

Institutional Reform and the Informal Sector (IRIS) Project

Quarterly Report: July 1 - September 30, 1994

INTRODUCTION

The Institutional Reform and the Informal Sector (IRIS) Project was authorized on May 24, 1990 for a period of five years, through a cooperative agreement between the U.S. Agency for International Development (USAID) and the IRIS Center at the University of Maryland at College Park. An accompanying basic ordering agreement allows for AID Missions to buy into the technical assistance activities, to meet objectives specific to the respective country. The goal of the IRIS project is to support institutional reforms that enhance competitive markets and democratic processes. The purpose of the Core cooperative agreement is three-fold and includes the following:

- To promote better institutions (legislative reform, regulatory reform, improved organizational structures, and strengthened decision-making processes);
- To build awareness of the role of institutions in economic development; and
- To expand the knowledge base on the relationship between institutions and economic growth and examine and examine new approaches to institutional reform.

The objectives of both the cooperative agreement and the respective basic ordering agreements are met with a variety of project inputs, defined by their appropriateness to the specific needs of a country or the international development community at large. Organizational development objectives are addressed through publications, workshops, technical assistance, and training. Collaborative research objectives call for designing technical assistance packages. Training needs are met with short term in-country and third-country programs, short-term US programs and/or internships. Information dissemination and outreach objectives are addressed through the IRIS clearing house and the IRIS newsletter. The development of a knowledge base for strategic approaches is furthered through working papers, books, monographs, articles, conferences, workshops, and seminars.

The status of project interventions and the resulting impact is reported to USAID on a quarterly basis, as defined in the cooperative agreement and eight (8) delivery orders currently in effect. The following report provides an overview of project activities and impact for the core project (Section One) and the respective field projects (Section Two) for the period July 1 - September 30, 1994.

SECTION ONE: CORE REPORT

I. PROGRESS TOWARD ACHIEVING THE PROJECT PURPOSES

1. Promoting better institutions

A. Legislative reform initiatives

a. Plans for reporting quarter

- **Chad:** IRIS/Chad would continue to provide technical assistance on business law harmonization and banking secrecy law reform.
- **Nepal: Contract Law.** A draft law was expected to be completed in the next quarter.
- **Poland: Collateral Law.** Official comments would be received and evaluated by the Commission for the Reform of the Civil Code before the draft was ready for submission to Parliament. Planning would be completed for a conference on collateral law and bankruptcy.
- **Russia: Collateral Law.** IRIS/Russia, in collaboration with the European Bank for Reconstruction and Development, would plan a late Fall international conference.

b. Activities during quarter

- **Chad: Business Law Harmonization.** IRIS/Chad continues work with Ministry of Justice legislative commission.
- **Chad: Banking Secrecy Law.** A reform proposal has been completed and is awaiting Government of Chad approval.
- **Nepal: Contract Law.** A revised draft of the Contract Law prepared by the Nepal Law Society incorporates extensive comments from a symposium sponsored by IRIS on May 27 and 28. Because the legislation has yet to be finalized, it is unlikely to be tabled during the first session of the new Parliament. However, because Contract Law has fewer philosophical and political overtones than Company Law, it might be easier to have the bill introduced in Parliament, irrespective of the party that forms the new Government.

- **Poland: Bankruptcy Reform.** In July, IRIS organized the visit of Dr. Cheryl Gray (World Bank) to initiate a study of enterprise restructuring closely connected to IRIS's former work on bankruptcy in Poland. Separately, IRIS and the Juridical Institute are publishing a major review of bankruptcy administration in Poland in time for the November Bankruptcy Conference of the Ministry of Justice. IRIS-Poland will be working closely with Deloitte & Touche's Budapest office which was selected by USAID to administer a regional bankruptcy project.
- **Poland: Collateral Law.** On September 7, 1994, the Commission for the Reform of the Civil Code adopted most of the emendments recommended by IRIS-Poland's collateral law coordinator, Dr. Tomasz Stawecki, and IRIS-consultant Dr. Maciej Tomaszewski to the Jablonna Draft. A new English-language translation was then produced. In addition the Ministry of Justice presented proposals for the organization of the central registry which were also included in the draft.

c. Plans for next quarter

- **Poland: Bankruptcy Law.** A study undertaken in conjunction with the Polish Juridical Institute will be completed in November.

B. Regulatory reform activities

a. Plans for reporting quarter

- **Nepal: Credit Rating Agency.** IRIS consultant Clara Lipson would examine the need for a credit rating agency. Preparations the previous quarter included meetings with the Deputy Governor of the Central Bank (S. P. Shrestha) and a representative of a local joint-venture bank.
- **Nepal: Fertilizer/Petroleum.** As a follow-up to a previous study, a workshop was planned to discuss issues related to subsidy and regulation.
- **Poland: Intellectual Property Reform.** A Fall 2-day seminar would bring together legal and technical experts to examine the legal infrastructure required for the development of the Internet, which would also support the creation of the central lien registry for collateralized lending that has been a major focus of IRIS/Poland.
- **Russia: Collateral Law.** Drawing in part on its experience in Poland, IRIS -- in collaboration with the European Bank for Reconstruction and Development -- would hold a conference in Russia to review the theory underlying secured lending and develop a

model for a Russian collateral registry. As in the related effort in Poland, this initiative will attempt to help overcome many of the barriers that prevent small businesses from being able to borrow from banks.

b. Activities during quarter

- **Nepal: Capital Market Development.** IRIS consultant Ravi Pieris's review of the public share trading operations at the Nepal Stock Exchange showed that the market, during the first four months of its operations, had made steady progress in terms of both share volume and turnover. His report, however, pointed out the need to establish a clearer demarcation of the jurisdiction of the two regulatory bodies, suggested short-term (back-office automation) and long-term (Central Securities Depository) solutions to the problem of the delay in completing transactions at the Stock Exchange. As a part of its policy advocacy program, IRIS sponsored a "Program for Policymakers on Capital Market Development" organized jointly by the Security Exchange Board of Nepal and the Unit Trust of India. The program was attended by high-level Government officials, including Governor H.S. Tripathy of Nepal Rastra Bank, Hon. P.R. Ligal of the National Planning Commission, and secretaries from various Ministries of the Government. The themes of the conference were three-fold: (1) preconditions for capital market development; (2) the importance of a fair, transparent, and non-duplicating regulatory framework; and (3) the need to educate the general public on developments in the capital market.
- **Nepal: Banking Reform.** IRIS Representative Praveen Dixit has been part of the Ministry of Finance Privatization Cell working group assisting with the restructuring of the Rastriya Banijya Bank, the largest commercial bank in Nepal. The Privatization team, along with consultants from INTRADOS/Price Waterhouse, has prepared an action plan for restructuring this state-owned bank. The decision to restructure was approved by the Council of Ministers based on recommendations made by the Nepal Rastra Bank following the visit of IRIS consultant Paul Rymaszewski. The IRIS representative has also been part of the NRB/ELPS team that is evaluating the operational efficiency of the two Grameen (Rural Development) Banks. He accompanied Prof Latifee from the Grameen Trust of Bangladesh to the Far Western Region Grameen Bank in Dhangadi to examine the operations of the bank.
- **Nepal: Consumer Protection/Antitrust Legislation.** The Consumer Protection Act, which incorporates comments received from a national symposia organized by IRIS and the Nepal Jurists Society, received approval from the Council of Ministers but failed to advance because of the dissolution of Parliament.
- **Nepal: Credit Rating Agency.** IRIS has also been assisting the Nepal Rastra Bank formulate a strategy for establishing a credit rating service in Nepal. IRIS consultant Clara Lipson completed a report (1) recommending that the existing Credit Information

Bureau confine its activities to bank lending information and be placed under the direct supervision of the Nepal Rastra Bank, and (2) describing how a credit rating service could be established in Nepal.

- **Nepal: Environmental Policy.** The Nepali carpet industry is often blamed for Kathmandu Valley's water shortages, environmental pollution, and population overflow. IRIS contracted with ESEC to conduct a study that examines i) reasons for the poor public perception of the industry, ii) how this image can be resolved without relocating the industry, and iii) the factors/incentives that need to be considered if the industry is to be relocated. The study indicated that i) the environmental impact (water and air pollution) of the carpet industry is minimal; ii) strict environmental standards need to be enforced on the carpet washing and dyeing industries; iii) relocation would be greatly facilitated if basic infrastructural facilities (water, phones, and feeder roads) were made available in the proposed relocation sites outside the valley, and iv) time-bound relocation subsidy could be used as an incentive to lure the industry out of the valley. Upon completion of the study, IRIS representative Praveen Dixit was made a member of a high-level task force headed by Hon. Prithivi Raj Ligal to prepare a relocation action plan for submission to the Government.
- **Nepal: Fertilizer/Petroleum.** The IRIS-commissioned follow-up study on fertilizer/POL products was completed, and discussions were held with Hon. Prithivi Raj Ligal, Member National Planning Commission, concerning the next course of action. The study reviews recommendations made in the original study; develops communication strategy to disseminate the need for change; recommends an action plan based on the recommendations; and examines the possibility of private sector involvement in the importation, storage, and sales of fertilizer/POL products. While the study has been completed, implementation will have to wait till after the elections.
- **Nepal: Taxation.** The IRIS representative continues to serve in the Ministry of Finance Value Added Taxes (VAT) Steering Committee. The steering committee oversees the work of the VAT task force which has been focusing on preparing legislation, designing registration forms, and identifying possible implementation bottlenecks. The IRIS representative has reviewed the proposed legislation and has participated in various Harvard/CAER discussions on the subject matter. The IRIS-supported Policy Analysis Wing (PAW) at the National Planning Commission (NPC) has submitted three reports--income tax, octroi, and customs tariff reforms--to the Ministry of Finance for use in the Annual Finance Bill FY 1994/95. The income tax study provides a comprehensive set of recommendations on expanding the tax base, modifying assessment procedures, altering the tax rates and payment system, improving administrative organizations, and introducing legal reforms. Many of these recommendations, especially those relating to tax rates and assessment procedures, were incorporated into the Budget Speech.

- **Poland: Collateral Law.** IRIS-Poland and Norway, SA, a company which works closely with the Norwegian Central Registries, organized a conference for high-level Polish and Lithuanian representatives in Oslo, Norway from September 21-25, 1994. The Polish delegation, lead by Vice-Minister Zdziennicki, participated actively in obtaining information useful to setting up such a system in Poland.¹

c. Plans for next quarter

- **Chad:** IRIS/Chad will continue to provide technical assistance on business law harmonization and lottery regulation.
- **Poland: Intellectual Property Reform.** IRIS/Poland, working in conjunction with the Ministry of Science and the Center for Emerging Technology Enterprises, will publish a model contracts manual for technology commercialization joint ventures.
- **Poland: Intellectual Property Reform.** IRIS will hold a two-day seminar where legal and technical experts to review the legal infrastructure needed for proper development of the Internet network in Poland.

C. Improved organizational structures

a. Plans for reporting quarter

- **Mongolia: Local Government Finance.** Participants in the first in the series of IRIS workshops would prepare a policy paper on intergovernmental grants.
- **Mongolia: Insurance.** The third in a series of workshops would address issues related to insurance, including the need to develop mechanisms of risk-spreading and risk-sharing.

b. Activities during quarter

- **Mongolia: Insurance.** Background research was conducted on existing institutions for insurance in Mongolia, including State agencies, private providers, and the legal framework. Research included interviews with government officials, representatives of private insurance companies, regulatory agencies, academics, members of parliament, and the foreign assistance community. Relevant laws and documents were compiled and

¹ On October 5, 1994 in Chicago, Deputy Prime Minister and Minister of Justice Cimoszewicz told Ronald Dwight, Director of IRIS-Poland that the MOJ intended to sign a contract with the Norwegians to begin setting up a central registry.

translated.

c. Plans for next quarter

- **Chad:** IRIS/Chad will continue to provide technical assistance to an Enterprise Network and an organization of women in private enterprise.
- **Mongolia: Environmental Policy.** Plans will be completed for a fourth workshop, to be held in Ulaanbaatar. Activities for the upcoming quarter will include recruitment of faculty, a meeting of Advisory Council to suggest participants, and identification of counterpart agency in Mongolia to host fourth workshop and provide logistical assistance.
- **Mongolia: Insurance.** An October conference to be held in College Park will introduce Mongolian policy makers to the development, operation, and regulation of insurance markets.

D. Strengthened decision-making processes

a. Plans for reporting quarter

- **India: Enhanced dialogue on policy reform.** The IRIS/India Working Paper series would begin in the upcoming quarter, developing policy-relevant research related to Indian reform efforts and increasing awareness of reform issues among scholars and donor organizations.

b. Activities during quarter

- **India: Enhanced dialogue on policy reform.** Drafts of six policy papers were completed, with the remaining papers undergoing review and revision.

c. Plans for next quarter

- **India: Enhanced dialogue on policy reform.** Policy seminars are to be held in New Delhi at the beginning of December 1994. An IRIS-India Working Paper Series will be initiated, and a background paper on the deregulation of the Indian telecommunications sector will be completed.

2. Disseminating information to build awareness of the role of institutions in economic development

A. Forums, conferences, presentations

a. **Activities during quarter**

Papers presented at Scholarly Meetings by IRIS staff and consultants:

Mancur Olson (Oslo, Norway, August 24) "Scandinavia in the Perspective of the Rise and Decline of Nations"

Mancur Olson (New York, American Political Science Association, September 2) "Interest Group Power in East and West: Why the Transition from Communism Is So Difficult."

Mancur Olson (European Economic Association, Maastricht, September 4) "The Secular Increase in European Unemployment Rates: Increasing Sclerosis in Labor Markets."

Brian Fikkert (U.S. International Trade Commission, September 23) "Reforming India's Technology Policies: Is There a Trade-Off Between Short-Run Efficiency and Long-Run Self-Reliance?"

Mancur Olson (UMCP Institute for Philosophy and Public Policy, September 30) Commentator, Conference on "Consumption, Global Stewardship, and the Good Life."

Training Provided to Scholars from LDCs and the NIS:

- **Chad:** In support of USAID/Chad private sector training activities, participants on US tour.
- **Chad:** Provided technical assistance to women in private enterprise, conducted a needs assessment for a newly created women's business association, and advised on business plan and marketing strategy for a new women-owned private enterprise.
- **Russia: Civil Code.** A two-week program to train Russian judges from the federal and regional levels in commercial law was held in September. This training -- which addressed topics including court administration, civil procedure, and alternate dispute resolution -- will allow Russian judges to implement more efficiently the new Russian Civil Code.
- **Russia: Collateral Law.** A training seminar on collateral law for Russian loan officer trainees was held in July. A study of commercial lending practices by Russian banks complements this project.

b. Plans for next quarter

Conference:

IRIS will sponsor a conference on the topic of "Economic and Political Institutions for Sustainable Development: Implications for Assistance" on October 24-25, 1994, at the New State Building. An agenda is included as an attachment.

Papers to be presented at Scholarly Meetings:

Mancur Olson (Economic History Association, Cincinnati, October 10) "Unrealized Economic Growth."

Mancur Olson (Social Science History Association, Atlanta, October 14) "Capitalism, Socialism, and Democracy: Economic Performance under Dictatorship and Democracy in East and West."

Christopher Clague (Conference: What Is Institutionalism Now?, College Park, October 15) "Economics, Institutions, and Development"

Brian Fikkert (Columbia University, November 14) "Reforming India's Technology Policies: Is There a Trade-Off Between Short-Run Efficiency and Long-Run Self-Reliance?"

B. Publications (articles, monographs, books, working papers, newsletter)

a. Activities during quarter

Draft book: Russell Hardin, Contested Community, July 1994.

Working papers:

Peter C. Ordeshook, "Institutions and Incentives: The Prospects for Russian Democracy," IRIS Working Paper No. 115, June 1994.

Rakesh Basant and Brian Fikkert, "The Effects of R&D, Foreign Technology Purchase, and Spillovers on Productivity in Indian Firms," IRIS Working Paper No. 116, June 1994.

Charles Kahn and Emilson C.D. Silva, "Brazilian Tax Collection Reform and Its Effects," IRIS Working Paper No. 117, June 1994.

Charles Kahn and Emilson C.D. Silva, "Optimal Provision of Public Goods under Costly Exclusion and Corruption," IRIS Working Paper No. 118, July 1994.

Barry Ames, "Electoral Strategy under Open-List Proportional Representation," IRIS Working Paper No. 119, July 1994.

Barry Ames, "Wheeling, Dealing, Stealing and Appealing: Bases of Voting in the Brazilian Congress," IRIS Working Paper No. 120, July 1994.

Louis Putterman, "Social Capital and Development Capacity: Relating Cultural Change and Economic Development with an Application to Rural Tanzania," IRIS Working Paper No. 121, July 1994.

Donald J. Robbins, "Worsening Relative Wage Dispersion in Chile During Trade Liberalization: Supply or Demand Driven Inequality," IRIS Working Paper No. 122, July 1994.

Donald J. Robbins, "Relative Wage Structure in Chile, 1957 - 1992: Changes in the Structure of Demand for Schooling," IRIS Working Paper No. 123, July 1994.

Donald J. Robbins, "A Note on Recent Policies for Higher Education in Chile," IRIS Working Paper No. 124, July 1994.

Jean-Marie Baland and Ashok Kotwal, "The Political Economy of Underinvestment in LDCs", IRIS Working Paper No. 125, August 1994.

Abhijit V. Banerjee, "A Theory of Misgovernance," IRIS Working Paper No. 126, August 1994.

Martin C. McGuire and Mancur Olson, Jr., "The Economics of Autocracy and Majority Rule: The Invisible Hand and the Use of Force," IRIS Working Paper No. 127, August 1994.

Timothy Besley and Alec Levenson, "The Role of Informal Finance in Household Capital Accumulation: Evidence from Taiwan," IRIS Working Paper No. 128, August 1994.

Jack H. Nagel, "Predicting the Political Consequences of Electoral Reform: How Many Parties Will New Zealand Have under Proportionate Representation," IRIS Working Paper No. 129, August 1994.

Gregory Clark, "Agrarian Institutions and Agricultural Productivity: Africa in the European Mirror," IRIS Working Paper No. 130, September 1994.

Brian Fikkert, "An Open or Closed Technology Policy? The Effects of Technology Licenses, Foreign Direct Investment, and Domestic and International Spillovers on R&D in Indian Firms,"

IRIS Working Paper No. 131, September 1994.

Karla Hoff and Joseph E. Stiglitz, "Some Surprising Analytics of Rural Credit Markets," IRIS Working Paper No. 132, September 1994.

David Stark, "Recombinant Property in East European Capitalism," IRIS Working Paper No. 133, September 1994.

Donald Cox, Emmanuel Jimenez, and Wlodek Okrasa, "Family Safety Nets During Economic Transition: A Case Study of Poland," IRIS Working Paper No. 134, September 1994.

Martin Neil Bailey, "The Importance of Institutions in Long Term Growth," IRIS Working Paper No. 135, August 1994.

Avner Greif, "On the Political Foundations of the Late Medieval Commercial Revolution: Genoa During the Twelfth and Thirteenth Centuries," IRIS Working Paper No. 136, September 1994.

IRIS Miniconference on "The Paradoxes of Poverty," May 27, 1994, IRIS Working Paper No. 137.

IRIS Reprints:

Peter C. Ordeshook and Olga V. Shvetsova, "Ethnic Heterogeneity, District Magnitude, and the Number of Parties," *American Journal of Political Science*, vol. 38, No. 1, pp.100-23, February 1994. IRIS Reprint No. 46.

Mancur Olson, "Why has the Economic Performance of Spanish-speaking and English-Speaking Countries Been so Different?" *Institutional Roots of the Political Economy of Costa Rica*, Jorge Corrales Quesada, ed., published by CIAPA, IRIS, and the Legislative Assembly of Costa Rica, chapter 9, 1993. IRIS Reprint No. 47.

Mancur Olson, "Por Que ha sido tan Diferente el Desempeno Economico entre los Paises de Habla Hispana y Los de Habla Inglesa?" *Raices Institucionales de la Politica Economica Costarricense* Jorge Corrales Quesada, ed., published by CIAPA, IRIS, and the Legislative Assembly of Costa Rica, chapter 9, 1993. IRIS Reprint No. 47.A.

Karla Hoff, "The Second Theorem of the Second Best," *Journal of Public Economics*, Vol.45, pp. 223-242., 1994. IRIS Reprint No. 48.

Andras Nagy, "Import Liberalization in Hungary," *Acta Oeconomica*, vol. 46 (1-2) 1994, pp. 1-26. IRIS Reprint No. 49.

Additional publications by IRIS staff and fellows include:

Brian Fikkert, "World Trade: The Uruguay Round," *The Public Justice Report*, vol 17, no. 5, September-October.

Brian Fikkert, "Recent U.S. Trade Policy: Getting Tough at What Price," *The Public Justice Report*, vol. 17, no. 6, November-December.

To improve the accessibility of IRIS research, particularly for USAID missions and host country scholars and officials, summaries of 162 IRIS working papers, reprints, and country reports and full-text copies of 29 papers were made available electronically via anonymous FTP. Instructions for accessing this information were included in the Summer newsletter and publications lists also distributed to USAID missions in the quarter.

A summer volume of the IRIS Update was mailed in September to an expanded list of USAID personnel, including in particular many more mission directors and economists than IRIS has previously reached. The possibility of electronic dissemination of newsletter material was explored with CDIE.

3. Expanding the knowledge base on the relationship between institutions and economic growth and examining new approaches to institutional reform.

A. Research

a. **Activities during quarter**

The IRIS Index Project: Two research projects in progress, entitled "Institutions and Economic Performance: Property Rights and Contract Enforcement" and "Democracy, Autocracy, and Development: Some Empirical Findings," will be presented to an audience of scholars and development practitioners from USAID, international donors, and others in an October 24-25 conference in Washington, DC. The Knack-Keefer paper "Inequality, Property Rights, and Growth" will be presented at the Meetings of the American Economic Association in January.

Additional areas of on-going research by IRIS staff and fellows include an examination include an examination of the impact of caste on labor and tenancy markets in rural India (Anand Swamy and Brian Fikkert); the relation between income and literacy growth in India (Swamy); the impact of liberalization of India's technology policies on self-reliance and welfare (Fikkert); and several issues related to China's successful economic reforms, including industrial agglomeration and the effects of training and compensation on labor turnover (Fikkert). Mancur Olson (with Martin McGuire) is currently investigating taxation and public good provision in autocracies and

democracies.

B. Scholarships/Internships

a. **Activities during quarter**

ii. PROJECT IMPACT DURING REPORTING QUARTER:

- **Armenia: Market Environment.** IRIS placed two long-term advisors (economics) in Yerevan to assist in the establishment of institutional development of the Armenian Center for Economic Policy Research and Analysis (CEPRA). CEPRA supports Armenian activities by funding studies by Armenian economists on GNP accounting, taxation, and the agriculture sector, assisting Armenia in preparations for negotiations with the IMF and orienting a banker training program with respect to GAPP accounting standards.

CEPRA AND IRIS made arrangements for the Prime Minister of Armenia, Hrant Bagratian, along with several colleagues, to attend the World Symposium on Trade Efficiency in Columbus, Ohio, October 17-21. The symposium was on reducing the costs of international trade by exploiting new information technologies.

CEPRA has been asked to provide assistance for a conference for the working group on Cooperation in Science and Technology under the Black Sea Economic Coordination (BSEC), November 10-11 in Yerevan.
- **Nepal: Company Law.** The IRIS-assisted Company Law was to be one of the first pieces of legislation to be tabled before the summer session of Parliament. It had received clearance from the Council of Minister after the Ministry of Industry acquiesced to the request of the Ministry of Law and Justice to table it as an amendment to existing legislation rather than as a new piece of legislation. The future of this bill depends on the Government that comes into power following the elections. If the ruling Congress Party was to again form the Government, then the bill could, in all likelihood, be passed during the first sitting of the new House in December. If the opposition Communists Party was to come to power, then there might be changes to the Bill, especially to provisions that require minimum regulations on private companies.
- **Nepal: Consumer Protection.** The future of this legislation looks promising. Both the ruling and opposition parties would like to see a consumer protection legislation soon. However, whereas the current version focuses on consumer protection in terms of disclosure (adulteration, product origin, expiry dates), deception (false promotion, concealment of facts, duplication), and safety (health hazard, physical injury), the version prepared by the Opposition concentrates on price control.

- **Poland: Central Registry.** The organization of a central lien registry is a key portion of collateral law reform. Over the summer, IRIS-Poland and Norway, SA, a company which works closely with the Norwegian Central Registries, organized a conference for high-level Polish and Lithuanian representatives² in Oslo, Norway from September 21-25, 1994. The Polish delegation, lead by Vice-Minister Zdziennicki, participated actively in obtaining information useful to setting up such a system in Poland.³
- **Russia: Market Environment.** IRIS is in the process of placing three LTAs (economists and lawyers) to assist the Working Center for Economic Reform (WCER) in development of a Policy Analysis Unit (PAU) on natural monopolies to undertake the formulation and evaluation of policy options for regulatory reform in specific sectors. Following passage of a law on natural monopolies (submitted to Russian parliament in July, 1994) considerable work will need to be done in designing and implementing appropriate sector-specific regulatory frameworks, institutions and policies. PAU will review the current situation of industries or sectors considered to be natural monopolies, formulate proposals for the design and implementation of industry-specific regulatory regimes for natural monopoly industries, provide advice, technical assistance and training to recently formed federal energy commission.
- **Russia: Market Environment.** IRIS arranged a two week workshop in Washington, DC on price regulation policy which was attended by Russian economists and government officials (September 5-16). Members of the Duma, Duma Economic Committee staff and Western experts reviewed the role of price regulation in a market economy. An understanding was achieved regarding the significant disadvantages of widespread government regulation and the arguments against it and how to limit the damage such regulation could do.
- **Ukraine: Market Environment.** IRIS has provided one long term advisor (lawyer) and is in the process of placing two more, who will serve as advisors to the Antimonopoly Committee of the Ukrainian government. IRIS has also provided several short term advisors on unfair competition to assist with a draft law for parliament on transportation competition issues. An IRIS trade regulation expert also assisted in the preparation of a draft decree to specify the minimum content of advertising of investment funds.
IRIS arranged and conducted a training tour for 12 Ukrainian Customs officials, October 5-14, 1994. The officials spent time at the U.S. Customs Service headquarters and Customs field centers in California, New York and Maryland. Also included were

² See Attachment I, list of participants.

³ On October 5, 1994 in Chicago, Deputy Prime Minister and Minister of Justice Cimoszewicz told Ronald Dwight, Director of IRIS-Poland that the MOJ intended to sign a contract with the Norwegians to begin setting up a central registry.

several international airports and seaports. Instruction and demonstrations included such topics as customs organization; establishment of ports of entry; personnel administration, including requirement, selection, hiring, and controls; information management; automated import procedures; free trade zones; bonds; and passenger and cargo clearance. This work is part of a broader program to assess the training and equipment needs of Ukraine Customs as Ukraine moves toward GATT membership.

III. OTHER ISSUES: Administrative, technical, and/or financial issues that might need further explanation and/or USAID attention.

SECTION TWO: QUARTERLY FIELD REPORTS:
Chad, India, Mongolia,
Nepal, Poland, and Russia



**ECONOMIC AND POLITICAL INSTITUTIONS
FOR SUSTAINABLE DEVELOPMENT:**

IMPLICATIONS FOR ASSISTANCE

OCTOBER 24-25, 1994
EAST AUDITORIUM, NEW STATE BUILDING
2201 C STREET, NW
WASHINGTON, DC 20523

Monday A.M.

9:00 Opening Remarks: Carol Lancaster, Deputy Administrator, USAID

9:20 I. ECONOMIC AND POLITICAL INSTITUTIONS AS RULES OF THE GAME

Recent developments in the analysis of institutions and their relationship to economic development... institutions as structures of incentives... individuals and organizations are viewed, along the lines of the New Institutional Economics, as making choices about which rules to obey and whether to work to change the rules... session will describe insights about development that have emerged from this new approach.

- A. Mancur Olson, University of Maryland and IRIS, "An Intellectual Framework for Sustainable Development"
- B. Christopher Clague, University of Maryland and IRIS, "The New Institutional Economics and Economic Development"

Discussant: Carol Lancaster

10:30 II. EFFECTS OF SOCIETAL INSTITUTIONS ON ECONOMIC DEVELOPMENT: EMPIRICAL EVIDENCE

New statistical evidence that societal differences in institutions profoundly affect economic outcomes... new measures of the state of property rights and contract enforcement in a large sample of countries and their effects on rates of growth and investment... the concept of social capital, which is closely related to the institutional framework... empirical examples of the effects of social capital on economic outcomes.

- A. Christopher Clague, Philip Keefer, Stephen Knack,* and Mancur Olson, University of Maryland and IRIS, "Institutions and Economic Performance: Property Rights and Contract Enforcement"
- B. Robert Putnam, Harvard University, "Social Capital and Sustainable Development: A Theoretical Sketch with Empirical Illustrations"

Discussants: Norman Nicholson, USAID; Hadi Esfahani, World Bank

12:00 Keynote Address: Jim Hoagland, *Washington Post*

Monday P.M.

**III. REFORM AND SUSTAINABILITY OF LOCAL INSTITUTIONS:
IRRIGATION, HEALTH, AND CREDIT MARKETS**

Conditions under which local organizations become viable or sustainable and conditions under which they disintegrate... in terms of the institutional approach presented in Session I, the question is, under what conditions do local organizations become institutions?... in what ways can external assistance strengthen local institutions and avoid weakening or destroying them?... specific examples of irrigation users' associations, health services delivery systems, and microenterprise programs.

1:30 PART I

- A. Elinor Ostrom, Indiana University, "Investing in Capital, Institutions and Incentives"
- B. Jonathan Isham, Deepa Narayan and Lant Pritchett, World Bank, "Does Participation Improve Project Performance? Empirical Evidence from Project Data"
- C. Melinda Smale,* International Maize and Wheat Improvement Center (Mexico) and Vernon Ruttan, University of Minnesota, "Cultural Endowments, Institutional Renovation, and Technical Innovation: The 'Groupements Naam' of Yatenga, Burkina Faso"

Discussant: Jerome Wolgin, USAID

3:30 PART II

- D. Thomas Bossert, University Research Corporation, "Sustainability Through Health Reform: What Can Donors Do?"**
- E. Elisabeth Rhyne, USAID, "Microenterprise Finance as Institution-Building"**

Discussants: Kenneth Schofield, USAID; Vernon Ruttan; Praveen Dixit, IRIS/Nepal

5:00-6:30 RECEPTION

Tuesday A.M.

9:00 IV. WHAT COMPONENTS OF DEMOCRACY CONTRIBUTE TO ECONOMIC DEVELOPMENT?

There are different types of autocracies and different types of democracies... how do the characteristics of these regimes affect the institutions of property rights and contract enforcement, which were shown in Session II to have an important influence on economic progress?... theoretical arguments and statistical evidence on the relationships between regime characteristics and economic outcomes... implications for donor policies.

- A. Christopher Clague, Phillip Keefer,* Stephen Knack, and Mancur Olson, "Institutions and Economic Performance: A New Look at Democracies and Growth"**
- B. Stephan Haggard, UCSD, "Democracy, Economic Policy, and Performance"**

Discussants: Joan Nelson, ODC; Larry Garber, USAID

10:45 V. IMPLEMENTING INSTITUTIONAL REFORM IN FORMERLY COMMUNIST SOCIETIES

Societies in transition from communism face the problem of creating new institutions on a massive scale... gaps between policy pronouncements and implementation, between rhetoric and reality, between expectations and realizations, are typically larger than in other societies attempting economic and political reforms... what are the implications for these economies and for donors of an institutional approach to economic reform?

- A. Peter Murrell* and Georges Korsun, University of Maryland and IRIS, "The Transition to a Market Economy in Mongolia"**
- B. Charles Cadwell, IRIS, "Implementing Legal Reforms in Transition Economies"**

Discussants: Diane LaVoy, USAID; Ronald Dwight, IRIS/Poland

12:00 Keynote Address: Joseph Stiglitz, Council of Economic Advisors

Tuesday P.M.

1:30 VI. HOW CAN THE NEW INSTITUTIONAL ECONOMICS BE USED TO IMPROVE GOVERNMENTAL PERFORMANCE?

Institutional approach presented at this conference is very different from the strategy of "institution building" popular among donor agencies in the 1960s and 1970s... the new approach is guided by advances in the economics of information, the economics of organization, and the rational choice perspective in political science... these ideas lead to concrete proposals for improving the performance of government bureaucracies in less-developed countries... experiences of particular countries with performance-based rewards will be considered.

- A. Vito Tanzi* and Anthony Pellechio, IMF, "The Reform of Tax Administration Reform"
- B. Robert Klitgaard, University of Natal, South Africa, "Information and Incentives in Institutional Reform"
- C. Margaret Levi* and Richard Sherman, University of Washington, "Rational Compliance with Rationalized Bureaucracy"

Discussant: Samuel Skogstad, Georgia State University

3:15 VII. IMPLICATIONS FOR DONORS' POLICIES AND PROGRAMS

What are the implications of the institutional approach presented at this conference for donor agencies? If this institutional approach is fruitful, how, if at all, should AID and other donors change the way they conduct business?

- A. Robert Picciotto, World Bank, "Putting Institutional Economics to Work: From Participation to Governance"
- B. Mancur Olson, IRIS, "Perforating the Stovepipe: How to Integrate Institutional Economics into AID Programming"
- C. Panel Discussion: Colin Bradford, USAID; Janet Ballantyne, USAID

[* denotes presenter for multi-author papers]

IRIS CENTER, 2105 MORRILL HALL, UNIVERSITY OF MARYLAND, COLLEGE PARK, MD 20742

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Quarterly Field Report: Chad

I. ADMINISTRATIVE DATA

Reporting period: July 1, 1994 - September 30, 1994

BOA No. ANE-0015-R-1019-00

Delivery Order No. 07

AID project office: G/EG/SMIE

AID Office funding the delivery order: G/EG/SMIE

AID Office Project: Institutional Reform and the Informal Sector (IRIS) Project

II. PERFORMANCE INFORMATION

1. Project purpose summary statement.

A. The purpose of the IRIS project in Chad is to support the Government of Chad's ("GOC") promotion of the private sector by providing technical assistance, conducting studies, identifying policy changes to be implemented and designing the follow-on institution-building efforts to implement the strategy and programs from the multi-donor private sector roundtable. This complements the broader purposes and scope of the IRIS project, which are to promote better institutions, to build increased international awareness of the role of institutions in economic development and to expand the knowledge base on the relationship between institutions and economic growth and examine new approaches to institutional reform.

B. A key objective of the USAID/Chad development strategy is to encourage development of the private sector as the primary engine for fostering economic growth in the country. To this end, the IRIS/Chad project provides technical assistance to business associations and groups and to government legislative commissions working on legal and economic reform issues, to promote an environment more conducive to private sector development.

C. During this reporting quarter, the IRIS/Chad project focussed on three major activities. The first involved providing technical assistance to a recently created Enterprise Network for Chadian entrepreneurs. In addition to formulating an action plan for the coming year and supplying documents and video tapes on current business topics, the IRIS/Chad project arranged for an outside technical consultant to provide training for Network members in lobbying and strategic planning. A second major activity involved working with, and supplying comparative legal materials to, a Ministry of Justice legislative commission for a regional project to harmonize business laws in Francophone Africa. Finally, a third focus of activity targeted technical assistance to women-owned enterprises and business associations.

2. Progress report

A. Technical implementation¹

Activities planned for the reporting quarter	Current status	Explanations
Distribute customs fraud study.	4	USAID/Chad views distribution as controversial.
Provide technical assistance on business law harmonization.	2	Continuing work with Ministry of Justice legislative commission.
Provide technical assistance on banking secrecy law reform.	1	Reform proposal now awaiting GOC approval.
Provide technical assistance to Executive Secretariat.	2	Executive Secretariat still pending UNDP project funding.
Provide technical assistance to Enterprise Network.	2	Outside consultant provides training and advice. Three additional Network members funded by USAID/Chad for quarterly meeting. New library started.
Provide technical assistance to women in private enterprise.	2	Needs assessment for newly created women's business association, advising on business plan and marketing strategy for a new women-owned private enterprise.
Assist USAID/Chad private sector training activities.	1	Private sector participants on US tour.
Participate in roundtable discussions on export law reform.	1	Completed.

Current status key:

- (1) Action completed
- (2) Action in process
- (3) Action delayed
- (4) Action canceled

¹ Status of activities as defined in the delivery order.

Activities planned for next quarter	Estimated Completion Date	Entity responsible for action
Provide technical assistance on business law harmonization.	2/95	IRIS/Chad
Provide technical assistance on lottery regulation.	12/94	IRIS/Chad
Provide technical assistance to Executive Secretariat.	2/95	UNDP
Provide technical assistance to Enterprise Network.	2/95	IRIS/Chad
Provide technical assistance to women in private enterprise.	2/95	IRIS/Chad

B. Project Administration

Activities planned for reporting quarter	Current Status	Explanations
Submit quarterly report.	1	Completed 7/94
Submit annual work plan.	1	Plan covers 6-month period through 2/95.
Project evaluation.	4	USAID/Chad forgoes scheduled evaluation due to project phase out.

Current Status Key:

- (1) Action completed
- (2) Action in process
- (3) Action delayed
- (4) Action canceled

Activities planned for next quarter	Estimated Completion Date	Entity responsible for action
Submit quarterly report	10/94	IRIS/Chad
Submit project property inventory and disposal plan.	12/94	IRIS/Chad

3. Other problems/issues and intended steps toward resolution:

A continuing problem facing the IRIS/Chad project is the slow pace under which the Executive Secretariat is undertaking its private sector advocacy role. A primary constraint is the lack of funding for staff and equipment. Financing has been pending under a UNDP private sector project, which has been under development for over a year. Regular meetings with UNDP officials prompted some progress on project implementation.

Financial reports of the IRIS/Chad project, current through July, 1994 have been submitted to the USAID/Chad Controller and the GDO/SP. The USAID/Chad Controller has been submitting bills of collection for approval to the IRIS/Chad project director who has forwarded them to IRIS/UMCP for payment. No payment delays have occurred during this reporting quarter. With no change in project activities required and sufficient funds remaining through February, 1994, no budget revisions or amendments are necessary.

III. FINANCIAL DATA

Following page.

Quarterly Field Report: IRIS-INDIA

I. ADMINISTRATIVE DATA

Reporting Period: July 1, 1994 - September 30, 1994

BOA Number: ANE-0015-1019-00

Delivery order Number: 13

AID Project Office: G/EG/SMIE (R. Mitchell, 522 SA-2)

AID Office funding delivery order: G/EG/SMIE

AID Office project: Institutional Reform and the Informal Sector (IRIS) Project

II. PERFORMANCE INFORMATION

1. Project purpose summary statement:

- A. Project Purpose: The objective of this program is to increase the understanding and awareness of the institutional aspects of economic issues in India and to generate a better knowledge base for decisions about economic policy. This will be achieved by carrying out a collaborative research program between Indian and American scholars. The program examines the current institutional framework in India, explores whether this framework constrains the economic liberalization process and determines whether there is need for reform. IRIS will disseminate the research results on the effects of institutions on economic growth to the research community, to politicians and government officials, to the media and the public in India.
- B. Relationship to USAID Program Strategy: The USAID program strategy in India is to help India make progress towards sustainable development by focusing on three primary program objectives: accelerating broad-based economic growth, stabilizing population growth, and protecting the environment. IRIS activities in India--as a part of the Mission's Technical Assistance and Support Project (TASP)--contribute to Mission objectives, especially to the objective of accelerating broad-based economic growth by providing economic policy research results and advocacy to increase the competitiveness of the Indian economy and to improve financial and regulatory environment.

C. Progress toward Project Purpose during the Reporting Period: The purpose of this project, namely increasing the understanding and awareness of the role of institutions in economic development in India and generating a better knowledge base for decisions about economic policy, has been furthered during the reporting period. Six policy papers commissioned earlier were completed. The work to disseminate the research results started during the period. The task of revising these papers into a publishable form was commenced. The work continued on the book which will include the best papers of the program. The plans for policy seminars to be held in New Delhi at the beginning of December 1994 were also drawn. Finally, to have adequate time to disseminate the research results through seminars and publications, IRIS applied for and was approved a 60-day no-cost extension of the project period.

2. Progress report

A. Technical Implementation¹

Activities Planned for Reporting Quarter	Current Status	Explanations (Problems, steps to resolve, etc.)
First Drafts of Six (6) Policy Papers Completed	1	See, Attachment I. <i>Note: Papers not circulated prior to their revision.</i>
Review and Revision of All the First Drafts and Completed Papers	2	
Book	2	IRIS is editing the best policy papers and publishing them as a book.
Launching of IRIS/India Working Paper Series	2	Revision of papers necessary before publication.
Preparation of Brief Background Paper on the Deregulation of the Indian Telecommunications Sector	2	IRIS Summer Intern working on the paper.
Planning of Policy Seminars	2	Scheduled for December 7, 1994. Draft Agenda sent to USAID/India.

¹ Status of activities as defined in the delivery order.

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Worldnet Tele-Video Conference	4	Instead of a tele-video conference policy seminars will be organized in New Delhi.
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Current Status Key:

- (1) Action Completed
- (2) Action in process
- (3) Action delayed
- (4) Action cancelled

Planned Activities for Next Quarter	Estimated Completion Date	Entity Responsible for Action
Completion of Policy Papers	10/31/94	Scholars
Review and Revision of Papers	12/31/94	IRIS and Scholars
Launching of IRIS-India Working Paper Series	12/31/94	IRIS
Book	1/95	IRIS and the Publisher
Policy Seminars	12/7/94	IRIS, NIPFP
Preparation of Brief Background Paper on the Deregulation of the Indian Telecommunications Sector	12/31/94	IRIS Summer Intern

B. Project Administration

Activities Planned for Reporting Quarter	Current Status	Explanations (Problems, steps to resolve, etc.)
Application for a 60-day No-Cost Extension	1	To have adequate time to disseminate the research results through seminars and publications (working papers and book), IRIS applied for a 60-day no-cost extension.
Planning of Policy Seminars	2	
Follow-On Work on Proposal for a Comprehensive Collaborative Policy Research Program submitted to USAID/India	2	
Financial Management of Completed Contracts	<u>2</u>	

Current Status Key:

- (1) Action Completed
- (2) Action in process
- (3) Action delayed
- (4) Action cancelled

Planned Activities for Next Quarter	Estimated Completion Date	Entity Responsible for Action
Organization of Policy Seminars in New Delhi	12/94	IRIS
Follow-On Work on Proposal for a Comprehensive Collaborative Policy Research Program submitted to USAID/India	12/94	IRIS, USAID
Financial Management of Completed Contracts	1/95	IRIS

3. Other problems/issues and intended steps toward resolution: Explain any less-than-anticipated accomplishments, problems or constraints, and actions proposed to remedy/address them (in addition to those addressed in preceding charts.)

III. FINANCIAL DATA

Following page.

- IV. ATTACHMENTS (demonstrating project progress toward defined objectives -- such as newspaper articles, relevant studies, seminar evaluation results, etc.)

Attachment I: Status of sponsored policy papers
(Note: Papers not circulated prior to revision.)

ATTACHMENT I to the IRIS-India Quarterly Report for July-September 1994

STATUS OF SPONSORED POLICY PAPERS

SCHOLAR	TOPIC	STATUS
*Dr. Anil Deolalikar (University of Washington) *Dr. Prem Vashishtha (National Council for Applied Economic Research)	The Cost and Financing of Government Health Services in India: Potential Reforms and Problems.	First Draft to be completed by October 31, 1994
*Dr. Ashok Guha (Jawaharlal Nehru University)	The Design of Decision Making: A Study in Economic Administration with Special Reference to Indian Economic Reform.	First Draft Completed; Editing in Progress
*Dr. Ashok Gulati (National Council for Applied Economic Research) *Dr. Pradeep Sharma (Planning Commission)	Need for Reform in Indian Foodgrain and Rice Marketing?: Case of Food Corporation of India.	First Draft Completed; Editing in Progress
*Dr. Kenneth Kletzer *Dr. Nirvikar Singh (University of California, Santa Cruz)	The Political Economy of Indian Fiscal Federalism.	First Draft Completed; Editing in Progress
*Dr. Arindam Das-Gupta (National Institute of Public Finance and Policy) *Dr. Dilip Mookherjee (Indian Statistical Institute)	Reforms in Indian Income Tax Enforcement.	First Draft to be completed by October 31, 1994.
*Dr. Govinda Rao (National Institute of Public Finance and Policy)	Fiscal Reforms and the Role of Sub-Center Governments.	First Draft to be completed by October 31, 1994.
*Dr. E. Sridharan (Center for Policy Research)	Coalition Theory and Indian Politics: Implications for Public Policy.	First Draft Completed; Editing in Progress

STATUS OF SPONSORED SHORT POLICY PAPERS

SCHOLAR	TOPIC	STATUS
*Dr. Pradeep Agrawal (Indira Gandhi Institute of Development Research)	Regulation and Reform of the Financial Sector in India: An Analysis of the Underlying Incentives.	Completed
*Dr. Isher Ahluwalia (Center for Policy Research)	Industrial and Trade Policy Reforms in India.	Completed
*Dr. Ramaswamy Aiyar *Dr. Hanumantha Rao (Institute for Financial Management and Research, Madras)	Indian Energy Scene--Problems and Prospects.	Completed
*Dr. Kaushik Basu (Cornell University and Delhi School of Economics)	Legal and Institutional Prerequisites of Market Reform in India.	First Draft Completed; Editing in Progress
*Dr. Mrinal Datta Chaudhuri (Delhi School of Economics)	Labor Markets as Social Institutions in India.	Completed
*Dr. Bibek Debroy (National Law School of India University)	Consumer Protection Legislation in Public Utilities in India.	Completed
*Dr. Brian Fikkert (University of Maryland)	Reforming India's Technology Policies: The Impacts of Liberalization on Self-Reliance and Welfare.	Completed
*Dr. Anand Gupta (Indian Institute of Management, Ahmedabad)	Privatization and India's Economic Reforms.	Completed
*Dr. Shashi Kolavalli (Indian Institute of Management, Ahmedabad)	Options for Improving Performance of Irrigation Systems in India.	Completed
*Dr. R.J. Mody (Sardar Patel Institute of Economic and Social Research)	Reforms in Non-Bank Financial Intermediaries.	Completed
*Dr. D.M. Nachane (University of Bombay)	Intellectual Property Rights in the Uruguay Round: An Indian Perspective.	Completed

Quarterly Field Report: Mongolia

I. ADMINISTRATIVE DATA

Reporting Period: July 1 - September 30, 1994

BOA Number: ANE-0015-B-00-1019-00

Delivery order Number: 10

AID Project Office: G/EG/SMIE (R. Mitchell, 522 SA-2)

AID Office funding delivery order: G/EG/SMIE

AID Office project: Institutional Reform and the Informal Sector (IRIS) Project

II. PERFORMANCE INFORMATION

1. Project purpose summary statement:

- A. The project endeavors to strengthen the capacity of key Mongolian decision makers from all spheres of the country's economic life to design and implement institutional reforms during the country's transition to a market economy. To accomplish this purpose a series of workshops and follow-up activities will address topical policy issues and present both general background materials and discussions of specific policy options for development and implementation.
- B. The USAID Program Strategy in Mongolia emphasizes encouragement and strengthening of the process of democratization and the promotion of economic growth. The project actively promotes these broad goals in the following ways. The workshops target a broad spectrum of Mongolians in order both to enable individuals from different sectors to better understand and articulate concerns and to enhance policy discussion and its results. The topical policy issues and corresponding points of institutional reform involve ingredients crucial to economic growth.
- C. The purpose of the project, namely "strengthening capacity of Mongolian decision-makers to design and implement institutional reforms", has been furthered during the reporting period by the development of information and background material in preparation for the third workshop in the series. This workshop will concern "Risk and the Institutions of Insurance" and will be held in College Park, beginning October 3, 1994.

2. Progress report

A. Technical Implementation¹

Activities Planned for Reporting Quarter	Current Status	Explanations (Problems, steps to resolve, etc.)
Meeting of Advisory Council to suggest participants for third workshop.	1	Due to summer vacations, Advisory Council members preferred to make individual suggestions rather than convening for a meeting. Their suggestions were received and forwarded to the AID Representative on September 5, 1994.
Forward participant requests for follow-up technical assistance to the AID Representative in Mongolia.	1	Workshop participants requested assistance in developing procedure for enforcement of the Law on Prohibiting Unfair Competition, and in the development of amendments to the Civil Code. Their request was forwarded to the USAID Representative on September 6, 1994. No response has been received.
Background research on existing institutions for insurance in Mongolia, including State agencies, private providers, and the legal framework.	1	Research included interviews with government officials, representatives of private insurance companies, regulatory agencies, academics, members of parliament, and the foreign assistance community.
Translation and compilation of laws and documents relevant to the third workshop.	1	Copies of these documents can be accessed by contacting James Anderson in Ulaanbaatar or Georges Korsun in College Park.
Design of third workshop, College Park.	1	Tasks included selection of lecturers, curriculum design, and lecture preparations.

¹ Status of activities as defined in the delivery order.

Logistical preparations for third workshop, College Park and Ulaanbaatar.	1	Tasks included the selection of classroom facilities for the third workshop (IRIS building on the UMD campus), hotel facilities and travel arrangements for Mongolian participants. In Ulaanbaatar, tasks included compliance with AID foreign participation requirements and coordination with US consular officer.
Obtain decision from USAID Representative on the subject of the fourth workshop.	1	The USAID Representative reported on August 16, 1994 that he had selected Environmental Economics as the subject of the fourth workshop.
Preparation of Policy Paper on Intergovernmental Grants	1	Workshop participant and Member of Parliament S. Nyamzagd prepared a brief paper on Unconditional Intergovernmental Subsidies in Mongolia.
Participation in a Sectoral Meeting on Management sponsored by UNDP.	1	James Anderson participated in an information exchange organized by UNDP addressing ideas for the Management Development Programme Planning and Policy Process, and the development of a Mongolian Business Development Centre.
Attended a Conference on Renovation of Legislation in Mongolia, sponsored by the Ministry of Justice and the Supreme Court.	1	James Anderson attended this conference at the Government House attended by over one hundred law makers, politicians, and members of the judiciary.
Begin background research for the fourth workshop.	2	Early preparations are aimed at identifying the key issues for Mongolia, and elaborating an appropriate curriculum. Interviews with officials from the Ministry of Nature and Environment, the Ministry of Energy, Geology, and Mining, other state officials, and numerous NGOs were conducted to begin this exercise.

Current Status Key:

- (1) Action Completed
- (2) Action in process
- (3) Action delayed
- (4) Action canceled

Planned Activities for Next Quarter	Estimated Completion Date	Entity Responsible for Action
Conduct workshop on insurance	10/17/94	IRIS- College Park
Continue preparations and background research for workshop on environmental economics.	12/30/94	IRIS-Mongolia
Design of the fourth workshop on "Environmental Policy", to be held in Ulaanbaatar.	12/30/94	IRIS-College Park
Recruitment of faculty for fourth workshop.	12/10/94	IRIS-College Park
Meeting of Advisory Council to suggest participants for fourth workshop.	11/30/94	Advisory Council; IRIS-Mongolia
Identification of counterpart agency in Mongolia to host fourth workshop and provide logistical assistance.	12/1/94	IRIS-Mongolia
Selection of topic for fifth and sixth workshops.	11/20/94	USAID Representative in Mongolia
Research/Workshop development trip to Mongolia by IRIS-College Park staff responsible for fourth workshop.	12/10/94	IRIS-College Park
Research/Workshop development trip to Mongolia by IRIS-College Park staff responsible for fifth workshop.	12/30/94	IRIS-College Park
Preparation of Policy Paper on Intergovernmental Grants	12/1/94	Workshop 1 Participants; IRIS-Mongolia
Forward participant requests for new follow-up technical assistance arising from the third workshop to the AID Representative in Mongolia.	11/15/94	Workshop 3 Participants; IRIS-Mongolia

B. Project Administration

Activities Planned for Reporting Quarter	Current Status	Explanations (Problems, steps to resolve, etc.)
Obtain formal, written approval for a no-cost extension from the USAID Mission Representative.	1	Written approval granted.
Travel to Beijing for the acquisition of supplies.	3	Schedules required that this activity be delayed until after the third workshop.
Initiate new PIOT to release incremental funding for the remainder of project.	2	Request to AID Representative made in August. Action commenced in October.
Hire new Project Assistants for the field office.	1	One full-time assistant (Ms.Sodontogos), and one part-time assistant (Ms. Uyanga) commenced work in September.

Current Status Key:

- (1) Action Completed
- (2) Action in process
- (3) Action delayed
- (4) Action canceled

Planned Activities for Next Quarter	Estimated Completion Date	Entity Responsible for Action
Initiate new PIOT to release incremental funding for the remainder of the project.	11/30/94	USAID Interim Representative William Hardy.
Travel to Beijing for acquisition of office supplies.	10/31/94	IRIS-Mongolia Field Coordinator
Travel to College Park by Field Coordinator on personal leave.	12/31/94	IRIS-Mongolia Field Coordinator

3. Other problems/issues and intended steps toward resolution. None.

III. FINANCIAL DATA: Following page.

Quarterly Field Report: NEPAL

I. ADMINISTRATIVE DATA

Reporting Period: July 1, 1994 - September 30, 1994

BOA Number: ANE-0015B-00-1019-00

Delivery Order Number: 367-0161

AID Project Office: G/EG/SMIE

AID Office funding delivery order:

AID Office project: Institutional Reform and the Informal Sector (IRIS) Project

II. PERFORMANCE INFORMATION

1. Project purpose summary statement:

- A. Project Purpose: To help the Government of Nepal formulate and implement policies that support a pro-market, private sector led economy by providing financial and technical assistance, identifying policy changes to be implemented, and advocating the need for crucial institutional reforms in the judicial and regulatory areas.
- B. Relationship to USAID Program Strategy: The USAID program strategy in Nepal is to help the economy enter a new era of economic prosperity by promoting market reform and addressing the health, education, and other needs of the rural poor. IRIS activities in Nepal contribute to Mission objectives by assisting with expertise on policy reform initiatives conducive to the growth of the private sector. IRIS's assistance on institutional and regulatory reform is especially helpful for small and micro enterprises which are crucial to the success of any poverty alleviation scheme
- C. Progress towards Project Purpose: IRIS-Nepal Project continues to provide Government and private sector organizations expertise on reform initiatives that further economic liberalization. Reform activities that IRIS has been associated with in the past year include assistance on business registration, tax reform, capital market development, and preparation of legislation of Company Law, Contract Law, and Consumer Protection.

IRIS's activities in the last quarter slowed down considerably because of the political turmoil in the country. On July 10, 1994, the Prime Minister Girija Prasad Koirala, after failing to win a crucial vote in Parliament, tendered his resignation to the King and recommended that mid-term polls be held on November 13. The following day the King dissolved the Lower House of Parliament, set November 13 as the election date, and asked the Prime Minister Koirala to head the care-taker Government. All this has led to a great deal of political and administrative uncertainty and has hampered the bureaucracy's zeal to move ahead with reform, especially those in the legal area. The IRIS-Nepal Project, consequently, has also been affected by these developments and has had to adjust to the changing situation.

IRIS representative Praveen Dixit continues to spend afternoons at the Ministry of Finance to help improve communications between the government and donor agencies, and between the Government and the private sector. During the last quarter, most of his time was spent in preparing the Annual Economic Survey and the Budget. Both of these took enormous amounts of time, more so because the budget had to be revised and promulgated as an Ordinance by His Majesty the King following the dissolution of Lower House of Parliament. In addition, he has also had to devote considerable time to other odd and ends such as facilitating the visit of the INTRADOS bank restructuring team, assisting the Government during the IMF's pre-budget mission, and reviewing legislation/policy issues on the Value Added Tax. He has also been appointed a member of the Government's post-budget monitoring team.

2. Progress ReportA. Technical Implementation

Activity	Duration (Months)	Remarks
Tabling of Company Law in Parliament	3	The Lower House of Parliament has been dissolved and mid-term elections are to be held in mid-November 1994.
Tabling of Consumer Protection Act	3	Parliament Dissolved
Carpet Relocation Study	1	Study presented to National Planning Commission. IRIS representative member of high level Government task force.
Assistance in establishing Central Depository System at Nepal Stock Exchange	2	Ravi Pieris's report in the subject matter received. IRIS representative met with the Director and the General Manager of BC Software Systems, Colombo to discuss some of the feasible options.
Banking Reform	2	IRIS representative part of MOF team to restructure Rastriya Banijya Bank. IRIS representative visited Far Western Rural Development Bank with Prof. Latifee of Grameen Trust of Bangladesh.
Policy Analysis Wing(PAW) Octroi Study	1	Study completed but could not be incorporated in budget because of dissolution of Lower House.

Policy Analysis Wing (PAW) Income Tax Study	1	Many of the procedural recommendations included; others to be considered for revised budget in December.
Credit Rating Agency	1	Clara Lipson has submitted her final report. Sent to appropriate authorities.
Liaison with Government officials	on-going	Helping communication between USAID and Ministry of Finance(MOF) as and when needed. Activities includes preparations of annual Economic Survey, Finance Bill (budget), help with VAT, assistance with banking, and capital market reform.
Workshop on Policy makers on Capital Market	1	Government officials attended the workshop. Extensive media and TV coverage.

Current Status Key:

- (1) Action completed
- (2) Action in process
- (3) Action delayed
- (4) Action canceled

Activity	Completion Date	Responsible Agency
Tabling of Company Law	Jan 1995	Ministry of Industry
Tabling of Consumer Protection Act	Jan 1995	Ministry of Supplies
Completion of Contract Law	Dec 1994	Nepal Law Society
Assistance on Central Depository Service at Nepal Stock Exchange	2	IRIS/UOM

Banking Reform	2	MOF Privatization Cell
Establishment of Credit Rating Agency	2	UTI/India, Nepal Stock Exchange, IRIS-Nepal
Liaison with Government officials	2	IRIS-Nepal
Economic Liberalization Project Secretariat Contract Review	2	IRIS,USAID

B. Project Administration

Action Completed	1	IRIS@MOSNEPAL.ERNET.IN
Installing E-mail	1	IRIS@MOSNEPAL.ERNET.IN

Current Status Key:

- (1) Action Completed
- (2) Action in process
- (3) Action delayed
- (4) Action canceled

3. Outstanding problems and issues and intended steps toward resolution:

Currently no outstanding problems.

III. FINANCIAL DATA.

Following page.

IV. ATTACHMENTS.

- 1) Detailed description IRIS/Nepal activities.
- 2) Trip report: Dixit/Latifee review of Grameen Bank operations.

IRIS-NEPAL ACTIVITIES AND ACCOMPLISHMENTS
--FOURTH QUARTER ACTIVITIES, FY 1994--
September 28, 1994

I. **BACKGROUND** The primary objective of the IRIS-Nepal project is to help the Government of Nepal formulate and implement policies that support a pro-market, private sector led economy by providing financial and technical assistance, identifying policy changes to be implemented, and advocating the need for crucial institutional reforms. Reform activities that IRIS has been associated with in the past year include assistance on business registration, tax reform, capital market development, and preparation of legislation on Company Law, Contract Law, and Consumer Protection.

II. **FOURTH QUARTER ACTIVITIES AND ACCOMPLISHMENTS** IRIS's activities in the last quarter slowed down considerably because of the political turmoil in the country. On July 10, 1994, the Prime Minister Girija Prasad Koirala, after failing to win a crucial vote in Parliament, tendered his resignation to the King and recommended that mid-term polls be held on November 13. The following day the King dissolved the Lower House of Parliament, set November 13 as the election date, and asked Prime Minister Koirala to head the care-taker Government. All this has led to a great deal of political and administrative uncertainty and has hampered the bureaucracy's zeal to move ahead with reform, especially those in the legal area. The IRIS-Nepal project, consequently, has also been affected by these developments and has had to adjust to the changing situation.

Company Law. The IRIS-assisted Company Law was to be one of the first pieces of legislation to be tabled before the summer session of Parliament. It had received clearance from the Council of Minister after the Ministry of Industry acquiesced to the request of the Ministry of Law and Justice to table it as an amendment to existing legislation rather than as a new piece of legislation. The future of this bill depends on the Government that comes into power following the elections. If the ruling Congress Party was to again form the Government, then the bill could, in all likelihood, be passed during the first sitting of the new House in December. If the opposition Communists Party was to come to power, then there might be changes to the Bill, especially to provisions that require minimum regulations on private companies.

Contract Law. IRIS has received a revised draft of the Contract Law prepared by the Nepal Law Society. This draft incorporates extensive comments from a symposia organized by the Nepal Law Society and sponsored by IRIS. The symposia--held on May 27 and 28--was attended by over 100 experts, including IRIS Associate Directors Phil Keefer and Thierry Van Bastelear, and formed a crucial part of the public awareness and feedback campaign that IRIS encourages in all of its reform activities. The symposia and statements of the IRIS representatives were reported in many local newspapers, magazines, and in the evening news. Because the legislation has yet to be finalized, it is unlikely to be tabled during the first session of the new Parliament. However, because Contract Law has less philosophical and political undertones than Company Law, it might be easier to have the bill introduced in Parliament, irrespective of the party that forms the new Government.

Consumer Protection/Antitrust Legislation. The Consumer Protection Act had finally received approval from the Council of Ministers and was to be tabled in the summer session of Parliament. But, because of the dissolution of Parliament, this could not be accomplished. The version that has been prepared by IDMA with IRIS assistance incorporates comments received from a national symposium organized on May 30 by IDMA and the Nepal Jurists Society. The symposium received extensive national coverage and was attended by representatives of various Governmental and private sector organizations as well as IRIS representatives Phil Keefer and Thierry Van Bastelear. The future of this legislation looks promising. Both the ruling and opposition parties would like to see a consumer protection legislation soon. However, whereas the current version focuses on consumer protection in terms of disclosure (adulteration, product origin, expiry dates), deception (false promotion, concealment of facts, duplication), and safety (health hazard, physical injury), the version prepared by the Opposition concentrates on price control. One potential problem: a lot of the current initiative on consumer protection is because of the personal interest of the current Minister of Supplies; without him, things could be different.

Fertilizer/Petroleum (POL) Products. The IRIS commissioned follow-up study on fertilizer/POL products has been completed. Subsequently, discussions were held with Hon. Prithivi Raj Ligal, Member National Planning Commission, concerning the next course of action. The study reviews recommendations made in the original study; develops communication strategy to disseminate the need for change; recommends an Action Plan based on the recommendations; and examines the possibility of private sector involvement in the importation, storage, and sales of fertilizer/POL products. While the study has been completed, implementation will have to wait till after the elections. Carpet Industry Public perception of the Nepali carpet industry is not very favorable. The industry is often blamed for Kathmandu Valley's water shortages, environmental pollution, and population overflow. Consequently, there has been considerable pressure to relocate the industry outside the Valley. IRIS contracted with ESEC to conduct a study that examines, among others, three issues related to the industry: i) what are the reasons for the poor public perception of the industry, ii) can this image be resolved without relocating the industry, and iii) what are the factors/incentives that need to be considered if the industry is to be relocated. Some of the findings of the study were: i) the environmental impact (water and air pollution) of the carpet industry is minimal; ii) strict environmental standards need to be enforced on the carpet washing and dyeing industries; iii) relocation would be greatly facilitated if basic infrastructural facilities (water, phones, feeder roads) were made available in the proposed relocation sites outside the valley, and iv) time-bound relocation subsidy could be used as an incentive to lure the industry out of the valley. Upon completion of the study, IRIS representative Praveen Dixit was made a member of a high-level task force headed by Hon. Prithivi Raj Ligal to prepare a relocation action plan for submission to the Government.

Taxes. The IRIS representative continues to serve in the Ministry of Finance Value Added Taxes (VAT) Steering Committee. The steering committee oversees the work of the VAT task force which has been focusing on preparing legislation, designing registration forms, and identifying possible implementation bottlenecks. The IRIS representative has reviewed the proposed legislation and has participated in various Harvard/CAER discussions on the subject matter.

Capital Market Development. IRIS consultant Ravi Pieris was in Kathmandu during June to review the public share trading operations at the Nepal Stock Exchange with a view to assisting the Exchange and the Securities Board in resolving any operational problems that they may have confronted since opening the trading floor in January 1994. Pieris reported that the market, during the first four months of its operations, had made steady progress with both share volume and turnover reflecting a fairly substantial growth. The report, however, points out that a number of measures should be pursued by both the Exchange and the Board to establish a clearer demarcation of the jurisdiction of the two bodies. In particular, provisions relating to listing as well as continuing listing by-laws, and the process of admitting new companies to the exchange should be reviewed.

Other recommendations made by Pieris concern the delay in completing transactions at the Stock Exchange. In this context, he recommends both short term (back-office automation) and long term (Central Securities Depository) solutions to the problem. After distributing Pieris's report, IRIS representative organized a meeting between the executive chiefs of both the Securities Board and the Stock Exchange to resolve the demarcation issues. Both of these executives have provided IRIS with reports that address Pieris's concerns. As a part of its policy advocacy program, IRIS sponsored a "Program for Policymakers on Capital Market Development" organized jointly by the Security Exchange Board of Nepal and the Unit Trust of India. The program was attended by high-level Government officials, including Governor H.S. Tripathy of Nepal Rastra Bank, Hon. P.R. Ligal of the National Planning Commission, and secretaries from various Ministries of the Government. The theme of the conference was three-fold: i) pre-conditions for capital market development, ii) importance of fair, transparent, non-duplicating, functionary regulatory framework, and iii) need to educate the general public on developments in the capital market.

In addition, IRIS has also been assisting the Nepal Rastra Bank formulate a strategy for establishing credit rating service in Nepal. IRIS consultant Clara Lipson spent two weeks in Nepal visiting with various public and private sector individuals. Her report recommends that the existing Credit Information Bureau confine its activities to bank lending information and be placed under the direct supervision of the Nepal Rastra Bank. The report then goes on to describe a detailed modality for establishing a credit rating service (NIISCRA) in Nepal. It concludes by proposing that two individuals, one each from the Securities Exchange Board and the Nepal Rastra Bank, attend an International Conference on Credit Rating in New Delhi during August 1994. Two individuals were sent as per Lipson's suggestions.

Banking Reform. IRIS Representative Praveen Dixit has been part of the Ministry of Finance Privatization Cell working group assisting with the re-structuring of the Rastriya Banijya Bank. Rastriya Banijya Bank is the largest commercial bank in Nepal, accounting for over a third of all deposits. The Privatization team, along with consultants from INTRADOS/Price Waterhouse, has prepared an action plan for restructuring this state-owned bank. The decision to restructure was approved by the Council of Ministers based on recommendations made by the Nepal Rastra Bank following the visit of IRIS consultant Paul Rymaszewski. The IRIS representative has also been part of the NRB/ELPS team that is evaluating the operational efficiency of the two Grameen (Rural Development) Banks. He accompanied Prof Latifee from the Grameen Trust of Bangladesh to the Far Western Region Grameen Bank in Dhangadi to examine the operations of the bank.

Policy Analysis Wing. The IRIS supported Policy Analysis Wing (PAW) at the National Planning Commission (NPC) submitted three reports--income tax, octroi, and customs tariff reforms--to the Ministry of Finance for use in the Annual Finance Bill FY 1994/95. The income tax study provides a comprehensive set of recommendations on expanding the tax base, modifying assessment procedures, altering the tax rates and payment system, improving administrative organizations, and introducing legal reforms. Many of these recommendations, especially those relating to tax rates and assessment procedures, were incorporated into the Budget Speech. Some other far-reaching long-term measures could not be included because of the political sensitivities involved in an interim Government budget. This same was true of the octroi study. Hon. Prithivi R. Ligal and the IRIS representative had discussed with the Minister of Finance the various options suggested for the abolition of the octroi. However, once Parliament was dissolved, the Minister decided not to address this issue in the budget, especially because it had been extensively politicized at the local level. The third study dealt with changes in customs tariff, sales tax, and excise duty. Most of the recommendations from this study, in particular those relating to valuation procedure, were included in the budget speech.

III. LIAISON WITH GOVERNMENT OFFICIALS

IRIS representative Praveen Dixit continues to spend afternoons at the Ministry of Finance to help improve communications between the Government and donor agencies, and between the Government and the private sector. During the last quarter, most of his time was spent in preparing the Annual Economic Survey and the Budget. Both of these took enormous amounts of time, more so because the budget had to be revised and promulgated as an Ordinance by His Majesty the King following the dissolution of Lower House of Parliament. In addition, he has also had to devote considerable time to other odd and ends such as facilitating the visit of the INTRADOS bank restructuring team, assisting the Government during the IMF's pre-budget mission, and reviewing legislation/policy issues on the Value Added Tax. He has also been appointed a member of the Government's post-budget monitoring team.

IV. FUTURE ACTIVITIES

IRIS activities for the next quarter remain uncertain. Mid-term polls are to be held on November 13 and the new Parliament has to be in session within two week of the elections. Then, the budget that was promulgated by the King on July 15 has to be either ratified or revised by the new House. How activities will shape up during the next quarter depends on the Government that comes to power.

V. CONCLUSION

IRIS-Nepal activities during the last three years has been functioning smoothly and effectively. The project itself is associated with reforms in many different areas. Policymakers are appreciative of the contribution that IRIS and the Economic Liberalization Project has made towards Nepal's economic reform agenda. Things, however, might be subject to change. New elections are to be held on November 13, 1994, and the outcome will

be crucial. If the present Government, including the Prime Minister, survives and comes back with a greater majority, the pace of reform can be expected to hasten. If a coalition Government or the opposition Communist Party were to garner a majority, the pace could slacken. For IRIS, a new government would mean new faces to deal with. The initial adjustments, therefore, could be very time consuming.

DRAFT

Sudur Pashchimanchal Grameen Bikas Bank: Trip Observations

Introduction: Praveen Dixit, the IRIS-Nepal representative, accompanied Prof Latifee of the Grameen Trust of Bangladesh to review the operations of the Sudhur Pashchimanchal Grameen Bikas Bank (Far Western Region Rural Development Bank). This trip report is based on the visit that took place between October 4-6, 1994.

General Observations:

- The Far Western Region Grameen Bikas Bank (GBB) appears to be a success in providing credit to rural households for income generating activities. It has a paid-up capital of Rs. 30 million, of which the Nepal Rastra Bank and the Government account for 75 percent of the total. Six commercial banks have share capital of Rs. 1.5 million each.
- The GBB serves two anchals--Seti and Mahakali. Most of its coverage is confined to the Terai districts--Kailali and Kanchanpur, though attempts are being made to expand to the Hill region--Dadeldhura. But logistics support is difficult to garner for the Hills.
- The GBB approach, it appears to me, is as much a group motivation technique as is a banking system. At times, it reminds you how propaganda machinery can be used to induce (brain wash) people to do things. But, easy access to capital/credit is the additional incentive that makes the system go.
- While the program has been in operation for nearly 18 months and appears to be functioning smoothly--loan repayment is nearly 100 percent--, signs of danger are emerging.

Cautions:

- Interest payments are subsidized to the tune of 80 percent by the Government for loans up to Rs 5,000. If you borrow Rs. 5,000, you make payments of Rs 100 per week for 50 weeks. This is the principal repayment. During the next 2-4 weeks, you make two more payments (Rs. 100 each) for an effective interest rate of 4 percent. The total subsidy is small (Rs 2.5 million), but money is not necessarily the issue. It is breaking the Grameen discipline of being self-sustaining that is at stake.
- In one assembly we went to, almost all the 12 center leaders complained about the Group Savings Fund (GSF). They were annoyed that 5 percent of the loan amount had to be mandatorily put into the group fund upon receipt of principal. In addition, they also had to pay interest on it and did not get the money back even if they left the system. Bank officials say the system has been devised in the said manner to prevent members from leaving the GBB. Perhaps what needs to be done to reduce member irritation is make more effective use of the funds.
- Sustainability is going to be extremely difficult in the Hills. Calculations have it that each branch needs approximately 700 members with loan size averaging Rs. 5,000 to make it

sustainable. The administrative costs (field assistants and a branch manger) have to be funded. This could be difficult even in the Terai region because of the scattered nature of villages. In the Hills, this will be almost impossible for two reasons: i) population is widely scattered, and ii) GBB field assistants will not be able to cover two meetings per day. Consequently, cross-subsidy between the Terai and the Hills will probably have to take place.

- The other danger that is creeping up is the different rates of interest subsidy for different loans. Interest subsidy is 80 percent for credit amounts up to Rs 5,000, and one-third for up to Rs. 15,000. Hence, two borrowers in the same Grameen Group could be paying different rates of interest. This could create morale problems in the future.
- One other emerging peril with the GBB is the large average loan that is being disbursed--average (Rs. 4,200) is more than 80 percent of the maximum (Rs. 5,000) allowed. In Bangladesh, the average was less than half the borrower's limit for the first tranche. Moreover, the loan size has escalated to Rs. 10,000 in many instances. We could start seeing defaults, especially if the animal dies. GBB has to be careful and ensure that some form of insurance exists.

Future:

- Eliminate the subsidy on interest in a phased manner. The subsidy could be gradually reduced from 80 percent for the first tranche loan to none in the third or fourth tranche. This should certainly be the case for the Terai region. Moreover, without eliminating subsidies, some of the NGO's in the business--Nirdhan and CSD--may have a hard time surviving. However, both these NGO's also receive subsidized funds from donor agencies and the Grameen Trust (interest cost 2 percent).
- Neither the GBB nor the NGOs raise capital from the market. The GBB uses its share capital, while the NGO's use donor money (IFAD) or the Grameen Trust loan (\$45,000).
- The opposition to the Group Savings Fund reflects the inadequacy of training to field assistants. Training has to be upgraded and monitored carefully.
- On the question of expansion, one needs to be careful about the pace. It is best to make the current ones efficient and self-sustaining before moving on to others.
- What can ELP look forward to? Among the activities of the GBB are social development programs such as skill training, sapling distribution, drinking water facilities, etc. With ELP's microenterprise focus, we need to devise programs to support these. The special activities are not self-sustaining, but forms a crucial ingredient of the Grameen package.
- We need to get the Executive Chiefs of the two GBBs (Eastern and far Western) together and figure out a social development program package. It would be best to co-ordinate this with other donor agencies.
- From a policy perspective, we need to figure out how to tie priority sector lending (12

percent), deprived sector lending (6 percent), and ADB lending. However, at the moment, funds are not an inhibiting constraint for the GBB.

October 11, 1994

Quarterly Field Report: POLAND

I. ADMINISTRATIVE DATA

Reporting Period: July 1, 1994 - September 30, 1994

BOA Number: ANE-0015-B-1019-00

Delivery Order Numbers: 11 & 18

AID Project Office: G/EG/SMIE (R. Mitchell, 300 SA-2)

AID Office funding delivery order: EUR/RME (Susan Gurley 4733 NS)

AID Office project: Institutional Reform and the Informal Sector (IRIS) Project (Robert Mitchell)

II. PERFORMANCE INFORMATION

I. Project purpose summary statement:

During the period June 1 to September 30, the IRIS-Poland II project ended on July 31, 1994 and IRIS-Poland III began on August 1, 1994. This report therefore covers the end of one project and the beginning of another closely related, but expanded project. Poland III differs mainly from Poland II in that it calls for collateral law reform activities in up to three countries in addition to continued activities in Poland. Its focus is the reform of the financial sector rather than on small and medium-sized enterprises.

- A. Project Purpose: The purpose of the IRIS-Poland II (Delivery order 11) project was to benefit the formation and development of Polish small business through reform of the institutional framework under which small businesses operate. This purpose is being accomplished through legal and regulatory reform processes concentrating on areas of critical importance to the health of small business in Poland. The emphasis is not on benefiting specific small businesses, but rather on improvement of the private sector institutional environment especially important to them.

The purpose of the IRIS-Poland III (Delivery Order 18) project is to create a positive commercial law institutional framework for the development of the financial sector in Poland and three other countries (Lithuania and two others yet to be chosen). This propose is being accomplished by assisting Poland and Lithuania to reform its collateral and bankruptcy law.

- B. Relationship to USAID Program Strategy: Poland has been one of the most successful of the C&EE countries in its transition to a market economy. There continue, however, to be great need to create employment and to expand the private sector, especially the SME sector where most new job creation occurs.

An important constraint to job creation and private sector expansion is the lack of credit. Numerous USAID financed studies and projects, the World Bank and the European Bank for Reconstruction and Development, have identified the absence of a modern commercial banking system as one of the principal blocks to further development. Without it, private capital cannot flow into the region for lending to credit worthy firms. This has not happened because Poland, and indeed each of the countries of C&EE, lack an effective collateral law which would enable banks to do asset-based lending to new and existing firms. At present, the only effective collateral is cash on deposit in the lending. Banks fear to lend, knowing collection is very uncertain and difficult. If an effective collateral law with a central registry to prevent fraud were enacted, commercial lending to the private sector would increase dramatically.

The IRIS-Poland II and III projects are assisting Poland in drafting and implementing its own collateral law. IRIS has encouraged the participation of local legal and banking associations in reforming their societies, leveraged upon other assistance and programs of the World Bank and EBRD to the financial sectors, and will lead to sustainable economic development by making bank credit available to new and existing businesses starved for credit. Poland III calls for extending this approach to up to three additional countries.

C. Highlights of program progress during the reporting period:

1. Bank Collateral Law Reform. The major focus of the IRIS-Poland Project continues to be Polish collateral law reform.¹ Since its inception, IRIS has been working with the top legal experts of Poland who form the advisory Commission for Reform of the Civil Code [CRCC], the Polish Ministry of Justice [MOJ], the National Bank of Poland [NBP] and Polish and foreign legal scholars to draft a collateral law which can be presented to the Polish Parliament for enactment. The main accomplishment of IRIS-Poland has been to create and support a local Polish-led coalition of academic, government, and business leaders interested in collateral law reform.

During the third quarter of 1994, the main activities involved writing of comments on the Jablonna Draft (March 25, 1994), the most recent collateral law draft of the CRCC. IRIS-Poland's collateral law coordinator, Dr. Tomasz Stawecki and IRIS-consultant Dr. Maciej Tomaszewski denoted certain small but important inconsistencies and defects in this draft and presented them to the Commission for

¹ Collateral law (sometimes called "secured transactions" or the creation of "charges" or "liens") is the legal institution whereby a creditor can take a "collateral interest" in certain goods (often those purchased by means of the loan) of the debtor. In case of default, the creditor is allowed to repossess and sell those goods ahead of other creditors to satisfy the loan.

consideration. On September 7, 1994, the CRCC met and adopted most of Dr. Stawecki's and Dr. Tomaszewski's suggested improvements. More importantly, the MOJ presented proposals for the organization of the central registry which were also included in the draft. Finally, IRIS-consultant Prof. Zedler presented changes prepared at IRIS's requests in the execution procedures. These changes designed to permit more self-help executions where debtors and creditors agree were accepted by the Commission. After the Polish draft was amended, an IRIS group spent several days amending the English translation to incorporate the changes in many provisions. Red-lined versions were prepared in Polish and English for distribution to interested parties.

Central Registry. The organization of a central lien registry is a key portion of collateral law reform. Over the summer, IRIS-Poland and Norway, SA, a company which works closely with the Norwegian Central Registries, organized a conference for high-level Polish and Lithuanian representatives² in Oslo, Norway from September 21-25, 1994. The Norwegian Ministry of Justice tried without outside assistance to computerize and rationalize its various registries for ten years from the mid-70's without success. The Minister of Justice hired a private, outside firm to do the work and it succeeded in organizing a system which is efficient, self-financing. The company is now owned wholly by the Ministry of Justice and sells information to banks, insurance companies, real estate brokers from its mortgage, lien, marriage, bankruptcy, and other registries. The Polish delegation, lead by Vice-Minister Zdziennicki, participated actively in obtaining information useful to setting up such a system in Poland.³

Lithuania. Immediately following the Norway Central Registries Conference, Mr. Dwight and Ms. Shapiro (USAID-Washington) visited Lithuania. Mr. Dwight, who stayed in Lithuania from October 25 to 27, identified individuals who would be the key personnel in a Lithuanian collateral law project. A definite decision has been made to move forward in Lithuania.

2. Bankruptcy Reform. In early July, IRIS organized the visit of Dr. Cheryl Gray of the World Bank. Dr. Gray has initiated a study of enterprise restructuring closely connected to IRIS's former work on bankruptcy in Poland. IRIS was therefore able to set up appointments

² See Attachment I, list of participants.

³ On October 5, 1994 in Chicago, Deputy Prime Minister and Minister of Justice Cimoszewicz told Ronald Dwight, Director of IRIS-Poland that the MOJ intended to sign a contract with the Norwegians to begin setting up a central registry.

with many key persons relevant to Dr. Gray's study. Later IRIS translated a short study prepared by Dr. Brol of the Juridical Institute on the recent status of bankruptcy administration in Poland.

Separately, IRIS and the Juridical Institute are publishing a major review of bankruptcy administration in Poland in time for the November Bankruptcy Conference of the Ministry of Justice. IRIS is also working closely with MOJ officials, Prof. Feliks Zedler and Dr. Brol who have been asked to revise Poland's bankruptcy laws on a priority basis.

Finally, IRIS-Poland will be working closely with Deloitte & Touche's Budapest office which was selected by USAID to administer a regional bankruptcy project. IRIS-Poland will assist with the Poland portion of the regional study.

3. Intellectual Property Reform.

Internet. At the request of the State Committee for Scientific Research's Director, Prof. Witold Karczewski, (equivalent of the Ministry of Science), IRIS worked during this quarter to organize a two-day seminar where legal and technical experts would meet to discuss the legal infrastructure needed for proper development of the Internet network in Poland. At present, the network is a big drain on the state budget. This could be easily avoided with proper planning for business access to this presently academic network.

Model Contract Project. The Center for Emerging Technology Enterprises is producing with IRIS cooperation, a series of model legal contracts for protection of intellectual property in technology commercialization projects. The English language models are complete, but it was found that the Polish translations were substandard. IRIS has therefore decided to delay the project to rewrite the translations at the high level.

Television Programs. Finally, Polish Television and IRIS have signed separate contracts with a production company to co-finance two TV programs: one focused on collateral law and the other on bankruptcy in Poland. These will serve to bring wide public awareness to these two important areas of legal reform.

2. Progress report

A. Technical Implementation

Activities Planned for Reporting Quarter	Current Status	Explanations (Problems, steps to resolve, etc.)
Foundation for Polish Science Meeting (July 1, 19)	1	IRIS-Representative, Justyna Misiurewicz briefs Mr. Andrzej Wach and Jerzy Sarnacki, specialists for the Foundation of Polish Science, on status of Technology Commercialization in Poland.
Cooperation with Commission for Reform of the Civil Code [CRCC] on Collateral Law Reform	2	IRIS-Director, Dr. Ronald Dwight Prof. Czachórski and Dr. Tomasz Stawecki, IRIS-Legal Consultant, meet on July 5, to discuss fall activities; translation of latest drafts is reviewed. Stawecki plays pivotal role in Sept. 7 CRCC meeting to review draft in two key areas.
Juridical Institute Meeting (July 5)	1	Ron Dwight meets with Dr. Brol to plan bankruptcy study and to discuss World Bank questionnaire.
Trip to Moscow, Russia (July 6-8)	1	Ron Dwight travels to Moscow
Dr. Cheryl Gray, Senior Economist at World Bank Visit re: Bankruptcy and Enterprise Restructuring Study. (July 11-15)	1	Dr. Gray investigates status of economic restructuring and bankruptcy in Poland. IRIS, at World Bank request, coordinates entire visit. ^{4,5}

⁴ See Attachment II.

⁵ See Attachment III.

Lithuanian AID Representative Meeting (July 25)	1	IRIS-Representative, Pamela Pollak meets with Lithuania AID representative to review status of Lithuanian collateral law.
Survey of Collateral Law reform in Central and Eastern Europe (July, August, September)	2	Questionnaires formulated and data is collected from various sources.
Trip/Seminar to Geneva, Switzerland (August 5)	1	At the request of Economic Commission on Europe of United Nations, Ronald Dwight speaks on "The Use of Real Property as Collateral for Financial Loans in C&EE."
Educational films about collateral law and copyright law (September 8-15)	1	IRIS and AFP Ltd. sign contract to produce films. Scripts have been approved.
Educational films about collateral law and copyright law (September)	2	Producer is negotiating contract with Polish TV1
Newsweek Meeting (September 19)	1	Ron Dwight, Charles Van Der Mandele of Polish Business Advisory Service meet with Newsweek Correspondent Andrew Nagorski.
IRIS/AID/IDLI Meeting (September 20)	1	Ron Dwight, Patricia Shapiro, Bill Loris discuss training of "Implementation of Collateral Law."
World Bank/IRIS Meeting (September 20)	1	Ron Dwight meets with Lucia Świątkowska to discuss collateral law reform.

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Blaziejewko Conference IRIS/CETE [Center for Emerging Technologies] Model Contracts Project (September 21)	2	Justyna Misiurewicz attends conference on Innovation and Entrepreneurship Centers of Poland and presents IRIS/CETE Intellectual Property manual of model contracts for technology commercialization joint ventures.
Translation of Polish Collateral Law into English (September)	1	Following substantive Sept. 7 revisions and additions, IRIS- Poland produced a new English language translation in time for Norwegian Registry Conference.
Translation of Hungarian Draft Collateral Law into Polish and English	1	At request of CRCC, IRIS translated and edited draft Hungarian law.
Trip to Oslo, Norway (September 21-25)	1	Registry Conference for 9 Poles, 3 Lithuanians and 15 other experts on collateral registry organization.
Trip to Vilnius, Lithuania (September 26-29)	2	Exploratory trip to Lithuania to consider of collateral law project with Patricia Shapiro, Esq. for four days.
U.S.-Europe-Poland Action Commission (CSIS-Zbiniew Brzezinski, Chairman) (September 25)	1	IRIS prepares a paper on Collateral Law reform. Pawel Kunachowicz, IRIS Representative makes presentation. ⁶

- (1) Action completed
- (2) Action in process
- (3) Action delayed
- (4) Action cancelled

⁶ See Attachment IV.

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Planned Activities for Next Quarter	Estimated Completion Date	Entity Responsible for Action
Publish model contracts manual for technology commercialization joint ventures.	12/94	IRIS-Working together with CETE and KBN [Ministry of Science]
NASK Workshop	10/94	IRIS, NASK [Science and Academic Computer Network]
Bankruptcy study with Juridical Institute	11/94	IRIS with Polish Juridical Institute

B. Project Administration

Planning Activities for Reporting Quarter	Current Status	Explanations (Problems, Steps to resolve, etc.)
Inventory of all assets for IRIS	1	
Purchase computer equipment	2	
Renew salary structure	2	
Sign Poland III contract	1	
USAID/IRIS Meeting (August 25)	1	Ronald Dwight meets with Don Pressley, Poland USAID Rep. regarding Poland III contract problems.
USAID Contractor Retreat (August 31-September 1)	1	Ron Dwight attends the workshop session. From this evolves the "Legal Reform Working Group".

Current Status Key:

- (1) Action Completed
- (2) Action in process
- (3) Action delayed
- (4) Action cancelled

Planned Activities for Next Quarter	Estimated Completion Date	Entity Responsible for Action
IRIS audit	11/94	Auther Anderson
Set up financial system for new program	12/94	IRIS-Poland
Set up office in Lithuania	12/94	IRIS-Poland
Set up office in second country to be chosen.	12/94	IRIS-Poland
Hire Lithuanian Coordinator	12/94	IRIS-Poland, IRIS-CP

III. FINANCIAL DATA

To Be Defined.

IV. ATTACHMENTS

- Attachment I List of participants at Norweigen Resgistry Conference.
- Attachment II: USAID Newsline article describing Dr. Cheryl Gray's visit.
- Attachment III: Letter from Dr. Cheryl Gray thanking IRIS for its assistance.
- Attachment IV: Speech for U.S.-Europe-Poland Action Commission, Banking and Investment Action Team Meeting of September 22, 1994.

Lithuanian AID Representative Meeting (July 25)	1	IRIS-Representative, Pamela Pollak meets with Lithuania AID representative to review status of Lithuanian collateral law.
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CONFERENCE NORWAY - POLAND
ON COMPUTERIZED CENTRAL REGISTERS
(REAL ESTATE, MORTGAGE, CADASTER & OTHER REGISTERS)
Oslo, 21st-23th September, 1994

LIST OF PARTICIPANTS

1. Vice Minister of Justice, dr. Bohdan Zdziennicki.
2. Director Michal Zalewski, Department of Organization and Data Processing, the Polish Ministry of Finance.
3. Dr. Jerzy Jaskiernia, President of the Economic Committee of the Polish Sejm,
4. Prof. dr. hab. Witold Czachorski, President of the Commission for Reform of the Civil Code (CRCC).
5. Dr. Jan Brol, member of the CRCC.
6. Prof. dr. Adam Brzozowski, member of the CRCC and Dean of the Law Faculty of Warsaw.
7. Director Felicja Myszurska, the Polish Ministry of Justice.
8. Director Jaroslaw Wyszowski, the Legal Department, the Polish Ministry of Physical Planning and Construction,
9. Director Remigiusz Piotrowski, Chief Surveyor of Poland, the Polish Ministry of Physical Planning and Construction.
10. Mrs. Danuta Blaszczyk, Chief of the Department of Physical Planning and Urban Economy, the Polish Ministry of Physical Planning and Construction,
11. Dr. Jan Maciej Czajkowski, Mayor of the City of Zgierz and Vice President of the Association of Polish Cities.
12. Mrs. Patricia Shapiro, Chief, Legal and Financial Reform Division, Agency For International Development-Regional Mission for Europe, USAid, Washington.
13. Director Ronald A. Dwight, IRIS-Poland Project, Warsaw.
14. President Tadeusz Jarzembowski, Holding-Wars, Warsaw.
15. Marketing Director Tomasz J. Malinowski, Holding-Wars, Warsaw.
16. Deputy Director Witold Radwanski, EBRD, Warsaw.
17. Mr. Jan-Hendrik M. Røver, EBRD, London.



18. Senior Engineer Gotfred Rygh, the Norwegian Mapping Authority.
19. Manager Svein Kile, Sparebanken NOR.
20. Director Erik Fossum, the Brønnøysund Registers.
21. Technical Director Helge Onørud, the Ministry of Environment and Chairman for the Commission³ of FIG.
22. Senior Engineer Olav Østensen, the Norwegian Mapping Authority and Chairman of the ISO-Committee for Geographic Information/Geomatics.
23. Adviser Harald Sandhåland, the Norwegian Ministry of Foreign Affairs,
24. Director Per Chr. Selmer, Tinglysingsdata A/S.
25. Marketing Director Kristian Strønen, Tinglysingsdata A/S.
26. Mr. Paul Ahlbom, Tinglysingsdata A/S,
27. President Trygve Tamburstuen, Norway Group A/S.
28. Director John Schjelderup Olaisen, Norway Group A/S
29. Manager Helge Klitzing, the Research Council of Norway.
30. Mr. Bogdan Marczewski, Counsellor, Deputy Head of Mission; the Embassy of the Republic of Poland.
31. Commercial Counsellor Tadeusz Fiszbach, the Embassy of the Republic of Poland.
32. President Knut Almaas, the Trondheim Court.
33. Director Kasper Holand, the Ministry of Finance.
34. Manager Hallvard Garberg, Sparebanken NOR.
35. Director Jon B. Fjalestad, Norway Mapping Group.
36. Director Lars Jorkjend, the Ministry of Justice.
37. Dr. Tomasz Staweczy, Attorney with the IRIS-Poland Project and Lecturer at the Warsaw University Law School.
38. Director Helge Sagen, Dun & Bradstreet Soliditet A/S.
39. Director Odd Storm-Paulsen, the Norwegian Ministry of Justice.
40. Manager Knut Olav Moen, Sparebanken NOR.

NORWAY GROUP A-S



41. Mr. Hugh Piggott, English Collateral Law.
42. Mr. Henryk Walczewski, Judge of the Cracow Court.
43. Mr. Adam Wasilewski, the IRIS-Poland Project.
44. Mrs. Jadvyga Aleksaite, Head of the Private Law Division of the Department of Laws, the Ministry of Justice of the Republic of Lithuania.
45. Mrs. Janina Izdonaite, Judge of the Supreme Court of the Republic of Lithuania.
46. Director Hilde Kolberg Strømme, the Norwegian Ministry of Justice.
47. Ms. Izabela Kurza, Polish interpreter.
48. Mr. Igor Dzialuk, adviser to the Polish Minister of Justice.



VOBUM 23 no 4 July 1994

LOCAL ENVIRONMENTAL MANAGEMENT PROJECT (LEM)

The Local Environmental Management Project (LEM) is a three-year technical assistance and training project conducted by the Research Triangle Institute (RTI) of Research Triangle Park, North Carolina, USA. The project assists selected local governments in Poland and Hungary to strengthen their ability to manage local environmental problems by focusing on solving technical, management and financial difficulties in one specific project, e.g. waste water systems and landfill management. LEM operates under a 3 year contract between RTI and the Environmental and Natural Resources Division of AID/EUR.

The LEM's project has three objectives:

1. to demonstrate that local governments in Poland and Hungary can effectively manage their environmental problems if given adequate and consistent support;
2. to assist project municipalities in producing reliable and technically acceptable proposals for the funding of environmental projects to be presented to national and international funding agencies;
3. to make available for use by other municipalities the project findings.

A subpurpose of the project is to act, through the project manager, as broker-liaison by matching municipal requests for technical assistance not supplied by LEM with various AID supported projects.

LEM efforts in Poland concentrate on sewage management in south, central and western regions of Poland. The technical assistance and training is conducted through a series of short term consultancies by US technical specialists in local government and environmental management who are then matched with Polish technical experts during project implementation. In Poland the training courses being developed cover such topics as sewage plant operators training, waste water management, project management and public information. When the LEM project is completed, its work will be continued by various governmental and non-governmental agencies as part of their sustained training offered in environmental improvement. For more information call Urszula Kwaśniewska at (012) 23-08-55, (012) 23-08-61.

EXPERTS UPDATE

VOCA 27-96-51, 26-51-80 and ACDL 27-23-12, 26-83-83

BANKER TO BANKER PROJECT

Name/Location	Scope of Assistance	Phone/Fax	Arr./Dep
Lawrence Dudley	and Banker to Banker	26-51-80	18 July/
Angus Nott /	Project	(VOCA)	5 August
Kąty Wrocławskie			
Łądek Zdrój			
Kalisz Province			
Neil Kevin Smith and	Banker to Banker	26-51-90	18 July/
David Shelby /	Project	(VOCA)	29 July
Grodzisk Wielkopolski			
Konin Province			

VOCA 27-96-51, 26-51-80

Name/Location	Scope of Assistance	Phone/Fax	Arr./Dep
Thomas Brewer /	Coop promotion and	26-51-90	6 August/
Przemysł Province	development	(VOCA)	30 August
Andy Kalnski /	Advise on computerized	26-51-90	9 August/
Brwinów	communication system	(VOCA)	30 August
	implementation		
William Albanos/	Financial management in	26-51-90	8 August/
Tarnów Province	meat processing industry	(VOCA)	20 August

IRIS POLAND PROJECT

July 11 through 15, Cheryl Gray, the principal economist for transition economics at the World Bank, visited Poland to investigate the status of economic restructuring and bankruptcy in Poland. The IRIS-Project, in cooperation with the World Bank, arranged a full schedule of meetings in Warsaw, Cracow and Łódź with experts in the bankruptcy field. Vice Minister of Justice Zieliński met with Dr. Gray for a detailed discussion about the Polish bankruptcy experience. During the meeting, the World Bank representative extended an offer of assistance to the Polish government in its efforts to reform the bankruptcy process. Dr. Gray's itinerary also included meetings with Dr. T. Stawecki, an IRIS-Poland legal consultant, the chief judges of the bankruptcy divisions in Łódź and Cracow and the Polish Lawyer's Association.

CAL INFO-LINE

Please phone CAL at: 635-89-44 635-86-50
Fax (48) (22) 31-79-20
Sat. phone (48) 39-12-08-55

- Katarzyna Osiecka (database, newslines, upcoming experts, cultural events)
- Jim Van Bergh (seminars)

Editor would like to welcome warmly newcoming volunteers of MBA Enterprise Corps. The group will go to Zakopane to participate in a two-week training program. Welcome to Poland.

FROM:WB CECTM 202-676-0083 TO:48 22 452512 451856 JUL 18, 1994 1:20PM #298 P.01

The World Bank
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

1818 H Street, N.W.
Washington, D.C. 20433
U.S.A.

(202) 477-1234
Cable Address: INTBAFRAD
Cable Address: INDEVAS

July 18, 1994

Mr. Ron Dwight,
Ms. Suzanne Ferlic,
Mr. Gerard Sadoch
IRIS - Poland

Fax No. 48 22 452512 or 451856

Dear Ron, Suzanne, and Gerard,

I want to thank you once again for the very kind assistance you provided in arranging meetings in Poland last week. The opportunity I had over the course of the week to meet with judges, trustees, bankers, and lawyers in Warsaw, Krakow, and Lodz has given me and the World Bank a much better picture of the progress made to date, as well as the challenges that remain, in the areas of debt collection and enterprise restructuring.

I would also like to express my high regard for IRIS-Poland. The patient assistance that IRIS has provided in reforming the collateral law is in my opinion a model of what foreign technical assistance should be. I hope that the draft collateral law is adopted soon and the registry can be set up quickly, and that reforms in bankruptcy are not too far behind.

Sincerely,



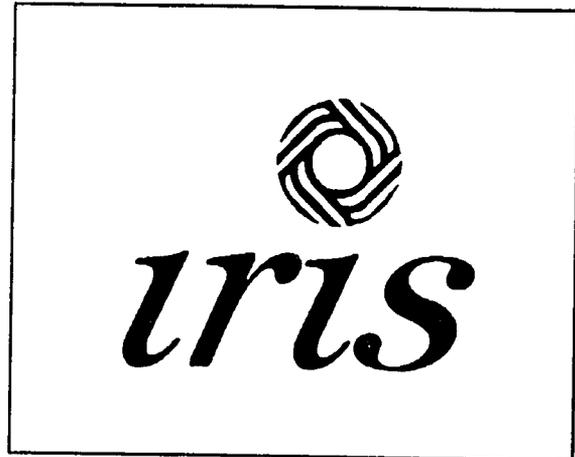
Cheryl W. Gray
Principal Economist
Transition Economics Division
Policy Research Department

IRIS-POLAND PROJECT

Funded by USAID

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USA: (301) 405-3052; fax:405-3020



September 19, 1994

U.S.-Europe-Poland Action Commission
Banking and Investment Action Team Meeting of September 22, 1994
c/o Center for Strategic and International Studies
Washington, DC

Dear Mr. Chairman:

I appreciate the invitation of the Commission to comment on Polish collateral law reform. Because I am now in Oslo, Norway with most of the principal Polish legal experts and Ministry of Justice officials involved in formulating a new collateral law for Poland to examine the Norwegian central lien registries, I asked if the Commission would permit IRIS Attorney Paweł Kuchanowicz to read this letter to the Commission.

The lack of an effective collateral law in Poland is one of the principal blocks to the development of modern finance in Poland and a block to the development of the entire banking system. Poland cannot reasonably expect foreign investment of the 50 billion dollar estimate needed in the next decade with the present collateral environment. Anyone who tells you that Poland now has a pledge system which, while complicated, is commercially effective is a liar or a public relations expert or both. My comments will cover first, the bad news -- the current state of affairs; second -- why this situation has not changed for three years; third, then the good news -- the excellent proposal which Minister of Justice Cimoszewicz has already distributed for inter-ministerial discussion; and finally, suggest what this Commission can do to help.

1. The Bad News -- the Current Legal Situation.

Article 1025 of the Polish Code of Civil Procedure gives you the basic picture. If a creditor bank goes through the trouble and expense of a full scale lawsuit, wins a judgment, and the collateral is still around for the bailiff or kormornik to seize and sell (and he generally gets 25 cents on a dollar), the proceeds of the sale must be distributed after the costs of the sale as Section 1025 provides: after the costs of the execution proceedings, (1) alimony of any employees of the debtor; (2) wages and unpaid pensions; (3) taxes, whether registered or publicly noted; (4) usufruct fees -- essentially state ground rents; (5) any bank loans; and (6) secured creditors. Thus even

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if a bank is not a secured creditor, it ranks on the same level as banks who are secured creditors. You are fifth in line in the best of circumstances. If you are not a bank but a just a ordinary secured creditor, under Section 310 of the Civil Code and 1026 of the Code of Civil Procedure, assuming something is left over after banks get paid, the creditor with the most recent pledge is paid first . Yes, you heard correctly -- the last shall be first just as in the Bible.

The most disturbing thing about Section 1025 is that tax claims, known or unknown, can always erode any collateral, and they do not have to be registered or publicly listed anywhere. And you cannot easily obtain certificates from the tax man that all taxes are paid in full. We call these "secret tax liens," and they are the bane of any investor in this part of the world. The simple notation of a clerk at the Ministry of Finance prior to the sale, even years after a mortgage has been registered, can evaporate your collateral moments before the bankruptcy court gives final approval to pay your collateral. In every bankruptcy proceeding, it is a waiting game to see if the tax man will make an appearance at the 11th hour and 59th minute to take all. Recently, a foreign company which had purchased a piece of real estate with the best and most expensive legal advice available in Poland found that two years after the transaction closed, the Ministry of Finance claimed that since the bankrupt seller had not paid its taxes in full, title was defective. The buyer is left with a lawsuit against another government ministry which guaranteed good title. Bottom line, every piece of Poland and every object might be collateral for the State Treasury, but it's often impossible to find out if such a lien is there.

The Section 1025 priority given to all banks, whether secured creditors or not, means that if bank # 1 takes a security interest in a debtor's property, and then the debtor gets a unsecured loan from bank #2, in bankruptcy, all banks share equally. Thus any security interest is liable to be eroded if your debtor takes out any other loans at a later date from a "bank."

The lack of a central register for collateral allowed massive fraud to occur in the early part of the transition to the market economy. Under present law, each bank keeps its own collateral register. Mr. Kuchanowicz has with him case studies prepared for IRIS by the Gdansk Institute of Market Economics illustrating how debtors used the same collateral over at a number of banks, pocketed the loan proceeds, and disappeared along with the collateral like Emerson's Arabs folding their tents in the night. Bankers, their hands burned by these painful experience with Poland's collateral law, now routinely demand the only worthwhile collateral -- a cash deposit in their bank for 150% of the loan amount to cover principal and interest. So if you have the money, you can borrow it.

2. Why hasn't the problem been quickly resolved?

As an institutional economist, I believe that a nation's wealth which is widely distributed and enduring is a product of a legal and institutional infrastructure which carefully defines and protects individual rights. Only in such an environment are individuals willing to postpone consumption to save and invest. Legal infrastructures are not changed overnight, but like vast buildings are constructed brick by brick. The transition to a market economy legal infrastructure is a work of decades not years.

Poland began the transition with a legal infrastructure considerably better than

most of its neighbors owing to its prewar legacy. It was easy to incorporate and get going. But now after leaving the starting line, we are finding that businesses are swimming in cement. Why? Let me speak about the legal reform environment in Poland.

The community of top civil and commercial lawyers in Poland and the other former communist states is very small, since for forty-five years or longer the vast majority of law students studied criminal law. The nomenclatura elite needed legions of criminal lawyers to stay in power, not civil lawyers. They already owned everything de facto, and sending the spoils to Switzerland did not require many civil lawyers. Those who studied civil and commercial law in Poland since the war have been a small group although often of very high quality. This demographic reality means that the Ministries of Justice in this part of the world and governments generally are still almost exclusively staffed by the criminal lawyer *srodowisko* -- and they are not about to give up their positions and privileges without a fight to a group whom they regarded as peripheral for half a century.

Until Mr. Cimoszewicz became Minister of Justice last fall, the Ministry of Justice in Poland has been led by individuals with little interest or expertise in civil law. Their legal reform priorities included putting crucifixes and priests in public schools and pushing abortion into back alleys. More seriously, this attitude meant that the Commission for Reform of the Civil Code -- whose membership includes the top civil law minds in Poland -- had a budget so ridiculously small that it could not afford to pay for train tickets for top experts to attend meetings in Warsaw. When they did come, it paid them \$8 for a day's work -- less than the cost of a round-trip tax fare from the railway station in Warsaw.

Despite this situation, Prof. Witold Czahorski, Chairman of the Commission for Reform of the Civil Code, and others with the support of Hanna Gronkiewicz-Waltz, President of the National Bank of Poland, and with technical assistance from IRIS to underwrite research, have worked for two years to draft a new Polish collateral law. Let me emphasize that only Polish lawyers, bankers, and academics can do this job properly. Earlier efforts to draft a Polish collateral law in London or New York were not only an insult to Polish legal expertise, but statutes whose enactment would have seriously disfigured Poland's legal structure. In my opinion, foreigners cannot draft effective laws for these economies. A local coalition of experts is necessary to draft laws that fit properly into the legal environment and to implement laws which they understand and support as their own work. I could give several examples where foreign drafted laws have been enacted and left unused or unenforced.

3. The good news -- the current collateral draft and program.

The good news is that this situation has now changed dramatically. We have a Minister of Justice whose top priorities include collateral law reform, the creation of a central lien and economic registry, and a Commission for Reform of the Civil Code with a budget - still too small but growing. Last March, the Commission finished the main work on the draft collateral law, and Mr. Kuchanowicz has copies of the latest draft, including the improvements made last September 7, in Polish and good legal English. We would appreciate your comments on it. The proposal calls for a central lien registry, permits all banks in Poland and later other creditors to file liens, abolishes secret tax liens by requiring the tax man to file his liens in the central registry or to go

to the back of the line, and permits creditors to repossess collateral and to have a notary public sell it without court proceedings.

4. What your Commission can do to help in this reform.

What can the Commission do? Those in the financial community can continue to emphasize the importance of a new collateral law to all sectors of the Polish government. This means putting the enactment of a new collateral law explicitly into the conditions of disbursement. We cannot assume that Poland will enact this reform because it is rational and logical to do so. There are unfortunately many people here in business and government who regard the current atmosphere of legal confusion as well suited to their business methods. The World Bank has been helpful in this, but not as forceful as it might have been. Specifically, those dealing with the Ministry of Finance must emphasize that secret tax liens must go and that the Ministry must play on even ground by agreeing to register its tax liens in the central registry. This will be no small fight, since the tax department of the Ministry of Finance will be violently opposed to giving up its long privileged position to jump to the head of the execution line. It should be emphasized to Minister of Finance Kolodko that the continuation of the secret tax lien system will mean dramatically lower foreign assistance and lending.

You should also urge your governments to put more funding into supporting reforms in the legal infrastructure by locals. This means money for carefully selected groups of experts to hold meetings, do research, hold conferences, travel to neighboring jurisdictions, and support of civil and commercial law programs in law schools. It also means supporting the judiciary with reasonable salaries, conferences, and other support. Poland's excellent and honest judiciary is being decimated by minuscule salaries, case overload, and its inevitable outcome -- creeping corruption. Without a good judiciary, you have a Mexican situation -- good laws but no justice.

In summary, we have probably put the cart before the horse in the development of an effective road to a market economy. Millions for privatization, but pennies to build the legal foundation for the financial road upon which privatized companies must travel.

Thank you for your attention. IRIS looks forward to working with you in advancing collateral law reform in Poland and in the other countries where we are working owing to the funding and strong support we have received from the United States Agency for International Development. I wish to thank Mr. Donald Pressley, the local head of USAID, and Patricia Shapiro of USAID-Washington for their strong support of our efforts, and to acknowledge the enormous pro bono assistance we have received from the Warsaw offices of Weil, Gotshal and Manges and Dickinson & Wright in our work.

Very truly yours,

Ronald A. Dwight
Director

#3 C:\WP51\RDICSI5

Quarterly Field Report: Russia Commercial Law Project

I. ADMINISTRATIVE DATA

Reporting Period: July 1, 1994 - September 31, 1994
Project Title: Russia Commercial Law Project No. 110-0007
BOA Number: ANE-0015-B-00-1019-00
Delivery order Number: 12
AID Project Office: G/EG/SMIE (R. Mitchell)
AID Office funding delivery order:
AID Office project: Institutional Reform and the Informal Sector
(IRIS) Project

Report to be supplied.