2010 is the legal basis for the establishment of the employment relationship. In this regard, quite importantly, the scope foresees the application of its provisions also to foreign citizens that are employed within the territory of Kosovo<sup>156</sup>, but foreign employees must fulfil special criteria as well.

On this note, these criteria are established within the **Law** No. 03/L-136 *on Granting Permit for Work and Employment of Foreign Citizens*, which is been adopted in 2009. The purpose of the latter is the regulation of employment matters, the procedure and conditions for granting work permit.<sup>157</sup> The text of the law provides an extensive list of exemptions to the requirement of work permit, with the intention of facilitating the employment procedure to foreign citizens in Kosovo.

Although a full assessment of the compatibility of legislation is not available, the requirement of the work permit for EU and foreign citizens is evident. The latter, is a restriction on the free movement of workers according to Article 45 of the Lisbon Treaty. The rationale is that an EU citizen must not be treated differently because of his nationality in respect of any conditions of employment and work. In this regard, the

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<sup>156</sup> Labour Law, Art. 2(3).

<sup>157</sup> Law on Granting Permit for Work and Employment of Foreign Citizens, Art. 1.

existing arrangements and the procedure for obtaining work permits for EU citizens' amounts to a restriction of the right of EU jobseekers and EU citizens to accept a job. Considering the above, the legislation which would be fully compliant with Article 45 of TFEU would abolish this requirement. In this regard, it can be questionable whether the current proper step is solely the acceleration of procedures for issuing work permits, so that the abolishing of such would happen only upon accession.

Another aspect of the free movement of workers includes the right of the worker's family members to move and reside freely within the territory in which the worker is employed. The latter is specifically foreseen within the Directive 2004/58 on the Right of citizens of the Union and their family members to move and reside freely within the territory of the Member States. The adoption of the general principles of this directive, namely the abolishing of any possible existing restrictions will ensure one of the fundamental aspects of the free movement of workers, that of the family members also being the beneficiaries of the freedom of movement.

All of the above is relevant in scenarios when foreign citizens seek work permit in Kosovo. On the other hand, whereas Kosovo has not signed any agreement on the free movement of persons, thus the free movement of workers from Kosovo towards other countries is restricted, subject to countries national laws.

- *Coordination of the Social Security System*

As an illustration, the legal framework in the area of domestic social insurance in Kosovo consists mainly of *Law No. 02/1-17 on Social and Family Services*; the *Law No. 04/L-081 on amending the social and family services law*; *Law No. 04/L-101 on Pension Funds*; and, *Law No.2003/23 on Disability Pensions*.

However, none of the above contains rules which concern the coordination of the social security system. In this regards, according to the Feasibility Study for SAA "...there is currently, depending on the sector, either no insurance system at all or no system suitable for coordination."

Considering the above, the lack of legislation is fairly complemented by a number of inherited bilateral agreements with EU member states from the former SFRY. Generally, the provisions of the inherited agreements are currently being enforced only within the area of retirement pensions, family pensions and partially for disability pensions. Kosovo has entered in extensive negotiations with Switzerland, Austria, and Germany in renewing these agreements, with Switzerland in particular. The latter has terminated the agreement unilaterally in 2010 and considering the fact that the largest numbers of Kosovo citizens have migrated in this territory, these negotiations are principal. Generally, there is a fairly low number of bilateral agreements with EU member states and other countries, which essentially calls for the remedy of the situation through opening of new negotiations for international bilateral agreements on social security systems. Although the negotiation of these agreements calls for the application and use of relevant EU rules concerning limited coordination of social security scheme, that is: the Regu-

lation 883/2004 on the coordination of social security systems, and the implementing regulation No. 987/2009, and the domestic system might not be able to digest these rules - deviations are allowed if the other negotiating party to the agreement does not object.

### **2.1.3. Right to Establishment and Freedom to Provide Cross-border Services**

This section provides an overview of some of the primary legislation relevant in the area of the right to establishment and freedom to provide cross-border services, namely the laws on business organisations; banks, microfinance institutions and non-bank financial institutions; pension funds of Kosovo, compulsory motor liability insurance; licensing, monitoring and regulation of insurance companies and mediators; and on postal services.

- ***Right to Establishment***

The current legal framework which enables economic operators who are legally acting and established in another state to set up or carry on their economic activity in Kosovo is the *Law No. 02/L-123 on Business Organization*, amended by the Law No. 04/L-006. This law concerns businesses which are organized as personal business enterprises, general partnerships, limited partnerships, limited liability company or a joint stock company,<sup>158</sup> whereas it clearly limits its scope when the matter concerns "...licensing and regulating of the activities of a business organization and the accounting, financial reporting and labour and employment practices of business organizations are not within the scope of the present Law."<sup>159</sup> These legislative acts allow foreign companies to set up their business under same conditions as domestic businesses, consequently the legal framework being non-discriminatory.

To date, there is no data on any detailed assessment conducted with the purpose of assessing the compliance level of the law on business organizations with EU legislation. Generally, the idea that is created on the overall progress of company law is related to the simplification of business registration procedures. However, considering the relevance of this area of internal market, and in order to further harmonize the rules, a complete legal framework assessment needs to be conducted. There is an extensive list of company law directives which can be considered for adoption,<sup>160</sup> and this assessment would potentially target the provisions/areas which need to be changed.

On another point, as an illustration, the Directive 2003/58/EC contains rules for electronic/ online registration of businesses. Some of the rules of this directive are already implemented into the law. Namely, the electronic submission of documents and the electronic issuance of registration certificates (as well as notices and other communications). However, electronic registration provisions have not been implemented yet. The

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<sup>158</sup> Law No. 02/L-123 on Business Organizations.

<sup>159</sup> Ibid., Article 1(2).

<sup>160</sup> List of directives, [http://ec.europa.eu/internal\\_market/company/official/index\\_en.htm#directives](http://ec.europa.eu/internal_market/company/official/index_en.htm#directives).

latter would simplify the registration procedure and reduce the costs involved.

Another aspect of the freedom of establishment which is interconnected with the freedom to provide cross-border services as well as recognition of professional qualifications (see discussion below) are the special establishment provisions for the self-employed persons to pursue their activities. The two bodies of legislation with main relevance are the law on accounting, financial reporting and audit, and the law on the bar for lawyers.

Initially, the *Law No.04/L -014 on Accounting, Financial Reporting and Audit* adopted in 2011 allows for foreign practitioners to offer services in this area, thus to pursue their profession, generally subject to same requirement as domestic persons. However, regardless of the non-discrimination principles, the recommendations of the Feasibility Study for SAA call upon the review and amendment of the law.

Then, the *Law No. 03/L-117 on the Bar*, namely the Regulation of the Kosovo Chamber of Advocates on the Licensing of Foreign Lawyers of 2011 operates on the basis of reciprocity. Thus, the lawyer requesting the license to practice law in Kosovo should provide the chamber with proof of reciprocity.

- *Freedom to Provide Services*

The legal framework in the area of freedom to provide services is necessary to be assessed in the light of which activities are considered as services. This would also help in determining the overview of all the legislation involved. Currently, in Kosovo, services are mostly being offered in the area of banks, insurance, pensions, investment funds, and retail financial services for individual customers, payment services, travel and communication.

In terms of the legislative framework, Kosovo has begun establishing the latter, mainly in the area of financial services, both banking and insurance. The main pieces of legislation which regulate financial services area are two laws. The *Law No. 04/L-093 on Banks, Microfinance Institutions and Non-Bank Financial Institutions*, through which it is regulated that the establishment of foreign bank branches is subject to same requirement as for the banks. The *Law No. 04/L-101 on Pension Funds of Kosovo* provides for the right of financial institutions to be pension providers.

The *Law No. 04/L-018 on Compulsory Motor Liability Insurance* grants the right of insurance companies to provide services in this area. Currently, the area of insurance operates under the *UNMIK Regulation No. 2001/25 on Licensing, Monitoring and Regulation of Insurance Companies and Mediators*, and the law is in the drafting process.

The securities area operates according to *Law No. 03/L-175 on Public Debt*, whose main objective is to "... to provide the Republic of Kosovo the authority to borrow money; to make loan guarantees, to pay expenses for debt issuance and to pay the principal and interest on its State Debt."

To date, there is no genuine identification of the areas which are not aligned with EU *acquis*. An issue which needs to be considered and addressed in the near future is the complete transposition of the EU Services Directive, alternatively, the alignment of the existing legislation with the latter. Although this directive does not cover the financial services, it is entirely addressed to regulating the provision of services in construction industry; retail trade; the regulated professions; tourism; real estate; and private education. A *gap analysis* of the existing legislative framework in cross border provision of services would help in identifying the barriers which need to be removed, mainly **legal and administrative barriers to the provision of services**. In other words, the licensing requirements are a highly sensitive issue for consideration.

Lastly, an area which falls within the provision of services is the tourism. The latter is regulated by the *Law No. 03/L-168 on Tourism and Touristic Services*. This law regulates the relations between public institutions, natural and legal persons, domestic or foreign, who practice tourist activities in Kosovo, and generally does not pose stricter requirement for foreign persons, legal or otherwise.

Consequently, according to the Feasibility Study for SAA, “the legal framework for trade in services allows for a relatively open economy to foreign service providers. In terms of market access, for most services, there are no legal restrictions on foreign firms establishing a commercial presence in Kosovo”. Furthermore, the figures according to this documents state that the export of services is approximately 10% of GDP, while imports account for approximately 7.5% of GDP.

- *Postal Services*

The *Law No. 03/L-173 on Postal Services* is adopted in 2010, and supersedes the old law of 2003. The main objective of the law is the “provision of universal postal service and other postal services, protecting the interests of users, ensuring their equal and non-discriminatory treatment, promotion of free and effective competition in the provision of postal services, promoting continuous improvement of quality of service and ensure confidentiality of correspondence for the user in the entire territory of the Republic of Kosovo”.<sup>161</sup>

Generally, the main EU directive in provision of postal services is the Postal Directive 2002/39/EC; therefore Kosovo’s legal framework should be brought in compliance with this directive. One of the possible deficiencies identified within the law on Postal Services is the impact of reserved postal services to the distortion of competition. In this line, the law provides that the weight limit of the reserved services (which are services performed exclusively by the Public Postal Operator) is 1 kg. According to this, the Public Post reserves the area for items less than 1 kg, which is far above the threshold that is set by the Postal Directive, currently 50 gr in the EU member states.

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<sup>161</sup> Law on Postal Services, Art. 1

- ***Mutual Recognition of Professional Qualifications***

Two main bodies of legislation which are of relevance in the area of recognition of professional qualifications are the Law on Higher Education and the Law on Vocational Education and Training.

The *Law No.04/L-037 on Higher Education* is the legislation which provides the legal basis for the recognition of diplomas and qualifications which are obtained abroad, although it does not specifically provide a clear distinction between academic recognition and professional recognition. Notwithstanding the latter, it is clear that the overall legislative framework allows the recognition of a foreign diploma, particularly based on the Administrative Instruction No.8/2010 for Principles and Procedures of Recognition of Diplomas of Higher Professional Schools and University Degrees earned outside the Republic of Kosovo. The main principle proclaimed within the latter is the right of foreign citizens to request the recognition of a diploma earned abroad.

Then, the *Law No. 02/L-42 on Vocational Education and Training* does not explicitly set rules on the recognition of professional qualifications, although it indirectly defines the qualification as "...vocational or professional abilities of a worker recognized at international, national or sector level..."<sup>162</sup>

On a different note, Kosovo is not a party to formal agreements with EU member states in the area of mutual recognition of professional qualifications - with one agreement in force, as of February 2012 - the agreement which is a product of the technical dialogue with Serbia.

Considering the state of the current legislative framework, the Directive 2005/36/EC on the recognition of professional qualifications should be considered for further harmonization of the domestic legislation. The latter can be achieved through amending the current legislation, or otherwise through drafting and adopting a law on recognition of qualifications of regulated professions (see section on establishment for the regulated professions of accountants, audit, and lawyers).

#### **2.1.4. Free Movement of Capital**

The legislative framework in this area mainly includes: the law on banks, microfinance institutions, and non-bank financial institutions (also: Rule VI on Licensing of and Restrictions on Branches of Foreign Banks<sup>163</sup> Authorized by Sections 6 and 7 of the Regulation), foreign investment, law on business organizations, and the regulation on payment transactions.

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<sup>162</sup> Law on Vocational Education and Training, Art. 1.

<sup>163</sup> Rule VI on Licensing of and Restrictions on Branches of Foreign Banks Authorized by Sections 6 and 7 of the Regulation, <http://www.bqk-kos.org/repository/docs/2010/6a.pdf>.

- *Capital Movements*

The Central Banking Authority of Kosovo, now the Central Bank of Kosovo (CBK) in 2007 has adopted the *Rule VI on Licensing of and Restrictions on Branches of Foreign Banks*<sup>164</sup> *Authorized by Sections 6 and 7 of the Regulation*.<sup>165</sup> Further, the *Law No. 04/L-093 on Banks, Microfinance Institutions, and Non-Bank Financial Institutions* ensures that branches of foreign banks are subject to CBK licensing just as a domestic shareholder company which wants to engage in the banking business.<sup>166</sup> This guarantees the national and non-discriminatory treatment of foreign banks in Kosovo. The easy access in the financial sector in Kosovo is also demonstrated by the fact that around 80%<sup>167</sup> of banking sector is managed by foreign banks.

The *Law No. 02/L-33 on Foreign Investment* promotes the principle of non-discrimination and it grants foreign investors and their investments treatment no less favourable than the treatment it accords to any domestic investor and/or domestic investment, including foreign-owned banks.<sup>168</sup>

The *Law on Business Organizations* guarantees the right of companies from EU member states to actively participate in the management of the companies established in Kosovo, including the purchase of shares in a non-discriminatory manner, subject to provisions of the law.

One of the aspects of the free movement of capital for citizens is the purchasing real estate. There are no restrictions as to this, while the *Kosovo Constitution* guarantees the right of foreign persons to purchase immovable property in Kosovo.<sup>169</sup>

Last but not least, the *Regulation No. 2001/26 on Payment Transactions* allows persons to open accounts in foreign currencies and conduct payment transactions through these accounts.<sup>170</sup>

Generally, the movement of capital and payments has been reported as an area which has achieved progress since 2005 while the Feasibility Study for SAA states that Kosovo enjoys a liberal regime for capital movements.<sup>171</sup>

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<sup>164</sup> Ibid.

<sup>165</sup> Regulation No. 1999/21 on Bank Licensing, Supervision, and Regulation, <http://www.bqk-kos.org/repository/docs/2010/Regulation-1999-21.pdf>.

<sup>166</sup> See generally the Law on Banks, Microfinance Institutions, and Non Bank Financial Institutions, <http://kuvendikosoves.org/common/docs/ligjet/Law%20on%20banks%20microfinance%20institutions%20and%20NBI.pdf>.

<sup>167</sup> Kosovo 2011 Progress Report, p. 29, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2011/package/ks\\_rapport\\_2011\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2011/package/ks_rapport_2011_en.pdf).

<sup>168</sup> Law No. 02/L-33 on Foreign Investment, Art. 4.

<sup>169</sup> Constitution of the Republic of Kosovo, Art. 121.

<sup>170</sup> Regulation No. 2001/26 on Payment Transactions, Section 2.

<sup>171</sup> Commission Staff Working Document accompanying the document Commission Communication on a

One of the priorities remains the implementation of Basel II risk requirements. The objective of this convention is to improve the reliability of the financial system. In this regard, according to the Central Bank of Kosovo “secondary regulations on capital and liquidity risk management, which are components of Basel II and Basel III, have been drafted and are expected to enter into force soon.”<sup>172</sup>

- *Payment Systems*

There is no primary legislation in the area of payment systems, but the preparation of the law is underway. In this regard, the Law on Central Bank determines the promotion and the safe supervision, sound and efficient payment, clearing and securities settlement systems<sup>173</sup> as well as other payment system tasks.<sup>174</sup> To date, the *Regulation* No. 2001/26 *on Payment Transactions* has been used.

On a different aspect, the SWIFT code is an element with major importance in payment system. However, due to mainly political elements, there are no results, and the negotiations over the Kosovo’s SWIFT code are on-going.

#### 2.1.5. Public Procurement

The adoption of an adequate law on public procurement has posed a constant issue since 2002. However, the *Law* No. 04/L-042 *on Public Procurement*, which has entered into force on October 5, 2011, is in accordance with the general principles of public procurement, namely the equality, non-discrimination and transparency (Article 7), in the process of publication of notices, procurement procedure selection, award of contracts, and design of technical specifications. The scope of the law includes the works of contracting authorities with economic operators, public service operators and diplomatic missions – under specific rules.

In this regard, the current law is largely based on the EU Public Sector Directive and the EU Utilities Directive, by incorporating their key mandatory provisions. The adoption of the law in this version has not been an easy path, particularly considering many amendments of it. In this regard, the adoption of the current law is assessed as an achievement by the Feasibility Study for SAA stipulating that the “law reflects adequately the main principles of a sound public procurement system and is consistent with international good practices in public procurement. The new law has been almost completely har-

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Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, f. 24, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

<sup>172</sup> Answers to the questionnaire on the preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 197, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

<sup>173</sup> Law on Central Bank, Art. 8(1)(3).

<sup>174</sup> Ibid, Art. 22.

monised with the EU directives and all secondary legislation has been in force since March 2012.”<sup>175</sup> An extensive list of secondary implementing legislation is reported to have been adopted, which is available in the Public Procurement Regulatory Commission (PPRC) website.<sup>176</sup>

The proper implementation of this law is also subject to the integrity and professionalism of public procurement officers. In this regard, the Procurement Code of Ethics which has been adopted provides a set of standards for the behavior of public procurement officers. Furthermore, an issue which is very specific in procurement system is the liability of procurement officers, and the aspect that ensures that the violation of the procurement law is subject to criminal liability.

In terms of remedies, it is essential for the economic operators to be able to have access to the decisions of the Review Body, which have been reached upon complaints. The creation of the reliable system of publishing decision to the public and the interested parties will further ensure the transparency level.<sup>177</sup>

In general, the current legislative framework provisions are in line with the general principles of public procurement, which form part of the EU *acquis*. These rules provide basis for abolition of practices which otherwise would have a great impact in the distortion of competition among economic operators. However, as pointed out earlier, the personal liability of the persons involved should be fully used to establish a proper procurement system, with no loopholes for outside influence.

### 2.1.6. Company Law

The Law No. 02/L-123 on Business Organisations is the main law in this area in Kosovo, which has been amended by the Law No. 04/L-006. Nevertheless, another law which regulates certain aspects of company law is the Law No. 2003/4 on Liquidation and Reorganization of Legal Persons in Bankruptcy and the Law No. 02/L-115 amending it, as well as the Law No. 03/L-222 on Tax Administration and Procedures.

Whereas some countries in the region have opted for separate laws which define specific aspects of company law, Kosovo has chosen to include the rules on company law, mergers, and rules on the operation and maintenance of the business registry in one single law. The *Law on Business Organisations* provides a list of business types which are

<sup>175</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 36, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf). An extensive list of secondary legislation is available at [http://krpp.rks-gov.net/Default.aspx?PID=StdForms&LID=1&PPRCMenu\\_OpenNode=62](http://krpp.rks-gov.net/Default.aspx?PID=StdForms&LID=1&PPRCMenu_OpenNode=62).

<sup>176</sup> Available at [http://krpp.rks-gov.net/Default.aspx?PID=StdForms&LID=1&PPRCMenu\\_OpenNode=62](http://krpp.rks-gov.net/Default.aspx?PID=StdForms&LID=1&PPRCMenu_OpenNode=62).

<sup>177</sup> Public Procurement Law, Art. 117(2).

allowed to be registered, including personal business enterprises, general partnerships, limited partnerships, limited liability companies, joint stock companies, and foreign business organizations. The recognition of foreign business organization (FBO) category is of particular importance. The latter implies that if they register under that name, foreign companies may engage in business activity in Kosovo to the same extent as a Kosovo business organisation. Hence, this law does not impose restrictions to foreign companies provided those intend to be established and conduct business in Kosovo. The following presents three different topics for consideration.

Firstly, in order to facilitate business start-ups, Kosovo has adopted the approach which lowers the minimum capital requirements for both, limited liability companies and joint stock companies – that is €5,000 for the former and €10,000 for the latter. Nonetheless, the minimum capital requirement of €10,000 for joint stock companies is not in line with Article 6 of the **Directive 2012/30/EU**. This Directive subscribes the amount of not less than €25,000.<sup>178</sup> A question which can be raised at this stage is related to the necessity of clarifying what minimum capital requirement prevents from. Generally, it is considered that this requirement does not prevent companies to enter into risk-full projects, hence it does not offer guarantee to the creditors of the company, and it does not prevent the creditors for the company to go bankrupt. In this regard, if the minimum requirement is not a safeguard against the above, the deviation from the Directive 2012/30/EU could be well-reasoned.

Secondly, this law also contains the rules on mergers of limited liability companies, which can result in the formation of a new company or the assimilation of one or more companies by another company. In principle, this law also allows mergers between domestic and foreign companies, although the rules on cross border mergers are not detailed. For this reason, it must be considered whether the harmonization of the law with the Tenth Directive, namely Directive 2005/56/EC on Cross-border Mergers of Limited Liability Companies, should be conducted, and to what extent would the provisions of this directive be suitable for the current situation.

Thirdly, another major aspect of company law is the shareholders voting rights and the protection of minority shareholders. Although the Doing Business 2013 of the World Bank maintains that “The amended law requires shareholder approval or related-party transactions and mandates greater disclosure both by directors to their board and by companies in their annual reports. In addition, the law allows shareholders to petition a judge for rescission of a prejudicial related-party transaction and clarifies the liability of directors.”<sup>179</sup> It is important to ensure full compliance with the Directive 2007/36/EC on

<sup>178</sup> Directive 2012/30/EU on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 54 of the Treaty on the Functioning of the European Union, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent Text with EEA relevance, **Article 6**, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32012L0030:EN:NOT>.

<sup>179</sup> Doing Business 2013: Smarter Regulations for Small and Medium-Size Enterprises, p. 78, <http://www>.

the Exercise of Shareholders' Voting Rights.

With minor exceptions, the Law on Business Organisations is generally considered as close to complete alignment with EU legislation. Most importantly, the freedom of establishment, closely connected with company law is granted to foreign companies, thus treatment no less favourable than to domestic companies. However, with the widening of the market, the needs to adopt new EU directives will come up.

According to available data, there is currently a lack of a corporate governance code, and principles of ethics. Whilst some of the issues related to the latter have been addressed in the law on business organizations, the adoption of the corporate governance code, in compliance with *acquis*, is necessary.

The *Law on Liquidation and reorganization of legal persons in Bankruptcy* aims to define the conditions and the procedure for the liquidation or reorganization of legal persons in bankruptcy. In comparison to the broad scope of the law on business organizations, this law governs the bankruptcy proceedings of general partnerships, limited partnerships, joint stock companies, and limited liability companies. The latter is particularly relevant since it affects the registration and the management of these types of companies, thus making reference to bankruptcy proceedings is inevitable. Article 10 of this bankruptcy law imposes upon the court the obligation to notify the national institution in charge of business registry on the opening and closing of a bankruptcy case.

Lastly, the *Law on Tax Administration and Procedures* is also to a certain extent relevant, particularly to the work of the business registration agency, and the dissolution of businesses. According to this law, the Tax Administration should provide the Business Registry Agency with details of unregistered business, disclose to it individual identification information for the purposes of deregistration or for advising it on taxpayer information. Furthermore, as the law stipulates, "Disclosure to Kosovo Business Registry is also authorized as necessary to verify the registration details of businesses registered with Kosovo Business Registry."

Lastly, although some administrative instructions have been issued, the subsidiary legislative framework on corporate accounting and auditing is not completed yet. The latter is very important since, the current law is only a framework law.

### 2.1.7. Intellectual and Industrial Property Law

- *Copyright and Related Rights*

The framework law which sets up rules on copyright and related rights is the *Law No. 04/L-065 on Copyright and Related Rights*. According to Article 1, this law protects

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[doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB13-full-report.pdf](http://doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB13-full-report.pdf).

copyright which based on intellectual property belongs to authors with respect to their works in several areas, including: the literary, scientific and artistic domain; as well as performers with relation to their performances; phonogram producers with relation to their phonograms; movie producers in relation to their videograms; audiovisual media service regarding their broadcasts; database producers related to their data base; publishers related to their publications; administration of copyright and the related rights; protection of copyright and the related rights; the enforcement of this law to the foreign persons.<sup>180</sup>

Thus, in order to ensure protections of the above, this law contains a list of provisions as to the legal remedies against infringement of these rights, which clearly intends to offer a level of protection for the right holders. While the compliance of this law with EU legislation remains to be confirmed, there is one particular issue which has been identified.<sup>181</sup> This issue is related to court injunctions against the so-called internet intermediaries. Because the availability of this injunction is foreseen as a sanction and remedy, by the Directive 2001/29/EC, one might discuss whether at this stage, such provision should be available in Kosovo. This directive imposes an obligation upon member states to ensure that right-holders are in a position to apply for an injunction against intermediaries whose services are used by a third party to infringe a copyright or related right.<sup>182</sup> In this regard, while the liability of internet intermediaries is not a burning topic, future law amendments could take into consideration such a requirement.

Generally, the current law provides no novelties with regards to the substantive copyright provisions; rather, the main changes which can be identified are the changes made in relation to the role and functions of the Office on the Copyright and Related Rights (see discussion below).<sup>183</sup>

- ***Industrial Property Rights***

The area of industrial property rights includes several pieces of legislation, including: the Law No. 04/L-029 on Patents, the Law No. 04/L-026 on Trademarks, the Law No.04/L – 028 on Industrial Design and the Law No. 03/L-165 on Determining the Rights and Protection of Topographies of Integrated Circuits. Furthermore, the framework is also complemented by the Law No. 02/L-98 on Protection of plants varieties.

The first three laws, on patents, trademarks, and on industrial design, have been drafted and adopted within the same period. The *Law No. 04/L-029 on Patents* is adopted with

<sup>180</sup> Law on Copyright and Related Rights, [http://gazetazyrtare.rks-gov.net/Documents/Ligji%20per%20te%20Drejtat%20e%20Autorit%20\(anglisht\).pdf](http://gazetazyrtare.rks-gov.net/Documents/Ligji%20per%20te%20Drejtat%20e%20Autorit%20(anglisht).pdf)

<sup>181</sup> Answers to the questionnaire on the preparation of the Feasibility Study for a Stabilisation and Association Agreement, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

<sup>182</sup> Directive 2001/29/EC on the harmonisation of certain aspects of copyright and related rights in the information society, Article 8, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2001:167:0010:0019:EN:PDF>.

<sup>183</sup> See generally <http://www.sdpkosove.com/news?page=1>.

the intention of providing procedures for registration of patents and the rights which derive from the registration and application of patent rights. One novelty in the new is the provision which provide that if the national interest requires, the invention of a citizen of Kosovo can be kept a secret for a period of time. However, this provision, the same as a number of other provisions will enter into force only when/if Kosovo joins the EU.

Throughout its text, the Patent Law refers to and recognizes the principles established by international conventions, such as the Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS). The above is important since it ensures the consultation of widely known rules, and this eventually provides a quality level of the legislation in force.

The *Law No. 04/L-026 on Trademarks*, in its Article 1, sets out requirements and procedures for the registration of trademarks, the rights derived through the registration and implementation of such rights. Furthermore, it is important to emphasize that the law does not discriminate against foreign trademarks, which is of utmost importance for the protection of intellectual property rights.

The *Law No.04/L-028 on Industrial Design* protects the industrial design rights provided that this design is new and that it has individual character. It has been assessed that one of the main novelties of the law is industrial design registration procedure.

Lastly, it is important to note, that the above mentioned group of laws is in compliance with the following corresponding EU legislation:

- Directive 98/44/EC on Legal Protection of Biotechnological Inventions;
- Directive 2004/48/EC on Enforcement of Intellectual Property Rights;
- Regulation 816/2006/EC on Compulsory Licensing of Patents Relating to the Manufacturing of Pharmaceutical Products for Export in Countries with Public Health Issues;
- Regulation 469/2009/EC on the Certification of Additional Protection of Medical Products; Regulation 1610/96/EC on Establishment of Defence Certification for the Protection of Plant Products;
- Directive 2008/95/EC on Approximation of Laws of Member States Relating to Trademarks;
- Regulation 207/2009/EC on Pro-Community Trademarks;
- WTO Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS Agreement);
- Madrid Agreement on International Registration of Trademarks and Protocol Relating to the Madrid Agreement on International Registration of Trademarks;
- Directive 98/71/EC on Legal Protection of Designs;

- Regulation 6/2002/EC on Community Designs (as amended);
- Paris Convention for the Protection of Industrial Property (as amended);
- WTO Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS Agreement); and
- The Hague Agreement on International Registration of Industrial Designs.

Another law which is relevant to this area is the *Law No. 03/L-165 on Determining the Rights and Protection of Topographies of Integrated Circuits*, which protects the rights on the shapes and layout, usually three-dimensional. The latter regulates the conditions and procedures for registration of rights and protection of topographies of integrated circuits and their enforcement.

With the above mentioned laws in the current state, one might say that the primary legislative framework is almost complete. However, there is one area of industrial property rights which is not yet covered and that is the geographical indications law. This draft-law has been drafted and submitted to the Kosovo Assembly for adoption.

- *Other relevant legislation*

In addition to the sector specific laws, there is a list of laws which contain intellectual property rights provisions, specifically with regards to the duties of institutions involved which have competencies in this area. These laws include: the Criminal Code, the Criminal Procedure Code, the Law No. 03/L-199 on Courts, the Law No.03/L – 170 on Customs measures for protection of intellectual property rights, the Law No. 03/L-181 on Market inspectorate and inspective supervision, and the Law No. 04/L-077 on Obligational Relationships.

The new *Criminal Code* has given a broader scope of provisions which deal with the intellectual property rights. This implies that some of the intellectual property rights infringements (which might as well be part of the specific abovementioned laws) are subject to criminal law. The incrimination of such must be used as a Furthermore guarantee towards the protection of IPR. As an illustration, the following are punishable by fine or imprisonment: unauthorized communication of trade secrets; the use or possession of another person's trademark of geographical origin; violation of copyright rights and patents. Furthermore, the manufacturing, producing, and selling false label is also stipulated as a violation. However, the **Criminal Procedure Code** seems to lack provisions on the manner of investigating intellectual property rights violations. This might position a challenge to the implementation of these provisions which are contained in the Criminal Code. Thus, the supplementing of the code of procedure with adequate provisions is necessary.

The *Law No.03/L – 170 on Customs Measures for Protection of Intellectual Property Rights* provides for the rules according to which the customs can act, when seized with goods suspected of infringing intellectual property rights, such as counterfeit goods

and piracy. Although the provisions of this law provide for the right of destruction of counterfeit and pirated goods (particularly the ones concerning public health), the lack of adequate facilities to conduct such actions, makes these provisions currently hardly implementable.

The *Law No. 03/L-181 on Market Inspectorate and Inspective Supervision*, within competences in other areas, also provides for competences of the market inspectorate in the area of intellectual property rights.

The *Law No. 04/L-077 on Obligational Relationships* is also relevant to this area considering the fact that it touches upon the contractual aspects of the intellectual property rights. For instance, the law has a number of provisions with regard to licence agreements – namely, Article 700 provides that “through a licence agreement the licence provider undertakes to wholly or partly cede to the licence acquirer the right to exploit a patented invention, technical know-how or experience, or a trademark, pattern or model, and the licence acquirer undertakes to make a specific payment for such”.

The *Law No. 03/L-199 on Courts* has changed the court that is in charge of the protection of intellectual property rights. While previously the Commercial Court in Prishtina has been competent to adjudicate intellectual property rights cases, currently the Commercial Matters Department within the Basic Court is in charge of this. Therefore, any case related to intellectual property rights will be subject to the latter’s competence to act.

The *Law No. 04/L-094 on Information Society Services*, adopted by the Assembly of Kosovo in March 2012, aims at facilitating electronic services in customer sales over the Internet, electronic banking and financial services, provision of government services through information technology, as well as application of electronic signature. This law also establishes the legal basis for carrying out Internet transactions for goods and services alike. The documentation in electronic form is legally defined as equal to traditional documentation presented in paper format, in order to facilitate electronic exchanges.

This law supersedes the former Law No. 2005/02-L23 on Information Society Services, as this has emerged as a need for harmonization with the EU *acquis*, namely to the EU directives, but also as result of the rapid development of information society services based on the use of information and communication technology, as well as usage of electronic payment and electronic trade services. Accordingly, this law establishes a comprehensive legal basis in compliance with these directives: it contains sections transposed from the EU directives on electronic trade, electronic signatures and electronic payments.

The *Law No. 03/L-166 on Prevention and Fight against Cyber Crime*, adopted by the Assembly of Kosovo in June 2010, aims at preventing and combating organized crime through concrete measures, including detection and sanctioning of criminal offences committed through computer systems, as well as the provision, observation and protection of human rights and personal data in that regard. This law also defines ways and procedures of communication between relevant Kosovan institutions and counterpart institutions of other countries that are responsible for combating this type of crime. It

also contains guidelines on prevention of cybercrime and regulates aspects of confidentiality, integrity and availability of data of computer systems, and regulates aspects of combating cybercrime offences, child pornography and other phenomena of this nature. This law also contains provisions setting out procedures for prosecution of perpetrators of cybercrime and procedures that are allowed for the use of computer system data. The Council of Europe Convention on Cybercrime was used as a base for drafting this law.

### 2.1.8. Competition Policy

- *State Influence in Competition*

The state can sometimes influence competition in the market as some sectors of the economy are managed by the Government or other structures, such as regulatory agencies. Some of these sectors, which also form part of the national debate, include energy, financial services, media, postal services, telecommunications, and agriculture. Therefore, one of the central reasons behind the Law on State Aid is the abolition of rules which allow for the government to interfere in such a way that it could abuse the dominant position of public- and/or state-owned monopolies.

The current state of affairs indicates that most of public-owned companies, such as the Kosovo Energy Corporation, Pristina International Airport, and Post and Telecommunication of Kosovo, hold dominant positions in the respective sectors. Therefore Kosovo has adopted the legislation which also defines some of the limits of state interference, and it includes the Law No. 03/L -185 on the Energy Regulator, Law No. 03/L-051 on Civil Aviation, Law No. 04/L-109 on Electronic Communications, Law No. 04/L-063 on Kosovo Railways, Law No. 04/L-044 on the Independent Media Commission, and the Law No. 04/L-042 on Public Procurement.

The *Law on the Energy Regulator* allows for interference of the government in two stages, which can be relevant for the purposes of this discussion. Initially, the government is allowed to give subsidies to vulnerable consumers, provided that these consumers are targeted in a transparent manner, least likely to distort competition in the supply of energy. Furthermore, Article 45 (2) of the law provides that “All subsidies to the energy sector shall be subject to the provisions of any applicable state aid legislation and the monitoring procedures provided for therein.”

The *Civil Aviation Law* makes the regulatory responsible for implementing civil aviation legislation and giving effect to policies adopted by the Ministry or the Government in the area of civil aviation.

*Law on Electronic Communications*, adopted by the Assembly in October 2012, establishes a comprehensive framework for electronic communication matters. The aim is to promote, through the principal of technological neutrality, competition and efficient infrastructure for electronic communications and guarantee suitable and appropriate electronic communications in the entire territory of Kosovo. Among others, this law also

provides for transition from the license regime to the regime of general authorization for provision of electronic communication services and networks. This also implies more opportunities and improvement of the quality of the environment for new investments and fair competition, which is also one of the major priorities of the Government of Kosovo.

Any potential new operator that is interested in providing electronic communication services and/or networks will not have to be supplied with a license for the provision of such networks and/or services if it does not use end resources, such as frequencies and numbers. A new operator only needs to observe conditions and regulations on the provision of electronic services and networks defined by this law and the subsidiary legislation implementing it. If an operator utilizes end resources (as a spectrum of frequencies and numeration), it must undergo same fair competition procedures and normally pay for the use of resources allocated to it. The use of frequencies and numbers, as well as the procedures for takeover of the use of these resources, are clarified and are complied with in a transparent manner.

An important part of this law consists of provisions that determine requirements for the construction, installation, use and maintenance of electronic communication infrastructure, by providing rights of way and rights on joint use of constructed infrastructure (including underground cable channels and antenna posts), in compliance with respective provisions of the existing EU legal framework. The Law on Electronic Communications is in line with the EU directives (the 2009 package of directives in this area, and the amended 2002 package of directives in the area of electronic communications).

The *Law on Railways* provides for granting of subsidies to the railway sector, when they serve the public interest, and when they are not contrary to state aid.

The *Law on Independent Media Commission* mandates the Commission to maintain a fair and open system for licensing and regulating the audiovisual media services and for managing Broadcasting Frequency Spectrum in accordance with the best international standard (Article 5.1). Contrary to the aforementioned laws, IMC members are appointed by the Assembly through an open procedure, rather than by a proposal from the government.

Lastly, the *Law on Public Procurement* is of relevance with regards to the component of fair competition in procurement of goods, which is promoted throughout the entire text of the law.<sup>184</sup>

In general, there are two common elements of Kosovo regulatory laws, namely the appointment procedure, whereas the appointment of the board members of the regulatory is done by the government, subject to the approval of the Assembly; and the dependency of this system from the Kosovo budget.

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<sup>184</sup> For more, see the section above on Public Procurement.

- *Antitrust and Mergers*

The main law in the area of antitrust and mergers is the *Law No. 03/L-229 on Protection of Competition*. It should be also noted that apart from the rules on antitrust and mergers, this law contains rules on the abuse of dominant position by companies, which is one of the core violations within the market competition. With the above covered by the law on protection of competition, and the monitoring of state aid covered by the state aid law (see below), the primary legislative framework covers all four main components of competition rules. The current law is largely based on the prohibitions set out in the relevant articles of the Treaty on Functioning of the European Union, i.e. Articles 101 and 102.

There has also been progress in terms of subsidiary legislation. While the Regulation on Criteria for giving a measure of the administrative sanctions, and the Regulation on Criteria and conditions for determining the relevant market have been adopted in 2011, according to the data available in the official website of the competition authority, four administrative instructions have been adopted in October 2012, namely:

- AI on Criteria and Conditions for Determination of Low Value Agreements
- AI on Forms of Submitting Requests and Criteria for determining Concentration of Enterprises
- AI on Criteria to Reduce or Release Administrative Measures; and
- AI on the Form and Content of the Identification Card.

Furthermore, the new *Criminal Code* also touches upon some of the aspect of protection of fair competition. This implies that anti-competitive behaviours are also criminal violations. For instance, two of the main foreseen prohibitions are: the misuse of the monopoly position and the incrimination of agreements in restriction of competition upon invitation to tender.

However, to date, no formal assessment has been done regarding the level of compliance of other laws which regulate issues related to protection of competition with the Law on Protection of Competition. The avoidance of conflicting provisions is of major importance for the legislation which regulates functioning of publicly owned companies.

Last but not least, there is one specific issue which has been raised in the Feasibility Study for SAA and that is the amendment of the current law in order to determine the dominant market position, thus to put adopt rules related to it in compliance with EU legislation.

- *State Aid*

The primary legislation in the area of state aid is the *Law No. 04/L-024 on State Aid*. This law is a rather new piece of legislation, as it entered into force in the beginning of 2012. The latter provides a detailed definition on what constitutes state aid, including: grants and subsidies; tax exemption, reduction and differentiation; remission of overdue payments and fines; remission of debt or covering losses; guarantees on loans or granting loans under low interest rates; and reduction of social insurance commitments. The State Aid law has been reported to be in compliance with the core provisions of the TFEU, namely articles 107, 108, and 109.

The current provisions allow the provision of state aid, but only conditional upon notification procedure to the competent authorities. Otherwise, the provision of state aid is considered unlawful by the State Aid Commission. Another important provision within the law concerns the state aid schemes, which essentially empowers the Commission to propose appropriate measures to align existing aid scheme with the law provisions. The provisions of the law are not relevant in the area of agriculture and fisheries, thus the scope of the law remains limited in this respect.

The current economic criteria according to which state aid is granted are foreseen in Article 6, which allows the provision of state aid to: promote the economic development of areas with low standard of living or a high rate of unemployment; remedy a serious disturbance in the economy as well as to execute an important state project; to facilitate the development of certain economic areas, to the degree that does not adversely affect trading conditions to an extent contrary to the common interest under the international agreements ratified by Kosovo; to promote culture and heritage conservation, to a degree which this aid does not affect seriously the competition; and other aid that is in accordance with the provisions of this law.

As regards the subsidiary legislation on state aid, the Ministry of Finance has adopted the Regulation No. 01/2012 on Procedures and Forms of Notification on State Aid, which has entered into force in October 2012. This regulation defines procedures of notification about state aid, illegal procedures of this type of aid as well as procedures of existing schemes and reporting and monitoring. This regulation also contains state aid notification forms and an annual report form. The Ministry has also prepared the Draft Rules of Procedure of the State Aid Commission. These rules are due to be adopted by the State Aid Committee at its first meeting. The Commission is due to be established by the Minister of Finance following his/her appointment.

However, subsidiary legislation on this area must be completed. Some rules to be considered for adoption include those on block exclusions, transparency of enterprises of public interest and specific rules on sectors.

### **2.1.9. Consumer and Health Protection**

- **Consumer Protection**

The main piece of legislation in the area of consumer protection is the Law No. 04/L-121 on Consumer Protection. However, other primary legal acts in this area include the Law No. 04/L-039 on Technical Requirements for Products and Conformity Assessment, Law No. 04/L-078 on General Safety of Products, and the Law No. 03/L-181 on Inspectorate and Market Supervision.

The Consumer Protection law has been drafted in compliance with the EU *acquis*, and protects the ten main consumer rights, namely:

- Right to protect the economic interests of consumers;
- Right to be protected from danger the life, health and property;
- Right to legal protection of consumer;
- Right to complain;
- Right to compensation in certain cases for indemnity;
- Right to consumer information and education;
- Right to use public services;
- Right of organization in consumer association, to protect their interests;
- Right to represent consumer interests; and
- Right to receive services in their own language, in compliance with the Law on the Use of Official Languages.

Inclusion of these rights in the current legislation is very important given that they represent the cornerstone of customer rights in the EU. Moreover, the Law covers customer protection rights in terms of sales and products and services alike (i.e. sale) and their protection in the area of public services, financial services, internet purchase and other conditions for the sales of goods and services.

A new concept that has been introduced in the Law on Customer Protection is resolution of customer disputes by the two current arbitration courts in Kosovo – the Permanent Tribunal of Arbitration (PTA) with the Kosovo Chamber of Commerce and the Arbitration Court with the American Chamber of Commerce. Customer access to courts of arbitration in Kosovo i.e. alternative dispute resolution pursuant to these provisions is inapplicable at this point of time. There are two reasons for that: The Law on Arbitration is not utterly clear about the possibility of access to arbitration for a customer that is considered as weaker party; tribunals' rules of procedure are not suitable for disputes deriving from customer rights, and existing procedural fees are very high for a customer as a weak party to proceedings. What was thought about during the preparation of the law might have been the legislation of some EU countries related to some alternative dispute resolution methods available to the customer, though such rules are not harmonized yet. On balance, same rules should not, by any means, apply to business and customers alike. Accordingly, it would also be good to address this issue when amending the current law.

The *Law on Technical Requirements for Products and Conformity Assessment* foresees

the consumer protection as one of its main objectives, whereas for instance, the manufacturer is obliged to protect the health and safety of consumers, and the importer is obliged to carry out testing of samples of marketed products, and keep a register of complaints of non-conforming products and product withdrawals.

The *Law on General Product Safety* also operates with the intention to protect the consumers from products which are not safe, whereas according to its provisions “Information related to safety characteristics of a product which should be available to the public for the purpose of protecting consumers’ health and safety cannot be considered professional secrecy”.

Lastly, the *Law on Inspectorate and Market Supervision* provides that one of the competencies of the market inspectorate is consumer protection. Therefore, the functioning of the market inspectorate is always under the assumption that the end result of its work should be in compliance with protecting consumers from products with risky and unsafe products.

Considering the abovementioned, the legal framework is considered to be formally complete. However, further completion and compliance of the latter with EU legislation is one of the conclusions to be inferred from the Feasibility Study for an SAA.

- **Health Protection**

The area of public health is divided into four main areas: tobacco control, blood/tissues and cells, organ donation and transplanting, patient rights in cross-border healthcare, and communicable diseases. These issues are regulated by several laws: Law No. 02/L-78 on Public Health, Law No. 2004/4 on Health, Law No. 02/L-36 on Tobacco and Law No. 03/L-157 amending the Law No. 02/L-36 on Tobacco, Law No.02/L-101 on Blood Transfusion and Control of the Blood and its Products, Law No. 02/L-109 on Prevention and Fighting of Infectious Diseases, Law No. 2003/22 on Sanitary Inspectorate, Law No. 02/L-38 on Health Inspectorate, Law No. 03/L-188 on Medical Products and Equipment, and the Law No. 02/L-128 on Narcotic Drugs, Psychotropic Substances and Precursors.

The framework provisions in this area represented by the *Law on Public Health*, whereas the definition of public health is as follows “an independent discipline dealing with identification and solving of all community problems from every health aspects, prevention of diseases, research on the aetiology of the diseases, health promotion, rehabilitation and re-adaptation of the handicapped, health education and social issues. Furthermore, the new *Law on Health* is aimed to establish rules for the Kosovo healthcare system, on activities are related to healthcare, as well as the health financing system. This law was adopted by the Kosovo Assembly in December 2012, but it was suspended and now is with the Constitutional Court, awaiting its verdict.

One of the laws which have been discussed the most is the *Tobacco Law*. The main objectives of this law include the protection of the population in general and children in specific from the implications of tobacco consumption. Furthermore, this law lays

responsibilities on the relevant institutions to increase the level of public knowledge and awareness regarding the risks of tobacco consumption and to protect the public from the exposure to smoking. Last but not least, the law intends to regulate and control tobacco products and their distribution, in compliance with the public health policies and objectives.

The harmonization of the current legislation with the EU legislation has been a subject for discussion, and the component of public smoking has been a burning issue. The Ministry of Health has reported that the new tobacco draft-law is in compliance with the Directive 2001/37/EC on approximation of Laws, regulations and administrative provisions of the member states concerning the production, presentation and sale of tobacco products; Directive 2003/33/EC on approximation of laws, regulations and administrative provisions of the member states concerning the advertisement and sponsorship of tobacco products; Decision 2003/641/EC on usage of colour images or illustrations as health warning on tobacco packaging; and the Council Recommendation on prevention of smoking and initiatives to improve tobacco control.<sup>185</sup> It has been reported that this law will include full (100%) smoking ban in public.

The *Law on Blood Transfusion and Control of the Blood and its Products* aims at regulating the activities relating to blood donation, test, processing, safeguard, transfusion and quality control and its components. However, this is also a framework law, considering that some of these issues are subject to regulation by subsidiary legislation. There is no current data whether these subsidiary legislative acts have been adopted.

The Law on Prevention and Fighting of Infectious Diseases regulates the activities of timely discovery, emergence recording, prevention, the prohibition of spreading and the treatment of infectious diseases, which are defined as diseases which are transmissible directly or indirectly from a sick person or the causer bearer to a healthy person as well as from animals and farming products.

Lastly, the Law on Sanitary Inspectorate sets out legal provisions s rule on the inspection of the food quality, measures related to fighting and eliminating contagious diseases, performing the hygienic and sanitary control of food facilities, facilities for maintaining of personal hygiene, public facilities and public dwellings with the aim of protecting the health of the population of Kosovo. The Law on Health Inspectorate sets out rules on the monitoring activities concerning the healthcare institutions.

Considering the above, the level of compliance with the EU legislation remains to be assessed. Furthermore, completion of the subsidiary legislation remains to be done. More specifically, the laws on transplanting of tissues and cells, and transplanting of organs have not yet been adopted. According to the information provided by the Ministry of

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<sup>185</sup> Answers to the questionnaire on the preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 364, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

Health, the draft-law on transplanting of tissues and cells is aligned with the Directive 2004/23/KE on setting standards of quality and safety for the donation, procurement, testing, processing, preservation, storage and distribution of human cells and tissues. Regarding the draft-law on organ transplanting, the European Commission has recommended the transposition of the Directive 2010/45 on quality and safety standards in organ transplantation. Furthermore, the area of patient rights in cross-border healthcare is not yet covered by primary legislation. In this context, due to the lack of health insurance, the provision of healthcare services abroad to the citizens of Kosovo, and vice versa, is regulated through bilateral agreements.

In general, a gap analysis needs to be undertaken, in order to assess the missing legislation, and the non-compliant provisions of the existing legislation.

## 2.2. Overview of the EU Acquis on Internal Market

Within the framework of EU integration, the area of the internal market is regulated by a number of primary and secondary acts of the *acquis*. This legislation consists of two main categories: principles embedded in treaties and specific provisions contained in other acts of the EU *acquis* (adopted by the EU institutions). The latter are further divided into two subcategories: (1) regulations, directives and decisions (legally binding instruments), and (2) recommendations and opinions (not legally binding).

As for the *principles embedded in the Treaty on the Functioning of the European Union* (Treaty of Lisbon), it states that the European Union has exclusive competence in the area of the internal market, namely the establishment of competition rules that are necessary for its operation.<sup>186</sup> This provision also provides that the Union shall establish the internal market, in the service of a social market economy, aiming at full employment and social progress, environmental protection and the promotion of scientific and technological progress.<sup>187</sup> On the other hand, the Treaty defines the internal market as an area in which the Union and the Member States have shared competence.<sup>188</sup> Finally, concerning general provisions, the Treaty requires the respect of animal welfare, and administrative provisions and customs of Member States, in particular regarding religious rites, cultural traditions and regional heritage.<sup>189</sup>

At the level of specific provisions, the area of the internal market in general is regulated by Chapter I, Articles 26 and 27, respectively. Article 26 obliges the Union to put into effect the necessary measures for the purpose of establishment or ensuring the functioning of the internal market, in accordance with the relevant provisions. Furthermore, this article defines the internal market as an area without internal borders in which the free

<sup>186</sup> Treaty on European Union and Treaty on the Functioning of the European Union, Article 3.1.(b), <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2010:083:FULL:EN:PDF>.

<sup>187</sup> Ibid, Article 3.3.

<sup>188</sup> Ibid, Article 4.

<sup>189</sup> Ibid, Article 13.

movement of goods, persons, services and capital, is provided. Thirdly, this article provides that the Council, upon proposal of the European Commission, sets the guidelines and conditions necessary to ensure balanced progress in all relevant sectors within the internal market. Article 27 obliges the Commission during the drafting of proposals for attaining objectives set out in Article 26, to take into consideration the extent of the efforts of those economies showing differences in development in order to maintain their viability. Consequently, the Commission may propose appropriate provisions, which may be in the form of derogations and which should be of temporary nature and cause minimal disturbance in the functioning of the internal market.<sup>190</sup>

Regarding the *free movement of goods*, the main standard set is the existence of the customs union, which implies a trade area for all goods where the establishment of any customs duty or any other measure with equivalent effect is prohibited, on imports and exports between Member States and the establishment of a common customs tariff in relations with third countries. As for products entering the EU market from third countries, it is considered that they are subject to free movement within the market after the completion of formalities relating to import and customs duties, which are of the equivalent value and are collected by customs authorities at the external borders of the Member States of the EU.<sup>191</sup>

As regards *freedom of movement of workers*, the Treaty obliges each member state to abolish any discrimination based on nationality against workers of other countries in terms of employment, remuneration and other conditions of work and employment. Furthermore, unless the restrictions are justified by reasons of public policy, public security or public health, freedom of movement of workers includes the right to:

- Accept offers of employment;
- Move freely within the territory of Member States for this purpose;
- Stay in a Member State for the purpose of employment, in accordance with the provisions governing the employment of nationals of that State (determined by law, regulation or administrative action); and
- Remain in the territory of a Member State after being employed in that State, subject to the conditions set out in regulations to be drafted by the Commission. These provisions do not apply to employment in the public service.

Regarding the decision-making procedures in the area of freedom of movement of workers, the European Parliament and the Council are obliged after consultation with the Economic and Social Committee, to issue directives or to create regulations setting out the measures necessary to implement the free movement of workers. This can be done in particular through:

- Ensuring close cooperation between national employment services;
- Waiver of those administrative procedures, practices and qualifying periods in

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<sup>190</sup> Ibid, Articles 26–27.

<sup>191</sup> Ibid, Articles 28–29.

related to the right to employment in vacancies that are available (whether they as a result of national legislation or agreements previously concluded between the Member States individually, whose application can be an obstacle to liberalization of the movement of workers);

- Removal of all such qualifying periods and other restrictions (prescribed by national legislation or agreements previously concluded between Member States) which impose on employees from other Member States conditions regarding the free choice of employment, except those imposed on the employees of the State concerned; and
- Creation of adequate mechanisms to bring offers of employment into contact with applications for employment and to facilitate the achievement of a balance between supply and demand in the labor market, in order to avoid serious threats to the standard of living and level of employment in different regions and industries.<sup>192</sup>

On the other hand, Article 47 of the Treaty provides that Member States should encourage the exchange of young workers in the framework of a joint program.

Another specific area within the free movement of workers, which also serves as a prerequisite for ensuring the latter, is the *coordination of social security schemes*. In this context, Article 48 of the Treaty requires the European Parliament and Council through the regular legislative procedure, to adopt legal measures that are necessary to provide freedom of movement of workers, respectively two types of measures for employed and self-employed migrant workers and persons in their dependency: (1) aggregation (for the purpose of obtaining and maintaining the right to benefit and calculation of the amount of benefit), of all periods taken into account under the laws of different countries, and (b) payment of benefits to persons resident in the territory of the Member States.

In the area of the *right for the establishment of companies*, the Treaty explicitly prohibits Member States to impose any restriction on freedom of establishment of companies, by any other Member State in their territory. Prohibition of these types of restrictions applies to individual citizens as well, and also to agencies, branches or subsidiaries of specific companies of any other Member State. More specifically, this freedom includes the right to undertake and carry out activities in the form of self-employment (for individuals) and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 54, under the conditions provided for the citizens of the state where the company is being established, and in accordance with the provisions on the free movement of capital.<sup>193</sup> Furthermore, the definition provided in the second paragraph of Article 54 refers to “companies or firms established based on civil or commercial law, including cooperative societies and other legal persons governed by public or private law, with exception of those legal entities that are registered as non for profit.”<sup>194</sup>

<sup>192</sup> Ibid, Articles 45–46.

<sup>193</sup> Ibid, Article 49.

<sup>194</sup> Ibid, Article 54, para. 2.

Regarding the decision-making procedures in the area of freedom of establishment of companies, Article 50 obliges the European Parliament and the Council, based on the regular legislative procedure, and after consultations with the Economic and Social Committee, to issue directives to ensure the implementation of these principles in concrete activities. According to this article, Parliament, the Council and the European Commission are obliged to perform duties arising from these provisions in particular through:

- Provision of, as a general rule, priority treatment to activities where freedom of establishment of companies provides particularly valuable contribution to the development of production and trade;
- Ensuring close cooperation between the competent authorities of the Member States in order to ascertain the correct situation within the Union, for the various activities concerned;
- Elimination of those administrative procedures and practices arising from national legislation or from agreements previously concluded between Member States, whose application is an obstacle to freedom of establishment of companies;
- Ensuring that workers of one Member State employed in the territory of another Member State may remain in that territory for the purpose of undertaking self-employment activities in that territory, in cases when they fulfill conditions which they are required to fulfill if they entered the country at the time when they intended to begin to undertake such activities;
- Enabling citizens of a Member State to purchase and use land and buildings situated in the territory of a Member State, as long as it does not conflict with the principles set out in Article 39 (2) (thus, based on the principle of prohibition of discrimination in employment, remuneration and working conditions);
- Implementation of progressive abolition of restrictions on the freedom of establishment of companies related to any branch of activities, in terms of: (1) the conditions for the establishment of agencies, branches or subsidiaries in the territory of a Member State, (2) subsidiaries in the territory of a Member State, and (3) the conditions governing the entry of personnel belonging to the main establishment into managerial or supervisory positions in such agencies, branches or subsidiaries;
- Coordinating, to the extent necessary, guarantees which in order to protect the interests of members and others, are required by Member States from companies or firms within the meaning of the second paragraph of Article 54, so that such safeguards measures are equivalent throughout the Union; and
- Ensuring that the conditions for establishment of companies do not disrupt the aid granted to companies by the member states.<sup>195</sup>

Article 51 outlines exemptions from these rules, which apply to activities associated with the exercise of official authority within the territory of the Member States, but also for other possible activities, which should be determined by the European Parliament and the Council, through regular legislative procedure. Further, Article 52 provides that the provisions within the framework of Chapter 2 (freedom of establishment of compa-

<sup>195</sup> Ibid, Article 50.

nies) and the measures undertaken to implement them do not prejudice the applicability of provisions stipulated by law, regulation or administrative acts providing for special treatment for foreign nationals for reasons of public policy, public safety or public health. Even in these cases, the Treaty obliges the European Parliament and the Council, through the regular legislative procedure, to issue directives for the coordination of these provisions.<sup>196</sup>

Another key provision which allows the application of the right for the establishment of companies is the one on the mutual recognition of qualifications. In this regard, Article 53 obliges the European Parliament and the Council, through the regular legislative procedure, to issue directives for the mutual recognition of diplomas, certificates and other evidence of formal qualifications and for the coordination of provisions stipulated by law, regulation or administrative acts in Member States concerning the pursuit of activities as self-employed persons. It is intended through these provisions to make it easier for persons to pursue activities as self-employed. Expressly excluded from this rule and medical and related professions, as well as pharmaceuticals, in which areas progressive elimination of restrictions depends on coordination of the conditions for their exercise in the various Member States.<sup>197</sup>

Another set of provisions regulate the treatment of companies or firms by each Member State in the territory of all Member States. In this context, Article 54 obliges Member States to treat companies or firms established in accordance with the law of a Member State, and which have the office, central administration or principal place of business within the Union, in the same way as natural persons who are nationals of Member States. For the purposes of this chapter, companies or firms are defined as “companies or firms established on basis of the civil or commercial law, including cooperative societies and other legal persons governed by public or private law, except those legal entities that are registered as non for profit organizations.” Finally, Article 55 obliges Member States to ensure equal treatment of nationals of other Member States as regards participation in the capital of companies or firms, as defined in Article 54.<sup>198</sup>

Chapter III of the Treaty of Lisbon regulates the area of *freedom to provide services across borders*. This chapter also begins with the provision that prohibits placing any restriction on the freedom to provide and receive services within the Union, for both companies operating in the territory of any Member State, as well as for nationals of any Member State. In conjunction with the latter, temporary provision of services by nationals of a Member State in any other member state is also allowed, based on the conditions and equal treatment with nationals of that Member State where the services are provided. In addition, the treaty allows the provision of services for third-country nationals if the European Parliament and the Council so decides, based on the regular legislative procedure. Furthermore, the treaty stipulates that services are provided in exchange for

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<sup>196</sup> Ibid, Articles 51–52.

<sup>197</sup> Ibid, Article 53.

<sup>198</sup> Ibid, Articles 54–55.

remuneration and their provision is governed by the provisions on the free movement of goods, capital and persons. In this context, Article 57 expressly provides that services include in particular the activities of industrial and commercial character, crafts and professions, whereas transportation services and the liberalization of banking and insurance services are regulated by the provisions in the area of transport, namely those of freedom of movement capital.<sup>199</sup>

As for *liberalization of specific services*, the Lisbon Treaty stipulates that this is regulated through directives adopted by the European Parliament and Council, according to the regular legislative procedure. In this regard, the treaty gives priority to those services which directly affect production costs and which help promote trade in goods. Furthermore, Member States are obliged to try to liberalize services beyond the scope of these provisions, if possible based on the general economic situation and that of specific services sectors, whereas the Commission is obliged to instruct the individual member states through recommendations. Finally, as regards the liberalization of services, while individual member states do not lift restrictions on individual services, they will apply these kinds of restrictions without distinction on grounds of nationality or residence, which applies only to issues covered by Chapter III of the Treaty (freedom to provide services across borders).<sup>200</sup>

Chapter IV of the Treaty of Lisbon regulates the area of *free movement of capital and payments*. Article 63 prohibits placing any restrictions on the free movement of capital and payments between Member States and third countries. This provision excludes the application of those restrictions against third countries which existed until the end of 1993, and which include direct investments (including in real estate), provision of financial services or the acceptance of securities in capital market ( except for Bulgaria, Estonia and Hungary, for whom the end date of 1999 applies). Secondly, as regards these three sectors of the economy (direct investment, including in real estate, financial services or securities), decision making is the responsibility of the European Parliament and the Council, based on the regular legislative procedure, and having as target free movement of capital to the greatest extent possible and without prejudice to other relevant provisions of the Treaty. Thirdly, only the Council (by unanimity after consulting the European Parliament and by a special legislative procedure) may adopt measures that constitute steps back in the liberalization of movement of capital and payments to or from third countries.<sup>201</sup>

Further, Article 65 sets other relevant provisions for the Member States as regards the regulation of these three types of capital, specifically the right of Member States to apply their national legislation in these areas of taxation (including legislation that distinguishes taxpayers which are not in the same condition based on residence and place of the capital investment), then to prevent violations of national tax laws and to establish

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<sup>199</sup> Ibid, Articles 56–58.

<sup>200</sup> Ibid, Articles 59–62.

<sup>201</sup> Ibid, Articles 63–64.

procedures for the declaration of capital movements for purposes of administrative or statistical information, or other measures which are justified because of public policy or public safety and security. These measures are not considered discriminatory and can be implemented without prejudice to the restrictions on freedom of establishment of companies and to be in compliance with the treaties. Finally, Article 66 provides that in exceptional cases, when the free movement of capital to or from third countries causes or threatens to cause serious difficulties in the functioning of economic and monetary union, the Council, upon the proposal from the Commission and after consultation with the European Central Bank, may take safeguarding measures against third countries for a period not exceeding six months if such measures are strictly necessary.<sup>202</sup>

The area of *competition* is regulated by Title VII of the Treaty of Lisbon. Nine articles within this part of the treaty define these principles and general rules: the prohibition of any practice of coordination / concentration of companies that may affect trade between Member States or that may distort competition in the internal market of the Union, abuse of dominant position by companies that cause the same effects in the market, prohibition of state aid (in cases where the aforementioned effects are caused). As above, responsible for passing legislation (regulations and directives) to implement these principles is the Council, upon proposal of the Commission and after consulting the European Parliament. On the other hand, the Commission is responsible for ensuring the implementation of this legislation (including through the monitoring of member states in these areas, penalizing violations and referring cases to the European Court of Justice).<sup>203</sup>

Lastly, the area of *consumer protection* is regulated by Title XV of the Treaty. The provisions under this title oblige the Union to contribute to protecting the health, safety and economic interests of consumers and to promote their right to information, education and to organize themselves in protecting their interests, all this in order to promote the interests of consumers and ensuring a high level of protection. This is expected to be achieved through completion of the internal market of the Union with measures that support, supplement and monitor the policies pursued by the Member States. Regarding the decision-making in conjunction with the latter, competency lies with the European Parliament and Council, after consultations with the Economic and Social Council, under the regular legislative procedure. Finally, these provisions do not prevent Member States to impose more stringent protective measures, but only require that these measures are in accordance with the treaties and that the Commission is duly notified.<sup>204</sup>

At the level of *specific provisions*, based on the structure of the chapters of the *acquis*<sup>205</sup>, the area of the internal market is covered by nine (9) chapters: Chapter 1 (*Freedom of movement of goods*), Chapter 2 (*Freedom of movement of workers*), Chapter 3 (*The right to*

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<sup>202</sup> Ibid, Articles 65–66.

<sup>203</sup> Ibid, Articles 101–109.

<sup>204</sup> Ibid, Article 169.

<sup>205</sup> Chapters of the *acquis*, [http://ec.europa.eu/enlargement/policy/conditions-membership/chapters-of-the-acquis/index\\_en.htm](http://ec.europa.eu/enlargement/policy/conditions-membership/chapters-of-the-acquis/index_en.htm).

*freedom of establishment of companies and provision of services*), Chapter 4 (*Free Movement of Capital*), Chapter 5 (*Public Procurement*), Chapter 6 (*Company Law*), Chapter 7 (*Intellectual Property Law, including Industrial Property Law*), Chapter 8 (*Competition Policy*) and Chapter 28 (*Protection of consumer and health*). Appendix 1 contains a detailed list of acts of the *acquis* of the EU applied to the internal market.

### **2.3. Policy Framework on Internal Market**

This section provides an overview of the policy framework on internal market in Kosovo, mainly focusing on the Private Sector Development Strategy 2013 – 2017, Sectoral Strategy of the Ministry of Labour and Social Welfare 2009 – 2013 and Strategy on Development of the Metrology Infrastructure 2010 – 2014. Other policy documents, such as the strategies on development of payments system, public administration reform and anti-corruption, also apply in some areas of internal market.

*Strategy for the Development of the Private Sector 2013 - 2017*, which is expected to be approved soon by the government in 2013, covers the area of free movement of goods, namely two specific areas: quality infrastructure (including metrology, accreditation and standardization) and market supervision.

This strategy includes two strategic objectives.

- Further development of quality infrastructure and institutional capacity for implementation and monitoring of relevant policies and legislation of conformity, with the aim of approximation with EU standards in these areas and thus facilitating the functioning of the internal market and external trade, in accordance with these standards; and
- Further development of legislation and policies in the areas of market supervision and consumer protection, with the aim of aligning with European standards in these areas.

Each strategic objective has specific objectives for each specific area, as shown in the following section.

The strategic objective of further development of quality infrastructure and institutional capacity for implementation and monitoring of relevant policies and legislation of conformity with the aim of approximation with EU standards in these areas and thus facilitating the functioning of the internal market and external trade, in accordance with these standards

Specific objectives:

Metrology:

- Increased capacity of existing laboratories and establishment of new metrology

laboratories in KCML and KLMI, covering the areas of metrology of mass, volume and flow, length, temperature and humidity, electrical size, time and frequency, pressure, prepackaging and density, strength and size associated with metrology in chemistry and precious metals. This means equipping laboratories with etalons and measuring equipment with the highest level of accuracy at the country level, storage of measurement capacity and establishing their measurement traceability; and

- Development of personnel capacities to perform all the required metrology services (regulation, measurements, type approval, metrological supervision, control of precious metals, prepackaging, etc.).

#### Accreditation:

- Provision of accreditation to all interested parties for accreditation of testing and calibration laboratories, inspection and certification bodies, increasing the number of accredited KAB, as well as the continued growth of the area of accreditation;
- Engaging in meeting the recommendations with the aim of Accession with full rights in the EA (European cooperation for Accreditation); and
- Continuous notification of accredited TVK with published guidelines and annexes of standards applicable in testing and calibration laboratories, inspection bodies and certification bodies approved by the EA (European cooperation for Accreditation), IAF (International Accreditation Forum) and ILAC (International Laboratory Accreditation Cooperation).

#### Standardization:

- Approval of all harmonized standards;
- Adoption of about 80% of EN standards such as SK, both these conditions for Kosovo's EU accession;
- Implementation of recognition (approval) of the 2000 standards / year; and
- Increase of technical and professional capacities.

#### Conformity Assessment:

- Approximation of domestic legislation with EU legislation for industrial products in accordance with the Directives of the New and Global Access and the requirements of 98/34/EC, 98/48/EC, 764/2008/EC, 765/2008 / EC 768/2008/EC and Directive 2001/95/EC on General Product Safety.

Strategic Objective Improving market supervision by approximating and implementing

legislation to improve the overall safety of products. As well as awareness of consumers in Kosovo about dangerous products that are found in the local market, by increasing promotional activities for information about dangerous products or other information relating to the increase in consumer awareness of their right to protection:

- Drafting, amendment and harmonization of legislation, as well as establishing a general framework of rules and principles relating to control of the market;
- Provision of an effective system of market supervision and consumer protection in Kosovo, which should ensure that the products in the local market will not endanger the lives and health of consumers;
- Elimination of all forms of illegal market behavior such as the gray market and unfair competition;
- Cooperation and coordination of institutions in the implementation of the market supervision activities;
- Supporting and strengthening civil society, which will advocate the interests of consumers before the institutions; and
- Raising awareness by making consumers more informed, aware, and educated.

The *MLSW Sectorial Strategy 2009 – 2013*, adopted by the Government of Kosovo in June 2009, is structured into strategic and operational objectives. Regarding *strategic objectives*, this strategy aims to: (1) Increase the level of employment and professional skills, depending on the requirements of the labor market, and (2) Development of cooperation with regional countries (EU members and those outside of the EU) to increase employment opportunities for the labor force in Kosovo.

At the level of *operational objectives*, in order to increase the level of employment and professional skills, depending on the requirements of the labor market, operational targets relevant to the area of the internal market are as follows: (1) Completion of legal framework for employment issues, (2) Coordination of standards and quality for the labor market; and (3) Review and modification of current design of professional curriculums and design of new curricula. On the other hand, the development of cooperation with regional countries (EU member states and those outside of the EU) to increase employment opportunities for the labor force in Kosovo aims the implementation of EU standards and cooperation in technical, material and human resources capacity building, through technical twinning agreements that will help the process of cooperation.

*Strategy for Metrology Infrastructure Development in Kosovo 2010 - 2014*<sup>206</sup>, adopted by the Government of Kosovo in June 2010, aims to create a competitive environment in the internal market of the country and its competitiveness on international markets by establishing fair criteria and technical standards for products and services, harmoni-

<sup>206</sup> Qeveria miraton Strategjinë për Zhvillimin e Infrastrukturës së Metrologjisë, <http://www.gapmonitor.org/?id=2&n=34>.

zation of legislation in this area with that of the EU and establishing mechanisms for its implementation. This strategy also foresees the creation of preconditions for the implementation of many EU directives in this area and over 20 thousand technical standards of the EU. Furthermore, this strategy obliges the Department of Metrology to develop and maintain a national metrology system, which shall enable the development of infrastructure of standard measurements as a basis to provide measurable and credible results in areas of public interest.

This strategy is based on the following basic principles:

- Alignment and comparison with international standards;
- Long term operational sustainability;
- Managing role of the KMD management in the development of the state system of metrology;
- Utilization of institutional capacity that meets the requirements for the quality of services provided
- Assessment of the quality of metrology services from a third party;
- Gradual development of technical level of metrology infrastructure standards;
- Appropriate use of existing infrastructure and metrology equipment; and
- Membership in key international organizations in this area.

This policy paper also explains in detail the current situation and identifies the problems and steps to be undertaken in developing the metrology system in Kosovo and the national measurement standards. This includes legal, industrial and scientific metrology, as well as adaptation in other areas and sectors related to this sector. A budget of about 3.1 million Euros (over the entire five-year period of implementation) is foreseen for implementation. This amount will also be used to establish the necessary laboratories for mass, volume and flow, electrical measurements, temperature and humidity, length, time, pressure, force, etc.

The *National Payments System Development Strategy*, adopted in 2009, defines the national payments system as an area which “encompasses everything that is concerned with the movement of money from payer to payee”.<sup>207</sup> This strategy is divided in nine pillars which are subject to development, and the main objective of the strategy is the replacement of CBK’s Electronic Interbank Clearing System, with Real Time Gross Settlement system, in order to minimize the systemic risks which are potential in large value net settlement systems. However, the implementation of the strategy is awaiting the adoption of the already drafted Law on Payment System.

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<sup>207</sup> Vision of the Future National Payments System, July 2009, p. 2, [http://www.bqk-kos.org/repository/docs/SistemiIPagesave/Vision\\_of\\_the\\_future\\_national\\_payments\\_system.pdf](http://www.bqk-kos.org/repository/docs/SistemiIPagesave/Vision_of_the_future_national_payments_system.pdf).

On market surveillance, the MTI Market Surveillance Department has initiated development of a sectorial strategy on this area. This strategy will cover areas of customs, as well as health, food, sanitary and labour inspection.

Lastly, the *Public Administration Reform Strategy* sets the public procurement as one of its objectives.<sup>208</sup> More importantly, the public procurement which in public is largely seen as affected by corruption is now part of the *2012 – 2016 Anti Corruption Strategy*.

- *Company Law*

In terms of policy making, the area of company law forms part of the *SME Development Strategy 2012 – 2016*. Even though company law is not the top priority of this strategy, the main goals related to it include: the development of capacities of the Municipal Business Centres (MBC); completion a Memorandum of Understanding between MBCs, KBRA and Small and Medium Enterprise Support Agency to strengthen the network of competences; to establish Business Information Points (BIPs) within upgraded MBC; and develop communication and reporting systems between MBCs, KBRA and SME-SA.<sup>209</sup>

- *Corporate Accounting and Auditing*

The main framework law in the area of corporate accounting and auditing is the **Law No. 04/L-014 on Accounting, Financial Reporting and Audit**. This law operates under the goal of regulating the “accounting and financial reporting system of business organizations ... audit requirements, qualifications for professional accountant, licensing of auditors, as well as foreign and local audit firms.”<sup>210</sup> Although the competent institutions have reported that the law has been drafted in compliance with the Fourth and Seventh directives, as well as the Eighth Directive for Approval of Responsible Persons to Perform Statutory Auditing, full compliance remains to be ensured. Furthermore, the Banking and Insurance Directive is also a directive which should have been taken into account when drafting the law.

The provisions of this law classify the business organizations for the purposes of financial reporting in three groups: large business organizations, medium business organizations, small business organizations, and micro enterprises. The latter is done in accordance with the annual turnover, gross assets at balance sheet, and number of employees.

There have been some remarks prior to the adoption of this law, particularly as to the requirement of the latter to prepare financial statements in compliance with the Inter-

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<sup>208</sup> Available at <https://map.rks-gov.net/userfiles/file/Strategjitet%C3%AB%20dhe%20Planet/STRATEGJIA%20E%20REFORMES%20SE%20ADMINISTRATES%20PUBLIKE.pdf>.

<sup>209</sup> SME Development Strategy for Kosovo 2012–2016, [http://www.sme-ks.org/repository/docs/190711\\_SME\\_Strategy\\_Final\\_angl\\_\\_441123573.pdf](http://www.sme-ks.org/repository/docs/190711_SME_Strategy_Final_angl__441123573.pdf).

<sup>210</sup> Law on Accounting, Financial Reporting and Audit, Article 1, [http://gazetazyrtare.rks-gov.net/Documents/Ligji%20per%20raportim%20financiar%20dhe%20auditim%20\(shqip\).pdf](http://gazetazyrtare.rks-gov.net/Documents/Ligji%20per%20raportim%20financiar%20dhe%20auditim%20(shqip).pdf).

national Financial Reporting Standards (IFRS). In this regard, the law does not exempt the small and medium sized business organizations from this requirement, which is considered too burdensome on these companies, particularly as to the costs of preparing such financial statements. With this in mind, the Fourth and Seventh directive should be transposed such as to avoid burdensome practices for the companies which are of no public interest.<sup>211</sup>

- *Intellectual and Industrial Property Law*

There are currently three main strategic documents adopted by the Government of Kosovo concerning intellectual property rights. The first document is the overall sectorial strategy; the second document is the customs aspect of intellectual property rights; and the third documents concerns piracy and counterfeiting.

The *Strategy on Intellectual Property Rights 2010 – 2014* is the main sector strategy. In general, the vision of the strategy is to create a sustainable and effective system for protection of intellectual property in Kosovo, which could help the economic growth. With this in mind, the following list provides the six main IPR sector strategic objectives for this period of time:

- Furthermore consolidation of the legal framework in line with International and European standards;
- Technical capacity building of IPR administration authorities;
- Technical capacity building of law enforcement institutions and enhancement of institutional cooperation and coordination;
- Establishment of collective management organizations for copyright and related rights, and development of a group of industrial property agents
- Raising awareness and education about IPR
- Accession of Kosovo to international institutions on IP and ratification of international conventions in this area.

Some of the actions for the implementation of the strategy, foreseen in the Action Plan (which has also been adopted), have already been completed – while others remain to be implemented.

*Kosovo Customs Strategic Operation Framework 2011 – 2014*<sup>212</sup> foresees that within its mission of economic development, the protection of trademarks is one of its objectives. Furthermore, within the sixth objective – namely, the application of legal powers and maximizing the use of law enforcement capacities, the Kosovo Customs have foreseen the application of measures to protect intellectual properties by legal powers and other means so that Customs can provide proper actions to be initiated against counterfeiting,

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<sup>211</sup> Reaction to the Law on Accounting, Financial Reporting and Auditing, adopted by the Assembly of Kosovo (SCAAK).

<sup>212</sup> Kosovo Customs Strategic Operation Framework (SOF) 2012-2014, [http://dogana.rks-gov.net/Uploads/Documents/KORNIZA\\_E\\_STRATEGJISE\\_OPERATIVE\\_2012-2014\\_eng.pdf](http://dogana.rks-gov.net/Uploads/Documents/KORNIZA_E_STRATEGJISE_OPERATIVE_2012-2014_eng.pdf).

piracy and intellectual property infringements.

The *National Strategy to Combat Counterfeiting and Piracy 2012 – 2016*, as the name itself suggests the main aim of the strategy is to fight the counterfeit and piracy. The most important objectives of the strategy are: the reduction of piracy and counterfeit, the identification of main causes of counterfeit and piracy, improving the productivity of creative industry, and the fight against the informal economy and create favourable conditions for foreign investments.

- ***Competition Policy***

Because the area of competition touches upon different aspects of economy, the strategic objectives of the government in inducing fair competition can be found generally in each economic development plan. However, to date, there is no sector specific strategy. The following address some of the competition issues:

The *Energy Strategy of the Republic of Kosovo 2009 – 2018*, foresees the development of electricity market and competition as one of its strategic objectives, whereas the application of EU approach regarding energy, environment and competition represents the focus of the strategy.

*Electronic Communications Sector Policy (or Digital Agenda for Kosovo) 2013 – 2020*, adopted by the Government of Kosovo in March 2013 (following adoption of the Law No. 04/L-109 on Electronic Communications, in October 2012) contains short- and long-term policies of the Government of Kosovo in the area of electronic communications. This policy document sets out priorities, objectives and obligations for the development of Information and Communication Technology (ICT), with the view to maximizing social and economic advantages provided by such technologies, mainly internet, as a very important instruments for economic, commercial and social activities, which's use enables provision and receipt of services, works, access to entertainment and communication, and free expression of opinions. This policy aims at improving the quality of lives of the people of Kosovo and of the business environment by providing opportunities for the use of the ICT and for increasing the number of Internet users in the country up to at least 85% by 2020.

This strategic document sets out three priorities: development of ICT infrastructure, development of electronic services and contents and promotion of their use, and enhancement of Kosovo people's skills in using the ICT. These priorities are commensurate with the objectives determined in the Communication from the European Commission, dated 19 May 2010, to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions titled *A Digital Agenda for Europe*. Taking into account the major economic importance of the electronic communications sector, and its enormous impact on social cohesion, education, health and human capacity-building in general as well as on the overall boost of Kosovo's competitiveness at the global level, implementation of this strategic document is of paramount importance.

The *Kosovo Trade Policy* (adopted in 2009) encourages competition, and sets the latter as one of the objectives in relation to the national economy as well as exports and imports.

Apart from the above, the online data provide the strategic objectives of Kosovo Competition Authority, namely, the organization and internal capacity of KCA, the completion of subsidiary legislation in compliance with EU legislation, the monitoring and initiations of investigations for competition infringements, and the advocacy for competition.

- *Consumer and Health Protection*
- *Consumer Protection*

In terms of the policy framework, the main strategic document is the **National Program for the Consumer Protection 2010 – 2014**. In summary, two main objectives of this programme are the following:

- Advancement and Furthermore development of the consumer protection, and
- Working toward the establishment of a stable market, with fair competition, which is protected by the legislation and the institutions from the unfair and misleading phenomena and practices which result in consumer harm.

This programme is developed in details, therefore the implementation of the latter can be easily reached if the enforcement of current legislative provisions is conducted appropriately. However, the implementation of this programme has not been satisfactory according to the Feasibility Study for SAA, which has required the improvement of implementation.

- *Health Protection*

**Health Strategy (2010 – 2014)** is the sectorial strategic document in Kosovo. The text of the strategy reflects on four main strategic objectives, namely the is the reduction of morbidity and mortality through increasing the quality of health services; the improvement of services and the improvement of management of existing resources; the functionality, reorganization, and completion of current infrastructure; and, the implementation and continuous development of Health Information System. Based on recommendations deriving from the SAPD, drafting of the Health Sectoral Strategy 2014 – 2020 is currently under way. This strategy will integrate all the existing strategies and plans in the health sector.

The *Health Information System Strategy 2010 – 2020* is divided in three phases, i.e.:

- Short-term actions (for the period 2011 – 2013) including infrastructure, design and implementation of HIS pilot system in two main regions (Pristina and Prizren), and the improvement of existing statistical system of health services;
- Midterm actions (for the period 2012 – 2014) leaving the pilot phase and transforming the HIS system in daily practice. Furthermore, monitoring of quality

- and assessing cost-effectiveness of health services will be done; and
- Long-term actions (for the period 2013 – 2020) with the objective of reaching a consolidated infrastructure of the HIS throughout the territory of Kosovo.

The *Mental Health Strategy 2008 – 2013* includes three main strategic objectives which in summary are: the prevention, treatment, and rehabilitation of mental diseases and disorders; monitoring, supervising, and continuous assessment of mental health services; and the development of legislation in the area of mental health.

The *HIV/AIDS Strategic Plan 2009 – 2013* has foreseen the following key objectives:

- Strengthening the information and data of the current situation;
- Strengthening the institutional framework, as well as the administrative capacities of the government and the civil society to implement the policies, programs, and services in a coordinated manner;
- Strengthening the legislative, policy, and financial framework for effective enforcement;
- Development of the quality of programs and services in order to fulfill the requests for prevention, care, support, and treatment of persons which are HIV positive; and,
- Expanding programs and services for persons which face the risk of HIV / AIDS.

### **3. Institutional Framework and Development in the Area of Internal Market**

#### **3.1. Free Movement of Goods**

- *Standardization*

Kosovo Standardization Agency (KSA) is the national body for standardization in the Republic of Kosovo which is responsible for developing, recognizing, adopting, approving and publishing standards in all sectors of the economy, excluding standards in the area of telecommunications”.<sup>213</sup>

Mainly because of political reasons related to memberships, KSA is not yet a member of any of the organizations, whether European (i.e. CEN and CENELEC), or international (i.e. ISO). However, it is a signatory to two bilateral agreements: the Memorandum of Understanding (MoU) with Ministry of Economy, Trade, and Energy of Albania and the MoU signed with the Standardization Institute of the Republic of Macedonia. In this regard, the agreement with Albania is of particular importance since CEN and CENELEC, both European standardization organizations have in principle agreed to this MoU, which enables the agency to adopt European standards within Kosovo territory.

The importance of achieving the membership status in CEN and CENELEC is a step which cannot be undermined. Unfortunately, the apparent obstacle towards member-

<sup>213</sup> Law No. 03/L-144 on Standardization, Art. 8(1).

ship is the first criteria/ out of three additional criteria set by CEN and CENELEC - Capability of becoming a member of EU or EFTA.<sup>214</sup> Further, the manner in which the latter is interpreted sets duties for both the government and the KSA. Namely, there must be a “Europe agreement” specifying the transitional period to accession, and “the process of approximation of the national system with that of EU must have reached such a point that the specific legislative framework for voluntary standardization is in place and fully operational”.<sup>215</sup>

The Professional Council of Standards (PCS)<sup>216</sup> composed of 9 members serves as an advisory body within KSA, which decides on the establishment of Technical Committees (TC). The total number of established TCs by KSA reaches 18.<sup>217</sup> The essential role of the TCS is to contribute in initiating and drafting new standards. For this reason they are composed of both private and public members, including ministries, chambers of commerce, and civil society members. Unfortunately, there is no relevant information on the level of involvement of the business community in the work of TCs. KSA is the body that can and is in charge of inducing the interested parties to actively participate in these committees, for two principal reasons: the needs of the businesses must take lead in influencing the content of standards in discussion; thus, consequently increasing their use, by the same parties which have worked on their adoption, regardless of their voluntary nature.

As provided above, the voluntary nature of the standards is usually perceived as an obstacle in their implementation. In the words of the European Commission “...awareness of the potential synergies between research, innovation and standardisation also needs to be raised through better education and training about standards...”<sup>218</sup> The lack of awareness of the business community on the importance on the use of standards can easily cripple the use of standards.

The Feasibility Study for SAA reports that a number of approximately 4,000 European standards are adopted as Kosovo standards.<sup>219</sup> In terms of new standards, adopted as

<sup>214</sup> CEN/CENELEC Guides, Guide 20, <http://www.cenelec.eu/membersandexperts/referencematerial/guides.html>.

<sup>215</sup> Ibid, p. 36.

<sup>216</sup> Administrative Instruction on Establishment of the Professional Council of Standardization, February 2011.

<sup>217</sup> List available at <http://mti-ks.org/?cid=1,649>; Administrative Instruction on Organization and Functioning of Technical Committees, June 2011; Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 27, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf);

<sup>218</sup> Communication from the Commission to the European Parliament, the Council, and the European Economic and Social Committee. A strategic vision for European standards: Moving forward to enhance and accelerate the sustainable growth of the European economy by 2020, p. 7 (2011), <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0311:FIN:EN:PDF>.

<sup>219</sup> These figures have been published in the Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo\*. However, the 2011 Kosovo Progress Report, published in October 2011 speaks of 3,400 standards.

Kosovo standards, the number reaches 850. It is very important that the current administrative capacities are directed towards adopting new standards, particularly the work on translating standards. The latter is a prerequisite for KSA which is in charge of offering adequate tools to achieve the free movement of goods and help domestic businesses to be more competitive.

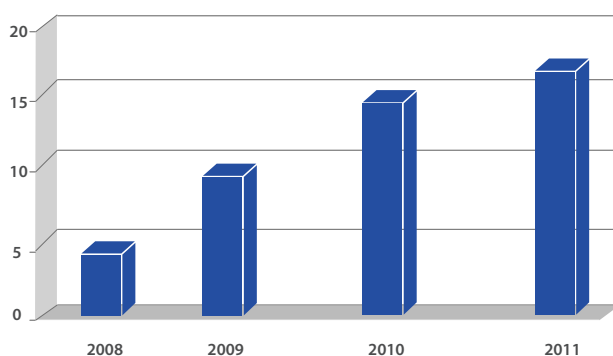
The active involvement of competent administrative capacities in following the developments in the area, through active communication with other European and international standardization agencies would potentially serve a good basis in terms of knowledge for the awareness raising campaigns towards the stakeholders.

- *Accreditation*

The Kosovo Accreditation Directorate (KAD) is the only independent national accreditation body in Kosovo, which is established within the MTI. The Accreditation Council Regulation has been adopted in February 2011, which confirms that this council functions within the Directorate, its main mandate being the representation of the interests of all the stakeholders (businesses and chambers of commerce are members). KAD has already received the membership status in the International Laboratory Accreditation Cooperation (ILAC), while from 2010 it is a member of International Accreditation Forum (IAF). By signing a contract in 2011, KAS became an associate member of the European co-operation for Accreditation (EA). Memorandums of understanding have been signed with Albania, Croatia, Turkey, and Macedonia. The fact that the membership status within the above mentioned institutions needs to be actively maintained by the Communication Office within KAD, should not be ignored – particularly as to the importance of the use of regulations and guidelines of IAF and ILAC.

According to the 2011 annual report of KAD, the number of assessors is 15 (lead assessors and other). The latter might serve as an indication to use the EA procedures in order to increase the number of experts and technical assessors, which are considered key players in delivering qualitative accreditation activities.

According to 2011 KAD Annual Report, the number of conformity assessment bodies in 2011 was presented as follows:<sup>220</sup>



<sup>220</sup> Available at <http://www.dak-ks.org/?cid=1,2>.

However, according to unofficial data, there are currently around 21 accredited conformity assessment bodies. The importance of these bodies remains crucial on the execution of services for conformity assessment, namely, performance of conformity assessment activities, including measurements, testing, verification, and controls. By way of comparison, also the year of 2011, 91 conformity assessment bodies have been accredited in Macedonia. Thus, the current number of accredited conformity assessment bodies must be an indicator that more is to be done in this area (e.g. one of the areas which could potentially be targeted is the accreditation of medical laboratories).

- *Metrology*

The development of metrology and its supervision are the responsibility of the Metrology Department (MD), operating within MTI, with general functions in scientific, industrial, and legal metrology. Since October 2010 this department is a liaison organization of the EURAMET - European Association of National Metrology Institutes. The Law on Metrology foresees the operation of two laboratories, the Central Laboratory (KCML) located in Prishtina, and the Metrology Institute located in Prizren, in charge of legal metrology. KCML, in charge of scientific metrology, is operational since 2010, and it includes the laboratories of mass, volume, electrical measures, flow, quality control of precious metal products, and laboratory of force and thermometry.

There is a remaining number of laboratories which need to be functionalized, e.g. laboratories of length, pressure, time and frequency laboratories, laboratory for density and reference materials laboratory. Furthermore, existing laboratories should be able to meet international standards. Because metrology and calibration are key requirements to reducing technical barriers to trade, and ensure equal measurements which fight against unfair competition between producers, the functionality and development of laboratories is an area which should be given priority. The latter should be also understood to include qualified staff which can provide qualitative services, towards building reliability and trust in the metrology system.

Lastly, the metrology law includes within its scope the metrology surveillance and inspections. This is an area which has been identified as lacking clear division of responsibilities between the scope of market inspectorate/surveillance and the metrology surveillance. The Decision of the Government in restructuring the MTI will clear out the issue.

- *Conformity Assessment*

The area of technical requirements and conformity assessment procedures is an EU area of active developments, particularly considering the new approach legislation. For this reason, the institutional capacities of MTI should be actively engaged on the developments, and possess technical knowledge in order to be able to actively cope with this constant-changing legislative and technical environment. In this regard, the availability of premises and functional technical equipment are equally important.

Last but not least, it is of utmost importance to make sure that the conformity assessment procedures are not duplicated. The latter may occur in scenarios when new European technical regulations are transposed in Kosovo which require a particular conformity assessment procedure. Should these scenarios occur, the doubling of procedures will result through directly causing barriers to trade.

- *Market Surveillance*

The Market Inspectorate (MI) is an executive body within the MTI and it is responsible for market supervision, which implies their ability to take a number of measures to stop the circulation of noncompliant products, in the territory of Kosovo. The organization and functioning of the Inspectorate is conducted under the two administrative instructions adopted in 2011. Further, a General Product Safety Unit functions within the Market Inspectorate. With 7 offices in all municipalities, the number of inspectors is approximately 120. According to the data provided in the Feasibility Study for SAA the MI has conducted 30,000 inspections since 2005.

An issue which has been identified with the market inspectorate legislation is the centralization of the market inspectorate. The latter has caused implementation problems, particularly with the position of municipalities which was generally against this (some of the reasons: the absence of local level inspectors would make way for the informal economy to further increase, the number of local inspectors to decrease, the revenues of the municipalities from the market inspectorate to switch to the MTI). Largely, it is perceived that the centralization of market inspectorate has indirectly caused decrease of the level of market inspections. The latter is problematic since it directly tackles the consumer protection area, where the product and health safety are of vital importance.

Last but not least, a body which is closely related with market inspection are the customs, particularly for the goods which are manufactured in other countries and intended to enter the Kosovo market. Thus, active cooperation of MI with the customs (as well as other institutions involved) is of fundamental importance. The Memorandum of Understanding which has been signed should be prioritized and actively implemented.

### **3.2. Free Movement of Workers**

- *Access to Labour Market*

The Department of Labour and Employment at the Ministry of Labour and Social Welfare (hereinafter MLSW) is the main body that is in charge of issuing work permits for foreign citizens. The numbers of these work permits which are issued each year are currently subject to the implementation of the governmental policy of foreign workers. Thus, the Government of Republic of Kosovo “according to the policies on migration, stay and labour market mobility, at the end of each year for the coming year, sets the number of employment permits for foreign persons, in accordance with the employ-

ment opportunities of foreign persons in our country”.<sup>221</sup> The body which monitors the enforcement of legislation in this area, and the issuing of work permits is the Labour Inspectorate. Since the entering into force of the Law No.03/L-136 the reported number of work permits issued in between 2010 and 2011 was 3290.

- *Coordination of the Social Security System*

The MLSW is the institution in charge of the area of coordination of social security. The trend of negotiating bilateral agreements has not gone through a rather desired pace.

The agreements with Austria (2012) and Germany (2011) are currently being implemented in retirement pensions and disability. Bilateral agreements in force are the ones with Macedonia and Albania as well. The current trends in the area of free movement of workers and the coordination of social security scheme in the EU require an enhanced institutional framework and human resources in order to properly understand and follow developments concerning this freedom. Furthermore, the human capacities which are capable of both opening new negotiations and properly implementing the existing bilateral agreement are fundamentally important.

### **3.3. Right to Establishment and Freedom to Provide Cross-Border Services**

- *Right to Establishment*

An essential condition in order to carry on their economic activity, which applies to domestic companies as well, is their registration at the Kosovo Business Registration Agency (KBRA). The latter is the only agency in charge of business registration, either foreign or domestic. The one-stop-shop policy of KBRA has facilitated the business registration procedure. It has been reported that 25 one-stop-shops in different municipalities are available to businesses, and a number of administrative steps are provided immediately (e.g. registration and VAT certificates, fiscal numbers). Furthermore, ARBK is successfully working towards simplifying the criteria for registration, and it has particularly done so by removing the minimum startup capital for limited liability companies, and reducing minimum startup capital for joint stock companies (from € 25,000 to €10,000). The practices, as per the legal framework are non-discriminatory.

It is important to note that the implementation of the online business registry would offer convenience to businesses, particularly foreign, which want to establish themselves in Kosovo. Furthermore, the benefits of an online registry can provide efficiency and lower costs for businesses. In this regard, an issue for consideration towards the implementation of the electronic registry would also be the adoption of the Law on Electronic Signatures, which is not foreseen in the 2013 legislative program.

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<sup>221</sup>

Law No. 03/L-136 on Granting Permit for Work and Employment of Foreign Citizens, Art. 4(1).

- *Freedom to Provide Cross-border Services*

Considering the nature of the legal framework in this area, many bodies form part of the institutional framework, MTI and the Central Bank of Kosovo being among them. For this exact reason the Coordination Body was established in 2010 with the main objective of harmonizing legislation in the services sector. A product of this body is a database, which should serve as a forum for reviewing the legal changes in this area. While it has already been reported that the database was launched, the actual start of its implementation and maintenance on the legal changes aspect would help towards assessing the compliance of current legislation with *acquis*.

The Central Bank of Kosovo as one of the institutions in charge of financial services, subjects companies to licensing. Often, the licensing system amounts to a legal and administrative barrier to trade in services. The review of the licensing system by the institutions in charge would help in identifying which licensing requirement actually amount to barriers to trade.

Generally, the statistical information on the provision of cross border services is lacking. As a consequence of this, many reports on trade of services provide different statistics, which puts doubt to the reliability of information. For this reason, the maintenance of the database which has been launched in 2011 is crucial, conditioned upon competent administrative capacities.

- *Postal Services*

The entity which is licensed to provide universal postal services is the Public Postal Operator, an entity monitored by the Telecommunications Regulatory Authority, with the competence of regulating the postal market in Kosovo. It is reported that the staff currently working in this sector is undergoing general and specialized training. However, one of the main hurdles in the proper modernization and operation of the public operator is the privatization process. Although considered a political issue it has impacted its performance, and to date the process has not been finalized.

- *Mutual Recognition of Professional Qualifications*

The Ministry of Education Science and Technology (hereinafter MEST) is the institution which has competences in the area of mutual recognition of professional qualification; respectively, the National Council for Recognition (NARIC) is the body operating within MEST, through which decisions on recognition and equivalency are reached, based on the Higher Education Lisbon Recognition Convention in European Area. The relevant structures within MEST are expected to further develop the procedures for recognition of foreign professional qualifications.

### **3.4. Free Movement of Capital**

One of the institutions in charge of issues arising in the area of free movement of capital and payments systems is the Central Bank of Kosovo. CBK within its structure has

two departments specifically designed for operations within this area. In this regard, the Licensing and Regulation Department concerns certain aspect of movement of capital, while the Payments Systems Department covers the other. The capacities which are available by the CBK for the supervision of the financial sector are adequate.<sup>222</sup>

Another institution which has stakes in capital movements is MTI, the Agency for Business Registration (see discussion above), as well as the Investment Promotion Agency, which is established according to Article 19 of the Law on Foreign Investment.

### 3.5. Public Procurement

The Public Procurement Law sets three main bodies which are in charge of its implementation. The PPRC is the regulatory agency in the public procurement area.<sup>223</sup> The PPRC is "...responsible for the overall development, operation and supervision of the public procurement system in Kosovo..." and its functions include but are not limited to: conducting investigation of procurement activities, issue opinions to contracting authorities regarding their decisions, establishing detailed rules for the correct implementation of the law, and offering assistance in the application and interpretation of the provisions of the law.<sup>224</sup> The three members of PPRC are nominated by the Government and endorsed by the Assembly, to which there are also accountable.

The Central Procurement Agency is the central executive agency within the Ministry of Finance and the main contracting authority.<sup>225</sup> Although the procurement power is not centralized, the government has the power to authorize CPA to conduct certain procurement activities on behalf of the government.

The Procurement Review Body is an independent administrative review body, whose main task is to review complaints from interested parties, and conduct investigations of possible violations in procurement activities.<sup>226</sup>

The 2011 Progress Report addresses the overlap of the competences between the three public procurement bodies as one of the challenges - as a consequence of these powers not being entirely defined by law. Although, in 2012<sup>227</sup> the analysis of this situation results in a clearer division of duties and relations between three main institutions, the duplication of functions when it comes to addressing the complaints and the supervision of

<sup>222</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 24, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).4

<sup>223</sup> Public Procurement Law, Art. 86.

<sup>224</sup> Ibid, Art. 87.

<sup>225</sup> Ibid, Title VII.

<sup>226</sup> Ibid., the powers of PRB are listed in Article 105.

<sup>227</sup> Kosovo European Partnership Action Plan 2012, [http://www.mei-ks.net/repository/docs/European\\_Partnership\\_Action\\_Plan\\_2012.pdf](http://www.mei-ks.net/repository/docs/European_Partnership_Action_Plan_2012.pdf).

the implementation will cause problems in its implementation.

According to Feasibility Study for SAA around 530 procurement officers are engaged in 161 contracting authorities (central, local, public companies, and other companies) in Kosovo. Procurement officers and other staff are trained in accordance with Article 25 of the law, which provides that the Kosovo Institute for Public Administration is responsible for developing trainings in this area, in cooperation with PPRC. According to this law, 15 days of training is the minimum threshold.

The professionalism of procurement officers plays a crucial role in procurement procedures, clearly stipulated by the law in Article 1(2): "This law also aims to ensure the integrity and accountability of public officials, civil servants and other persons conducting or involved in a procurement activity by requiring that the decisions of such individuals, and the legal and factual bases for such decisions, are free of any personal interest, are characterized by non-discrimination and a high degree of transparency, and are in compliance with the procedural and substantive requirements of the present law."

The latter illustrates the level of importance of competent staff in procurement activities. PPRC in cooperation with KIPA should work towards raising the quality of trainings offered, consequently achieved by full professionalism and independence of procurement officers.

### 3.6. Company Law

The main institution in charge of business registration and other aspects of company law is the **Business Registry Agency** within the Ministry of Trade and Industry. The competences and the scope of work of this agency are provided within the Law on Business Organizations. Mainly, the Agency works under the mandate of maintaining a register and conducting registration procedures for businesses which are subject to registration, as well as the ones that intend to dissolve their business.

The Agency has undergone constant reforms, and is reported to be working at full capacity. The introduction of the *one-stop-shop system* has considerably facilitated the workload of the agency. What's more important is that it has eased the registration route for businesses, whereas the procedure has been simplified. The innovation which has been introduced is the issuance of the business fiscal number, VAT certificate, and import-export certificate together with the business certificate in just 3 days. There are currently 26 municipal registration centres.

The number of staff seems to be sufficient, considering that the number of employees accepting the applications has been increased. However, just as in any other area, the constant education and training is needed. The education and training component should concern both, the technical and substantial aspects of company law. For example, Macedonia employs a staff of 13 responsible for harmonizing the national company law with European legislation, within the legal department of the ministry in charge. Thus com-

petent staff in following the EU company law trends as well as the relevant *acquis* is of utmost importance.

Another institution which contributes to the procedures at the Agency, namely the dissolution procedures, is the **Kosovo Tax Administration**. Currently, for all the procedures concerning deregistration or remission requests, the business registry asks for a tax statement from the tax administration which purpose is to ensure that all outstanding tax obligations of business seeking deregistration are fulfilled.

- **Corporate Accounting and Auditing**

The main body in charge of implementing the law is the **Kosovo Council for Financial Reporting**, formerly known as the Kosovo Board on Standards for Financial Reporting. The current Council for Financial Reporting is established within the Ministry of Finance. The functions and responsibilities of the KCFR are set within the law, making this body the regulatory in this area. According to Article 14 of the law, the functions of the KCFR are KCFR functions include: the drafting and approving Kosovo Accounting Standards; supervision and implementation of Auditing Standards; and licensing and keeping register of auditors/audit firms/professional associations of accounting and auditing. According to the available organisation structure within their website, the secretariat of Kosovo Council for Financial Reporting seems to have five employees.

The **Society of Certified Accountants and Auditors of Kosovo (SCAAK)** is a leading and only institution to offer professional accounting and auditing education in Kosovo. According to the law, the education provided by this institution should be in compliance with International Accounting Education Standards IFAC as well as with relevant EU directives. The current certification programme of SCAKK is directed towards three degrees, namely: accounting technician, certified, accountants, and audits. An rather old World Bank Report on Accounting and Auditing (2006) did identify a number of issues with regard to SCAAK education programme. The latter implied that the programmed did not address many topics of the Eight Directive.<sup>228</sup> To date, there is not report as to whether this has been addressed.

### **3.7. Intellectual and Industrial Property Law**

- **Intellectual Property Rights**

The intellectual property rights sector involves a number of institutional stakeholders, and this is also illustrated by the number of laws involved which regulate different aspects of this sector. The main institutions involved are: the Ministry of Culture, Youth, and Sports, the Ministry of Trade and Industry, the Ministry of Finance, Ministry of Internal Affairs, and the Ministry of Justice.

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<sup>228</sup> Report on the Observance of Standards and Codes (ROSC)-Kosovo: Auditing and Accounting p. 10, [http://www.worldbank.org/ifa/rosc\\_aa\\_kos.pdf](http://www.worldbank.org/ifa/rosc_aa_kos.pdf).

Considering the fact that several institutions are involved, the need for a body which would work under the mandate of coordinating these institutions and increasing their cooperation was necessary. For this reason, the *IP National Council - Intellectual Property State Council* was established in 2011. The sections to follow will give a more detailed overview and analysis of the above mentioned institutions.

- *Copyright and Related Rights*

The copyright component of intellectual property rights is under the competence of the Ministry of Culture, Youth and Sports, namely Office for Copyright and Related Rights (OCRR). One of the main functions of this administrative body is the issuance of authorizations, revocation, and supervision of collective administration rights. For this reason, OCRR has developed Rules for Granting Permit to Associations for Collective Management of Rights.

Furthermore, the OCRR is responsible for promoting the copyright and related rights to stakeholders, as well as ensure the up-to-date legislation. The above clearly indicates that the competences of OCRR given by the law are limited. In this regard, the increase of the number of staff, currently of comprised of four employees is not a burning issue. However, considering that their competencies are mainly of substantial nature (the legislative component particularly), the staff should be competent to follow the legislative changes in the EU legislation, and be able to conduct such in the national law.

- *Industrial Property Rights*

According to the Patent Law, the protection of patents, trademarks, industrial design, and names of origins, geographical indications and topographies is the responsibility of the *Industrial Property Office* within the Ministry of Trade and Industry. This office is operational since 2007, foreseen by the old law on patents, and functioning on the basis of the Administrative Instruction No. 2007/06 on the Organization and Functions of the IPO. The law provides a list of competences for the IPO, ranging from procedures of granting patents, certificates of inventions, or registration of trademarks; keeping and registers of the objects of the industrial property representatives; legislative competences, and representation of the IPO in international organizations.

Thus, considering this range of responsibilities, the adequate number of staff and the facilities to operate are of utmost importance. During 2012 the office operated with fourteen employees. Unfortunately, the latter has been identified as one of the challenges facing the IPO in the Feasibility Study for SAA. In particular, the competences in handling the procedures and maintaining the register are aspects which require competent staff and adequate premises. The former is important since the matters dealt with at the IPO involve quite material matters, which require specialized qualification in IP law.

- *Other relevant institutions*

One of the main institutions in charge of the enforcement of the IPR rights is the Ministry

of Finance, through the *Kosovo Customs*. The Law on customs measures for protection of intellectual property rights obliges the Customs to apply border measure measures for protection of intellectual property rights when the goods are suspected for infringing these rights. The IPR Unit functions within the Department for Operation and Investigation since 2011.

The *Market Inspectorate* within the Ministry of Trade and Industry is among the institutions involved in protection of IPR. The Market Inspectorate is responsible for the inspection of products placed on the market as well as producers in order to ensure consumer protection towards false marketed products, and ensuring the protection of copyright and industrial property rights.

The *Department for Economic Crimes and Corruption* within the Kosovo Police is currently in charge of investigation of IPR infringements. The outcomes of these investigations have to be reported to the prosecutor's office. The creation of a unit which would deal with IPR infringements only has been foreseen, however, it has not been put into practice yet.

The *Ministry of Justice* is in charge in the context of the involvement of the judiciary in the protection of intellectual property rights. The current competent Commercial Matters Department within the Basic Court has just started operating. The expectations are that because of the lack of intellectual property law qualifications, as well as following the reorganization of the court system the actions filed before the latter will not be quickly.

### **3.8. Competition Policy**

- *State Influence on Competitiveness*

The regulatory authorities of the current public owned enterprises are the institutions in charge of monitoring the sectors such as energy, telecommunications, aviation, media, and postal services. The main regulatory authorities currently are the following: Energy Regulatory Office, Regulatory Authority of Electronic and Postal Telecommunications and Civil Aviation Authority of Kosovo.

The *Energy Regulatory Office* which operates since 2004 within many other competences, has the power to grant, modify, suspend, transfer and withdraw licenses; supervise and control compliance with licenses; and fix and approve tariffs and tariff methodologies for regulated energy services.<sup>229</sup> Therefore, its two main components are the electricity and the district heating.

The *Regulatory Authority of Electronic and Postal Communications*, which has been operating since 2004, is a national regulatory authority in the area of electronic and postal communication services. This institution carries out tasks set forth by the laws in

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See Establishment of the Energy Regulatory Office, <http://www.ero-ks.org>.

force, and implements national policies and strategies of the sector of electronic communications, as developed by the MED. The authority is responsible for fostering effective competition in provision of electronic communication services and networks and accompanying premises and equipment, and other services, by encouraging investment in electronic communications infrastructure and new technological developments and high quality products, as well as by providing for non-discrimination and equality in dealings with electronic communications network and service providers. While this authority was established with the main aim of licensing and supervising the providers of telecommunication services, the Licensing/Authorisation and Monitoring Commission operates with the main aim of analysing, evaluating, and monitoring the licensing terms.

The *Civil Aviation Authority* is in charge of (within other powers) to Implement civil aviation legislation as well as implements the policies adopted by the competent ministry or the government in the area of civil aviation.

- *Antitrust and Mergers*

The main institution in charge of antitrust and mergers is the *Kosovo Competition Authority*. The competences, the scope of work, and the organization structure of the KCA is provided in the Law on Protection of Competition. The KCA has the status of the public independent institutions, but it is accountable to the Assembly. The managing of the activities of the KCA is conducted by the *Commission for Protection of Competition* which is composed of 5 members. Consequently, the accountability and the financing of these types of authorities by the state budget are considered to lower the level of their independency towards the government.

Article 28 of the Law, defines a list of duties and responsibilities of the Commission, including competences in development of legislation, adoption of decisions, issues punitive measures and conditions for their execution, conducts investigations, produces recommendations, and provides information and awareness campaigns on competition rules.

The abovementioned article gives a clear overview of the workload that this institution is subject to, hence implying the level of professionalism that is requested. But, to date, one of the main challenges of the KCA remains the lack of competent staff which would be able to implement of the tasks of the KCA. The latter can be easily divided on three different components: constant market monitoring, conducting of investigations, and continuous awareness rising campaigns. The issue currently lies as a two-tier challenge, namely the lack of staff in general, and the lack of staff with qualifications and background education in competition.

Furthermore, having in mind the fact that the KCA has adopted the Administrative Instruction on Criteria to Reduce or Release Administrative Measures, the legal basis to develop a Leniency Programme is set in place. The latter would provide information on this administrative instruction as well as promote the reasoning behind leniency, which is the reduction of complete avoidance of fines for companies that have participated in

prohibited agreements.<sup>230</sup>

Lastly, in terms of national inter-institutional cooperation, the KCA is a signatory to a number of memorandums of understanding, including the Kosovo Customs, Kosovo Central Bank, Regulatory Authority of Electronic and Postal Communications, Ministry of Finance, and the Ministry of Trade and Industry. On the other hand, KCA has signed a MoU with Albania and Macedonia, and most importantly it is a full member of ICN – International Competition Network.

- *State Aid*

According to the law on state aid, the State Aid Office, namely the decision making body – the State Aid Commission, within the Kosovo Competition Commission is foreseen to be established. In this regard, the European Commission has greeted the legislative body for choosing to establish this commission outside the scope of the ministry of finance, particularly considering that the current option could help in ensuring a level of operative independence from the government.

The appointment of the members of the Commission is done by the government, after the proposal of the Ministry of Finance. These members are mainly government stakeholders, namely: the Minister of Finance will sit as the Chairman, the Minister for European Integration and Minister of Trade and Industry as member; one member from the civil society, and the chairman of association of municipalities.

To date, there are no reports whether there have been any developments regarding the establishment of the institutional structure in charge of state aid, although it was foreseen to be done in the last quarter of 2012. It is reported that the issue concerns the lack of working premises. Therefore, the recommendations of the EC within the Feasibility Study for an SAA remain to be implemented. The implementation of the law and its entire functioning depends on the functioning of these structures.

Upon establishment of the institutional structure, a currently missing comprehensive state aid inventory on existing and future aid scheme should be established. This inventory would include all types of state aid (e.g. direct, indirect), and it would serve the purpose of providing information on the total amount of aid granted during one financial year by the government. The latter should also involve the review of current acts which might consider or constitute state aid, and make an assessment of whether these acts are in accordance with the State Aid law. Thus, the measures which might result as fulfilling the criteria of state aid should be notified and registered; while the others should be annulled. There are currently several areas which are subsidized (see discussion on state influence above), which need to be assessed.

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<sup>230</sup> European Commission–Competition: Cartels–Leniency, <http://ec.europa.eu/competition/cartels/leniency/leniency.html>.

In general, the data provided in the official website of the Kosovo Competition Authority is rather old. Apart from this, the essential information on the functioning, annual reports, organizational structure, decisions and other aspects of their work are lacking. This also includes the information on the State Aid Commission which functions within KCA. Consequently, the provision of relevant information on these two important areas of law, is essential to the public, and should constantly be refreshed and available.

### 3.9. Consumer and Health Protection

- *Consumer Protection*

When it comes to institutions which contribute in the consumer protection affairs, the list is quite extensive. However, two bodies which have the most competences in consumer protection area are: the Council of Consumer Protection, and the Consumer Protection Office.

The Consumer Protection Council is the main institutional body in the area of consumer protection, which is also regarded as the market regulator for consumer protection. This Council is also important with regards to the adoption and implementation of the national programme on consumer protection. The compilation of council is specific, whereas representatives of the following stakeholders shall appointed: two representatives of MTI, a representative from the Food and Veterinary Agency, one representative from the Kosovo Chamber of Commerce, one from the Alliance of Kosovo Business, one representative from the American Chamber of Commerce, the representative of consumer associations and one independent expert of the consumer protection area. The work of this council is subject to a monthly meeting with supervisory powers on the implementation of the legislation and the national programme.

The *Consumer Protection Office* according to the last Ministry of Trade and Industry restructuring, of 2012, has been upgraded into a *Consumer Protection Department*. This upgrading has been done considering the importance of the consumer protection in economic developments, whereas the head of this department is directly accountable to the MTI secretary general.

The role and the responsibilities of this department include the drafting and implementation of legislation as well as strategic documents in the area of consumer protection. Furthermore, it is responsible for supporting and maintaining cooperation with non governmental institutions in this area. Lastly, but with major importance, this department serves as the point for developing the manner of resolving consumer complaints, as well as undertaking the role of the educator of the consumer about its rights upon purchase.

The lack of adequate funds as well as the lack of human capacities has been a constant challenge for this department. To date, the number of staff reaches three persons. In order to be able to undertake its role, and the abovementioned responsibilities, the de-

partment needs to particularly work toward enhancement of administrative capacities.

- **Health Protection**

There are different institutions in charge of implementation the legislation and policies in the area of public health, as described in the following.

The *National Public Health Institute* (NPHI) is the main institution in charge of implementing public health policies. According to the Law on Public Health, NIPH is “the highest health, professional and scientific institution [which] organizes, develops, supervises and participates in application of the public health policies”. The NPHI has six departments and five (5) regional structures, whereas the number of staff is 292. The Ministry of Health aims to increase the number of NIPH staff: it has planned to hire eight (8) additional officers (in the sector of drinking water).

The Sanitary Inspectorate and Health Inspectorate have major competencies in the enforcement of the Law on Tobacco. The *Sanitary Inspectorate* within the Food and Veterinary Agency is an executive body which is in charge of monitoring the implementation of rules that are related to the public health. This inspectorate is divided in central and municipal level. The *Health Inspectorate* is an administrative body that carries out external professional monitoring of the health institutions.

The *National Blood Transfusion Centre* (NBTC) is a public health institution that provides blood transfusion services, as well as activities of educational and scientific nature. The infective clinic within the *University Central Clinic of Kosovo* has competencies in the area of infectious diseases.

Apart from the above, there is a number of institutions which are stakeholder in addressing public health issues, such as the regional hospitals, laboratories, and the main family medicine centres. Health protection services are provided at three levels: primary, secondary and tertiary. Municipalities, namely the main family medicine centers (MFMCs) are responsible for the provision of primary health care services, secondary healthcare is provided by regional and city hospitals (7 in total), while tertiary healthcare includes specialized health services provided by the healthcare institutions described above (UCCCK, NBTCCK and NPIH), including functions related to higher studies and scientific research at the Faculty of Medicine of the University of Prishtina.

Generally, the main challenge in this area remains the poor administrative capacity.<sup>231</sup> Furthermore, the lack of adequate facilities, particularly regarding the central hospital and regional centres is a challenge. In addition, the public health sector also faces a

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<sup>231</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, pp. 40–41, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

lack of human capacities which are adequate to address scientific issues as mentioned above. Lastly, this sector has major deficiencies in providing relevant data on most of the sectors that it covers. The available information to public, particularly regarding the information available in the respective websites is poor and out of date.

#### **4. Implementation and Enforcement in the Area of Internal Market**

With many legislative reforms since the beginning of 2000s, public procurement system in Kosovo has almost reached a well-developed legislative basis. However, the same does not go for the implementation and enforcement of the legislation in force. The lack of awareness of economic operators in relation to contracts and procurement procedures very often leads to violation of these procedures.

For this reason, the full capacity and functionality of the Procurement Review Body, which among other powers, has the power to “review complaints from interested parties containing allegations of violations of the present law”<sup>232</sup> is crucial. It has been reported that reasoning of the decisions issued by PRB is of little quality. For this reason, and considering the importance that these decisions have on the system and the operators, it would be desirable that the capacities of the review body are well trained in this aspect. The completion of PRB with competent staff, once again is interrelated to the provision of high quality trainings from KIPA.

According to 2011 Annual Work Report of PRB, there were 386 complaints of economic operators, 30 requests for review of CPA decisions (ex-APP), and only 1% against the interpretations given by the PPRC.<sup>233</sup>

Although an issue which has come up and it needs to be addressed from the current legislation, namely the lack of differentiation in procedure between low and medium value contracts, it has been generally reported that the procurement procedures have been reduced from seven to six.<sup>234</sup>

Lastly, one of the functions of PPRC under the law is the development of electronic procurement.<sup>235</sup> The rationale behind the use of e-procurement in the EU is to improve the transparency of and access to procurement opportunities; as well as to achieve cost reduction.<sup>236</sup> For the above reasons, PPRC should accelerate the application of this system. In this regard, the data provided by PPRC maintains that Kosovo will have an available

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<sup>232</sup> Public Procurement Law, Art. 105(1)(2.1).

<sup>233</sup> Available at [http://oshp.rks-gov.net/repository/docs/raporti-final%20\(1\).pdf](http://oshp.rks-gov.net/repository/docs/raporti-final%20(1).pdf) p. 19.

<sup>234</sup> Kosovo European Partnership Action Plan 2012, [http://www.mei-ks.net/repository/docs/European\\_Partnership\\_Action\\_Plan\\_2012.pdf](http://www.mei-ks.net/repository/docs/European_Partnership_Action_Plan_2012.pdf).

<sup>235</sup> Public Procurement Law, Art. 87 (2)(2.17).

<sup>236</sup> Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: A Strategy for e-Procurement, p. 3, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2012:0179:FIN:EN:PDF>.

e-procurement system in the first quarter of 2013.

- *Company Law*

The number of registered business has steadily increased starting from the year 2000. Although, the figures are subject to constant change, the number of businesses currently registered is around 120,000. In this regard, there is an on-going debate whether this number is realistic – and how many of these businesses are actually active and operating.

The Kosovo Tax Administration has declared that during 2012 only 50,000 of businesses have declared and paid the taxes.<sup>237</sup> This is an indicator that a large number of registered businesses are not active.

The online registration process for businesses is something which remains to be implemented. The implementation is reported as underway, while the main challenges arise in connection to the technical implementation of the project.

- *Corporate Accounting and Auditing*

The supervisory powers on the implementation of the law, are a power of Kosovo Council for Financial Reporting. For this reason, the investigations unit within the secretariat of the council, according to Article 23 of the law may “... warn the person, business organization, namely the professional association that is responsible for violating the law and to take concrete measures to ensure law enforcement Implementation and enforcement. Nonetheless, there are no available reports related to the workload in the investigations powers of the council for financial reporting – particularly with regards to the monitoring and enforcement of accounting and reporting standards by publicly owned companies.

Furthermore, the competent institution remains to ensure that the full translation of the International Financial Reporting Standards (IFRS), particularly for small and medium size enterprises is conducted. While this might have already taken place, the online available data is currently lacking.

- *Intellectual and Industrial Property Law*

As it has been presented in the previous paragraphs, the legislative framework in the area of IPR is close to completion, and this goes particularly for the primary legislative framework. The following paragraphs will give a brief overview of some of the achievements in the implementation and enforcement aspect of the legislation. Nevertheless, it should be noted that the general level of implementation and enforcement still remains at an undesirable level. For instance, according to the 2011 Progress Report “...piracy

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<sup>237</sup> Kosova-vend i bizneseve fiktive (Telegrafi, 18 February 2013), <http://www.telegrafi.com/ekonomi/kosova-vend-i-bizneseve-fiktive-46-13872.html>.

is widespread and commerce of pirated material takes place in public view without sanction”.

- *Copyright and Related Rights*

As it has been defined by law, the main authorization of OCRR lies in the licensing of copyright collectives. In this regard, just recently, the OCRR has licensed two copyright collectives, namely: the Association of Audiovisual Performers and Artists, and the Association of authors, producers and interpreters. Furthermore, another responsibility of the OCRR is the awareness rising on the area of copyright and related right to the stakeholders. Thus, several campaigns have already been conducted, comprising of media campaigns, conferences, and informative brochures.

On a different note, the copyright law provides for mediation as a dispute resolution mechanism in this area. It has been said that the OCRR provides for a list of mediators to interested parties. However, there are no data as to the level of use of mediation services by the parties. The implementation of provisions on mediation would help out the parties, and avoid court proceedings, which are usually very lengthy. If under usage of mediation is the issue, than it could potentially be related to the lack of public awareness of such dispute resolution mechanism.

The OCRR has worked towards the formalization of cooperation with non-institutional stakeholders, such as the Independent Media Commission, music producers, video production companies, writers, photographers, and publishing houses. The importance of continuously targeting these groups finds basis on the fact that these are the actual target groups on the awareness rising component of OCRR.

- *Industrial Property Rights*

The Intellectual Property Office at the Ministry of Trade and Industry has most of the responsibilities in the area of industrial property rights. Thus, the latter has used its capacities in three different directions, namely: cooperation with other institutions, accepting applications, maintaining a register, and providing information to stakeholders.

In terms of cooperation, there are three Memorandums of Understanding signed with countries in the region: Croatia, Macedonia, and Albania – as partner institutions. The figures provided in the Progress Report 2010 stipulate that: “1,480 decisions on trademarks and 147 on patents were taken. In 2010, the Industrial Property Office received 550 applications on trademarks, 85 on patents and 4 on industrial designs. The backlog of applications remains very high, with 17,000 trademarks 4,000 designs and 500 patents outstanding”. With these figures in mind, the lack of adequate human capacities strikes out as a challenge once again. Hence, in order to build up the capacity, the employment of new and qualified people is one of the essential measures to conduct.

One of the achievements which is reported is the establishment of a Trademark Database. However, there are no reports as to whether this database is operational yet.

- *Other enforcement aspects*

The Customs play a very important role in identifying and stopping goods suspected to infringe upon intellectual property rights at the border. The Kosova Customs, with the functionalization of the Department of Intellectual Property and completion of legal framework has, from 2010 to the present, undertaken a series of actions to combat forgery and piracy. In total, Kosova Customs have discovered 107 cases of goods suspected to infringe upon intellectual property rights and have acted *ex-officio* in 12 cases and upon requests for actions in 95 cases.

Many of these operations were carried out upon requests for customs supervision filed by importers of genuine goods. This indicates that the level of implementation also depends on cooperation between parties involved and respective governmental institutions. Figures presented in the SAA preliminary study (22 applications for 129 trademarks) indicate that the awareness of parties involved about the possibility of reporting potential breaches is increasing gradually.

The Kosovo Customs have during 2010 – 2012 stopped goods infringing upon intellectual rights at an amount of 51, 8168 units. Alcoholic beverages (48%) and shoe polishes (36%) have the largest share among the stopped goods. According to Customs stats, main places of origin of goods that constitute breaches of intellectual rights are China (79%) and Turkey (21%).

With the aim of raising public and business community awareness about customs measures to combat forgery more effectively and protect the public from threats to health and security, the Kosovo Customs have prepared brochures and manuals and organized media campaigns and conferences.

The enforcement of IPR has to be divided in three different areas. Quite importantly, Kosovo Customs have conducted operations for destruction of counterfeited goods. The first action to even take place was in March, 2011. A number of other operations followed, and all of these goods were counterfeited goods of famous trademarks (e.g. Nike, Gant, Lacoste, Prada, Timberland, Levi's, Puma, etc). Many of these operations were reportedly conducted after the application for customs surveillance which was done by the importers of genuine goods. This clearly indicates that the level of enforcement is also subject to cooperation of non-institutional stakeholders with the institutions in charge. The figures shown in the Feasibility Study for SAA – 22 applications for 129 trademarks, are indicative that the awareness of interested parties in reporting possible violations is slowly rising.

On a different note, the statistics provided by the Kosovo Police on the violation of the IPR show visible discrepancies between the actual situation and the figures. For instance, the number of criminal charges for the period January – March of 2012 is three. The latter might be taken as a general indication that not many cases are usually under investigation. Also, the low number of investigations by the police might be attributed to the lack of the specialized unit which can deal with IPR. The latter would also be

comprised of police officers who would be competent to handle these investigations, therefore recognise infringements as well.

The judiciary is also of major importance for the protection of intellectual property rights. Generally, it has been considered that IPR specialization of judges and prosecutors is not adequate. However, regardless of the above, the former Commercial Court has handled some cases of IPR infringement. The figures provide that between January 2008 and March 2012, a total number of cases results in seventeen (17).

Lastly, one major element which is currently missing in Kosovo is a solid track record on investigation, prosecution and adjudication of IPR-related cases. The issues of old track records, as well as missing track records are evident. While this is also attributed to the not yet completely established institutional framework, its existence is crucial in assessing the state of affairs.

- *Competition Policy*
- *State Influence on Competitiveness*

In general, according to the figures provided by the Ministry of Finance, between 2007 and 2011 the public owned companies which are subsidized by the government include Kosovo Energy Corporation, imports of energy, Kosovo Railways, Central Heating, Water and Waste, and Trepça mines.

One of the areas which the government systematically subsidized is the energy sector. In this regard, the figures of 2011 show that a percentage of 1,5 of the GPD has been committed as an aid to the Kosovo Energy Corporation. Furthermore, the electricity imports have also been conducted through substantial subsidies by the government. To date, the quality of products offered by the state owned Energy Corporation remains weak, with the energy prices remaining high, consequently facing constant lack of consumer satisfaction.

However, regardless of the above, the level of influence is gradually decreasing, as the figures show. In 2008 the level of government expenditure to this area was 5%, while as previously mentioned, in 2011 it was 1.5%. Also, quite importantly, the intention of Furthermore reduction of these subsidies is also embodied within the Government of Republic of Kosovo Program 2011-2014.

In terms of price setting the Feasibility Study for SAA maintains that: "The price-setting mechanism in Kosovo is mostly free, with independent regulatory bodies regulating the prices of electricity, district heating, water, solid waste, postal services and some telecommunication services. Current governance arrangements as regards publicly owned enterprises ensure that government does not directly interfere in the price setting mechanism of their services.

- *Antitrust and Mergers*

The banking sector is one of the areas of competition, whereas over time, major concerns have been raised. However, according to the last report of national institutions to the European Commission, the competition in the banking sector is constantly increasing. While prior to 2010 the monitoring of the banking sector raised concerns on the level of concentration, the concentration level is continuously dropping.

The 2011 six month Analysis of Monitoring in the Banking Sector in Kosovo by the Competition Authority stated that “the banking system in Kosovo continues to be characterized by a high level of market concentration, where 77.4 percent of the total bank assets are managed by the three largest banks”. In this regard, it was also assessed that none of the operating banks hold a dominant position in the market, while the activity increase of smaller banks resulted in decrease of concentration level. Furthermore, the increased competition has been proved on different levels, such as: the different interest rates, point of sale terminals, different packages and offers etc.<sup>238</sup>

The insurance sector has also been reported as continually developing, with currently ten companies offering non-life insurance, and three companies offering life insurance. According to 2011 annual report of the Central Bank of Kosovo, third party liability insurance generates most of the premiums. Over time, some concerns have been raised in relation to the market operators in life insurance, considering the current number of only three operators. However, the latter seems to be a result of the low demand for life insurance. Consequently, the life insurance market during 2011 has comprised only a 1.39% of total gross written premiums.<sup>239</sup>

The Competition Authority has conducted investigations in several sectors, as per their competencies given by the law. The first decision reached by this body on collusive behaviour, and creation of monopoly was conducted in the sale of fiscal cash registers. Considering that this case had been handled in accordance with the old law, the fine that was issued reached the maximum of the old law, thus, 100.000 Euros fine.

Another decision reached by the KCA is on the agreement on price fixing of fuel derivatives of thirteen different sale points in one municipality. The decision of the KCA ordered the annulment of the decision on price fixing. The investigation proceedings in this particular case showed also the lack of awareness of the economic operators on competition rules – while the participants to this prohibited agreement were not aware that the agreement was a hardcore violation of competition law.

According to the Feasibility Study for SAA, the KCA has conducted 32 cases on the different prohibition of the competition law. However, there are only two published decisions available at the official KCA web site. With this in mind, as well as the general lack

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<sup>238</sup> See the 2011 Analysis of Monitoring in the Banking Sector in Kosovo, [http://ak.rks-gov.net/repository/docs/Analysis\\_of\\_Monitoring\\_BSK\\_311011.pdf](http://ak.rks-gov.net/repository/docs/Analysis_of_Monitoring_BSK_311011.pdf).

<sup>239</sup> Ibid.

of reports on this area, make it rather difficult to give a detailed overview of the work conducted by the competition authority. Thus, importance should be given to the latter, through strengthening the transparency of the activities conducted by the Competition Authority (unless trade secret provisions prohibit this).

The KCA should use its current capacities to continuously monitor and investigate economically important areas.

There is no current available data whether any requests for mergers have been deposited at the KCA.

- *State Aid*

Considering that this area has been supplied just recently with specific legislation, as well as that the competent bodies have not been established yet, the end result consists of lack of developments on the enforcement and implementation of the state aid law.

All prior subsidies for the public owned companies have been given on the basis of the budgetary plans (see discussion above on state influence).

- *Liberalisation*

No major progress has been reported in the area of liberalisation. Concerning the area of telecommunication, it has been reported that the authority in charge of this area has imposed a five-year suspension of issuing licenses for new mobile phone operators.<sup>240</sup> This policy has been decided imposed by then Telecommunications Regulatory Authority, pursuant to the Government Decision No. 6/124, dated 13 May 2010, which stipulates that the TRA should not issue license to the third mobile telephony operator in Kosovo for the next five years. That decision ran counter to rules of competition, especially given that provision of protection to an existing company in the market damages the customers, as it reduces competition and prevents decrease in prices. This policy, which was restricting free market competition, remained in force until 2011, when the new Law No. 04/L-109 on Electronic Communications was adopted, which abolished the license regime and introduced the regime of general authorizations for provision of electronic communications services and networks in Kosovo.

Generally, as previously discussed, a number of undertakings continue to enjoy, exclusive rights, in the energy sector, transport, postal services, telecommunication services, and media broadcasting. Therefore, additional efforts need to be made towards market liberalisation in line with the EU legislation.

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<sup>240</sup> Bertelsmann Stiftung's Transformation Index (BTI) 2012: Kosovo Country Report, p. 18, <http://www.bti-project.de/fileadmin/Inhalte/reports/2012/pdf/BTI%202012%20Kosovo.pdf>

- *Consumer and Health Protection*
- *Consumer Protection*

According to the Ministry of Trade and Industry the 2012 Annual Report the number of consumer complaints has increased by 70 – 80%, in comparison to 2011.<sup>241</sup> This is a good indicator that the Consumer Protection Department has achieved to inform the consumers on their right to complain upon purchase of products and services. The latter is also a result of a rather intensive awareness rising campaign. Again, according to the MTI Annual Report, this Department has conducted activities which have included media campaigns, roundtables, open discussions with universities, and constant spread of informative brochures. The easy accessibility of consumer to depositing or filing complaints has also been done through the availability of the free-of-charge mobile and landline phone number.

However, although the number of deposited complaints has risen, the challenge still remains as to the capacities of collecting and processing these complaints, and this is directly related to the administrative capacities of the Consumer Protection Department.<sup>242</sup>

The implementation of the programme for consumer protection has moved forward another step, with the opening of the first advisory centre in Prishtina, which is created with the aim of offering and providing free information and advice in different consumer areas, such as food safety and public services.

Furthermore, the responsibility of the Department for Consumer Protection to support other organizations which concerns three target groups: 1) government institutions involved in consumer protection, 2) nongovernmental organizations, and 3) regional organizations has somewhat developed. These institutions include: the Market Inspectorate of MTI, Sanitary Inspectorate of Veterinary Agency, Veterinary and Phytosanitary Inspectorate, National Public Health Institute, Environmental Protection Agency, Customs, courts and ADR institutions, Kosovo Association for Consumer Protection, civil society, chambers of commerce, and regional organizations in Albania, Macedonia, Croatia, and Montenegro.

With regards to the above, the inter-institutional cooperation needs to be enhanced. The latter goes particularly to the cooperation with the market inspectorate and the customs. For instance, the practice shows that the food safety is one of the major issues and subject to numerous complaints by consumers. Thus, in general, a lot remains to be done in order to fully implement the current programme and the proper enforcement of legislation.

<sup>241</sup> 2012 Annual Report of the Ministry of Trade and Industry, p. 13, [http://www.mti-ks.org/repository/docs/MTI\\_Raport\\_Progresi\\_2012\\_Dhjetor\\_103727.pdf](http://www.mti-ks.org/repository/docs/MTI_Raport_Progresi_2012_Dhjetor_103727.pdf)

<sup>242</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, pp. 28–29, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

- *Health Protection*

According to the EU assessment documents on Kosovo, the area of public health is an area where limited progress has been made, in general, and in which great challenges remain to be addressed.

The enforcement of the Tobacco Law has faced difficulties, therefore its implementation is still considered weak. The results of inspections bring about the ineffectiveness of the law provisions which divide smoking and non-smoking area in 30%/70%. However, the intention to make the provisions of the tobacco law stricter, towards full ban of smoking in public areas, might result as more effective. Another element which can be helpful in enforcing these provisions is the heavier sanctions and measure against the persons violating the law: the draft-law on tobacco control has foreseen fixed fines and increase of the number of oversight and execution bodies, including the Kosovo Police and the Anti-Corruption Agency.

In terms of achievements in the area of communicable diseases, the good news is that the immunization of the population is reported to have reached the rate of 95%. The National Centre for Blood Transfusion has also achieved some progress, with blood collection figures in 2012 increasing to 13%. Although the blood transfusion is voluntary, the level of awareness among the population seems to have risen.

In terms of reliable data, the NPHI could undertake a study on the level of consumption of tobacco in Kosovo. Such a study has not been conducted since 2005. Major challenges are faced in the area of organ transplanting. With the currently lacking legislation, the adequate infrastructure, and competent professionals remain a challenge. It also reported that the Ministry of Health does not possess a registry of the number of citizens in need for transplants.

- *Summary of key Challenges Identified in the Area of Internal Market*

This chapter provides an overview of the major developments in all the areas falling under the sector of internal market in Kosovo. It starts off by discussing and analysing the legislative framework and identifying some of the main shortcomings. Then, a brief overview of the policy framework applying in this sector is provided. Lastly, it presents an overview of the institutional framework and its functionality. It also tackles implementation and enforcement. Taking into consideration the above, the following provides a summarized outline of the main challenges identified in each area of internal market.

#### Free Movement of Goods

- The legislative basis, i.e. the completion and harmonization of national legislation with EU legislation. The adoption of new approach directives and European standards remains a challenge. A complete legal framework in the area of market surveillance should be considered with priority for the reason that it en-

ables the Market Inspectorate to closely monitor the products on whether they meet the requirements of public health or public safety. Another aspect which is tied to the modernization of the legislative framework is the institutional capacities which should be able to implement the legal framework as well as to follow the developments in this area.

- Furthermore, one of the major challenges put forward by a number of reports, the EU Progress Reports in particular; remain the lack of human, administrative, and technical capacities. The latter reflects directly in the low level of awareness towards the importance of the adoption of new European standards, which would help market functioning; promote competitive products; and it would help in the protection of the health and safety of consumers. In terms of technical capacities, the number of conformity assessment bodies and the functionality of metrology laboratories remains a challenge.
- As far as the international cooperation area is concerned, the membership in international organizations of the agency of standardization and metrology department remain a challenge, and are of crucial importance, i.e. the membership in ISO, CEN, and CENELEX.
- In general terms, the institutional structure within MTI has posed some challenges, and its restructuring as per the decision of the Government should be completed.
- In terms of policy making, the implementation of the existing strategic documents remains a challenge. Furthermore, the sectors which still lack policy documents should be prioritized for development by MTI.

### Free Movement of Workers

- In terms of the legal framework, a challenge is completion and harmonization of national legislation with EU legislation, particularly the harmonization of legislation regarding equal treatment of EU workers established in the territory of Kosovo, and the rights of their family members. In addition to this, the legal framework on the limited coordination of social security systems should be drafted and completed, in compliance with EU *acquis* as much as possible, by taking into consideration the domestic developments on social security.
- In terms of institutional capacities, one of the major challenges remains the lack of human, administrative, and technical capacities, which would be capable of implementing the legal framework in the area of free movement for worker and limited coordination of social security systems.
- In terms of international cooperation on the coordination of social security schemes, the lack of bilateral agreements poses a challenge, particularly agreements which could be reached with the EU member states.

## Right to Establishment and Freedom to Provide Cross-border Services

- The legislative framework setting, i.e. the completion and harmonization of national legislation with EU legislation, particularly the harmonization of legislation regarding the right to establishment of companies, establishment of self-employed persons, the freedom to provide services, and recognition of professional qualifications. EU companies and self-employed persons should be guaranteed the right to establishment and to provision of services.
- Then, one of the major challenges remains the lack of human, administrative, and technical capacities, which would be capable of implementing the legal framework in this area.
- In terms of international cooperation, bilateral agreements in the area of mutual recognition of professional qualifications should be accomplished.
- One of the major issues is the lack of availability of data in the area of provision of services, which includes a two-tier system: firstly, the existence of a database with the outline of all legislative acts which form part of the area of services, and secondly, the constant availability of to-date figures on the provision of services in Kosovo.

## Free Movement of Capital

- The main challenge in the area of capital movement and payment system remains the legislative setting, i.e. the completion and harmonization of national primary and secondary legislation with EU legislation. An assessment of the existing legislation would help to identify and abolish any possible discriminatory measures.
- On an international level, the Kosovo's SWIFT code is still a major challenge.

## Public Procurement

- The legislative framework, its completion and harmonization with EU legislation is still one of the major challenges in the area of public procurement. Furthermore, this issue needs to be prioritized considering the nature of public procurement.
- To date the implementation of the general principles embraced within the law by the procurement officers, and the institutions in charge in general remains a concern. In this regards, the Code of Ethics should be ensured full implementation.
- One of the challenges remains the implementation of the e-procurement system.
- In terms of institutional framework, the organizational structure and the lack of clear definition of competences remains a challenge.

- The administrative capacities and their training is still a concern. In specific, the quality of the decisions of the Procurement Review Body is questionable.

## Company Law

- The legislative basis, i.e. the complete compliance of national legislation with EU legislation. In specific, the law on business organization should consider detailed rules on cross-border mergers, and protection of small shareholder voting rights. Furthermore, drafting and adopting subsidiary legislation in the area of company law is necessary. In relation to this, the Corporate Governance Code should also be considered for adoption. On the other hand, the harmonization of current legislation in accounting and auditing is also a pressing issue. To date, there is a lack of subsidiary legislation in this area.
- Furthermore, one of the major challenges put forward by a several reports, remains the competent human, administrative, and technical capacities available. The staff of KBRA should be subject to constant education and training, particularly regarding the legal developments. On the other hand, the KCFR should be ensured full functionality.
- In terms of policy making, the implementation of the existing strategic documents remains to be completed. There is a lack of a sector specific policy document on the area of company law, and to date, company law has been regarded mainly from the viewpoint of the functionality of business registry.
- In general terms, the availability of reports related to the workload of KCFR should be ensured. Furthermore, the translation of the International Financial Reporting Standards (IFRS) is also necessary.
- Intellectual and Industrial Property Law
- The legislative basis – although this is an area which has reached considerable achievement in its compliance with *acquis*, the following of latest development in this area is a necessity. With one framework law missing, the adoption of the Law on Geographical Indications would complete the primary legislative framework. Furthermore, drafting and adopting subsidiary legislation in the area of IPR is necessary.
- Furthermore, one of the major challenges put forward by a several reports, remains the competent human, administrative, and technical capacities available. The latter goes particularly for the lack of staff in the Intellectual Property Office. The IPO should employ staff qualified in intellectual property law.
- In terms of policy making, the implementation of the existing strategic documents remains to be completed. There are two main elements which should be given priority, namely the awareness rising of the public and stakeholders on IPR, and the implementation of the anti counterfeit strategy.
- The implementation of the policy framework is directly related to the inter-institutional cooperation. Thus, priority should be given to the cooperation be-

tween the triangle of OCRR/IPO, Customs, and the Market inspectorate.

## Competition Policy

- The legislative basis, i.e. a formal assessment needs to be conducted regarding the level of compliance of other laws which regulate issues related to protection of competition with the Law on Protection of Competition. Furthermore, the law itself needs to be amended in order to determine the dominant market position. On the other hand, one of the necessities remains the completion of the state aid legislation with subsidiary legislation. Lastly, a currently missing comprehensive state aid inventory on existing and future aid scheme should be established.
- In terms of institutional capacities, one of the major challenges remains the lack of human capacities functioning within the Kosovo Competition Authority. Thus, there is currently lack of staff and lack of qualifications to undertake all the responsibilities which have been given to KCA by the law. The current capacities should be used to constantly monitor the economic areas which might be problematic. On the other hand, the establishment of the state aid institutional structure is of major importance.
- The KCA should consider the increasing of activities in advocacy and awareness rising. The latter can also be done with the help of a Leniency Programme which should be considered for establishment within KCA.
- In terms of policy making, the drafting of a sectoral strategy might be needed. Furthermore, the implementation of the existing strategic documents remains to be conducted.
- In general terms, the data provided in the official website of the Kosovo Competition Authority is old. For instance, there is no available data whether any requests for mergers have been deposited at the KCA; and there are only two published decisions available. Thus, the lack of public information imposes a challenge to have a specific overview of what has been done in this area.
- In terms of market liberalisation, additional efforts need to be made in line with the EU legislation.

## Consumer and Health Protection

- The legal basis remains a challenge, both in the area of consumer protection and that of public health. The current law on Consumer Protection should be fully harmonized with the EU legislation. Moreover, given that the area of consumer protection includes a number of other laws, it is important that laws are not in conflict with each other, thus conflicting provisions should be avoided (for example, by clarifying the mechanisms for resolving disputes outside the courts in the Law on Consumer Protection). On the other hand, the legal framework in the area of public health and its completion is necessary. For example, amendment

of the Law on Tobacco is foreseen, which could potentially improve the current level of law enforcement. Moreover, the legislative component that needs to be addressed urgently is that in the area of blood tissue and organ transplantation.

- In terms of the strategic framework, the two areas (consumer protection and public health) remain behind in terms of implementation of the existing strategies. Inter-institutional cooperation between the Consumer Protection Department, Market Inspectorate and Customs should be increased.
- In terms of the institutional framework, lack of adequate funding and lack of human capacities have been persistent challenges to the relevant authorities in the area of consumer protection. The same challenges are faced by the institutions in the area of public health, particularly hospitals, which still face lack of facilities.
- Lastly, the area of public health faces major shortcomings in providing relevant data in most sectors it covers. Information available to the public, particularly with regard to the information available on respective web-pages, is weak and is not updated.

## Chapter V: Customs and Taxation

### 1. Customs

An effective customs administration is essential to smooth trade and business development, as well as creating an environment that will attract and secure foreign investment.

Kosovo Customs is one of the two main government bodies in Kosovo in charge of collection of taxes. The tax system in Kosovo, founded over the last decade, is relatively young. It was established in August 1999, under Pillar IV of the United Nations Interim Mission in Kosovo, with the responsibility of ensuring application of fair and uniform customs regulations and other provisions applicable to goods that are subject to customs control. Following the Declaration of Independence and entry into force of the Constitution of the Republic of Kosovo, the formerly UNMIK Customs Service was transformed to Kosovo Customs, in December 2008.

Unlike in many countries in the region, the customs system in Kosovo is considered to be streamlined and simple. Since its establishment, this system has been going through numerous changes and modifications aimed at aligning it with the EU *acquis* and European standards. To this end, the area of customs in Kosovo was also supported by donors, in terms of development of legislation, policies and capacity-building, with a view to development of the whole customs system into a modern revenue collection administration.

However, there is still work to be done to tackle some of remaining issues of rather strategic significance: development of essential IT systems, alignment of revenue payment procedures used by the banks and the customs authorities, as well as development and utilization of efficient taxpayer registration and risk management systems.

#### 1.1. Legal and Policy Framework in the Area of Customs

##### 1.1.1. Domestic Legal Framework on Customs

This section provides an overview of the legal framework relevant for the area of customs in Kosovo, mainly the Kosovo Customs and Excise Code and the Law on Excise Tax. Other laws applicable to this area that are covered by this paper include those on integrated management and control of the state border, customs measures for the protection of intellectual property rights, and value-added tax.

The *Customs and Excise Code of Kosovo No. 03/L-109*, adopted by the Assembly of Kosovo in November 2008, regulates basic elements of the system for customs protection of the economy of Kosovo, as well as the rights and obligations of all operators in applying customs legislation.<sup>243</sup> The Customs Code was drafted with the technical assistance

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<sup>243</sup> Customs and Excise Code of Kosovo, Article 2, [http://www.assembly-kosova.org/common/docs/ligjet/2008\\_03-L-109\\_en.pdf](http://www.assembly-kosova.org/common/docs/ligjet/2008_03-L-109_en.pdf).

of international customs consultants and was based on the EU Customs Code of 1992. This has been an advantage for Kosovo Customs due to the fact that the framework of laws and regulations has been in line with EU standards right from the beginning, and is now fundamental for closer association with EU. Nonetheless, as is discussed below, there are a number of other improvements that are necessary to be undertaken in order to update and improve the current legal framework.

In the context of current international trade, modernization of customs legislation is a necessity and demand for many countries in order to reduce constraints and non-tariff barriers on trading of goods across borders. The latest and most up-to-date, the EU Customs Code of May 2008, sets out the model legal framework for countries which are either members or aspire to be members of the European Union. However, it should also be stressed that it is essential for the Customs Code of Kosovo to reflect the standards and practices for customs administration that are specified in the EU Customs Blueprint (of May 2008) titled "Pathways to modern customs". In this regard, the Customs Code of Kosovo has reflected over 70% achievement. However, more has to be done, notably in matters related to further modernization of customs control, the application of information and communications technology (ICT), trade facilitation and the establishment of trade administration which supports economic development in Kosovo.<sup>244</sup>

Application of the procedures authorized by modern customs legislation – maximum use of information technology; risk management, post-clearance audits of traders, financial guarantees, and special simplified treatment for authorized traders – can have a major economic impact on the economy of Kosovo. Currently, Customs collects about 63% of all government revenue. The full incorporation and implementation of the above-mentioned modern procedures should substantially improve revenue collection.

Kosovo's customs legislation is largely in line with the EU Customs Code. However, one major challenge of implementation of the Customs Code is Article 10 and 11. Under these provisions, any person may appoint a representative in his dealings with the Customs to perform the acts and formalities laid down by customs legislation. Representation within the meaning of Article 10 may be carried only by a legal person registered as representative by the Customs. A representative must be holder of a license issued by the Customs. Currently the *spediteur* industry in Kosovo is not regulated and there are no procedures in place for licensing of customs agents.

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<sup>244</sup> "Customs blueprints are practical guidelines laying down clear criteria based on EU best practice, against which a customs administration is able to measure its own operational capacity. They can be used to analyse gaps between the existing situation in individual countries and the blueprint standards and thus provide a basis for plans to undertake customs reforms. They can also help to ensure that any assistance requested or provided is structured, consistent and properly targeted, with clear objectives and measurable results." – from the Foreword to the EC's Customs Blueprints, *Pathways to Modern Customs*, pp. 5–6, [http://ec.europa.eu/taxation\\_customs/resources/documents/common/publications/info\\_docs/customs/customs\\_blueprint\\_en.pdf](http://ec.europa.eu/taxation_customs/resources/documents/common/publications/info_docs/customs/customs_blueprint_en.pdf).

In addition, The World Customs Organization provides the standards and procedures that should be invoked to assign the status of “Authorized Economic Operator” (AEO) to an importer or exporter. An AEO is determined by the customs administration to be a low-risk or no-risk entity for the administration customs procedures on the basis of a comprehensive risk assessment. An AEO may not be subject to compliance verification at the time of export or import, as the case may be, and consequently shipments by an AEO can be treated through simplified clearance procedures. Amendments to the Customs Code were passed last year, yet no bylaws regulating AEO have been adopted yet by Kosovo Customs.

The *Law on Excise Tax*, amended in 2008 and 2009, provides a list of goods subject to excise tax. The goods subject to excise taxes include: coffee, wine, cigarettes, and other tobacco products, oils, fruit juice and other drink concentrates, cars and other motor-operated vehicles. Fixed amounts are provided for certain goods.

Kosovo Customs during 2011 has raised the activity in the area with the aim of collecting revenues from excise taxes. During 2011, the implementation of Kosovo Government decision no. 03/13 has commenced for the excise tax on gambling, that after additional arrangements has collected over 6 million euro revenue from this area while before there were no collections. During year 2011 there were 11 new companies licensed for the import of tobacco products.<sup>245</sup> Under this law, there may exemptions from excise tax, for manufacturing, heating and raw materials, upon prior approval of Kosovo Customs, pursuant to and for the purposes stipulated in Article 236 of the Customs and Excise Code of Kosovo, also applying to specific rates for goods produced in Kosovo.

The *Law No. 03/L-065, on Integrated Management and Control of the State Border*<sup>246</sup>, adopted by the Assembly of Kosovo in May 2008, sets out responsibilities of the competent authorities regarding the integrated management and control of the state border. It is applied without prejudice to the specific mandate of international organisations on the ground, as provided for in the Constitution of the Republic of Kosovo. Interagency co-operation is to be carried out by the Border Police, Kosovo Customs and phyto-sanitary and veterinary services, as defined in the National Strategy for Integrated Border Management. Provisions in this Law will apply to all persons entering or leaving Kosovo except those who are claiming or might reasonably be expected to claim asylum. In such cases the Law on Asylum will apply. Implementation of Integrated Border Management is especially difficult in northern Kosovo, due to the political nature of relations with Serbia. Because of strained relations between the countries, exchange of data information and joint border control may be a potential issue.

The *Law No. 03/L-170, on Customs Measures for Protection of Intellectual Property*

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<sup>245</sup> 2011 Annual Report, Kosovo Customs, p. 15, <http://dogana.rks-gov.net/Uploads/Documents/Raport%20vjetor%202011%20%20FINAL%20ANGLISHT.pdf>.

<sup>246</sup> Law on Integrated Management and Control of the State Border, [http://www.assembly-kosova.org/common/docs/ligjet/2008\\_03-L065\\_en.pdf](http://www.assembly-kosova.org/common/docs/ligjet/2008_03-L065_en.pdf).

*Rights*<sup>247</sup>, adopted by the Assembly of Kosovo in December 2009, provides for the procedures for action by the Customs when goods suspected of infringing intellectual property rights are in the following situations:

- Declared for release for free circulation, export or re-export according to the provisions of Customs and Excise Code;
- Found during the goods control being entered in or leaving the Customs Territory of the Republic of Kosovo;
- Placed under a transit procedure, Customs warehouse procedures, inward-processing procedures, processing under Customs control and temporary import; or
- Placed in a free zone and free warehouse, in accordance with provisions of Customs and Excise Code.

Kosovo Customs has made efforts to enforce IPR: goods have been seized (and in some cases destroyed) and significant fines were imposed. In general, counterfeit products and piracy remain issues of concern in Kosovo. Punitive measures against industrial property rights infringements still need to be clarified. Destruction procedures for goods harmful to public health are not fully defined. They cannot be put into practice because of gaps in the legislative framework as well as inadequate administrative capacity, including adequate facilities to destroy dangerous goods. Piracy is widespread and commerce of pirated material takes place in public view without sanction. Kosovo needs to carry out a rigorous assessment of the scale of the challenge in order to design the most appropriate tools and put in place the necessary institutional framework to fight piracy.<sup>248</sup>

The *Law No. 03/L- 146, on Value Added Tax*<sup>249</sup>, adopted by the Assembly of Kosovo in December 2009, establishes the system of Value Added Tax (VAT) in the territory of the Republic of Kosovo. VAT includes application of overall tax in consumption for goods and services that is exactly proportional with the cost of goods and services. VAT is calculated in this cost according to the applicable norm, it is loaded in different phases of the production, delivery and living cycle of the trade with goods and services, and in the end it is carried forward from the last consumer. VAT is charged in accordance with the provisions of the present Law, on:

- Supply of goods and services made for consideration within the territory of Kosovo by a taxable person as meant by Article 4 of this Law and acting as such, and the importation of goods in Kosovo;
- VAT on importation shall be charged and payable in accordance with the arrangements for Customs duties.

Furthermore, according to EU's assessment, the informal sector in Kosovo is fuelled by

<sup>247</sup> Law on Customs Measures for Protection of Intellectual Property Rights, <http://www.assembly-kosova.org/common/docs/ligjet/2009-170-eng.pdf>.

<sup>248</sup> Kosovo 2011 Progress Report, pp. 38-39, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2011/package/ks\\_rapport\\_2011\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2011/package/ks_rapport_2011_en.pdf).

<sup>249</sup> Law on Value Added Tax, <http://www.assembly-kosova.org/common/docs/ligjet/2009-146-eng.pdf>.

weaknesses in tax and expenditure policies and, in law enforcement, including the fight against corruption and organized crime. It reduces the tax base and the efficiency of economic policies. As a measure to combat the informal economy, the Kosovo tax administration continued to issue fiscal numbers and to install fiscal cash registers. However, these registers are still not systematically used.<sup>250</sup>

The *Law No.04/L-048, on External Trade*<sup>251</sup>, adopted by the Assembly of Kosovo in November 2011, defines the general rules for the exercise of external trade between persons settled within and out of the territory of Kosovo in compliance with the best International practices. Activities of external trade in Kosovo may be carried out by natural and legal persons, while trade for commercial purposes may be carried out only by persons registered for carrying out the economic activity in Kosovo.

### 1.1.2. Overview of the EU Acquis Applicable in the Area of Customs

Under the framework of EU integration, the area of customs is regulated by a number of primary and secondary EU *acquis* acts. This legislation consists of two broad categories: principles enshrined in the treaties and specific provisions contained in the rest of EU *Acquis* acts issued by EU Institutions, the latter subdivided into two categories: (1) regulations, directives and decisions (legally binding instruments), and (2) recommendations and opinions (legally non-binding).

As far as *principles enshrined in the Treaty on the Functioning of the European Union* (*Lisbon Treaty*) are concerned, it stipulates that the Union shall have exclusive competence in the area of customs union.<sup>252</sup> The treaty defines the scope of the Customs Union as covering all trade in goods and involving the prohibition between Member States of customs duties on imports and exports and of all charges having equivalent effect, and the adoption of a common customs tariff in their relations with third countries.

The area of customs union in the EU is regulated based on the following four underlying principles:

- The need to promote trade between Member States and third countries;
- Developments in conditions of competition within the Union, with a view to improving competitive capacity of undertakings;
- The requirements of the Union as regards the supply of raw materials and semi-finished goods, with the Commission in charge of avoiding distorting conditions of competition between Member States in respect of finished goods; and

<sup>250</sup> Kosovo 2011 Progress Report, p. 31, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2011/package/ks\\_rapport\\_2011\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2011/package/ks_rapport_2011_en.pdf).

<sup>251</sup> Law on External Trade, <http://www.assembly-kosova.org/common/docs/ligjet/Law%20on%20external%20trade.pdf>.

<sup>252</sup> Treaty on European Union and the Treaty on the Functioning of the European Union, Article 3.1., <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2010:083:FULL:EN:PDF>.

- The need to avoid serious disturbances in Member States' economies and to ensure rational development of production and expansion of consumption within the Union.<sup>253</sup>

In relation to products entering the EU market from third countries, they are considered to be in free circulation within this market after import formalities are complied with and customs duties or charges of an equivalent effect are levied by Customs authorities of the Member State bordering EU's external border. Article 30 prohibits Customs duties on imports and exports and charges having equivalent effect between Member States, including customs duties of a fiscal nature, while Article 31 stipulates that Common Customs Tariff duties are fixed by the Council, on a proposal from the Commission.<sup>254</sup> Lastly, with regard to customs cooperation, the Treaty stipulates that "Within the scope of application of the Treaties, the European Parliament and the Council, acting in accordance with the ordinary legislative procedure, shall take measures in order to strengthen customs cooperation between Member States and between the latter and the Commission."<sup>255</sup>

At the level of specific provisions, based on the structure of *acquis* chapters, the area of customs is covered by Chapter 29, on *Customs Union* (see Annex 1 for a list of acts applying in the area of customs).<sup>256</sup> It consists of 1,027 acts in total, divided into the following nine categories:

- General (10 acts);
- Statistics (218 acts);
- General customs rules (18 acts);
- Basic customs instruments (286 acts);
- Application of the Common Customs Tariff (388 acts)
- Specific customs rules (63 acts);
- Mutual assistance (6 acts);
- Proceedings and penalties (8 acts); and
- International customs cooperation (30 acts).<sup>257</sup>

### 1.1.3. Policy Framework Relevant for the Area of Customs

This section provides an overview of the policy framework relevant for the area of customs, mainly focusing on the Kosovo Customs Operational Plan. Other policy documents relevant for this area that are also analyzed here include the Action Plan of the Economic Vision of Kosovo 2011 – 2014, and Kosovo's Trade Policy.

<sup>253</sup> Ibid, Article 32.

<sup>254</sup> Ibid, Articles 28–31.

<sup>255</sup> Ibid, Article 33.

<sup>256</sup> Chapters of the *acquis*, [http://ec.europa.eu/enlargement/policy/conditions-membership/chapters-of-the-acquis/index\\_en.htm](http://ec.europa.eu/enlargement/policy/conditions-membership/chapters-of-the-acquis/index_en.htm).

<sup>257</sup> EUR-Lex: Customs Union and free movement of goods, <http://eur-lex.europa.eu/en/consleg/latest/chap02.htm>.

The Kosovo Customs *Strategic Operation Framework 2012 – 2014*, adopted in 2012, is the strategic operation framework for the Kosovo Customs. It indicates what this law-enforcement agency is mandated to provide for towards investing the public contribution from Kosovo budget, and also defines the purposes and objectives that are realized through operative units, respectively Customs Directorates. This is a repetitive plan which covers a three-year, midterm period, covered by the Mid-Term Expenditure Framework, and is updated annually in terms of budgetary expenses and revenue collection planning.

Objectives of the action plan are the following:

- Objective 1: Collection of due revenues in due time from VAT in importation, excise and customs duties. Actual projects of Ministry of Finances regarding the approved revenues as part of KB for the year 2012 are €867 million.
- Objective 2: Promotion of communication and national cooperation with business community in Kosovo, governmental and international services with other Customs administrations in the region and broader by aspiring the permanent membership in the World Customs Organization.
- Objective 3: Development of capacities within the service in order to advance integrity, development of resources, policies, legal framework, in achieving more transparency and using best practices also in implementation of the EU Customs Blueprint and achieving the standards aimed for by this document.
- Objective 4: Use of powers and procedures of Customs and Excise Code for better effect in enhancing compliance and to facilitate the economic activities in cooperation with traders. To achieve adequate equilibration amongst trade facilities and controlling, by using techniques that utilizes risk assessment, profiling and selectivity.
- Objective 5: Comprehensive functioning of customs activities in Border Crossing Points at the border with Serbia in the north of the Republic of Kosovo (Jarinjë and Bërnjak);
- Objective 6: Application of legal powers and maximizing the use of rule of law capacities.<sup>258</sup>

The *Action Plan of the Economic Vision of Kosovo 2011 – 2014*, adopted in 2011, describes the economic development planning framework and proactive commitment of the Government in the economic growth and development of the country. The plan is a document of objectives and concrete activities, based on the achievements to date, and is part of the planning framework within the key midterm strategic documents, including the Government Programme 2011 – 2014, Mid-Term Expenditure Framework (MTEF) 2012 – 2014, European Partnership Action Plan (EPAP), and other sectorial and inter-sectorial Government documents. The Plan is prepared in cooperation with all government stakeholders, is discussed and has taken into account the comments of non-government stakeholders, especially the business community.

<sup>258</sup> Strategic Operation Framework 2012-2014, Kosovo Customs, [http://dogana.rks-gov.net/Uploads/Documents/KORNIZA\\_E\\_STRATEGJISE\\_OPERATIVE\\_2012-2014\\_eng.pdf](http://dogana.rks-gov.net/Uploads/Documents/KORNIZA_E_STRATEGJISE_OPERATIVE_2012-2014_eng.pdf).

Strategic priorities in this document are structured in the following five sectoral pillars:

- Maintaining Macro-Fiscal Sustainability;
- Investments, Investment Environment, and Private Sector Support;
- Development of Public Infrastructure;
- Revitalization of Agriculture sector; and
- Human Capital Development.<sup>259</sup>

The *Kosovo Trade Policy*, adopted in 2009, is continuation of the 2004 document and some previous governmental documents on the trade regime of Kosovo. Based on the fact that the situation in the trade balance remains unchanged, the institutions of Kosovo (in particular, Ministry of Trade and Industry) have committed to meeting the recommendations brought forward by the previous documents, as well as undertake additional steps that aim at promoting the export sector. The design of this policy has been treated in the context of EU integration process. Changes in this document also take into consideration the signals from the business community in Kosovo and other economic stakeholders. It was drafted jointly by the MTI and experts of the area. The external expertise consisted of local and international consultants, supported jointly by the MTI and the UNDP office in Kosovo.

The policy document is divided into three main parts:

- The first part is concentrated in current trends of Kosovo's foreign trade. This section discusses briefly the barriers, comparative advantages and potential markets for products of Kosovo;
- The second part analyses the present trade regime and the dimensions of the institutional environment which are important for promotion of export;
- The last part concentrates on the specific directions Kosovo should take in terms of trade policy, setting out a clear vision for increasing the potential of the export sector in Kosovo.<sup>260</sup>

Kosovo Customs is an important mechanism for execution and implementation of the Trade Policy adopted in 2009.

To summarize, Kosovo Customs has prioritized the implementation of a range of strategic documents and policies, of which the most important are as the following: Feasibility Study for SAA, Visa Liberalization Roadmap, Blueprint for Customs, Government Plan (the part within the scope of the Ministry of Finance), Kosovo Economic Vision Action Plan, the Customs Strategic Framework 2013 - 2015, National Strategy against informal economy, Strategy against organized crime, Anti-Drugs Strategy, the Strategy against money laundering, National Security Strategy, Strategy for integrated border management (IBM), and Strategy on anti-terrorism.

<sup>259</sup> Action Plan for Economic Vision of Kosovo 2011-2014, [http://www.kryeministri-ks.net/repository/docs/Action\\_Plan\\_of\\_the\\_Economic\\_Vision\\_of\\_Kosovo\\_2011-2014.pdf](http://www.kryeministri-ks.net/repository/docs/Action_Plan_of_the_Economic_Vision_of_Kosovo_2011-2014.pdf).

<sup>260</sup> Kosovo Trade Policy, Ministry of Trade and Industry, August 2009, [http://www.mti-ks.org/repository/docs/Trade\\_Policy\\_of\\_Kosovo\\_2009.pdf](http://www.mti-ks.org/repository/docs/Trade_Policy_of_Kosovo_2009.pdf).

## 1.2. Institutional Framework and Development in the Area of Customs

*Kosovo Customs* is an executive agency that operates under the Ministry of Finance. Its mission consists of three dimensions:

- Fiscal Dimension – collection of revenues for state budget;
- Dimension of customs and trade facilitation - ensuring the implementation of customs procedures; and
- Defence Dimension - prevention of negative phenomena - combating tax evasion and entry of prohibited goods through customs points.

KC is organized on a hierarchal form, consisting of 56 operating units and 18 customs checkpoints, employing 622 staff in total. It is a multiethnic institution, with an adequate representation from all the communities living in Kosovo. In the staff recruitments, it encourages the employment and increasing the number of members of minorities with smaller percentage, as well as the persons with limited movement abilities and it aims to continuously work towards meeting legal obligations and best practices regarding gender equality. Each end of the year, KC analyzes personnel needs, reviews the actual structure and presents its new organisational structure.

The Board of Directors consists of the Customs Director General, Law Enforcement Director, Revenue Operation Director, Finances and Systems Director, and Legal Director. Kosovo Customs has been developed progressively and it contains each element of a modern customs service since its establishment, in controlling revenues, progress and development of systems, communication promotion and cooperation with the business community, building human capacities and professionalism, intelligence and anti-smuggling elements, policies and legal units, along with the Central Directorate's functions.<sup>261</sup>

## 1.3. Implementation and Enforcement in the Area of Customs

According to the EU's Feasibility Study for the Stabilisation and Association Agreement with Kosovo, Kosovo Customs have carried out significant modernization efforts, including significant progress in terms of administrative and operational capacity building, as also demonstrated by a number of operations against smuggling and organized crime carried out (mostly focusing on the seizure of counterfeit spirits and contraband tobacco). This report also acknowledges the efforts on enforcement of the intellectual property rights, as well as the fight against smuggling of narcotics and money laundering.<sup>262</sup>

In September 2012, Kosovo Customs has introduced the new software system of ASY-

<sup>261</sup> Strategic Operation Framework 2012-2014, Kosovo Customs, [http://dogana.rks-gov.net/Uploads/Documents/KORNIZA\\_E\\_STRATEGJISE\\_OPERATIVE\\_2012-2014\\_eng.pdf](http://dogana.rks-gov.net/Uploads/Documents/KORNIZA_E_STRATEGJISE_OPERATIVE_2012-2014_eng.pdf).

<sup>262</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

CUDA. This new system has replaced the old British system of TIMS that had been used by customs in the past. ASYCUDA is UNCTAD developed software that is used in over 90 countries worldwide. It is considered to be one of the most sophisticated systems for customs administration.

Kosovo also applies the concept of Integrated Border Management (IBM), introduced by EU, which provides clear instructions in drafting national strategies and action plans in the Western Balkan countries. Joint border management is in accordance with international standards and best practice, and is the ultimate operational mechanism for improving national security and for facilitating trade. Joint border management is the cutting edge for the administration of border controls.<sup>263</sup> While the EU, in principle, requires any country interested to accede it that they run their borders efficiently, in line with this concept, its application is also crucial within the Kosovo Visa Liberalisation Roadmap. Kosovo has a legal framework, as well as a strategy and action plan on IBM, which require that all the three law enforcement agencies (Kosovo Police, Kosovo Customs and Kosovo Veterinary and Food Agency) fully cooperate in border control and management, in line with the IBM concept. While further development and application of this concept at the border-crossing points and borderlines with Albania, Macedonia and Montenegro is moving smoothly, implementation of the IBM, EU-mediated Agreement with Serbia has started only now.

To summarize, the major progress listed by KC in 2012 as regarding the implementation of policy and legal framework in the field of customs include revenue collection of more than € 844 million, the operation of the Customs ASYCUDA System, facilitation of trade procedures, implementation of the Law on Excise of the Games of Chance and combating negative phenomena, respectively smuggling (1,050 total customs' offenses and € 2.5 million customs collected from fines and seizures), crime (40 criminal charges, with the alleged deviation in over € 24 million) and corruption (7 cases initiated).

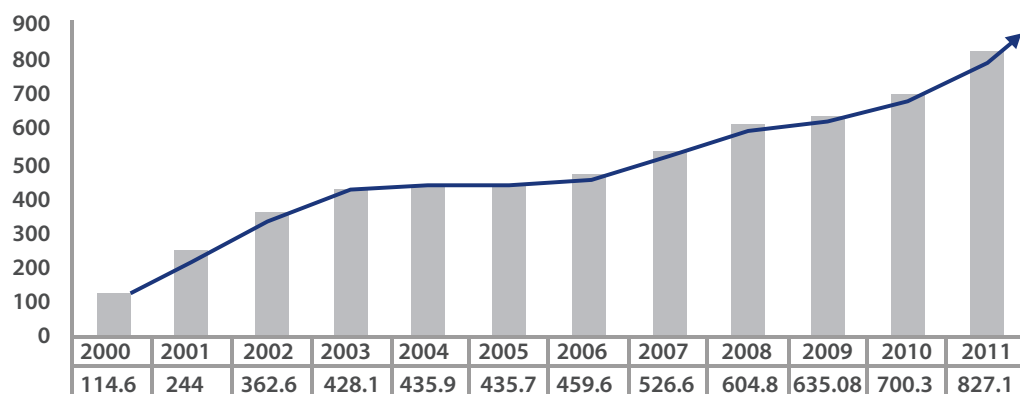
The main priorities of KC for the current year are as follows:

- Customs reform and modernization;
- Revenue collection;
- Capacity building and combating organized crime and smuggling, informal economy, IPR, smuggling of prohibited goods;
- Combating money laundering and tax evasion;
- IT development (in particular in the field of law enforcement); and
- Improvement of infrastructure.

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<sup>263</sup> National Strategy of Kosovo for Integrated Border Management, April 2009, <http://www.mpb-ks.org/repository/docs/Strategjia%20Anglisht.pdf>.

Fig. 5.1: Revenue Collection by Kosovo Customs over the Last Decade



Source: Kosovo Customs

Table 5.1: Variation in percentage of customs collections between 2011 and 2010

In million euro			
Revenues collections	2011	2010	18.15%
Revenues in total	827.1	700.03	16.34%
Customs taxes	121.1	104.09	16.34%
Excise	284.5	232.5	22.37%
VAT	419.5	361.3	16.11%
Others (offences, sales of seizures etc)	2.2	2.2	0.00%

Source: Kosovo Customs

Customs duties are charged according to classification of imported goods in a six-digit harmonized system. The Customs Tariff is the legal instrument which sets out the fiscal levies on imported goods. The following goods are exempt from customs duties: pharmaceutical products, goods imported by UNMIK, KFOR, UNHCR, ICRC, Red Cross, or by donors who have contracts with UNMIK; goods used for agricultural production and some listed raw materials for heavy industry; and goods imported by foreign diplomatic and consular missions. The tariff nomenclature provides for a customs rate of 10 percent for all goods imported into Kosovo. However, as a consequence of regional free trade under CEFTA and tariff exemptions for certain goods, Kosovo applies an average tariff rate on imported goods of approximately 5.3%.

Customs tariffs or duties are an important component of a nation's trade and economic policy. They are taxes imposed on goods imported into a country<sup>1</sup> for the purpose of collecting revenue for the government and protecting domestic producers from imports of goods. For example, as reported by the WTO, approximately 9% of all EU tariffs exceed a 15% rate with a number of these exceeding 100%. Notably, Albania currently has possibly the most liberal tariff regime in the West Balkans. Its tariff consists of six rates or "bands" - 0%, 2%, 5%, 6%, 10%, and 15%. Kosovo has only two, the flat rate of 10%

duty and 0%. In order to promote the local production, the new Kosovo customs code applies a reduced rate of zero percent customs duty on the following: most of the raw materials, most of the equipment for manufacturing and all agricultural raw materials (such as seeds etc.) and equipment.<sup>264</sup>

Kosovo Customs currently collects over 60 – 70% of the Kosovo's budget. Aside from collection of duties, customs is also responsible for collecting VAT and excise tax at the border. Achievement of revenue projection for year 2012 is €867 million OR €40 million more than 2011. Factors that affected the growth of revenues in previous year by 18%, according to the customs analyses, are the following:

- Modifications of policies and fiscal rates during 2010 by law 03/L-220 for excise on oils and tobacco;
- Growth of import on the main goods categories such as oils, tobacco, vehicles etc.;
- Risk management – application of selective controls and focus on high risk shipments;
- Return of control on crossing points in the north of Kosovo;
- Import permission for vehicles older than 8 years and the raise of the excise rate;
- Application of excise tax on gambling;
- Exchange of information with countries in the region, as well as awareness of importing companies regarding their obligations, etc.<sup>265</sup>

## 2. Taxation

In addition to the customs area, the existence of an effective tax administration is also essential, not only to smooth trade and business development and to creating an environment that will attract and secure foreign investments, but also to a functioning revenue system at all levels of government.

The Tax Administration of Kosovo is the executive tax authority, responsible for implementing tax-related legislation. The tax system in Kosovo was established a decade ago and has been continuously developing since then. The first legal act to introduce an independent Kosovo tax system was the 2000 Regulation on Tax Administration and Procedures, at the outset of UN administration in the country. The Tax Administration of Kosovo has 756 employees. The Central Office is responsible for execution of tax policy, determination of standards and organization of implementation and enforcement of regulations on taxation, and overall revenue collection. There are also 10 regional offices operating within TAK (3 in Prishtina, and 1 in Mitrovica, Ferizaj, Gjilan, Peja, Prizren and Gjakova, each, as well as a Large Taxpayers Office), which are responsible for organizing immediate enforcement of the tax rates in force, as well as for monitoring and collection of taxes. The Local Tax Units are also responsible for immediate enforcement

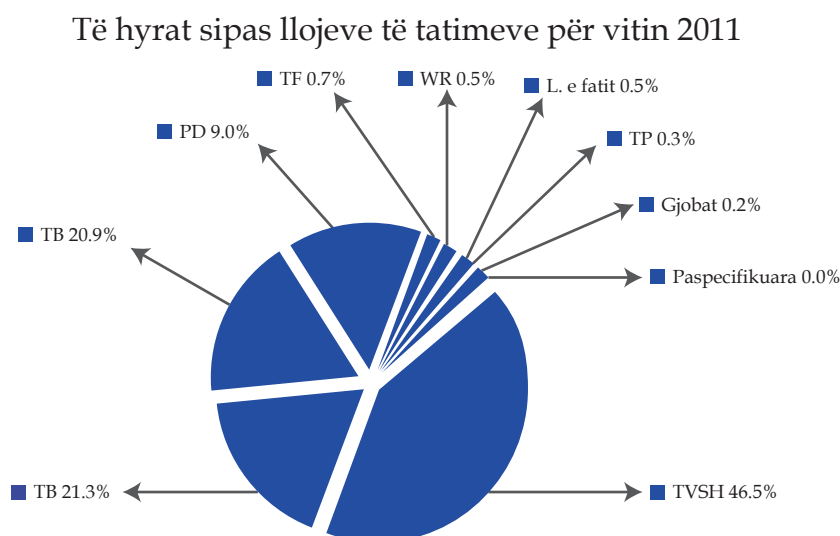
<sup>264</sup> Kosovo Tax Highlights, Deloitte, p. 3.

<sup>265</sup> Annual Report 2011, Kosovo Customs, p. 15, <http://dogana.rks-gov.net/Uploads/Documents/Raport%20vjetor%202011%20%20FINAL%20ANGLISHT.pdf>.

of the rates in force, as well as monitoring and collection of taxes.

Since the establishment of the tax system, an important goal of Kosovo has been continuous alignment of the whole taxation system with the EU *acquis* and European standards. To that end, the system has since then been going through numerous changes and modifications, also supported by the donor community, in terms of development of legislation, policies and capacity-building, with a view to development of the whole system into a modern revenue collection administration. Currently the taxation system is generally considered to be streamlined and simple. However, there is still work to be done to tackle some of remaining issues of rather strategic significance: further development of its IT system, alignment of revenue payment procedures used by the banks and the tax authorities, as well as development and utilization of efficient taxpayer registration and risk management systems.

Fig. 5.2: Revenues according to specific taxes during 2011



Source: Tax Administration of Kosovo

(Terms: TP – Presumptive Tax; TF – Profit Tax; TVSH – Value Added Tax; TB – Withholding Tax; PD – Tax on Individual Business; WR – Monthly statement of withholding tax and payment of interest, dividends, royalties, rental, lottery winning and gambling; CD – Corporate Tax; L. e fatit – Gambling Tax; Gjobat – Fines; Të Paspecifikuara – Other)

## 2.1. Legal and Policy Framework in the Area of Taxation

### 2.1.1. Domestic Legal Framework in the Area of Taxation

The domestic legal framework applicable in the area of taxation is presented under each category of taxes, in this section.

### 2.1.2. Overview of the EU Acquis Applicable in the Area of Taxation

Within the EU integration framework, the area of taxation is regulated by a number of primary and secondary EU *acquis* acts, mostly of non-binding and guidance nature. As with other areas, this legislation consists of two broad categories: principles enshrined in the Treaties and specific provisions contained in the rest of EU *Acquis* acts issued by EU Institutions, the latter subdivided into two subcategories: (1) regulations, directives and decisions (legally binding instruments), and (2) recommendations and opinions (legally non-binding).

The *Treaty on the Functioning of the European Union* (Lisbon Treaty) prohibits Member States from imposing any internal taxes (be them direct or indirect) on the products of other Member States in excess of that imposed to similar domestic products. It also prohibits them from imposing any taxation to other Member States' products with the aim of indirectly protecting their own domestic products. Thirdly, it stipulates that in the cases of products exported to other Member States, no Member State is allowed to impose any repayment of internal taxation that would exceed the internal taxation imposed on them, directly or indirectly.<sup>266</sup>

It further regulates prohibitions to Member States on charges other than turnover taxes, excise duties and other forms of indirect taxes, specifically prohibiting granting of remissions and repayments in respect of exports to other Member States, as well as countervailing charges in respect of imports from them. Such measures may be applied only if previously approved, for a limited period, by the Council, on a proposal from the Commission. Lastly, the Treaty broadly sets out the procedure on harmonisation of legislation: "The Council shall, acting unanimously in accordance with a special legislative procedure and after consulting the European Parliament and the Economic and Social Committee, adopt provisions for the harmonisation of legislation concerning turnover taxes, excise duties and other forms of indirect taxation to the extent that such harmonisation is necessary to ensure the establishment and the functioning of the internal market and to avoid distortion of competition."<sup>267</sup>

At the level of specific provisions, based on the structure of *acquis* chapters, the area of taxation is covered by Chapter 16, on *Taxation* (see Annex 2 for a list of acts applying

<sup>266</sup> Treaty on European Union and the Treaty on the Functioning of the European Union, Articles 110 and 111, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2010:083:FULL:EN:PDF>

<sup>267</sup> Ibid, Articles 112 and 113.

in this area).<sup>268</sup> It consists of 176 acts in total, divided into the following five categories:

- General (7 acts);
- Direct taxation (7 acts);
- Indirect taxation (134 acts);
- Other taxes (6 acts); and
- Prevention of tax evasion and avoidance (22 acts).<sup>269</sup>

## 2.2. Policy Framework and Development in the Area of Taxation

This section provides an overview of the policy framework relevant for the area of taxation mainly focusing on the Tax Administration of Kosovo's Strategic Plan 2010 – 2015 and Tax Compliance Strategy 2012 – 2015. Other policy documents relevant for this area that are also analyzed here include the Action Plan of the Economic Vision of Kosovo 2011 – 2014, Kosovo's Trade Policy, Kosovo SME Development Strategy, and Strategy and Action Plan for Fighting Informal Economy.

The *TAK Strategic Plan 2010 – 2015*, was adopted in 2010. The efforts over the period of this Strategic Plan will be primarily directed at broadening the tax base and collecting the proper amount of tax from all taxpayers. This is planned to be done through increasing the technical capacity and increasing the amount of information available to TAK for ensuring that everyone is reporting and paying their fair share of taxes.

The strategic plan contains 12 main objectives (formulated in the form of components):

- Commitment to obligations established by the statute (charter) of taxpayers;
- Ensuring the integrity of the database,
- Working with public in order to ensure continuous education about paying tax obligation
- Improved technical capacity of taxpayers education staff and use of new methods for providing information to the public;
- Setting up processes that will assist with filing and timely processing of declarations and payments;
- Prevention and early intervention;
- Increase the effectiveness of control programs and risk analysis and identification of opportunities focusing on those issues and controls of higher impact on compliance and generate more revenues;
- Reducing opportunities for tax evasion and tax avoidance;
- Early and effective collection activities
- Information Technology;
- Human resources, and
- Accommodation.

<sup>268</sup> Chapters of the acquis, [http://ec.europa.eu/enlargement/policy/conditions-membership/chapters-of-the-acquis/index\\_en.htm](http://ec.europa.eu/enlargement/policy/conditions-membership/chapters-of-the-acquis/index_en.htm).

<sup>269</sup> EUR-Lex: Taxation, <http://eur-lex.europa.eu/en/consleg/latest/chap09.htm>.

These objectives will help TAK achieve its compliance and revenue goals, while at the same time ensuring that the systems are up-to-date, the staff is well-trained, laws are effectively applied, and the staff performs its work with integrity and fairness. A difficulty that has faced the TAK throughout the years, which remains a challenge today, is the ability of the administration to reach the remaining businesses and individuals who should be paying taxes, but are not currently doing so.

In cooperation with IMF, the Tax Administration of Kosovo is working towards development of a *Tax Compliance Strategy 2012 – 2015*, which is in accordance with TAK Strategic Plan 2010 – 2015. The overall objective of this Strategy is to facilitate the compliance process by creating a compliance environment in which easy administrative procedures, systematic guidance of the taxpayers and a variety of incentives will make the taxpayers comply with their tax obligations to the highest extent possible. During the period of this Strategy, TAK efforts will focus on the expansion of the tax base and collection of the appropriate amount of tax from taxpayers. According to the strategy, this will be achieved through increased technical capacities and volume of information available to TAK, which would ensure that taxpayers are reporting their taxes correctly, thus contributing to increased tax revenues. Therefore the strategy will guide TAK compliance activities towards reducing the tax gap, being the gap between the potential revenue and the revenue actually collected.

TAK has also drafted the *Annual Risk Management Plan*, which contains activities that have to be undertaken to tackle non-compliant taxpayers. Implementation of this plan has resulted in a report containing measurement indicators, which also indicates an increase in the amount of revenues, due to the increase in the number of taxpayers.

Similar to the Strategic Plan, this plan contains 13 main objectives (formulated in the form of components that target specific groups of sector business entities and others):

- Non-recorders in construction;
- Non-recorders in agriculture and minerals;
- Non-recorders in professional services, arts and entertainment;
- Debts and delays in payment;
- Non-declaring, banned-declaring, under-declaring and delays in the declaration;
- Non-registration of workers by employers;
- Under-declaration of salaries of workers;
- Under declaring/micro businesses;
- Under declaring/ small businesses;
- Incorrect addresses and economic activities;
- Non-provision of fiscal cash registers;
- Non-recorders in real estate (lessors), and
- Failure to keep the documentation in order.

The *Action Plan of the Economic Vision of Kosovo 2011 – 2014* also tackles the area of taxation. One of its strategic priorities is maintaining macro-fiscal sustainability. More specifically, with the aim of achieving economic growth and ensuring economic sus-

tainability, the Government of Kosovo will continuously work on improving efficiency in public spending and continuously increasing budget revenues. The Government of Kosovo aims at maintaining an overall budget deficit of 2% of GDP in the period 2011-2014. This strategic priority consists of several activities to ensure macro-fiscal sustainability of budget revenues and expenditures; implementation of the Public Financial Management Action Plan; further development of the financial market; activities related to fiscal facilities for businesses and certain groups of citizens; completing fiscalization of all operating businesses during the mid-term period; full implementation of the Government Program for Prevention of Informal Economy; and other related activities.<sup>270</sup>

Within the framework of implementing the *Kosovo Trade Policy*, the Government of Kosovo took major steps in making the tax policy more conducive to business and investments (the new tax schedule entered into force on 1 January 2009). Kosovo is now applying tax rates very competitive relative to the region of South East Europe (SEE). In addition, tax system is conducive to export activities. Exports are not charged with VAT or custom tariff. In the case of VAT, it should be clarified no VAT charge will be applied either on imported inputs (VAT rebate applies), other production inputs, or final exported products. In other cases, VAT is uniform and as such is collected for all goods, only in some specific cases when certain products are exempt from VAT. As pointed out above, goods destined to the foreign markets are not charged with customs fees. On the other hand, imports, with some exemptions, are charged with customs tariff of 10%.

Within the *Kosovo SME Development Strategy 2012 – 2016*, adopted in July 2011, the Government of Kosovo recognizes the importance of Small and Medium enterprises (SMEs) to the Economic Development of Kosovo. More than 99% of enterprises in Kosovo are Small and Medium Enterprises (SMEs). The Institution responsible for formulating the SME Development Strategy 2012-2016 with vision to 2020 (the SME Strategy), is the Ministry of Trade and Industry (MoTI) through the SME Support Agency (SMESA). The SME Strategy spans the five years from 2012 to 2016 and came into effect on January 1st 2012. The SME Strategy identifies measures (Strategic Goals, Goals and Strategic Objectives) that need to be undertaken to advance reforms that will lead to a dynamic SME Sector and generate new jobs for Kosovo.

Since 2008, a number of key achievements have taken place which has led to some improvement of the business environment for SME in Kosovo. Major tax reform was enacted and VAT collection was reorganized with the introduction of electronic fiscal register cashiers, despite some opposition from business associations. These major steps were an attempt to reduce informality in the SME sector and to try to improve relations between the business community and the state. Tax revenues have significantly increased due to the decrease of the tax rate from 20% to 10% in combination with improved compliance, a broadening of the tax base and a larger and more efficient reorganization of the tax

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<sup>270</sup> Action Plan for Economic Vision of Kosovo 2011-2014, [http://www.kryeministri-ks.net/repository/docs/Action\\_Plan\\_of\\_the\\_Economic\\_Vision\\_of\\_Kosovo\\_2011-2014.pdf](http://www.kryeministri-ks.net/repository/docs/Action_Plan_of_the_Economic_Vision_of_Kosovo_2011-2014.pdf).

collection process.<sup>271</sup>

In order to prove that the fight against informal, tax evasion, labour market irregularities, unfair competition, corruption etc, are priorities of this Government, the latter adopted the *Governmental Programme and Action Plan 2010-2012 on Prevention of Informal Economy in Kosovo*, in September 2010. The general objective of the governmental program for the prevention of informal economy is the empowerment of the implementation of the Government Policy Priorities, which includes economic growth, good governance, poverty alleviation and social stability. The primary objectives of the governmental program and action plan on the prevention of informal economy are focused in the improvements of various subjects such as: organizational structures of responsible authorities, legislation, the coordination of official duties and sources of responsible authorities, cooperation agreements between responsible authorities, the treatment for public and private institutions, development of the entrepreneurial sector and the decrease of labour market distortions, the awareness of the influence and prevention of informal economy, information technology systems and the instruments of responsible authorities, as well taxes.<sup>272</sup>

### 2.3. Indirect Taxation

Indirect tax is a tax collected by intermediary or third party from the person who bears the ultimate burden of the tax, for example consumers and businesses. The retail store will file a tax return at a later date and forward the tax proceeds to the government, as well as tax return. In Kosovo types of indirect tax are that of the Value Added Tax and Excise Tax. For import/export community VAT and Excise Taxes are collected by customs at the border. Kosovo relies heavily on indirect taxes collected at the border: only 14% of all tax revenues stem from direct taxes. VAT is 16% and only companies with a yearly turnover above 50000 are subject to it.

#### 2.3.1. Value-Added Tax (VAT)

The VAT regime in Kosovo follows the main principles of VAT with some subtle differences such as taxes on exports of services and a requirement to pay VAT at the border. Thus, it is a tax that is added to the sale of all goods and services.

VAT Tax has been a major source for budget revenues. Value added tax (*Law No.03/L-146*) is applied to all importers and businesses with an annual turnover in excess of 50,000 Euro. The VAT rate stands at 16 percent and is levied on all goods and services, with exemption for certain agricultural and capital goods (on which VAT is zero per-

<sup>271</sup> Kosovo SME Development Strategy 2012-2016, [http://www.sme-ks.org/repository/docs/190711\\_SME\\_Strategy\\_Final\\_angl\\_441123573.pdf](http://www.sme-ks.org/repository/docs/190711_SME_Strategy_Final_angl_441123573.pdf).

<sup>272</sup> Strategy and Action Plan for Fighting Informal Economy 2010-2012, [http://www.kryeministri-ks.net/repository/docs/Strategjia\\_per\\_parandalimin\\_dhe\\_eliminimin\\_e\\_punes\\_se\\_femijeve\\_ne\\_Kosove\\_2011-2016.pdf](http://www.kryeministri-ks.net/repository/docs/Strategjia_per_parandalimin_dhe_eliminimin_e_punes_se_femijeve_ne_Kosove_2011-2016.pdf).

cent). Exporters receive full VAT reimbursement for exported goods. The Law on VAT is in compliance with the recommendations of the International Monetary Fund, and the current EU VAT Directives.

## **2.4. Direct Taxation**

The term 'direct tax' generally means a tax paid directly to the government by the person whom it is imposed. Taxes on income, company profits and wealth are all directly paid to the government. We essentially have no choice in whether or not we pay direct tax. For example, the personal income tax in Kosovo applies in four rates: 0%, 4%, 8% and 10%.<sup>273</sup> There is also a 10% corporate tax rate.<sup>274</sup> In 2011, direct taxes amounted only to 3.2% of the GDP.<sup>275</sup>

### **2.4.1. Profit Tax**

The rate of profit tax in Kosovo is 10%. That is the same rate as corporate income tax. According to the new system of Corporate Income Tax, any small corporation who opts to become subject to real profit tax, may carry forward the losses differently from presumptive tax which was applied only on gross sales of corporation. However a number of very small corporations will continue to be subject to 'presumptive' tax. For example, they pay a fixed amount for a quarter, if their gross sales are below €5,000 annually, and 3% (trade, etc.) and 9% (services etc.) tax on gross sales, if their turnover is between €5,000.01 – €50,000 annually, if they choose not to become subject to real income taxation.<sup>276</sup>

So, all taxpayers with annual gross income of €50,000 or less, derived from economic activity, who are not required to, or do not opt to maintain books and records required of larger taxpayers, are charged on a quarterly basis as follows:

- 3% of gross income from trade, transport, agricultural, and similar commercial activities, but not less than €37.50;
- 9% of gross income from services, professional, vocational, entertainment and similar activities, but not less than €37.50;

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<sup>273</sup> Law No. 03/L-161 on Personal Income Tax, Article 6, [http://www.atk-ks.org/wp-content/uploads/2010/09/Ligji\\_2009\\_3\\_L161.pdf](http://www.atk-ks.org/wp-content/uploads/2010/09/Ligji_2009_3_L161.pdf).

<sup>274</sup> Law No. 03/L-162 on Corporate Income Tax, Article 6, [http://www.atk-ks.org/wp-content/uploads/2010/09/Ligji\\_2009\\_3\\_L162.pdf](http://www.atk-ks.org/wp-content/uploads/2010/09/Ligji_2009_3_L162.pdf).

<sup>275</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 39, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

<sup>276</sup> Handbook on Taxes in Kosovo, Tax Administration of Kosovo, [http://www.atk-ks.org/wp-content/uploads/2010/09/Doracak\\_mbi\\_tatimet\\_A.pdf](http://www.atk-ks.org/wp-content/uploads/2010/09/Doracak_mbi_tatimet_A.pdf).

- 9% of gross income for taxpayers with no turnover (who must submit a 'no tax due' return for the respective quarter).

### 2.4.2. Personal Income Tax

The Law on Income Tax, of December 2008 regulates the personal income tax regime. As it is the case with introduction of the corporate income tax, this legal regulation aims to introduce one single tax for all sources of income generated by individuals, as well as personal business enterprises, partnerships and other business organisations that generate gross income.

Pursuant to the *Law No. 03/L-161 on Personal Income Tax*, the personal income tax applies to natural persons receiving income from Kosovo sources, and also to foreign incomes received by Kosovo residents. As of 1 January 2009, the rate of personal income tax is at four rates:

- 0% – for annual taxable income amounting to €960 or less;
- 4% – for annual taxable income exceeding the amount of €960 and up to €3,000, including the amount of €3,000;
- 8% – for annual taxable income exceeding the amount of €3,000 and up to €5,400, including the amount of €5,400, and plus €81.60 of the amount over €3,000; and
- 10% – for annual taxable income exceeding the amount of €5,400, plus €273.60 of the amount over €5,400.<sup>277</sup>

Taxable persons are resident and non-resident natural persons who receive income in Kosovo. A resident is defined as a natural person who has his principal residence in Kosovo. A natural person is also deemed resident if physically staying in Kosovo at least 183 days in one fiscal year. Therefore, the following individuals are subject to Kosovo's personal income tax: residents on taxable income derived from Kosovo source income and foreign source income; and non-residents on taxable income derived from Kosovo source income.

The taxable income for a tax period is calculated using the difference between gross income and any allowed deductions. Gross income consists of income from: a) wages, b) business activities, c) rent, d) use of intangible property, e) interest, f) dividends, g) capital gains, h) lottery or other game of chance prizes, i) pensions and h) any other income that increases the taxpayer's net worth.

Withholding tax on salary and pension contribution must be declared and paid by the employer not later than the 15<sup>th</sup> date of the month following the month of deduction from the salary. Annual personal income tax returns are due on or before 1 April of the year following the tax period.

<sup>277</sup> Law No. 03/L-161 on Personal Income Tax, Article 6, [http://www.atk-ks.org/wp-content/uploads/2010/09/Ligji\\_2009\\_3\\_L161.pdf](http://www.atk-ks.org/wp-content/uploads/2010/09/Ligji_2009_3_L161.pdf).

Table 5.2: Personal Income Tax Rates

Annual Income (€0 - €960)	0%
Annual Income (€960 - €3,000)	4% of the amount over €960
Annual Income (€3001 - €5,400)	€81.6 + 8% of the amount over €3,000
Annual Income (€5,401 - above)	€273.6 + 10% of the amount over €5,400

Source: Tax Administration of Kosovo

### 2.4.3. Corporate Tax

On 18 December 2008, the Kosovo Assembly adopted the Law on Corporate Income Tax (Law No.03/L-113), which entered into force on 1 January, 2009.

The following is subject to corporate income tax:

- Corporations or other business organizations that have the status of a legal person under applicable law in Kosovo;
- Companies operating with public or socially owned assets;
- Organizations registered with UNMIK as non-governmental organizations; and
- Permanent establishments in Kosovo of non-residents. Such permanent establishments include, but are not limited to, plants, branch offices, representation offices, factories and construction sites.<sup>278</sup>

The rate of corporate income tax depends on annual income, and ranges from 0% to 10% of the taxable income. Certain revenues like some revenues of non-governmental organizations where those organizations have the public benefit status certificate are exempted from corporate income tax. Depending on their annual income, domestic legal entities and permanent establishments of foreign legal entities are taxed as depicted in the following table (Law No. 03/L-162).

Table 5.3: The amount of corporate income tax (which is paid quarterly in advance, based on quarterly net income or profit projections):

Annual Income €0 – €5000	37.5 euro / quarter
Annual Income €5,001 – €50,000	3-10% of income
Annual Income €50,000 and above	10% of profit

Source: Tax Administration of Kosovo

<sup>278</sup> Legal Guide to Kosovo: Corporate, tax and employment law and other regulations (WolfTheiss, 2nd Edition), [http://www.wolftheiss.com/tl\\_files/wolftheiss/RegionalDesks/Kosovo/WT\\_Kosovo%20Guide.pdf](http://www.wolftheiss.com/tl_files/wolftheiss/RegionalDesks/Kosovo/WT_Kosovo%20Guide.pdf).

#### 2.4.4. Property Tax

Immovable property tax is set and regulated by the *Law no. 2003/8 on Immovable Property Tax in Kosovo*.<sup>279</sup> This law defines thus type of tax as a municipal one, and also establishes standards and procedures to be complied with by Municipalities in administering it. Revenues collected from this tax belong to Municipalities and will be used by them in accordance with the Law on Public Financial Management. Property tax was introduced in 2003. The Municipal Assembly of each Municipality determines the rate of property tax on annual bases.

This rate ranges from 0.05% to 1% of the market value of the property for each of the following categories:

- Residential property;
- Commercial property;
- Industrial property; and
- Agricultural property.

#### 2.5. Institutional Framework and Development in the Area of Taxation

In terms of its organisational structure, the *Tax Administration of Kosovo* consists of the Central Office, a Large Taxpayers Office and nine Regional Offices. The Central Office consists of the Office of the Director General (including the Executive Office, Office of Internal Audit and the two Deputy Directors-General, one in charge of compliance operations and one of support services), Legal Office, Modernization, Planning and Analysis Directorate, Directorate for Taxpayer Services, and the Information Technology Directorate.<sup>280</sup> There are also 10 Regional Offices: 3 in Prishtina, then in Peja, Prizren, Gjilan, Mitrovica and Gjakova (1 each), as well as a Large Taxpayers Office. TAK currently has a total of 756 employees.

Concerning the IT, TAK has developed internal subsystems, which are linked to systems of other institutions, such as those of the Central Bank, Treasury, Kosovo Customs, etc. In addition, in cooperation with MTI, through the One Stop-Shop Centre, TAK enables registration of taxpayers at one place and providing them with fiscal numbers within a day, while it has also developed the Risk Management Module, which is functional.

TAK has signed memoranda of cooperation with the following institutions: Kosovo Customs, State Prosecutor, Kosovo Business Registration Agency, Financial Intelligence Centre, Post and Telecommunication of Kosovo and several ministries. An integral part of these memoranda is closer cooperation on information exchange and conducting joint activities. TAK has continuously received technical assistance from various internation-

<sup>279</sup> Law on Immovable Property Tax in Kosovo, [http://www.assembly-kosova.org/common/docs/lig-jet/2003\\_8\\_al.pdf](http://www.assembly-kosova.org/common/docs/lig-jet/2003_8_al.pdf).

<sup>280</sup> Organisational Structure of Tax Administration of Kosovo, <http://www.atk-ks.org/wp-content/uploads/2012/10/STRUKTURA-ORGANIZATIVE-ATK-21-02-2012-2.pdf>.

al organisations, including the European Commission, USAID, and IMF, on capacity-building, as well as development of policies, legislation, guidelines and procedures.<sup>281</sup>

During 2011, the Modernization and Strategic Planning Directorate concentrated its efforts on management and development of projects and coordination of activities with the relevant departments aimed at initiating new projects envisaged by the TAK Strategic Plan. Particular efforts have been put in coordinating donor activities on the project for development of SIGTAS and making the Call Centre functional.<sup>282</sup>

A priority for TAK in 2011 was building of capacities to improve taxpayer services. Key achievements in 2011 include:

- Development of the Compliance Strategy 2012 – 2015 and the Risk Tackling Comprehensive Plan, as a performance management tool as well as TAK operational plans for 2012;
- Continuation of the implementation of the cash registers project;
- Acceleration of procedures for issuing fiscal numbers on the day of application
- Operationalization of the Call Centre for taxpayers who have tax liabilities worth €500 – €3,000;
- Operationalization of the Tax Investigation Unit;
- Development of the data processing system;
- Launch of the e-declaration project; and
- Disclosure of purchases exceeding €500 from suppliers.

Regarding municipal taxes (property tax and municipal charges and fines), *Municipalities* are responsible for planning and setting duties, tariffs and rates. This is regulated by municipal regulations.

## 2.6. Implementation and Enforcement in the Area of Customs

Referring to the Feasibility Report, the tax authority needs to be able to adjust the policies and identify the means to improve the effectiveness of tax collection. The focus needs to be on enforcement. Work efficiency needs to be increased as well as cooperation between the Tax Administration, the police and courts. The core IT system (SIGTAS) is to be replaced by modern infrastructure. A challenge remains in improve the capacity of the IT system in Tax Administration and advance its transformation into a modern administration through delivering a new IT system which will bring the revenue collection mechanisms closer to EU standards.

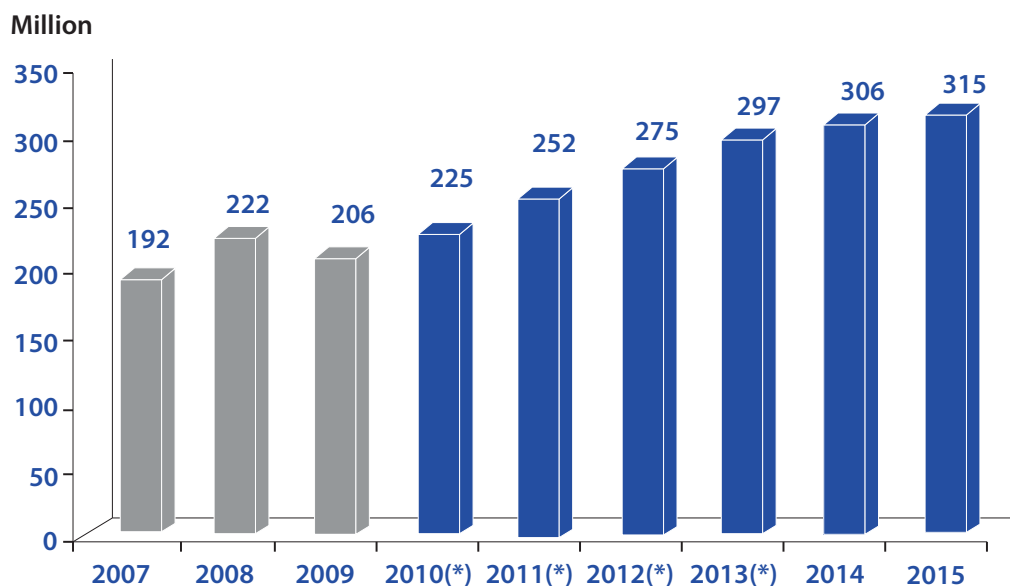
<sup>281</sup> Kosovo's Answers to the EC Questionnaire on the Preparation of the Feasibility Study for a Stabilisation and Association Agreement, p. 131, [http://www.mei-ks.net/repository/docs/Answers\\_to\\_the\\_questionnaire\\_on\\_the\\_preparation\\_of\\_the\\_Feasibility\\_Study\\_for\\_a\\_Stabilisation\\_and\\_Association\\_Agreement.pdf](http://www.mei-ks.net/repository/docs/Answers_to_the_questionnaire_on_the_preparation_of_the_Feasibility_Study_for_a_Stabilisation_and_Association_Agreement.pdf).

<sup>282</sup> 2011 Annual Business Report, Tax Administration of Kosovo, [http://www.atk-ks.org/wp-content/uploads/2010/09/Raporti-Vjetor-2010\\_v\\_fundit\\_shtyp\\_ENG.pdf](http://www.atk-ks.org/wp-content/uploads/2010/09/Raporti-Vjetor-2010_v_fundit_shtyp_ENG.pdf).

In terms of taxation, special attention should be paid to consolidation of communication between the TAK and taxpayers, through utilization of the Call Centre, which enables online submission of tax statements by all entities and for all types of taxes. This centre is in operation since 2011, and as a result of its work, extra revenues amounting to €2 million have been collected during 2012 only. In 2010, TAK has also started with implementation of the Electronic Declaration project, through which more than 23,000 taxpayers have been registered so far, which carry out electronic declaration of VAT, source-held tax and pension contributions. TAK will continue to issue fiscal numbers and functionalize fiscal cashboxes, with a view of combating fiscal evasion and informal economy, which is a special priority for the Government this year.<sup>283</sup>

The Figure 5.3 below contains data on projections of income during 2007 – 2015. According to the TAK data, out of these projections, income amounting to €221 million have been collected during 2010, €261 million during 2011, and €284 million during 2012.

Fig. 5.3: Projection of Revenues



Source: Tax Administration of Kosovo

<sup>283</sup> Kosovo European Partnership Action Plan 2012, pp. 15-16, [http://www.mei-ks.net/repository/docs/European\\_Partnership\\_Action\\_Plan\\_2012.pdf](http://www.mei-ks.net/repository/docs/European_Partnership_Action_Plan_2012.pdf).

Table 5.4: Tax Rates in the Western Balkan Countries

Types of Taxes	VAT	Corporate Profit Tax	Personal Income Tax
Country			
Kosovo	16%	10%	0 – 10%
Macedonia	18%	10%	10%
Serbia	18%	10%	10 – 20%
Bosnia and Herzegovina	17%	10%	0 – 10%
Croatia	17%	20%	12 – 40%
Montenegro	17%	9%	9%

Source: Investment Promotion Agency of Kosovo

## 2.7. Fiscal Evasion and Fiscal Cashiers

Although we have a good foundation of business and individuals that are responsible taxpayers, the challenge of the Tax Administration remain in the ability to reach ALL business and individuals who have managed to manipulate with the system, to ensure that everyone is contribution their fair share of tax payment.

A tax gap is the amount of taxes that go uncollected due to non-compliance with the tax laws. It is “what is missing” (the tax gap equates the potential tax yield minus the actual tax revenues). It is only by gaining an understanding of a country’s tax gap that a government can decide how to successfully go about improving tax compliance levels and hence increase the overall level of revenues available to fund the government budget.

Although, according to TAK data, the amount of revenues collected has increased for 40% since 2009 (which has significant impact in reducing tax gap), based on other macro-economic data available, the total estimated tax gap in Kosovo (for the core central government taxes, namely VAT, income tax, corporate tax, and excise duties) reaches an average of €400 – €450 million. This equates to roughly 10% of GDP.

Unpaid VAT is the biggest culprit in the tax gap – with annual losses estimated to amount to roughly €200 million – followed by a personal income tax gap of about €100 million per year. Corporate and business income taxes probably represent only about €80 million of the tax gap. Lost excise taxes amount to roughly €15 million (mostly in spirits-related excise taxes). The rest of the tax gap likely arises from estimation error (no small issue in a survey of this size), various other taxes that were not analyzed (gambling taxes, “corruption taxes”, direct smuggling), and the way Kosovo’s black market economy distorts the formal sector.<sup>284</sup>

<sup>284</sup> Tax Gap Analysis in Kosovo, Crown Agents, Department for International Development, September 2011.

Table 5.5: Estimated tax gap in Kosovo<sup>285</sup>

Tax Type	Estimated Tax Gap
Value Added Tax	€200 million
Excise Tax (mostly spirits)	€15 million
Personnel Income Tax	€100 million
Corporate and Business Taxes	€80 million

The problem and difficulties with implementation of the fiscal cashiers has started in 2010. Ministry of Economy and Finance (at the end of 2009) had initially licensed only two companies responsible for the sale of fiscal cashiers. These two companies were later fined by the Commission of Competition for monopoly which resulted in high prices for supply of fiscal cashiers.

Therefore, purchasing a simple fiscal cashier from the Gekos company, with capacity of registering up to 1000 products, would cost 260€. Other models include those with capacity of registering 3000 products 55B EJ (€325), MP-55B (€289) and MP-55EJ (€379). A larger fiscal cashier with capacity of registering 5000 products would cost 480€. Besides the fiscal cashier, business would need to be supplied with fiscal printers as well. The prices for the fiscal printers are much higher than fiscal cashier. They range from the lowest price of €449 up to €1,100.

The terminal for connection with Tax Administration of Kosovo costs €155, Display for Clients 110€, and a drive F-Link for the fiscal printers €125. All these prices do not include the VAT tax of 16%.

Considering the small and medium size business market in Kosovo, the prices for purchasing a fiscal cashier are very high. Therefore, we still have a large number of businesses that do not use the new system. At the beginning of the program implementation, out of 40.000 active businesses, only 6500 of them purchased the fiscal cashiers.

### Summary of key Challenges Identified in the Areas of Customs and Taxation

- The situation in the north poses a specific challenge for Customs. In the two customs checkpoints at the Kosovo – Serbia border, situated in the north of the country, Kosovo Customs continues to operate only in cooperation with EU-LEX. Following the incidents in July 2011 and subsequent agreements on the customs stamps and IBM in the scope of the Belgrade – Pristina dialogue, very limited commercial traffic passes through the two gates in the north. All commercial vehicles continue to be directed to the Mitrovica Terminal for customs clearance. Revenue is not collected at these two gates. Goods subject to excise, sanitary and phytosanitary controls are not allowed to enter via these two cross-

<sup>285</sup> Ibid.

ing points.

- Due to the lack of efficient customs surveillance at the border line between the north of Kosovo and Serbia, goods frequently enter Kosovo in the north without customs clearance.
- Certificates of origin for the goods to be exported are validated by customs for goods originating both in the north and in the rest of Kosovo. Currently, Kosovo Customs faces a challenge in terms of access to the territory of the north. This has implications for the respect of rules of origin for the goods entering country's territory through this part of the border. In practice, the requests for certificates of origin are scarce.<sup>286</sup>
- Modern trade administration requires the support appropriate information and communications technology in all aspects of interaction between importers, exporters and customs brokers (spediteurs) and the trade administration. Many customs procedures such as transit, warehousing, transshipment can be more efficiently controlled through the use of the appropriate modern technology. However, the introduction of a fully automated e-Customs system requires adoption within the Law of provisions related to legal application and acceptance of electronic signatures across the broad spectrum of administrative and business relations.
- Ensuring timely and transparent appeal procedures (fairness) is also a critical element in fiscal and trade administration, and when an administrative official makes a decision that is unfavourable to an individual or a business, there must be recourse for businesses to an independent, transparent, fair and responsive appeal procedure. The objective is to settle any administrative disputes with as little cost and time spent by the aggrieved person or enterprise, so that more costly and time-consuming formal appeals to the court system can be limited. An ideal guideline is to settle administrative disputes within a 30-day period of an appeal being lodged.
- Tax evasion remains widespread. To address this challenge, a taxpayer compliance management strategy (2012-2015) is in force. The main challenge of the Kosovo Tax Administration is reaching all individuals and businesses that are not paying taxes.

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<sup>286</sup> Commission Staff Working Document accompanying the document Commission Communication on a Feasibility Study for a Stabilisation and Association Agreement between the European Union and Kosovo, p. 39, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/ks\\_analytical\\_2012\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/ks_analytical_2012_en.pdf).

## Summary of Challenges Identified in the Areas Covered by the Thematic Roundtable No. 4<sup>287</sup>

### Trade

- Increasing trade deficit in goods, lack of diversification of goods exported, dominance of low value added goods in the export structure, and the risk of discontinuance of positive balance in the export of services
- Legal gaps in the legislation on quality infrastructure, customs and contingency measures, and its insufficient approximation with the acquis
- Insufficient coherence and implementation of Trade Policy, and its ad hoc nature
- Lack of fiscal and economic policies sufficiently in favour of local businesses and lack of incentive policies for them (direct subventions for agriculture and for credit interest)
- Lack of sufficient capacities of the Department of Trade, particularly in the area of market protection and for conducting studies on the impact in Kosovo's economy in the context of preparation and implementation of SAA part on trade
- Lack of sufficient capacities of business community associations to contribute to the development of legislation and policies and to functioning of coordination structures, as well as insufficient awareness of businesses on trade policies and legislation
- Insufficient level of reflection of businesses' requirements, needs and suggestions in trade legislation and policies
- Unsatisfactory functioning of coordination mechanisms in the area of trade
- Availability and low quality of statistical data and insufficient cooperation at the technical level among institutions which possess statistical data relevant for the area of trade
- Insufficient and inadequate implementation of legislation and policies (increase of customs base for the import in goods, non-implementation of CEFTA Agreement, unfair competition, lack of effective market oversight, implementation of anti-dumping measures and other protective measures on ad hoc basis and based on individual businesses rather than on a wider approach based on industry and economic sectors, very weak legal infrastructure and low efficiency of courts, corruption, smuggling, informality, fiscal evasion, communication with municipal administrations, identification sectors of competitive advantage sectors)

### Industry and SMEs

- Lack of a favourable investment climate
- Administrative and other similar burdens on functioning of enterprises (in particular public enterprises)
- Insufficient access of SMEs to finances

<sup>287</sup> This section summarizes the main challenges deriving from the discussion materials for each area and from the plenary meeting of the Thematic Roundtable (held on 24 April 2013) and serves as a working material for the joint workshop of all thematic roundtables of the Task Force for European Integration.

- Lack of a completed and functional system on bankruptcy of enterprises
- Insufficient quality and implementation of policies for modernization, restructuring and strengthening of SMEs (funds, capacities of institutions and SMEs)
- Very considerable mismatch of data in the area of SMEs, as well as insufficient cooperation and coordination among the relevant institutions and with the business community
- Insufficient implementation of legislation in the area of industry and SMEs
- Difficulties of moving the informal economy into the formal ones
- Lack of the 'regulatory guillotine' and of a Regulatory Impact Assessment (RIA) mechanism
- Lack of adequate industrial development policies that would contribute to activation of economic growth resources, particularly in the production sector
- Lack of a well-structured and fully functional dialogue among public institutions and private sector on all aspects of industry SME development
- Non participation in EU programmes (Programme for the Competitiveness of Enterprises and SMEs (COSME) 2014 – 2020, Competitiveness and Innovation Framework Programme (CIP) and the European SME Week campaign)

Existence of a functional market economy and capacity to cope with market forces of the Union

- Lack of the necessary institutional capacities (competition, IPR, energy efficiency, environment, food safety, employment and social policies, public health policies)
- High level of corruption and bureaucracy
- Insufficient approximation of national legislation with the *acquis* (particularly on free movement of goods, competition and IPR, etc.)
- Weak enforcement (particularly weak efficiency of courts and other stakeholders linked to the legal system)
- Lack of well-educated and skilled labour force (the quality of education does not respond to market needs, underdeveloped policies and insufficient funds for lifelong learning, and coordination among the central and local levels)
- Insufficient approximation with EU standards regarding recognition of professional qualifications and company law (including accounting, auditing and corporate governance)
- Insufficient implementation of structural reforms in agriculture (harmonization of veterinary, sanitary and phytosanitary rules with EU standards, data collection and processing)
- Insufficient approximation of the legal framework with EU standards on freedom of movement of capital, payments system and quality infrastructure, and its insufficient implementation)
- Industrial property rights: insufficient protection of companies from EU market

Internal Market

- Legal gaps and insufficient harmonization of national legislation with the *acquis* (equal treatment of workers and the right of their family members, coordination of social security schemes, the right to establishment, free movement of self-employed persons, freedom to provide services and recognition of pro-

fessional qualifications, public procurement, cross-border mergers, protection of the right to vote of small shareholders, corporate accounting and audit, company law, geographical indicators, dominant position in the market, state aid, market liberalization, consumer protection and public health)

- Lack of sufficient institutional capacities for implementation of the legal and policy framework (conformity assessment, metrology, public procurement, intellectual and industrial property rights, competition protection, consumer protection and public health)
- Insufficient development and implementation of strategic documents (free movement of workers, public procurement, company law, competition policy, consumer protection and public health)

#### Free movement of goods

- Lack of membership of the Standardization Agency and Department of Metrology in international organizations

#### Free movement of work

- Lack of bilateral agreements, in particular with EU member states, on coordination of social security schemes

#### The right to company establishment and the right to service provision across borders

- Lack of bilateral agreements for mutual recognition of professional qualifications
- Lack of data in the area of service provision (legal acts and regular updated data on services' provision in domestic market)

#### Free movement of capital

- Lack of a comprehensive assessment of legislation (with a view to identifying and addressing possible measures)
- Lack of a SWIFT Code of Kosovo

#### Public procurement

- Initiation of implementation of an e-procurement system
- Lack of clear definition of competences
- Disputed quality of decisions of Procurement Review Body

#### Company Law

- Lack of a law and secondary legislation in the area of corporate governance
- Lack of a full functionality of Kosovo Council on Financial Reporting (including data availability)
- Lack of translation of International Financial Reporting Standards (IFRS)

## The right of intellectual and industrial property

- Insufficient public awareness

## Competition policies

- Lack of state aid institutional structures
- Insufficient awareness of businesses
- Lack of updated data available to public

## Consumer and health protection

- Lack of a comprehensive assessment on implementation of legislation and policies in the area of consumer protection
- Insufficient promotion of legislation, policies and guidelines on protection of consumer rights and implementing mechanisms
- Lack of civil society organizations specialized in the area of consumer protection (at central and local level)
- Insufficient public awareness on consumer rights and mechanisms for their protection
- Lack of updated data on most of the sectors in the area of public health protection

## Customs and Taxation

- Lack of complete customs control in two points in the north of Kosovo and smuggling of goods in that area
- Non implementation of requirements for certificate of origin
- Lack of an electronic customs system (e-Customs)
- Non implementation of customs appealing procedures (to ensure a fair treatment) in a fast, transparent and efficient manner
- High level of fiscal evasion
- Lack of a more advanced system than SIGTAS (Standard Integrated Government Tax Administration System)

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