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Investing in the Future:

Report of the Task Force for Small and Medium Enterprise in Poland

GEMINI Technical Report No. 60

GEMINI

GROWTH and EQUITY through MICROENTERPRISE INVESTMENTS and INSTITUTIONS
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PREFACE

The GEMINI project is pleased to reproduce the report of the Task Force for Small and Medium Enterprise (SME) on "Investing in the Future" in Poland. The report represents the work of many donor, government, and private sector agencies that participated in the work of the "Group of 24," which supported this work. The GEMINI project provided a Secretariat for the Task Force and has helped produce and disseminate its work.

The Government of Poland, through the Prime Minister, has accepted and endorsed the Task Force report. The President of Poland also has endorsed the report, and has called for the formation of a bipartisan group of political and private sector leaders to foster the creation and adoption of a new economic reform policy and mandate, explicitly based on SME expansion, to transform the economy. The President has urged that the government, the private sector, and the donor agencies continue their cooperation begun in the Task Force in tackling the report's recommendations.

The report provides an excellent analysis of the problems facing small businesses in Poland. This analysis reflects the general findings of the GEMINI project in its previous work on the construction and agribusiness subsectors and on small business finance. The Task Force's recommendations for action provide a smorgasbord of possible solutions to business problems. The GEMINI project supports some of these solutions, but cannot support others.

GEMINI strongly supports the priorities set by the Task Force for SME policy development: reform of the basic enabling environment (including the establishment of an Office of Advocacy in the Government of Poland to do so), financial systems reform, and information and counselling provided at regional level. GEMINI does not support all of the action recommendations offered by the Task Force, and in particular does not support the use of subsidies to provide finance to SMEs. It should be remembered by the reader that the recommendations expressed herein represent the views of the individuals on the Task Force, and do not necessarily reflect the opinions of the GEMINI project or of the U.S. Agency for International Development.

Matthew Gamser
GEMINI Project Director

Investing in the Future

Report of

the Task Force for Small and Medium Enterprise

Poland

May 1993

Secretariat of the Task Force:

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with the kind assistance of
the Cabinet of the Minister for Entrepreneurship Promotion
and the GEMINI Small Business Project

This report presents the views of the members of the Task Force in their individual capacity and cannot bind the institutions which they represent.

The recommendations have been based on three months of investigations which by their nature have been incomplete. Since the background is constantly changing, in some cases recommendations have been overtaken by events and work has already started. More detailed information should be found for each individual recommendation when a detailed work plan is produced.

Costs presented in the report are purely indicative and should not be interpreted as commitments from either foreign donors or the Polish government.

Preface

Investing in the future - this means in the Polish context mainly investment by hundreds of thousands of entrepreneurs in their small and medium-sized businesses, with the aim of creating income and employment. As we all know, these enterprises are playing a key part in the transition of Poland towards a modern, market oriented economy. Poland will have to find its place within an enlarged European Community. Therefore, promotion of small and medium-sized enterprises means facilitating Poland's access to the European Community.

A lot has been achieved in this transitional process. The private sector is growing steadily and strongly. The Government is striving to create the favourable framework required to bring this process to full fruition. Poland's international friends and partners have pledged important amounts to assist this transition process.

The bulk of the work, however, is still ahead. The business environment needs continuous improvement, the enterprises need better access to capital and advisory services, and donors need to make their assistance more effective. Being aware of all these constraints, the Polish Government, the private business sector and the donor community organised in the "Group of 24" have undertaken to combine their efforts aimed at developing the small and medium-sized business world in Poland by establishing this SME Task Force.

The present report is the result of three months of concentrated work of the Task Force. It contains a set of priority recommendations which all aim at actions to be taken in the shortest possible time, involving the Government, the financial sector, the donors, but most importantly, also the target group itself, the entrepreneurs and their organisations.

The intention is to maintain the Task Force beyond this first phase, as an instrument for effective implementation of these and other actions still to be developed. It has been a unique exercise in Poland so far, and we do have reasons to believe that it can produce results which will go far beyond of what has been achieved already.

We therefore encourage the Task Force members to continue their fruitful work also in the next phase which should see substantial progress in the implementation of the actions recommended in this report. We would also like to thank the Task Force secretariat for their intelligent and tireless efforts in compiling this report.

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Executive Summary

Background

The private sector has emerged at an impressive speed in Poland. The liberalisation of the economy has led to many new entrepreneurs establishing their own firms, while those already in business now have better prospects for expansion.

About 1.7 million private enterprises are currently registered and more than 5 million people work in the private sector (more than 9 million including agriculture). These figures indicate that the private sector is a sector of very small or micro enterprises. The share of the private sector in the total GDP is about 42%, being only 28% in 1989.

Sustaining this growth of the private sector is important for a number of reasons. The private sector, and in particular small and medium-sized enterprise (SMEs), will form the backbone of a market economy and in the future will, as in most other countries, give the majority of employment. In addition, support for small enterprise can help in demonopolisation as part of the process of transformation as well as in social stability through the creation of a middle class.

Since the sector is new and does not have a powerful political lobby or clear and comprehensive institutional support, and given that the size of firms is typically very small, it is important that at this stage further support is given to the development of the sector in general. Many foreign donors have recognised this factor and made SME development one of their priorities in giving aid to Poland. Equally, the Government of Poland has recognised the importance of this sector by appointing a Minister without portfolio with specific responsibility for Entrepreneurship Promotion.

To try to harmonise these various actions, and to create better coordination, a Task Force has been set up consisting of representatives of the Government of Poland, the G-24 donor community, the Polish banking sector and the private sector, to produce a recommended list of actions for the development of small and medium enterprise. The Task Force met six times during February, March and April 1993 to discuss the constraints affecting the sector, and possible actions to overcome them.

Constraints to SME Development

The constraints for SMEs identified by the Task Force on the basis of documents, reports and interviews are numerous and diverse and affecting practically all aspects of business. Constraints were initially grouped into nine major fields: general environment; enabling environment; entrepreneurship promotion; financing; information and counselling; technology; privatisation; trade, export, import; and foreign assistance. After discussion, it was felt that it was not possible to deal with all these areas in the initial phase of the Task Force's work and therefore work should concentrate on three fields, namely:

- enabling environment
- financing
- information and counselling

This prioritisation does not mean that the other areas should be ignored - for example, the macroeconomic environment, including the rate of inflation, has a major effect on, for example, the ability of the banking sector to deliver finance to SMEs at an acceptable interest rate. In addition, these areas cannot be treated wholly in isolation: development of policy towards the SME sector must interact with any general macro-economic policies, whilst any actions which require foreign funding must take account of the limitations under which foreign donor programmes operate.

As a result of discussion of the constraints in the three areas against the background of existing and proposed initiatives, some 37 recommendations for action were proposed by the Task Force. All of these actions are feasible and should be carried out in due course. Nonetheless, it was felt useful to agree which were the crucial actions to be carried out immediately and as a result 9 actions were highlighted for particular attention by Task Force members. It is expected that the Task Force will continue its work and that over time new priorities will take over, including actions which are not a priority in the first phase.

Priority Actions

As an absolute priority, Task Force members emphasised the need to support the ***reform of civil and commercial law***. This is a precondition to the effective functioning of the banking system, where lack of adequate collateral law and a central collateral register hamper credit assessment and consequently access to finance by SMEs. After this reform, the major financing instrument emphasised by Task Force members was to support ***pilot guarantee schemes,*** both mutual and loan guarantee schemes. Guarantee schemes operate in a number of other countries where they are used to extend the collateral to which SMEs have access. In the period of transition it is felt best to have closely monitored pilot projects to discover whether this instrument can also be effective in Poland.

The government should also take action to develop an ***umbrella policy*** towards the SME sector and to place this in ***an SME Act*** stating the government's intentions towards the sector.

Not all actions should be taken at a national level, however. In addition to national actions, donors should try to fund ***regionally-based projects***. A number of different suggestions for action were given, including an approach of "coaching" regional business promotion agencies.

Donors can also help by developing instruments using examples from abroad. This is important for careful preparation of detailed proposals in complex but important

areas. A particular suggestion was for *analysis of the tax system* and fiscal measures in order to develop effective proposals to stimulate SME investment. There should be a parallel *review of the capital market,* which also has considerable importance in generating finance, in order to develop proposals to accelerate development of this sector. This process should be complemented by a *regulatory review* which should be repeated at regular intervals in order to ensure that regulations which adversely affect SME development are identified and modified.

Although much of the discussion around financing related to financing instruments, continued *training of bank personnel* was also seen to be of considerable importance in developing the banking sector and consequently their services to SMEs.

Finally, in order to address the need for information of both donors and intermediaries serving the SME sector in the field of information and counselling, it was proposed to set up an *SME Information Centre* to coordinate the flow of information.

Other Actions

Other actions can be most easily presented in the context of the three fields identified above.

In the field of the enabling environment, general SME policy should be addressed. As well as the *umbrella policy,* the Minister for Entrepreneurship Promotion should take a number of actions to improve coordination and communication among government departments and with the private sector. Such actions include the creation of a *Coordinating Committee* with other Ministries, the creation of a *Council for Entrepreneurship* including representatives of the private sector, and addressing the needs of the regions by *regional representatives or liaison people,* and *regional meetings.* The Minister should also have a clear *role of advocacy* and a right to intervene in the legislative process where this affects SMEs. In order develop policy on the basis of appropriate information, a *Research and Analysis Unit* should be established. Finally, there should be an *awareness campaign* to ensure that policy makers and legislators are aware of the particular problems of the SME sector.

Laws and regulations are also important parts of the enabling environment. As well as the *SME Act,* a *regulatory review,* and *support for civil and commercial law reform,* actions should be taken to *stabilise the regulatory framework,* and to give the Minister for Entrepreneurship Promotion the right of *obligatory assessment of new regulations.* Finally, two further specific areas were highlighted as needing particular attention, namely *public procurement,* and *accounting regulations.* These areas can have a particular effect on SMEs and therefore changing regulations should take the sector into account.

Tax policy can also be used to help SMEs. It is proposed that a study is carried out on *tax measures to stimulate investment by SMEs.* Also, particular areas for attention would include: *equal treatment of income from dividends and interest, a*

study on tax incentives for investment in SMEs, and *support to the tax control service* in order to make the tax system fairer.

In the field of finance a number of recommendations for financial instruments were made in addition to pilot projects on *guarantee schemes*. Consideration should be given to the idea of a *grant scheme with commercial loans* on the basis of monitoring the current STRUDER initiative and its success or failure, and *credit lines with preferential terms* since both these initiatives would help reduce the cost of capital to SMEs. As well as *support for the development of the capital market*, support should be given in developing a national *clearing chamber* to help improve banking services and *a credit rating service* to assist in risk assessment. Finally, as before, the importance of *bank personnel training* should not be forgotten.

As far as actions to support information and counselling activities, apart from the *SME Information Centre*, actions should take place at a regional level. Regional actions can include, as well as *coaching of business promotion agencies, funding of other specific regional projects, training for voievodship offices, establishment of telephone help lines*, and making a *study on regional development*. All these actions should assist in the better delivery of services to SMEs at a local level.

The special needs of *medium-sized enterprises* should not be forgotten, since they often have greater needs for sectoral consultancy and management training services. Institutions assisting this sector should therefore be supported.

Finally, support for *organisations of entrepreneurs* can help in all of the above actions by enabling the private sector to help itself. As part of the debate on business registration and whether there should be compulsory membership of business organisations, it is proposed that there should be a *study on business registration systems* to see how this could most effectively be performed using existing institutions.

Final Remarks

Although there are many recommendations listed, many of them are ongoing or can be performed by existing institutions. Wherever possible it is clearly better that an existing institution active in the field carries out an action rather than that a new body is created - this applies, for example, to the establishment of the Research and Analysis Unit and the SME Information Centre.

Nonetheless, much of the work of initiating these actions will fall on the Cabinet of the Minister for Entrepreneurship Promotion which has only limited size. If the recommendations are to succeed, strengthening of the Cabinet will be essential.

Finally, it should be noted that this is only the first step in the process of jointly developing measures to support the SME sector in Poland. It is to be hoped that the Task Force will continue its activity with regular meetings and that over time the other fields and constraints can be addressed.

List of Recommended Actions

Time scale indications: I - ongoing, II - as soon as possible, III - within a year
Underlined actions are priorities

Ref.	Action	Initiator	Major Actors	Time
GENERAL SME POLICY				
3.2.2	Umbrella policy	MoEP	other Ministers	I
3.2.3	Coordinating Committee	MoEP	other Ministers	II
3.2.3	MoEP standing for advocacy	MoEP, Council of Ministers	Prime Minister	III
3.2.3	Council for Entrepreneurship	MoEP, business organisations	Prime Minister	II
3.2.3	MoEP Regional Representatives	MoEP	regional business organisations and authorities	I
3.2.3	Regional meetings of MoEP	MoEP	Regional Representatives	II
3.2.4	Research and Analysis Unit	MoEP	donors, Bureau for Foreign Assistance	II
3.2.5	Awareness campaign	all Task Force members, business organisations etc.		II
LAWS/REGULATIONS				
4.2.2	SME Act	MoEP	Council of Ministers	III
4.2.3	Stabilising regulatory framework	MoEP	Min. of Justice, Council of Ministers	III
4.2.4	Regulatory Review	MoEP	Min. of Justice	III
4.2.5	Obligatory Assessment of proposed new regulations	MoEP	other Ministries	III
4.2.6	Support for Civil Law reform	MoEP	Min. of Justice, donors	II

4.2.6	Public Procurement Act	MoEP	business organisations	II
4.2.6	Accounting System	Accounting organisations	Min. of Finance	I
TAXES				
5.2.2	Study on tax measures to stimulate investment by SMEs	MoEP	donors, Bureau for Foreign Assistance, Min. of Finance	III
5.2.3	Equal tax treatment of income from dividends	MoEP	Min. of Finance, Council of Ministers	II
5.2.4	Study on tax incentive for investment in SMEs	MoEP	donors, Bureau for Foreign Assistance, Min. of Finance	II
5.2.5	Support to tax control service	Min. of Finance	donors, MoEP, Min. of Finance	III
FINANCE				
6.2.2	Support for Clearing Chamber	Union of Polish Banks, NBP, MoEP, donors, National Clearing Chamber, Telebank		II
6.2.3	Bank personnel training	Phare PIU, Foundation for Development of Financial Sector, Task Force for Training, Bureau for Foreign Assistance		I
6.2.4	Improvement of the Capital Market	NBP, SEC, Stock Exchange, Min. of Finance, Union of Polish Banks		I
6.2.5	Credit Rating Service	Union of Polish Banks, donors		I
6.2.6	Mutual Guarantee Scheme (pilot project)	MoEP, Bureau for Foreign Assistance., NBP, local initiatives		II
6.2.6	Loan Guarantee Scheme (pilot project)	MoEP, Bureau for Foreign Assistance., NBP, donors		II
6.2.7	Grant Scheme based on commercial loans	MoEP, Bureau for Foreign Assistance., NBP, donors		II
6.2.8	Credit Line with preferential terms	MoEP, donors, Bureau for Foreign Assistance, Ministry of Labour		III

INFORMATION and COUNSELLING

7.2.2	SME Information Centre	MoEP	donors	III
7.2.2	Donor-funded regional initiatives	MoEP	donors, Bureau for Foreign Assistance	I
7.2.2	Funding for specific projects at grass roots level	MoEP	donors, Bureau for Foreign Assistance	III
7.2.2	Training for Voievodship Offices	MoEP	donors, Voievodship offices	III
7.2.2	Telephone help-lines	MoEP	donors, regional authorities	III
7.2.2	Study on Regional Development	MoEP	CUP, donors	III
7.2.2	Coaching Regional Business Promotion	MoEP	donors, Bureau for Foreign Assistance	III
7.2.3	Support of the medium-sized sector	MoEP	donors, Bureau for Foreign Assistance	I
7.2.4	Support for Organisations of Entrepreneurs	Council for Entrepreneurship, MoEP, donors		I
7.2.4	Study for business registration system	Chambers	MoEP, donors,	III

MoEP = the Minister for Entrepreneurship Promotion
NBP = National Bank of Poland
SEC = Securities and Exchange Commission
CUP = Central Planning Office

1. Introduction

1.1 Background

Increased investments by small and medium enterprises (SMEs) in profitable projects is seen as a key to economic recovery and development in Poland. In spite of many measures undertaken by the Government of Poland and the Donor Community in respect of the SME sector, currently SMEs face major obstacles in their development.

Measures taken so far have proved to be insufficient in the face of the problems. A large and growing number of potential and existing SMEs are unable to overcome the obstacles to profitable investment. On the other hand, large amounts of foreign loans have remained unspent.

Against this background, the Polish government and the G-24 donor community established a Task Force in February 1993 with the objective of recommending measures aimed at a sustainable increase of profitable investments by SMEs. Terms of Reference are presented in Annex A. Members of the Task Force have been representatives of Ministers (for Entrepreneurship Promotion, European Integration and Aid Coordination, Finance), of Polish banks (National Bank of Poland, Union of Polish Banks), of the Polish private business world, as well as representatives of the G-24 donor community (World Bank, Commission of the European Communities, European Bank for Reconstruction and Development, USAID, and the Federal Republic of Germany). Several other Ministries, organisations, foreign donors and individuals participated actively in the work of the Task Force, during the public sessions as well as through interviews and written contributions. A list of Task Force members is enclosed in Annex B whilst Annex F lists persons interviewed by the secretariat.

This report presents the recommendations worked out by the Task Force between February and April 1993. The report was compiled by the Task Force secretariat, a group of four experts funded by the Commission of the European Communities under the PHARE programme.

1.2 Policy Objectives

Small and medium sized enterprises are expected to contribute to the economic welfare of Poland, in particular to economic growth and job creation. As experienced in many other countries, SMEs are already contributing to competition in markets for goods and services and guaranteeing a permanent process of creativeness and innovation, essential elements of economic development. In Poland this role of SMEs has been recognised and the Polish government has defined the tasks of the Minister of Entrepreneurship Promotion accordingly.

In Resolution No 139/92 of the Council of Ministers (see Annex C) it is stated that the Minister of Entrepreneurship Promotion undertakes activities in the field of shaping economic, legal, social and organisational conditions for the promotion of entrepreneurship and the development of small and medium enterprises.

It is in this frame that the Task Force for Small and Medium Enterprises has worked out the major strategy for reaching this objective. In particular it has considered actions to reach a sustainable development of the SME sector.

Some basic principles have to be addressed in the design of an adequate SME policy and these are explored below.

1.3 Basic Principles

1.3.1 *SME Target Group*

Since the Polish economy is in transition, various categories of private firms exist with different legal forms. Firms originate from a variety of sources including: new start-ups; continuation of the former private sector; and privatisation of State Owned Enterprises. Most of these are very small firms, although a certain category of firms have already reached a certain scale which guarantees survival better. Moreover, SMEs have emerged in all sectors of economic life but in particular in trade.

Taking into consideration these aspects the SME sector should be seen as quite heterogeneous in legal status, size and sector.

To define policy instruments, these aspects should be taken into consideration, which means that the target group of SMEs should be defined more precisely when these measures are elaborated in more detail. This will favour more effectiveness of policy initiatives than considering every measure or instrument applicable for all SMEs.

In particular it should be considered which economic activity or sector of SMEs should be addressed.

It should be emphasised that strengthening the competitiveness of the Polish economy and thus creating economic growth and more employment can be more directly reached by stimulating the manufacturing sector or other balance of payment oriented sectors like transport, wholesaling and tourism. On the other hand, stimulating the SMEs in general or in other sectors is providing the Polish economy with an entrepreneurial class that guarantees creative entrepreneurship in the long run.

1.3.2 *Regional Approach*

SMEs need an approach on the national level especially as far as it concerns macro-economic conditions and the enabling environment, in particular related to the legislative and regulatory framework. However, the action-radius of SMEs is rather limited as they are operating quite strongly on the local and regional level. That is why initiatives should be developed or stimulated at the local and regional levels as well. In order to harmonise, to avoid overlapping and to facilitate certain actions, both national support and cooperation with local and regional actors should be envisaged.

1.3.3 *Non-discriminatory Policy for SMEs*

In the Polish transitional economy it should be stressed that the private sector and in particular SMEs are facing a rather discriminatory position. As a result, rather than looking for preferences, the first stage should be that they are not discriminated against. It should be stressed that if SMEs are expected to be the backbone of the Polish economy in the future, as it is in all market economies, then special attention is required to eliminate at least this discriminatory position. Developing specific instruments to support and to stimulate SME development in particular in this phase of the transition period can be considered as investing in the future prosperity of Poland.

1.3.4 *Policy Organisation*

The problems of SMEs are very diverse and concern the policy areas or fields of almost all ministries. As a result, many of the policy instruments necessary to reach the SMEs belong to the field of other ministries. That is why it should be recommended that there is good cooperation between the Minister for Entrepreneurship Promotion and the other ministries and a commitment of all ministries to the SME sector.

As the Minister for Entrepreneurship Promotion has not his own ministry but is operating from his Cabinet in the Office of the Council of Ministers, activities for SMEs can to a certain extent only be initiating, stimulating or consulting. Implementation is to a great extent dependent on staff and capacities of other ministries and/or extra governmental organisations.

1.3.5 *Financial Constraints.*

The feasibility of the implementation of the actions depends on the financial possibilities in Poland. Being faced with serious budget deficits the Polish government will have to look for financial means for strengthening the SME sector at present. It is important to look for budget-neutral solutions favouring the SME sector on one hand: on the other hand concerted actions by bi/multilateral donors and organisations should be sought in order to strengthen the financial capabilities

of the Polish government and to develop a genuinely large scale programme for developing SMEs.

1.4 Methodology and Structure of the Report

The methodology followed in the process of reaching the actions recommended in this report is based on the concept of the policy cycle. Taking into consideration the above mentioned objectives of an SME policy, first an investigation of the problems and constraints has been carried out. Based on the results of this information-gathering phase the Task Force selected three major policy fields out of nine possible ones and these were:

- Enabling Environment (general SME policy, legislation, and taxes),
- Finance, and
- Information and Counselling.

For each policy field an inventory of possible actions has been made. The Task Force selected the most feasible ones which were recommended for implementation. In the following chapters this process is presented.

In Chapter 2 a short analysis of the position of the SME sector is provided. The support systems geared to the SMEs are presented together with a list of the constraints in the different policy fields.

In Chapters 3 - 7 the selected policy fields are discussed and concrete actions are recommended. In each of these chapters first a short analysis of the obstacles in the policy fields is given. These analyses emerge in appropriate actions or packages of actions that are recommended by the Task Force. In particular, attention is paid to the implementation phase: which steps are needed, who should be initiator or actors involved, and what are the institutional and financial aspects of the actions. Very rough estimates of the costs involved in carrying out the tasks are also presented. In general these costs represent the annual costs of running the various projects.

Finally, in Chapter 8 specific points which emerged from designing the programme or packages of actions in the previous chapters are discussed together with a general review of the recommendations.

2. State of the Art

2.1 Introduction

In this chapter, the state of the SME sector is analysed to show which constraints most urgently need to be addressed. First a brief overview is presented on facts and figures of the private sector. An overview of the activities which already exist to support SMEs as well as donor-funded projects and financing instruments of the banks is given. Thereafter, the constraints registered in literature, reports and mentioned by many experts on SMEs are listed. In the concluding paragraph the major constraints to which SME policy should be oriented are discussed.

2.2 Statistical Information

From the late seventies onward private firms in Poland were gradually released from central planning. Unincorporated firms received opportunities for development earlier than the incorporated, which were enabled to boom after the adoption of the Law on Economic Activity in 1988.

At the end of 1992 there were about 1.7 million private enterprises (excluding agriculture) producing approximately 471 billion złoty[1]. That means that about 42% of the total GDP in Poland comes from the private sector. Including the agricultural sector the share of the private sector in the total GDP rose from 28% in 1989 to about 48% in 1992.

Since 1989, the growth of the private sector in comparison to the state owned sector has been impressive. Growth figures of the GDP in real terms for the private sector were estimated to be 7.1 % in 1990, 33.3% in 1991 and for 1992 the estimates go up to 12%. The outlook of the Polish economy for this year is optimistic: there are certain indications that Poland is emerging from the recession. Exports are doing well and the private sector is strongly contributing to this economic recovery.

The dynamism in the private sector is illustrated by the investment figures as well. Of the total gross domestic investment in 1989 35% was in the private sector. This figure increased to 41 % in 1990 and it is estimated that in 1991 this figure has been slightly higher.

The share of the investment of private enterprises in manufacturing are lagging behind, while those in construction and trade are much higher. In the manufacturing sector approximately 15% of the total investment was carried out in the private sector in 1990.

[1]Note: all figures relating to 1992 GDP in this section are preliminary estimates calculated by the Main Statistical Office (GUS).

This production boom in the private sector is in balance with the development of employment: the share of the private sector can easily be estimated to exceed already 55% (including agriculture), the share at the end of 1991. At the end of 1992 more than 5 million people worked in the private sector. Including private agriculture this figure was more than 9 million.

A part of the increase in private production is due to reclassification of former public entities (notably cooperatives) and changes in ownership (privatisation). Interesting is that the growth rate of the "old"-reclassified private sector was exceeding the growth rate of the private sector as a whole, both in 1990 and 1991.

As concerns the different categories of legal forms the unincorporated firms (1.63 million) showed a growth figure of number of enterprises of 14.8% in 1992, a bit less than in 1991 (25%). The strongest relative growth could be registered with incorporated firms (legal units), of which those that are completely domestic owned showed growth figures of 33% and 23.7% in 1991 and 1992 respectively. The incorporated firms set up with participation of foreigners rose considerably from less than 5000 in 1991 to more than 10000 in 1992: a doubling.

Incorporated firms are of a larger size than the unincorporated. Incorporated have an average employment of 14.7 when they are completely domestically owned. Incorporated firms with foreign participation show an average employment of 23.1, while the unincorporated have an average of 1.6 per firm including entrepreneurs.

At the end of 1992 the largest number of private enterprises owned by legal persons were in the trade sector (38%), while in manufacturing 21% were active. Measured in employees the share of the manufacturing sector is highest (36%), while that in trade is only 30%, indicating that the average size of the manufacturing enterprise exceeds considerably that of the trade sector.

If the unincorporated firms are considered in 1991 approx. 880,000 out of a total number of approx. 1.42 million enterprises belonged to the category of very small or micro firms (< 5 employees), which is about 62%: it should be considered however that these figures include the entrepreneur but do not take into consideration those employees that are working on short term contracts.

If only the private enterprises in manufacturing with more than 5 employees are considered then the following size-class distribution of employment can be shown:

small firms	18.5%
medium sized	52.0%
large firms	29.5%

The small firms in the manufacturing sector as well as in the construction sector are defined as firms between 6-50 employees and medium sized firms between 51 and 500 employees.

From this it can be seen that in the manufacturing sector the number of jobs in the medium-sized firms is considerably higher than in the small or large firms.

In conclusion, it can be stated that the private sector is experiencing substantial growth and can contribute to the recovery of the economy. It should be realised, however, that at least outside the manufacturing sector the firms are generally small and vulnerable.

2.3 Existing Support Institutions and Donor Funded Projects in the SME Sector

There are a wide variety of different initiatives on the ground in Poland: private, public, and funded by foreign aid. Since the network of support organisations has grown organically with little overall coordination, these initiatives in some cases complement each other and in other cases act almost in competition. Equally, whilst in some areas there are many activities in support of the development of private enterprise, in other areas the level of activity is very low, and this does not relate to the actual needs of the area.

On the Polish side there are a number of different networks of business support institutions, mostly giving basic advice, information, and training to very small enterprises and entrepreneurs who wish to start in business. Such networks include those set up by the Economic Foundation of NSZZ Solidarność, Regional Development Agencies (mostly supported by the Industrial Development Agency), local Chambers of Commerce and of Craftsmen, a number of Management and Business schools and a variety of independent local initiatives such as incubator projects. A number of national initiatives complement this, including the Foundation for Socio-Economic Initiatives, FISE, (supported by the Ministry of Labour) which operates through regionally based Agencies for Local Initiatives.

Foreign donors have supported some of these initiatives, including FISE and certain local chambers, as well as setting up new institutions, such as Business Support Centres (supported by PHARE through the Cooperation Fund) and hosted mostly by Chambers of Commerce, and Regional Management Centres established through the British Know How Fund which offer advice and counselling to the private sector as well as management training. As well as initiatives aimed at small enterprise, the International Finance Corporation, in association with the European Bank for Reconstruction and Development and USAID has set up Polish Business Advisory Services, a consultancy and training organisation based on commercial terms and aimed at management training and sectoral consultancy for medium sized private enterprises as well as the training of Polish consultants to form an indigenous consultancy sector. The German government has funded a parallel initiative, coaching medium sized enterprises using foreign expertise.

Current initiatives suffer from lack of overall coordination and in general the institutions are weak and lacking in resources (other than those provided by foreign aid).

A more comprehensive list of projects is presented in annex D.

2.4 Banks and Other Financial Institutions relevant to SMEs

Although a new banking structure has been established, it is still in the process of development and does not always serve the SME sector very well. This is partly due to lack of experience of the banks themselves, but also due to lack of an adequate environment. For example, inadequacy of collateral law and the lack of a collateral register makes assessment of the value of collateral very difficult.

The situation of the banks makes them particularly risk averse owing to the problems of risk assessment, the high rate of failures, and the lack of adequate collateral law. In addition, the regulations of the National Bank of Poland related to the necessary ratios for private banks have caused them to increase their own capital rather than give more credit to SMEs. This tendency has meant that SMEs have inadequate sources of credit, particularly long term credit. A more detailed description of the constraints hampering the financing of SMEs is presented in chapter 6.

There have been a wide variety of different foreign funded initiatives aimed at disbursing credit to the private sector. A large number of foreign credit lines are largely unspent and a major reason for this has been the difficulty of using the existing banking system and the fact that simply adding a credit line does not remove the reasons for risk aversion indicated above. This is most clearly illustrated by the fact that the most successful foreign initiative is the Polish American Enterprise Fund which has done credit appraisal itself and used the Polish banks only as 'windows'.

There are a number of initiatives related to other financial instruments, such as guarantees and equity schemes but as yet none of these has reached a sufficient stage of development or size to have any real impact on the SME sector. The STRUDER programme will have pilot regional projects for both types of actions, but they are only at the formation stage at this moment.

Other financial services are largely undeveloped. Such services include leasing, factoring, and relevant insurance services. Equally, the services which support the banks, including a national clearing chamber and appropriate credit rating agencies are only now being put in place. Nonetheless, there are a number of donor-funded initiatives to develop additional services, for example the PHARE financial sector development programme which provides support to the accounting, insurance, and tax administration sectors as well as banking training.

A more comprehensive presentation of the financial sector is presented in Annex D.

2.5 Overview of the Major Constraints

The constraints for SME development, and in particular in investing in SMEs, that could be identified in the Polish economy are numerous and very diverse. In the following list, which was developed from a variety of sources and presented to the Task Force, the constraints are listed in nine policy fields without giving a specific ranking, either for the policy fields or for the constraints.

2.5.1 *General Environment*

Macro-Economic

- high inflation
- recession (national and international)
- large government budget deficit
- high interest rates
- high taxes

Underdeveloped Infrastructure

- telecommunication
- market information system
- transportation system
- distribution systems
- business space availability

Business Climate

- suspicion and negative attitude towards successful entrepreneurs
- weak business ethics (trade practices, long payments)
- limited entrepreneurial tradition
- lack of favourable government policy

Informal Sector

- unfair competition (bribes, etc.)
- tax evasion
- massive illegal imports

2.5.2 *Enabling Environment*

Policy, Legal and Regulatory Framework

- no formal government policy or action plan for the private sector
- insufficient quantitative and qualitative policy related information on SMEs
- unsatisfactory and inadequate influence of private business on the policy making process

- legal and regulatory framework is often not clear and transparent, changes too often and leaves wide discretion for arbitrary civil administration and court decisions
- government administration and juridical system is not compatible with the creation of a private sector market driven economy
- legislators, administrators and courts lack experience and guidance in fostering the free market economy
- insufficient communication and coordination between various government institutions and ministries
- serious gaps and imperfections in laws (see other fields for example collateral law under financing)
- public procurement practices unfavourable to SMEs

Fiscal Policy

- inadequate tax enforcement and collection capabilities which lead to an excessive administrative burden on private business
- business perceive taxes as too high
- tax legislation is changing too often (even retrospective)
- no tax incentive for investment
- unequal tax treatment of dividend and interest on personal income
- high custom duties on imported equipment and raw materials

2.5.3 *Entrepreneurship Promotion/Assistance to Start-ups*

External

- difficulties with start-up finance/insufficient equity investment
- growing necessary minimum initial capital
- insufficient information, technical assistance and training for start-ups
- limited entrepreneurship promotion

Internal

- lack of knowledge and experience on running business in a competitive market
- limited entrepreneurial tradition
- limited personal assets and savings

2.5.4 *Financing*

a. *Equity Capital*

External

- unavailability of domestic capital
  - lack of venture capital institutions and instruments
  - unequal tax treatment of dividend and interest on personal income
  - underdeveloped security and capital markets
- no tax incentive for business investment

- limited flow of foreign investment

Internal

- too much reliance on debt financing to capitalise business
- low profitability of many businesses
- businessmen are reluctant to put their own capital in fixed assets (focus on short term business activity)
- entrepreneurs are reluctant to jointly invest in and "share" control of business

b. Credit

External

- high collateral and or guarantee requirements
  - banks meet problems in taking possession of the collateral
    - no asset/collateral registry
    - loop holes in the land and housing registry
    - lack of adequate property law
    - no collateral law
    - poor bankruptcy law
  - lack of standard procedure and market price information to guide valuation of assets/collateral
- high interest rates (nominal and real), due to inflation and bank margins
- banking services underdeveloped and time-consuming
  - underdeveloped clearing system
  - overdraft hardly available
- low risk investment alternatives (government bills and bonds)
- difficult access to long term financing
- actual or formal minimum loan size requirements are too high for most SMEs
- risk aversion by banks
  - banks have less experience in assessing private sector creditworthiness and risk evaluation
  - banks need other institutions to share the risks (for example credit guarantee institutions)
  - no incentives/strong disincentives to take risk by state owned bank management
  - the high rate of bad loans make banks more cautious on risk taking
  - undercapitalisation of banks
  - major taxes levied on banks when writing off bad loans
  - required credit documents are too detailed and time-consuming for SMEs
- banks avoid giving small loans (operational costs, etc.)
- lack of flexibility by banks to restructure debts

Internal

- problems with preparation of application forms and other credit documents including a business plan
- focus on "low costs" foreign exchange loans and without understanding of foreign exchange risk

Other

- inter enterprise credit *zatory*
- underdeveloped legal framework and institutions for leasing, factoring and insurance

2.5.5 *Information and Counselling*

External

- insufficient development of a business assistance support network
- limited availability of information necessary for good business decisions, especially information on:
  - markets
  - financing
  - technology
  - management
  - SME-support organisations
  - legislation and regulations
- private advisory and consulting firms are too expensive for SMEs
- big differences in the quality of information and advisory services available

Internal

- insufficient awareness of the importance of information and advice sharing among entrepreneurs
- lack of knowledge among entrepreneurs how to collect and use information for their own benefits.
- limited knowledge and lack of experience in free market business, in particular:
  - marketing
  - finance/accounting
  - management
  - customer services
  - quality control

2.5.6 *Technology*

External

- undeveloped institutions and mechanisms for technology commercialisation and transfer
- unavailable financing for R&D and technology upgrading
- brain flight

- intellectual property protection

Internal

- adaptation to international market norms and standards
- technological backwardness of SMEs affects quality and limits flexible reaction to market signals
- insufficient awareness of the necessity of technological and quality improvement, product design and production processes
- lack of knowledge on technological developments
- unawareness of the importance of R&D
- lack of financial means for R&D and modernisation of the production processes
- high custom duties on modern equipment

2.5.7 *Privatisation, SMEs and SOEs*

- no policy or programme which integrate SME development with SOE privatisation
- limited SME access to assets of SOEs being privatised
- problems of SOE affect SMEs
- insufficient information on privatisation process
- monopoly situation of some public sector enterprises, especially in regional markets

2.5.8 *Trade, Export, Import*

- difficulties in adaptation to world norms and standards
- lack of market information on foreign markets
- lack of information on foreign regulations
- relatively high costs for SMEs to access foreign markets
- high custom duties on import equipment and raw materials
- foreign import quotas on various products
    - actual preferences for SOEs
- unfair competition due to illegal import
- developing/transforming industries are threatened by competitive import

2.5.9 *Foreign Assistance*

- insufficient coordination
- insufficient information on foreign assistance
- assistance perceived as not based on the priority needs of the private sector and tend to be inflexible
- private business and the government have little or no influence in shaping foreign assistance for private business

- business unsatisfied with significant part of foreign assistance spent on foreign consultancies and privatisation
- limited implementation of the results of foreign studies
- inadequate monitoring of implementation of foreign assistance
- no coordination and linkage between financial and technical assistance
- foreign credits (credit lines) do not reach SMEs

2.6 Conclusion and Selection of Major Policy Fields

In the preceding paragraphs it was indicated that the private sector and the smaller firms in particular have been emerging strongly in the last few years. In spite of the actions undertaken to support SMEs directly, either by strengthening the banking sector - an essential actor - or through economic development, this has not resulted in a smooth development of the SME sector. Many obstacles have been identified that are obstructing the private sector from prospering and exploiting its full potential.

The Task Force has discussed at length the numerous constraints and has selected out of the nine policy fields indicated, three major fields to which the SME policy making should be orientated, being :

1. The enabling environment: attention should be paid to the general policy aspects related to SMEs, as well as to legislation, regulations, and taxes.

2. Finance: in particular the clearing system, training of bank personnel, credit facilities.

3. Information and counselling; in particular integration with regional policy.

The obstacles in the other six policy fields which were not discussed in detail are nonetheless considered important for the further development of the SME sector. Alongside the priorities indicated in this document, it is important to recognise the need to address the other constraints, in particular those related to the macro-economic environment, which have a large effect on the effectiveness of the actions in the report. For example, nominal interest rates are closely related to the level of inflation, and therefore high inflation means reduced demand for investment credits.

Equally, it is important that actions taken to support SMEs fit in with actions of the government in other sectors and therefore, for example, SME policy should not contradict the general macro-economic policy of the government.

Finally, in seeking funding for the actions recommended, the limitations of donor funding caused by the different procedures used by different donors and the difficulty of effective coordination and cofinancing should also be taken into

consideration. Grant and loan aid need to be more effectively interlinked and the government should strengthen its coordination mechanisms in this respect.

3. General SME Policy

3.1 Elaboration of Constraints

Lack of a coherent SME government policy or an action plan is a major constraint causing other constraints for the development of the sector. It lacks first of all an umbrella policy which would confirm the recognition of the importance of SMEs for economic growth and general welfare, commit the government to foster SME development and provide a basis for specific SME policies by all the ministries in a coordinated manner.

The following reasons for the lack of a policy have been identified:

- Among other important questions that the government had to address, formulation of policy favourable to SME and the private sector in general has not been a priority. Some policy makers found policy for the public sector, then covering almost all the economy, more important. Others believed that the private sector would take care of itself. In particular, departments responsible for SME and entrepreneurship promotion were located in the Ministry of Industry which, being overwhelmed with the problems of SOEs and heavy industry, could not give priority to SME development.

- It seems that overall strategic objectives of government SME policy have not been developed. One has to answer the questions: *why do we want to support the SMEs? What are the long term objectives?* Without clear strategic guidelines defining specific policies is difficult.

- In 1989-92 attempts to formulate a comprehensive government policy towards the SME sector failed. Changes in cabinets and officials responsible for SMEs and entrepreneurship promotion caused delays and eventually no binding decisions were made. For example a document "Assumptions for the Government Commissioner for Entrepreneurship Promotion" prepared in the Ministry of Industry was revised several times and never approved. "Assumptions" defined certain objectives, and a set of short and long term actions (including established of a government Commissioner at the minister level, development of information and counselling system, measures for promotion of entrepreneurship, etc.)

- Institutions responsible for SME and entrepreneurship promotion were too weak to foster the formulation of such a policy. Their institutional weakness and inadequate resources limited their actions. In particular they could not implement any significant advocacy function.

- Since several ministries, agencies and institutions were involved in SME and entrepreneurship promotion, difficulties arose in coordination and elaboration of a common policy.

- The government has lacked policy-related information on SMEs and the constraints SMEs face. To formulate such a policy one needs reliable information and adequate communication between the policy makers and the business community. It lacked monitoring procedures and instruments.

- The business community has been politically too weak, inadequately organised and has not developed lobbying instruments to influence policy-making effectively. It has not clearly articulated its demands. Business people were often reluctant to collaborate with the policy makers. Since the business community is not sufficiently integrated, none of the chambers or associations can act as the single representative of the SME sector.

- There has been a lack of adequate efforts and recommendations on the part of donors in stimulating the government in SME policy issues.

3.2 Recommendations

3.2.1 *Introduction*

Some of the barriers to the formulation of an SME policy have become lower. In particular, observers have noticed growing (but still unsatisfactory) awareness among policy-makers of the importance of the development of the SME sector (and the private sector in general). Appointment of the Minister for Entrepreneurship Promotion is a sign of this and increases the opportunities for formulation and adoption of a coherent government policy towards the private sector and SMEs in particular. However, several other barriers still limit the possibility for formulation, adoption and implementation of such a policy.

To overcome these barriers and to develop a coherent SME policy as well as for current and future effective policy-making the following actions are recommended.

a. Initiate systematic policy process for coherent SME policy through adoption of an SME umbrella policy.

b. Improve the communication and coordination
   - between the ministries and government agencies dealing with SMEs;
   - between the government and the business community and business support institutions.

c. Support trends to integrate the business community at the regional and national level and assist efforts to develop lobbying instruments.

d. Provide the government with sufficient SME policy related information.

e. Initiate a campaign to increase the awareness of importance of SMEs for economic growth and general welfare.

These actions are described in the following paragraphs.

3.2.2 *Umbrella Policy*

Action:

- ❑ To proceed with the ***umbrella policy*** the Minister for Entrepreneurship Promotion, who is mandated to prepare drafts of governments programmes for private entrepreneurship support, should prepare a Policy Statement to be adopted by the Council of Ministers.

Function:

- The Statement will confirm the recognition of the importance of SMEs for economic growth and prosperity through increases in competitiveness and employment generation. SMEs have proved their essential role in this in many countries, in particular in the period of economic transformation. The small business contribution to the welfare of the Polish people, in the long run, will occur through competition between SMEs which will produce lower prices, better quality of output, and innovative goods and services.

- It will confirm that the government recognises the necessity to produce a policy regime which is supportive of competitive small businesses. The government should focus on establishing conditions in which SMEs can function effectively: produce or distribute goods and services, make profits, invest and, some of them, fail.

- It will define long and medium term objectives of government policy towards SME sector. This may be the basis for target group selection (see chapter 1).

- The statement will provide an umbrella over specific policies towards the SME sector by all the ministries in a coordinated manner, in particular for appropriate legislative steps and fiscal policy (SME Act, regulatory review, instruments stabilising regulations, obligatory assessment of new regulations, investment incentives, etc.). It will be a political frame accepted by the whole government for the advocacy role of the Minister.

Steps:

- The Minister for Entrepreneurship Promotion initiates the action drafting the statement.

- The statement will be made more precise during consultations with other Ministers, with comments coming from business community representatives and experienced business support institutions, and

- finally approved by the Council of Ministers.

The statement should be based on:

- the social and economic policy objectives defined in the Government Programme, the Assumptions for Social and Economic Policy, etc.;
- the Council of Ministers resolution regarding the scope of work of the Minister for Entrepreneurship Promotion;
- the Task Force report;
- proposals from business organisations.

The umbrella policy will not replace specific policies, it can only make a base for them.

3.2.3 *Improving Communication and Coordination*

To adopt a coherent SME policy as well as for current and future effective policy-making, ***government has to improve internal communication and coordination*** as well as SME advocacy in the government. The following actions are recommended to be undertaken as soon as possible:

- ❑ Establish a special *Coordinating Committee* consisting of officials in charge of SME development (from Ministry of Industry and Trade, Ministry of Labour, Bureau for Foreign Assistance, Ministry of Finance, Ministry of Justice, etc.).
  - The Committee should be set up by the Prime Minister at the initiative of the Minister for Entrepreneurship Promotion;
  - It should be chaired by the Minister for Entrepreneurship Promotion;
  - It should meet periodically to discuss specific policies in relation to overall SME policy, current and programmatic issues, coordinate SME related activities of various ministries, and improve collaboration between the ministries.
  - The Cabinet of the Minister for Entrepreneurship Promotion will serve as the Committee secretariat.

  Estimated cost: $10,000

- ❑ To fulfil his ***role of the advocate of the SME sector*** in government and the member of the government mandated to formulate and foster government SME policy, the Minister for Entrepreneurship Promotion should be given appropriate standing required to allow him to intervene in legislative development and regulatory proceedings, e.g.
  - the Minister should assign and if necessary hire several persons to advocacy staff and procurement staff;
  - a Research and Analysis Unit be created at arm's length from the Minister (see 3.5);

- more substantial funds be assigned for these tasks from the government and donor sources.

Estimated cost: $100,000

To improve the communication between the government and the business community, channels for communication at national and regional level need also to be created, in particular:

- ❑ Create an advisory body - the *Council for Entrepreneurship* - to the Prime Minister or the Minister for Entrepreneurship Promotion (who is mandated to represent the government in contacts with entrepreneurs).

Function:
provide the government with first hand opinion of business community leaders on relevant issues, increase their influence on policy-making process, develop the advocacy role of the Minister for Entrepreneurship Promotion.

- The Council should consist of delegates of major business associations. The business organisations should be appointed following defined rules of admission (to encourage self-organisation and integration of the business community) such as membership, geographic or sectoral coverage, etc.

- The Council should be mandated to consult on all SME-related draft legislative acts prepared by the government as well as those draft economic programmes and regulations which the minister presents to the Council.

- The Cabinet of the Minister for Entrepreneurship Promotion will provide logistic support to the Council.

Steps:
- provision for a Council for Entrepreneurship is included into the umbrella policy statement;
- the Minister for Entrepreneurship Promotion drafts the Council's charter to be approved by the Prime Minister;
- the Prime Minister appoints the business organisations as members and they appoint delegates.

Cost: besides some operational costs and certain member's costs, the Council should be enabled to contract out certain research and analysis projects. These projects could be funded by foreign assistance. The estimated cost would be $50,000.

- ❑ Appoint *representatives/liaison people of the Minister for Entrepreneurship Promotion at the regional/voievodship level.* This is a temporary solution to improve communication between the local business communities, the Minister for Entrepreneurship Promotion and regional/local authorities as well as to stimulate establishment of autonomous regional Councils of Entrepreneurs. This action has already been initiated.

Function:

- Representatives will be the Minister's voice in the regions and the voice of the regional business community to the Minister.

- They will initiate and facilitate contacts between the business and local administration and have advocacy role at the regional level.

- They will initiate and facilitate research and analysis efforts to provide the Minister with policy-related information on SMEs in their region.

- They will stimulate the establishment of regional Councils of Entrepreneurs which will take on the functions assigned temporarily to the representatives.

Steps:

- The Minister defines terms of reference for the representatives.

- The Minister consults with regional business organisations and local authorities regarding candidates for representatives.

- Appointed representatives develop their channels for communication with local business community, local authorities and business support institutions.

Cost: because representatives are usually Voievodship office economic development department employees they should be given a small budget for tasks which exceed their present duties and to cover additional research cost when requested. Donor's assistance should be made available to support their training and efforts. Estimated cost: $5,000 per representative.

- ☐ Convene periodic *meetings of the Minister with regional business community* leaders, local authorities and business support institutions.

Steps:

- The Minister for Entrepreneurship Promotion prepares and makes public a Calendar of meetings in different regions.

- Minister's representatives organise the meetings in their regions in cooperation with local business community leaders.

Function: as for the advisory body.

Costs: pm

In addition to these actions, it is important to encourage trends toward integration and development of business associations. Additional measures are presented in section 7.

3.2.4 *Research and Analysis Unit*

To make proper decisions the government needs reliable SME policy-related information. Availability of essential data and information is also critical for effective advocacy. Without the factual base, arguments made by the SMEs or by the Minister will be looked on as special interest pleading. Effective information can highlight the real nature of the problem and can clarify why the desired policy is important not only to SMEs but also to the general welfare.

The Cabinet of the Minister for Entrepreneurship Promotion should sponsor or conduct research on the role of SMEs in the Polish economy, including studies of the manner in which SMEs and entrepreneurship affect the economy, and studies of the manner in which the economy, regulations and policies affect SMEs. This may be obtained through the *creation of a Research and Analysis Unit* (RAU) which will provide the government with the necessary SME-related information.

Function:

- The Unit will gather and analyse quantitative and qualitative information on existing SMEs, analyse trends in the sector, needs, opportunities and threats for SME development and other information collected for specific questions. The Unit should also report annually on the state of the sector.

- The Unit will either carry out itself or contract out monitoring and assessment of effects of specific government policies as well as projects for SME support and entrepreneurship promotion.

- A data collection function should be defined depending on lack of SME related data in main data collection agencies.

- The Unit should organise a "think tank" to deepen analysis of major issues.

- Analysis of draft laws and regulations as a part of obligatory assessment procedure may also be assigned to the Unit.

- The Unit should work at arm's length from the Minister for Entrepreneurship Promotion.

The above research and analysis activities have been done to some degree by several research institutes and assistance projects. The unit should use the information and expertise accumulated in major business support institutions. Their knowledge may be useful to: identify specific needs and opportunities of SMEs especially at the regional level; provide concepts and instruments for business support positively tested by one institution which may be applied elsewhere; define appropriate procedures for selection, financing, monitoring and evaluation of assistance projects.

Steps:

- Responsibility for the implementation of the new Unit should be given to a member of the Cabinet of the Minister for Entrepreneurship Promotion who should be given the task to produce a plan within one month detailing the costs, responsibilities and funding opportunities for the Unit. Production of this plan will involve discussions with donors and interested organisations working in Poland. Clearly, opportunities for funding, particularly from the donor side, may have an influence on the exact nature of the new Unit.

- On the basis of the study scope of work and specific functions are defined.

- These research and analysis tasks may be contracted to an independent institution (existing or newly created), selected on a competitive basis. This model has proven effective in other countries. A close working relationship between the unit and the Cabinet of the Minister for Entrepreneurship Promotion should be developed.

- The Unit should be obliged to use at least 50% of funds it has available to contract out with non-governmental or private institutions for research, analysis or information collection.

A foreign assistance project should be set up to support these efforts in funds, expertise and information.

Costs: assuming 10-15 staff and a foreign advisor gradually withdrawing, for the basic research and analysis with little data collection:
year 1: $350,000; year 2: $300,000; year 3 and later: $250,000.

3.2.5 *Awareness Campaign*

Whilst observers have noticed growing awareness of the importance of the development of the SME sector (and the private sector in general) the level is not yet satisfactory, even among policy makers, legislators, etc. An ***awareness campaign*** - concerted efforts of the Minister, business associations, entrepreneurship promotion institutions, donors, etc. is therefore recommended to all Task Force members. For example:

- the Task Force Report should be exploited for this purpose. The Report or its summary should be distributed among policy makers, legislators, media, etc.

- public statements or press releases at other occasions highlighting the importance of entrepreneurship and SMEs;

- awards for journalists, newspapers, tv/radio programmes, promoting actively entrepreneurship and positive thinking on SMEs.

Costs: $50,000

4. Law/Regulations

4.1 Elaboration of the Constraints

Entrepreneurs, bankers, business support providers state that various laws and regulations are inadequate for a modern market driven economy, in particular in the regulatory framework for financial institutions serving SMEs. Frequent and sudden changes of regulations make impossible any serious business planning and may affect even a well prepared enterprise. The problems of SMEs are not sufficiently considered in the legislative process. Legislators, administrators and courts lack experience in fostering a free market economy.

4.2 Recommendations

4.2.1 *Introduction*

It is the basic duty of the government to create and foster the legal and regulatory framework, institutions and mechanisms needed to keep the market working smoothly - to facilitate exchange between private individuals and private companies. The SMEs cannot themselves set the official rules by which markets effectively operate. The long term goal of the government policy towards SMEs should be to accomplish this structural activity.

Specific legislative steps should reflect the objectives of the umbrella policy and address major constraints identified in the legal and regulatory framework. The following measures are recommended:

a. SME Act;
b. Stabilisation of the Regulatory Framework;
c. Regulatory Review;
d. Obligatory Assessment of proposed new regulations;
e. Specific issues: speeding up the Civil Law reform and the Public Procurement Act.

4.2.2 *An SME Act*

The main expression of the adoption of an SME umbrella policy may be ***an SME Act***. Its function is to:

- strengthen the recognition of the importance of SMEs and the government's commitment to foster SMEs and entrepreneurship;
- provide a legal basis for various policy measures;
- create more confidence in the government among entrepreneurs.

In such an act it should be:

- emphasised that SMEs are important for economic growth, prosperity, competitiveness and labour generation;
- stipulated that comprehensive measures will be taken in the fields influencing the SME sector;
- acknowledged that the government is to take legislative steps required to implement appropriate measures;
- defined which firms belong to the SME sector;
- stipulated that SME policy formulation and implementation is a joint effort of the Government and the SME sector, in which both carry responsibility, respecting each others positions.

Specific measures may be presented depending on policy objectives adopted. In particular, the Act should include provisions for:

- relative stability of regulations influencing the environment of business;
- regulatory review;
- obligatory assessment of all legislation/regulations that may affect SMEs;
- creation of an advisory body to the government - Council for Entrepreneurship.

Steps:

- provision for the Act should be included in the Policy Statement. During consultations on the Policy Statement the Minister for Entrepreneurship should discuss the issue bilaterally with other Ministers and the Prime Minister;

- the umbrella policy having been adopted by the government, the Minister for Entrepreneurship Promotion should draft the Act on this basis. Use of foreign assistance to provide western experience of SME legislation is recommended.

- the draft is submitted to the Council for Entrepreneurship and for interministerial consultation;

- when approved it will be sent to the Parliament. SME organisations and Chambers increase their lobbying efforts to ensure support for the Act in the Parliament.

Costs: steps are a part of duties of the Minister. Some foreign assistance to present and advise on western experiences. Estimated costs: $25,000.

4.2.3 *Stabilising the Regulatory Framework*

Poland is undergoing deep transformation and changes in laws and regulations are inevitable. However, for the economy certain balance of change and stability is

necessary. The government should make *special efforts to avoid sudden and frequent shifts* which will increase business people's confidence in stability of regulatory framework and ability to plan, such as:

- Guarantees of a minimum length of time between an act being adopted and coming into force, except where special circumstances require otherwise. This should apply especially to acts that require some adaptation efforts in enterprises. The relative burden for SMEs must be taken into consideration.

- Wherever possible strategic programmes of legal and regulatory reforms and directions for changes in regulations should be published. It may take form of "Calendars of Proposed Regulations" published by the ministries. The programme of adaptation to the EC norms and standards may serve as a framework.

- Advocacy staff of the Minister for Entrepreneurship Promotion should be obliged to raise the issue explicitly and loudly when too frequent change occurs.

Steps:

- specific legal conditions to introduction of these instruments and possible adverse effects should be investigated by the Minister for Entrepreneurship Promotion staff with outside legal experts and possibly Ministry of Justice. Experience of similar instruments and their results in other countries can be provided under a foreign assistance project.

- provision for such measures to be included in the Policy Statement;

- the Minister for Entrepreneurship Promotion staff draft the documents with assistance from outside Polish and foreign experts;

- provision for such stabilising mechanisms can be included in the SME Act or adopted in other appropriate form to be defined during the process.

Costs: pm

4.2.4 *Regulatory Review*

To identify and examine specific constraints in present legal and regulatory framework, a *regulatory review* should be undertaken.

Steps:

- Provision for such a Review is to be included into the umbrella policy.

- A Review Commission should be established by the Minister for Entrepreneurship Promotion, consisting of lawyers, business practitioners, consultants, etc. (5-10 persons).

- Several partial lists of legal and regulatory constraints have already been prepared (for example, by Union of Polish Crafts, and GEMINI) and may be used as a basis. Chambers and Associations should be invited to submit their recommendations to the commission.

- Identified constraints should be prioritised by the Minister in consultation with the Council for Entrepreneurship. The priority constraints will be elaborated and options for amendment or removal investigated.

- Action to address the elaborated constraints will be initiated and supported by the Minister. The Minister should bring them in attention of other relevant ministries, the Ministry of Justice and Ministry of Finance in particular.

Provision for such a regulatory review can be included in the SME Act.

Foreign assistance should support the Commission efforts. The Review may be repeated annually, but of course on a much smaller scale.

Costs: Main review costs are estimated at $100,000; annual review costs at $25,000

4.2.5 *Obligatory Assessment of Laws and Regulations*

To limit the possibility of introduction of new laws and regulations adverse to SMEs, all proposed laws and regulations that may influence the SME environment should be sent to the Minister for Entrepreneurship Promotion for examination.

Steps:

- Provision for such an obligatory assessment to be included into the umbrella policy.

- The Minister assigns analysis of drafts to a selected staff or to a specific committee as necessary. This may also be a function of the Research and Analysis Unit. Transparency, simplicity and relative costs for SME should be given particular consideration.

- Analysis should be presented to the Council for Entrepreneurship.

- Assessments should be presented to relevant bodies: other ministries, Governmental Committees (KERM, KSERM), Parliamentary Commissions.

- the Minister for Entrepreneurship and his advocacy staff should endeavour to convince relevant bodies regarding the problems of SMEs.

Provision for such an obligatory assessment should be included in the SME Act. If not, such a Review should be made obligatory by strengthening the Resolution of the Council of Ministers of November 20, 1992, par. 3.2.1.

Time: the analysis should start as soon as possible. For example the Public Procurement Act analysis may serve to develop procedures for analysis and consultation. Regular obligatory assessment will start when the umbrella policy is approved.

Costs: pm. depends on volume of new regulations, but can be approximately $100,000.

4.2.6 *Specific Issues*

There are a number of regulatory problems identified and already being considered. In particular:

Civil Law Reform

The Ministry of Justice Commission for the Reform of Civil Law has worked on several acts essential for the banking sector. To speed up and improve the process of the reform the Commission should be supported in these efforts. It is recommended that at the initiative of the Minister for Entrepreneurship the following steps are undertaken:

- Priorities are set among the laws needing reform. ***Collateral Law, Acts on Commercial and Collateral Register,*** will all necessarily be priorities due to their importance in financing of SMEs.

- Appropriate funds are allocated to the Commission (for experts, operational costs, etc). A Foundation for Polish Civil Law Reform is now being created which donors (both foreign and Polish) should use to channel the funds. An international board of directors led by Polish jurists will be able to direct money to needed reform projects. Progress of work will depend on funds available.

- A reasonable schedule for prioritised tasks should be set with the Ministry of Justice and the Commission.

- The Union of Polish Banks should continue to organise meetings with the members of the Commission to discuss questions which bankers face in practice. The Minister for Entrepreneurship Promotion should support such contacts.

- When a draft law is ready, the Minister for Entrepreneurship Promotion and other interested parties (banks, business representatives) should convince the government to use the fast legislative track or extended (decree) powers (if granted).

Costs: pm

Public Procurement

The public procurement system is of high importance for SMEs. Until now procurement practices have been unfavourable to SMEs. A draft Public Procurement Act is being prepared in the Central Planning Office and will soon be sent for interministerial consultation. The following steps are recommended:

- The Minister for Entrepreneurship Promotion Cabinet analyses the draft. Possible effects of the new public procurement system for SMEs should be carefully examined.

- Measures to compensate SMEs for their relative disadvantages (caused by smaller size, lack of collateral etc.) should be planned in advance. Study of relevant policies in other countries be undertaken in the Cabinet. Foreign assistance will be helpful to find appropriate concepts.

- The Minister for Entrepreneurship Promotion should ensure that the Act includes provisions allowing for introduction of measures to decrease barriers that SMEs face in access to public procurement. SME organisations should similarly lobby in the Parliament for SME favourable provisions in the Act.

- When voted for, the government and business organisations should publicise the rules defined in the Procurement Act, and sponsor the training to be carried out by the Bureau for Public Procurement on how to deal with SMEs.

- Facilitating SME access to public procurement will be a major task for the Minister for Entrepreneurship Promotion staff. They should develop close working relationship with the Bureau for Public Procurement.

Costs: pm

The Accounting System

Accounting is an essential device to measure and evaluate the enterprise. The present accounting system is not appropriate to a modern market driven economy and does not provide businesses with useful information. Reforming the principles and regulations ruling the accounting system would

- help companies better understand and resolve their own problems;
- help banks in assessing prospective borrowers;
- help the tax authorities, etc.

For these reasons it is recommended that the Association of Accountants in Poland should initiate a joint action with the Ministry of Finance to review the existing regulations and principles of accounting in Poland and to study possibilities of

improvement. Although accountancy regulations are primarily the responsibility of the accountancy profession, the current state of transition and the effects on, for example, tax matters, means that the government should be involved in any proposals for change.

For this task a group of experts should be contracted. Foreign assistance project(s) should support these efforts.

5. Taxes

5.1 Introduction

SMEs do not have enough financial means to invest. This problem can partly be solved by giving them certain tax preferences. Poland has a serious budget deficit problem and room for tax incentives is limited. Nonetheless it is possible to adopt a number of policy measures which would not necessarily have negative budgetary effect. Incentives for SME investment and employment generation can pay themselves back by increased revenue from a larger private sector.

There is a need for equity capital, particularly for SMEs (also see chapter 6, Financing) and there are private persons willing to invest in SMEs but the existing tax system does not stimulate investment in private businesses. There are no tax incentives to stimulate equity financing. The existing regulations even discourage equity financing since as regards income tax interest from savings and government bonds are considered as tax free and dividends not. Risk-free government bonds used to finance budget deficit are an attractive alternative for investment in business.

The third constraint related to taxes is the current situation whereby taxes are perceived as very high by entrepreneurs but control is rather limited. Consequently much private economic activity goes on in the informal sector. It therefore creates no revenue for the state through taxes and enlarges unfair competition to entrepreneurs paying taxes.

5.2 Recommendations

5.2.1 *Introduction*

If adopted, the umbrella policy/SME Act will provide a basis for a more active tax policy towards the SMEs or targeted groups among the SMEs, depending on the policy objectives.

To stimulate investments by SMEs tax measures should be developed. This action is described in 5.2.2.

To stimulate private persons to invest in the equity of SMEs
the following tax measures must be implemented:

- income from dividends should be treated equally with income from bank savings in terms of tax
- a certain percentage of investment in equity by private persons should be tax deductible.

These actions are described in 5.2.3, respectively 5.2.4

In the final paragraph an action is described to improve the tax collecting system.

5.2.2 *Tax Measures to stimulate Investment by SMEs*

Functioning

As described there are limited tax measures to stimulate investments by SMEs. Examples of possible tax measures could be:

- extending the application of regulations which allow for tax deductions for job generating investment in equipment in high unemployment regions. Their effects should be monitored and, if possible, application of this incentive extended to other regions, sectors, etc.
- extending the income tax deduction (for both legal and natural persons) for investment in SOEs under privatisation.
- other incentives which proved to be good instruments in other countries should be considered, for example: a general profit apportionment scheme under which companies with sharp profit fluctuations spread profit/losses over a certain numbers of years backwards as well as forwards; an allowance for self-employment; tax deductions for investment related to objectives of the SME-policy, such as investment in new technologies or Research and Development, etc.
- complementary measures on tariffs, for example reducing the tariffs on raw materials and means of production should also be investigated.

Advantages/Disadvantages

Advantages:

- the tax measures will improve the possibilities for SME to invest.
- tax measures will reach all the firms

Disadvantages:

- without any restructuring of the government budget, tax incentives will in the short run lead to an increase of the government budget deficit. In the longer run, however, an increase of the tax revenues can be expected from the increased profits of the firms.

Implementation steps

To develop these measures a project must be started consisting of the following steps:

1. make a comprehensive expert review of current tax legislation, in close cooperation with the Ministry of Finance, in order to develop detailed revenue-neutral measures to improve the way the tax system affects the SME sector
2. make an inventory of possible tax measures which can be implemented in Poland on the basis of the existing tax system and on the basis of information abroad.
3. analyse the effects of the selected measures on:
   - behaviour of companies and on
   - the tax revenues of the government.

4. study the possibilities for changes in the tax system such that this measure has no negative consequences for the government budget (budget neutral).
5. introducing measures with limited scope and monitoring the results.

Actors
The Cabinet of the Minister of Entrepreneurship Promotion, the Ministry of Finance, and the Bureau for Foreign Assistance should approach foreign donors for assistance of this project.

Time schedule
This action can be started immediately.

Financing
Steps 1 to 3 should be financed in the framework of Technical and Financial Assistance programmes of foreign donors.

Costs
Steps 1 to 3 involve ad hoc costs.
Estimated costs $ 100,000

5.2.3 *Income of Dividends versus Interest*

Functioning
The tax system must be changed so that income from dividends is treated in the same way as income from interest.

Advantages/Disadvantages
Advantages:
- due to this measure there will be more equity investment available for SMEs
- investment by private persons will decrease the debt/equity ratio.
- most SMEs are sole traders and most of them raise their capital from private persons including relatives and friends. Therefore these tax measures can have a real, if marginal, effect on a larger number of SMEs than venture capital institutions can.

Disadvantages:
- in the case that tax on dividends is decreased without any restructuring of the government budget, the measures will in the short run lead to an increase of the government budget deficit. In the longer run however an increase of the tax revenues can be expected due to the fact that the firms invested in will become legal and due to their increased profits.

Implementation steps and actors
The Cabinet of the Minister for Entrepreneurship Promotion should submit to the Council of Ministers an appropriate draft to amend the existing regulations.

Time-schedule
This process should be started in the short term.

Costs
With the activities of the Cabinet of the Minister of Entrepreneurship Promotion no extra costs are involved, because they these activities to their normal tasks.

5.2.4 *Tax Incentive for Private Persons investing in SME*

Functioning
As described there is a need for equity capital, particularly for SMEs and there are private persons willing to invest in SMEs. To stimulate private persons to invest in the equity of SMEs a certain percentage of this investment should become tax deductible.

Advantages/disadvantages
Advantages:
- due to this measures there will be more equity investment available for SMEs
- investment by private persons will decrease the debt/equity ratio.
- most SMEs are sole traders and most of them raise their capital from private persons including relatives and friends. Therefore these tax measures can have a real, if marginal, effect on a larger number of SMEs than venture capital institutions can.

Disadvantages:
- Tax measures, without any restructuring of the government budget, will in the short run lead to an increase of the government budget deficit. In the longer run however (and maybe even in the short run) an increase of the tax revenues can be expected due to the fact that this provision will be an incentive for firms to regularise their tax status. Over time, the profitability of firms with adequate capital can be expected to show solid growth.

Implementation steps
To develop this measure a project must be set up in which the following activities are carried out:
1. Information must be collected on the effects of similar kind of measures existing abroad.
2. On the basis of this information a simulation must be carried out to measure the effects of the measure in the short and long run in Poland
3. Possibilities for changes in the tax system must be studied in order that this measure has no negative consequences for the government budget (budget neutral).

Actors
The Cabinet of the Minister of Entrepreneurship Promotion should approach the Bureau for Foreign Assistance and foreign donors for assistance for the project. Actions should be carried out in cooperation with, or even under the management of, the Ministry of Finance.

Time schedule
This process can be started at short notice.

Financing
The additional costs of foreign experts, cooperating in the project can be financed in the frame of Technical and Financial Assistance Programmes of foreign donors. As far as extra work force is necessary it must be discussed with the donor involved.

Costs
The costs involved are all ad hoc costs. These costs comprise only the costs of the expert(s).
The activities of the other parties involved belong to their normal tasks so no additional costs are involved. However it may be necessary that these parties need extra work force. Estimated ad hoc costs of experts: $25,000

5.2.5 *Tax Collection*

Functioning
Much of the economic activity in the SME sector is conducted in the informal sector. The Ministry of Finance should be assisted in its efforts to improve tax collection.

Advantages/Disadvantages
Advantages:
- the tax revenues for the government will raise
- unfair competition between SMEs will be reduced
- SMEs will be obliged to improve their book-keeping

Disadvantages:
- For the SMEs, which are not paying the tax they are obliged to, the income and consequently their ability to develop the firm, will decrease.

Implementation steps
1. Consultation with the appropriate department of the Ministry of Finance regarding the progress of their activities and their needs.
2. If necessary provide the tax control department of the Ministry of Finance with expertise and assistance.

Actors
The Ministry of Finance and the Bureau for Foreign Assistance should approach foreign donors for assistance.

Time schedule
This action can be started in the short term.

Financing
This action should be supported in the frame of Technical and Financial Assistance programmes of foreign donors. As far as extra work force is necessary it must be discussed with the donor involved.

Costs

The costs of the identification mission are ad hoc costs. These costs comprise only the costs of the expert(s). Estimated costs: $ 25,000

The activities of the other parties involved belong to their normal tasks so no additional costs are involved. However it may be that these parties need extra work force.

6. Financing

6.1 Elaboration of Constraints

6.1.1 Payments

Underdeveloped regular banking services
Banks operate under very difficult conditions and like many aspects linked with transferring the Polish economy into a market economy, the regular banking services are still underdeveloped. Especially for private businesses, routine payments mean an extensive administrative burden and are very time consuming, time and energy which can better be used for making more well-considered decisions. One of the causes of the underdeveloped services is the underdeveloped clearing system between banks in Poland.

6.1.2 Credit

Banks do not finance private business adequately
Several reasons are mentioned why banks are not financing private business adequately in terms of overdrafts and term credit.

The first reason is that banks are undercapitalised and are therefore not able or not allowed to give loans.

Secondly, banks consider the operational costs of giving loans to SME too high in relation to the size of the loan.

A third reason mentioned is that banks have possibilities to invest their money into state bonds and bills or inter bank deposits which are less risky than private business. In criticising this attitude first it has to be stressed that it is one of the main obligations of banks not to put their money in risky business because they are lending not their own money but the money of those who deposited it at the bank. However to earn some profits, normal banking practice means that banks have to take risks. The basic problem is how to assess the risk of financial transactions.

Risk aversion
In dealing with this problem one has to bear in mind several reasons mentioned why Polish banks are even more risk-averse than average banks.

- Polish banks have become more risk-averse due to the high rate of bad loans.
- Polish banks have less experience in assessing private sector creditworthiness and risk.
- There is inadequate collateral law and in particular an ineffective collateral register which means that banks have no guarantee that the collateral is not already pledged.
- The existing bankruptcy law reduces the possibility that banks get some repayment when firms go bankrupt.

- Banks meet problems in getting sound information on businesses which want credit. At this moment banks have limited possibilities to check whether firms really exist and to gather reliable business information on business. When firms are registered they are registered at different courts depending on their legal form and in different regions. In any case these registers give insufficient information on the business activities of the firms. However, a new act on commercial registers is already in preparation.

Documentation, reports and interviews suggest that banks will give more credit to private business if there are other institutions to share the risks with.

Regarding the state owned banks there is another problem hampering the provision of loans to private business. There are no incentives but even disincentives to take risk by these banks. Due to the fact that there is no well defined definition of risk, managers of state owned banks can be prosecuted if the bank makes losses.

High interest rates
If loans are provided to private business many of them consider the interest rates (nominal and real) as too high. The high interest rates are caused by the high inflation rate and the bank margins charged by banks. The level of interest rates is determined by:

- the high saving rates banks must pay to attract current and time deposits
- the fact that banks must account for loan loss reserves.

The high rates banks have to pay on deposits is among others linked with the alternatives persons have in investing their savings, for instance in government bonds.

Regarding the attraction of deposits by banks it must be mentioned that the regulatory/legal framework regarding banks leads to unfair competition between banks. For example the fact that savings in state banks are guaranteed by the state and those of private banks not.

It can be expected that margins banks have to charge for overcoming loan loss reserves will diminish in the course of time as banks work more efficiently and restructure their portfolios.

The interest rate is linked to the rate of inflation and psychologically this seems very high. In any case the real inflation rate for different sectors of the economy varies and therefore the real interest rate for a loan varies with it.

Additionally the current depressed state of the economy means that many SMEs cannot make profits high enough even to cover normal bank margins.

Size requirements are too high
Most private business complain that the actual or formal minimum loan size requirements are too high. On the other hand banks stated that the operational costs of handling small loans is too high in relation to the revenues.

Loan monitoring
Private business which had bank loans complain that the banks are not flexible enough regarding rescheduling the repayment of loans. Banks keep too strictly to the rules and have a lack of experience in judging the development of business.

In addition, banks insufficiently monitor the loans provided to private business. Consequently banks are not aware of the development of the firms and are not able to assist the firms in time.

Application requirements
Private business approaching banks for loans complain that the required credit documents are too detailed and time-consuming to complete. Banks seem to be unable or even unwilling to assist private business, which can be assumed as one of the tasks of banks if they want to develop themselves in the future.

Hiring consultancy for completing the application forms by SME for this purpose can prove to be very expensive. One of the interviewees stated that the costs could be as high as 10% of the loan needed.

Another aspect regarding the application of loans is that private business are not willing or able to show banks their true financial position which makes it even more difficult for banks to make a sound judgement of the application.

Foreign exchange loans
There seems to be a tendency that the preference of private business for foreign currency loans rather than złoty loans because of much lower interest rates is decreasing. This may be partly because private business now seems to recognise the foreign exchange risk.

6.1.3 Equity

Unavailability of equity capital
One of the reasons of the lack of equity is the lack of domestic or foreign venture capital institutions at this moment. This lack is partly caused by a lack of bankable demand for venture capital. Due to the high operational costs and the high risk of venture capital participation this participation is only profitable if it concerns relatively large amounts of capital invested. In other words venture capital operations in smaller firms are in general not very profitable. In any case, especially in smaller firms, entrepreneurs are reluctant to jointly invest in and "share" control of their businesses. At this moment there are a lot of small firms and many large firms but only a relatively small number of medium-sized business in which it is profitable to invest venture capital.

A second reason which hampers the availability of equity capital is that there is not a developed security market where securities can be dealt in.

The existing tax system does not stimulate investment in private businesses. There are no tax incentives to stimulate equity financing. The existing regulations even discourage equity financing since as regards income tax interest from savings and government bonds are considered as tax free and dividends not.

6.1.4 Other Financial Institutions

There is a lack of financial institutions other than banks which can assist SMEs in their development. Institutions for, for example, leasing, factoring and insurance. Reasons can be found in the undeveloped legal framework for these institutions to carry out their activities properly. In addition, institutions which support the banking sector, for example in credit rating are poorly developed.

6.2 Recommendations

6.2.1 Introduction

In paragraph 6.1 an elaboration is given of the constraints which are hampering financing of SMEs. On the basis of interviews, documents and reports the Secretariat has selected possible actions to cover these constraints. In annex E these possible further actions are described.

These possible actions were discussed in the Task Force meeting and with individual interviews with the Task Force members. The final actions recommended by the Task Force are elaborated in this paragraph. In addition to these actions, a number of actions in other sections of the report have a bearing on the functioning of the banking system and financial instruments. Such actions include the development of collateral law and a collateral register; establishment of a commercial register; tax measures; and business support activities.

To improve the banking services two actions are recommended, namely:
- support for the establishment of a National Clearing Chamber
- support and coordination of training initiatives for bank personnel

These actions are elaborated in paragraph 6.2.2 paragraph and 6.2.3 respectively.

Two actions are presented to improve the environment for financial institutions. In section 6.2.4 actions to improve the capital market are elaborated and in section 6.2.5 actions to establish a credit rating service.

Lack of collateral by SMEs and the unwillingness of banks to take risks are mentioned as major constraints for bank financing of SMEs. To overcome these constraints a Guarantee facility should be set up. A distinction can be made between Mutual Guarantee Schemes and a Loan Guarantee Schemes. Due to the fact that

there are already initiatives to set up both kind of schemes and due to the fact that both have advantages and disadvantages it is recommended that actions are taken to set up pilot projects for both kinds of scheme. Paragraph 6.2.6 describes action to establish pilot projects for both Mutual Guarantee Scheme(s) and a Loan guarantee Scheme.

As mentioned before one of the reasons that banks are not willing to take risk is the lack of information on their clients. In chapter 7 (Information and Counselling) an action is described to develop a proper system of business registration.

Finally, two actions are elaborated to overcome the high costs of loans for SMEs. Paragraph 6.2.7 outlines the implementation of a Grant scheme based on Commercial Loans and in 6.2.8 attention is paid to Credit Line with preferential terms.

To improve the supply of equity to SMEs, a tax allowance for investments by private persons in SMEs is suggested. In addition, income from dividends should be treated similar as income from interest. Both measures are described in chapter 5 (Taxes).

6.2.2 *National Clearing Chamber*

Functioning
A National Clearing Chamber (KIR) has recently been set up with the task to introduce a national clearing system. In addition a company called Telbank is established. This company is building up a computerised inter-bank communication network. Both companies are owned by The National Bank of Poland, some individual banks and the Union of Polish banks. These initiatives should be supported.

Advantages/Disadvantages
A clearing system is a tool to improve the regular banking services. Especially for private businesses, routine payments mean an extensive administrative burden and are very time consuming, time and energy which can better be used for making more well-considered decisions.

Implementation steps
1. Consultation with the National Clearing Chamber and Telbank to identify the progress of their activities and their needs.
2. If necessary provide the National Clearing Chamber and Telbank with assistance such as, for example, the training of personnel in working with a computerised system.

Actors
The Union of Polish Banks in cooperation with a representative of the National Clearing Chamber and of Telbank should approach foreign donors for support. Negotiations with foreign donors should take place through the Bureau for Foreign Assistance.

Expert(s) in clearing systems in cooperation with a selected number of individual banks, the Union of Polish Banks, and the National Bank of Poland should identify the project and the necessary financial support for the project.

Time schedule
This action can and should be started immediately because the National Clearing Chamber and Telbank are already working on it and the sooner it works the better.

Financing
This action should be supported in the frame of Technical and Financial Assistance programmes of foreign donors. As far as extra work force is necessary it must be discussed with the donor involved.

Costs
The costs of the identification mission are ad hoc costs. These costs comprise only the costs of the expert(s). Estimated costs: $20,000

The activities of the other parties involved belong to their normal tasks so no additional costs are involved. However it may be necessary that these parties need extra work force.

The costs of implementing the assistance needed, are to be presented by the identification mission. Some of the costs may be ad hoc such as those linked to activities aimed at getting the system computerised (buying computers etc..).
The costs of other activities such as training will depend on aspects such as:

- is a course already developed
- the size of the course
- the number of persons who need to be trained, etc..

6.2.3 Training of Bank Personnel

Function
Currently there are a number of projects consisting of training bank personnel. It is recommended that the existing projects aimed at informing, advising and training banks should be supported and coordinated in fields such as:

- normal payments, overdrafts, letters of credit, etc..
- customer friendly activities such as informing clients on the services of the bank
- assessing creditworthiness and risk evaluation
- loan monitoring
- restructuring of loans like rescheduling the repayment of loans
- procedure on valuing assets/collateral, etc.

Advantages/Disadvantages
This training will improve the ability of banking personnel to work with SMEs and to provide them with all the banking services they need to run their business properly and efficiently.

Implementation steps
The existing initiatives being undertaken by the PHARE Programme Implementation Unit in the Ministry of Finance and the Foundation for the Development of the Financial Sector should be supported. The PHARE PIU is already creating an inventory of donor-funded initiatives.

Between these two bodies the following tasks need to be undertaken:
1. making an inventory on all existing activities taken in this field;
2. creating criteria (a national curriculum) on which the existing initiatives can be judged to improve the quality if necessary;
3. collection of information on the training which is missing. Courses on subjects which are not yet covered could then be initiated;
4. designing of a support scheme providing subsidies for costs of courses on subjects linked with financing of SMEs.

Actors
As well as the two bodies identified above, coordination with foreign donors should be done through the Bureau for Foreign Assistance. Training activities should be done in cooperation with the Task Force for Training and Human Resources in the Cooperation Fund which has been assigned responsibility for all training matters by the Polish government.

Time schedule
This action is already ongoing

Financing
The activities of the PHARE project at the Ministry of Finance, of the Task Force for Training and Human Resources, and of the Foundation for the Development of the Financial Sector cover what is required for this recommendation. Any further finance required could come from other foreign donors.

Costs
The recurring costs of actual training should be paid by the banks themselves on a commercial basis, at least in the long run.

6.2.4 *Improvement of the Capital Market*

Functioning
To speed up the evolution of a normal capital market, as well as better banks, a wide variety of instruments and institutions should be developed, including:
- broker arranged private placement of shares, to provide funds beyond those available from internal generation, and from relatives and friends;

order to provide each other with the necessary securities, in the form of guarantees to raise capital from commercial sources. These enterprises form a Mutual Guarantee Company which administers a Fund." Mutual Guarantee Schemes are mostly set up on a regional basis. Equally, it is possible to set up a Mutual Guarantee Scheme between main and sub-contractors in the distribution sector.

Under a Mutual Guarantee Scheme the firm approaches the Mutual Guarantee Company for a guarantee. The Mutual Guarantee Company than assesses the viability of the project taking into account the qualifications and characteristics of the entrepreneur. If approved the Company approaches the bank and negotiates the conditions of the loan.

Loan Guarantee Schemes
Under a Loan Guarantee Scheme banks can ask for a guarantee for loans which they provide to small and medium-sized business. The guarantee is given by a special Institution which administers a Guarantee Fund from which the losses are paid. In this case the Entrepreneur approaches the bank directly.

Funding
In the case of a Mutual Guarantee Scheme the Guarantee Fund is financed by firms becoming a member in order to get a guarantee. In existing schemes abroad two ways can be distinguished in which the SME pays for a guarantee, namely:

- a fee which will usually include an annual charge, in most of the systems a percentage of the sum guaranteed. Additionally a initial fee is charged to cover the appraisal and administrative costs.
- a participating interest in the risk fund or equity capital of the scheme. This participation is paid back to the firm when the loan is repaid.

In addition the Fund can be financed besides individual firms by national, local and regional government, business organisations, banks and other organisations interested.

The capital for the Guarantee Fund under the Loan Guarantee Scheme comes mainly from the government. SMEs getting a guaranteed loan should pay to the Institution a provision for administrative costs of the Guarantee Institution, as a certain percentage of the money guaranteed.

In both kinds of schemes the size of the Guarantee Fund must be above a certain minimum because the investment revenues and the extra fees must cover operational costs of the Institution and the losses. It is necessary that the capital of the Fund will be invested in risk free investments. Guarantee Institutions should not be obliged to pay any tax since they constitute a mean of facilitating financing for SME.

Eligibility criteria
Under a Loan Guarantee Scheme the government, as the main initiator and financier, should develop eligibility criteria for SMEs benefiting from the scheme

and the banks applying for the guarantees. The eligibility criteria for SMEs can vary depending on the objectives of the government. Criteria could be:

- linked with the activities of the firm, for instance SME in the manufacturing or export sector
- linked with the size of the firm such as firms with less than 100 employees, etc..

The banks applying for the loans should also meet certain criteria, for example:

- have enough regional cover
- meet certain solvency criteria
- give a certain percentage of their loans to SMEs to show that they are able and have enough experience to work with SME
- be willing to train their personnel to serve SMEs, etc..

Under a Mutual Guarantee Scheme the members themselves decide on the eligibility criteria.

Functions of the guarantee institutions

The Mutual Guarantee Company has the following functions:

- Commercial Function; attracting partners and researching and analysing their transactions
- Assessment function: All the applications are assessed by the Company.
- Control and Monitoring Function: in order to ensure that bad debts are kept to a minimum the Mutual Guarantee Company has to check that all partners fulfil their obligations. If non-fulfilment occurs an agreement must be made between the interested parties to minimise as much as possible the losses.
- Management of delayed payments: After the Company has paid to the defaulting party, the Legal Department will take the necessary steps to recover the portion already paid on the loan guarantee.
- Administrative functions: this will cover all tasks relating to payments, accounting, data processing, personnel matters, etc..
- Management functions: The Company will need a general manager who will be in charge of overseeing and coordination all other functions involved as well establishing and maintaining contacts with financial institutions and other entities.

The Institution responsible for the Loan Guarantee Scheme will have the following functions:

- Administrative function: this will cover all tasks relating to processing applications, contact with banks, payments, accounting, data processing, etc..
- Management function: the Institution will need a general manager who will be in charge of overseeing and coordination all other functions involved

The other functions depend heavily on the tasks of the Institution decided upon. In most existing guarantee schemes abroad the banks select the firms which need a guaranteed loan and the banks applying for a guarantee. This system is only possible under a well developed banking system. At the beginning of chapter 6 constraints were mentioned regarding the fact that SMEs cannot obtain or are not

willing to use bank loans. One of the constraints mentioned was that banks are not able to evaluate projects and to assess the risk. This problem must be solved in order to establish a viable guarantee scheme. Measures to be taken include:

- training the banks, but it will take some time before the banks have the necessary experience for judging good projects (see 6.2.3)
- giving the Guarantee Institution the task of assessing the projects brought forward by the banks. In this case the Institution must have experts who carry out this task. This can be seen as a double check. Although this double check will increase the administrative burden linked with the guarantee and make the whole procedure longer, it can be considered as necessary to reduce the losses of the scheme. In the long run when the banking structure will be improved this function can be abolished or at least reduced.

Special advantages of a Mutual Guarantee Scheme

Due to the fact that firms are guaranteeing each other a default of one company has consequences for all members. Because the Companies are set up regionally the members are known by each other. Due to this "social control" firms will do their best to repay the loan and in case of default repay the Company.

Role of the government in of both schemes:

Guarantee Schemes will only function if the government carries out the following activities:

- Supervision: the activities of the Guarantee institutions must be supervised so that the Fund is administered properly. In addition it has to be checked how the Fund is administered and in what way the capital of the Fund is invested
- The government may provide a re-guarantee so that the banks will see the Guarantee Institution as a reliable partner. In this case there must be clear rules and agreements.
- In both schemes government support is needed. Under the Loan Guarantee Scheme the government is the main financier of the Guarantee Fund. Abroad many governments also support Mutual Guarantee Schemes by the provision of part of the capital needed to start the scheme and of subsidies to reduce the costs of guarantees for SME. At the moment the government of Poland has a large budget deficit which hampers financing the re-guarantee fund and providing financial support to the Mutual Guarantee Company. Allowing an increase of the budget deficit seems to be out of the question so financial support for a Guarantee Scheme needs a restructuring of the government expenditures. Nonetheless, a certain willingness of foreign donors have been registered to finance guarantee schemes. In the STRUDER programme a budget is available for a guarantee fund. Due to the fact that this guarantee facility is not developed yet, the possibility should be examined whether it may be possible to use this budget for the establishment of a re-guarantee fund and for financial support of Mutual Guarantee Schemes in one or more of the four selected regions.

Extra role of the government for Mutual Guarantee Schemes

- The government must create the conditions to enable MGS to be established and to stimulate a positive attitude towards MGS among banks and SMEs.

Extra role of the government for Loan Guarantee Schemes

- The government must take the initiative to start the scheme.

Other conditions for both schemes:

- Banks must be able to provide loans to SME.
- Banks in the scheme must be ones willing to provide loans to SME.
- Banks must be willing to provide small loans although they consider the operational costs of giving a loan to SME as too high in relation of the size of the loan.
- Banks must be willing to take risk.
- Banks must be trained in assessing risk, evaluation of projects, valuing of collateral, etc..

Advantages to banks under both schemes:

- Banks get experience in giving loans to SME
- Reduction of risk

Additional advantages to banks under Mutual Guarantee Schemes:

- Reduction of operational costs such as marketing costs and research and operational costs, because the projects are assessed and monitored by the Mutual Guarantee Company.

Advantages to SME of both schemes:

- A Guarantee scheme improves the opportunities for SMEs to obtain financing even when they have a lack of collateral.

Additional advantages/disadvantages to SMEs under Mutual Guarantee Schemes:

- Mutual Guarantee Schemes improve the opportunities for SMEs to obtain financing and to improve the quality of the information on which banks have to decide.
- When an SME has paid its fee and is considered as a member of the Mutual Guarantee Company this means that it has to share in the losses of the Company and consequently it is not clear how much it gets back from the financial contribution.
- A Mutual Guarantee Company can provide SME expert advice on running a business such as marketing, management, production and accounting. If the transactions of the Company are increasing they are in a position to negotiate loans with more favourable conditions such as a lower interest rate or longer maturity periods.

b. Action to set up a pilot project for a Mutual Guarantee Scheme

Implementation steps

A programme must be started in which the following activities are carried out:

1. Review of the regulations to ensure that there are no legal barriers hampering the functioning of Mutual Guarantee Scheme.
2. Studying the feasibility of a re-guarantee facility and the feasibility of public financial support for Mutual Guarantee Schemes, including the feasibility to introduce a system of Mutual Guarantee Schemes in STRUDER.
3. Selecting one or more initiative(s) by a tender procedure.
4. Providing the selected Mutual Guarantee Scheme(s) with the necessary technical and financial support.
5. Development of a system (criteria) for monitoring the activities of the selected Mutual Guarantee Scheme(s) .
6. Monitoring the functioning of the selected Mutual Guarantee Scheme(s).

Time schedule

Step 1 and 2 of this programme can be started immediately (after agreement with a donor), especially when discussion with STRUDER shows a certain feasibility. On the basis of the results must be decided whether it is feasible to proceed with step 3, 4, 5 and 6. Step 4, the provision of technical and financial assistance, and 6, monitoring of the functioning, will last for a longer period.

Actors

The Cabinet of the Minister of Entrepreneurship Promotion should discuss with the Bureau for Foreign Assistance and foreign donors the possibility of financing the activities described under the different steps. The programme must be carried out by a team of Polish and foreign experts in consultation with the Ministry of Finance and other Ministries involved, the National bank of Poland, the Union of Polish banks and other parties interested in Mutual Guarantee Schemes (such as authorities, Chambers of Commerce, business organisations and individual banks).

Financing

All the activities mentioned under the different steps can be financed in the frame of Technical and Financial Assistance programmes of the foreign donors.

Costs

The costs of all the steps are ad hoc costs, except for the financial support of government of the fund if needed.
Estimated ad hoc costs of $ 75,000
The costs of the financial support can not be estimated, they depend on the size of the scheme, the functioning of the scheme etc..

c. *Action to set up a pilot project for a Loan Guarantee Scheme*

Implementation steps

For the establishment of Loan Guarantee Scheme a programme should be started consisting of the following activities:

1. Select one of the existing initiatives on the basis of:
    - All existing constraints hampering bank financing of Polish SMEs

- Relevant information in Poland such as the experience of the National Bank of Poland, the preparatory work of the Cabinet of the Minister of Entrepreneurship Promotion, the feasibility study of Gemini, the preparatory work of the Ministry of Finance Department of Financial Policy and Analysis, etc..
- Experiences abroad with Loan Guarantee Schemes
- Consultation with possible financiers and their conditions, etc..

2. Further develop the selected initiative so that it becomes operative.
3. Implementation of the Loan Guarantee Scheme. If financing is not available the selected initiative can operate as a pilot project in the four selected regions in the STRUDER project.
4. Technical assistance for the Guarantee Fund.
5. If the scheme is set up as a pilot project, criteria must be developed to monitor the scheme.

Time schedule
Step 1 and 2 can be started immediately especially when the scheme should be introduced in the STRUDER project. The results of step 1 and 2 will show the feasibility of starting the implementation of a Loan Guarantee Scheme.

Actors
The Cabinet of the Minister of Entrepreneurship Promotion should discuss with the Office for Foreign Coordination and foreign donors the possibility of financing the activities described under the different steps. The programme must be carried out by a team of Polish and foreign experts in consultation with the Ministry of Finance and other Ministries involved, the National bank of Poland, the Union of Polish Banks and other parties interested in Loan Guarantee Schemes.

Financing
The activities of the programme can be financed in the frame of Technical and Financial Assistance programmes of foreign donors.

Costs
The costs of all the steps are ad hoc costs, except the costs of financial support of the Guarantee Fund which will be recurring.
Estimated ad hoc costs of step 1, 2: $ 40,000.
The costs of step 3 and 4 depend on the results of step 1 and 2 and can not be estimated at this moment.

6.2.7 Grant Scheme based on Commercial Loans

Entrepreneurs state that the interest rates charges on loans are too high and that therefore it is not economic to take credit.

Two type of actions can be taken to lower the costs of credits:
- a Grant Scheme based on Commercial Loans
- a Credit Line with Preferential Terms

In this paragraph the Grant Scheme based on Commercial Loans is described. The next paragraph discusses the establishment of a Credit Line with Preferential Terms.

Under the "Grant Scheme based on commercial loans" SME can get a grant on the basis of loans which are granted by banks on the basis that the projects are viable and that the loans are given on normal banking terms.

It is however impossible that all SMEs can get this grant. On the basis of business activities of SME which have to be stimulated to improve the economic development of Poland a selection must be on target groups which can apply for the grant. Examples of target sectors could be:

- Manufacturing companies or companies investing in fixed assets
- Medium-sized expanding firms
- SMEs in relatively disadvantaged regions
- SMEs in potential growth regions
- Start up companies
- Companies which create additional employment
- Commercialisation of technology
- Export orientated companies.

The grant should come from a well-defined separate fund of money, controlled by a specific institution and with clear and public eligibility criteria. This institution needs to have effective double check systems for appraisal of the projects to avoid the obvious tendencies towards corruption caused by public subsidy.

Advantages/disadvantages

Advantages:

- If the grant is used for investment in equity the debt/equity ratio will decrease which makes firms less vulnerable to reverses in fortune.

Disadvantages

- If the level of the grant is connected with the size of the loan, the amount of subsidy obtained by an entrepreneur is dependent on the size of the loan rather than actual needs or merit of the project. Other grant schemes could be developed based on other factors.
- Loans will increase the debt/equity ratio of SMEs. This ratio is already relatively high, which make the SMEs more vulnerable for reverses. A grant scheme based on commercial loans could encourage SMEs to take unnecessary loans and consequently a higher increase of the debt/equity ratio than necessary.
- Due to limited resources on the Polish side an appeal should be done on donors to have such a support schemes established.
- Given the shortage of resources in Poland, the funds should be used to put in place the desperately needed enabling environment. Unless and until that work is fully funded, money should not be diverted to grants or subsidies to individual firms.
- There is an overwhelming experience that the recipients of such grants or subsidies tend to be firms with entrepreneurial expertise in getting grants

and subsidies, instead of in the business of business. The dream of something for nothing tends to distract entrepreneurs from their real business.

Implementation steps
In practice, the grant scheme proposed in the STRUDER project is an example of this type of scheme.

1. the results of this pilot programme should be closely monitored and evaluated on the effect on SMEs. To do this efficiently, criteria for monitoring and evaluating the effects must be developed before the start of the Programme so that is it is clear which data have to recorded. In this way information on the development is available at any point of time. In STRUDER there is already a budget for monitoring activities.
2. On the basis of the results it should be decided to which extent a scheme can be used to stimulate other business activities.

Time schedule
STRUDER is planned to start in Summer 1993. As described the activities under step 1 must be carried out before the start of STRUDER. Due to possible start up problems, unawareness of SME on the grant etc. a reliable assessment of the scheme can take place after 12 months.

Actors
The Cabinet of the Minister of Entrepreneurship Promotion must consult the Bureau for Foreign Assistance and the European Community on the criteria for monitoring and assessment developed under STRUDER. If necessary foreign donors should be consulted on getting technical assistance for the activities mentioned under Step 1.

Financing
The activities described under step 1 can be carried out in the frame of the Technical and Financial Assistance Programmes of foreign donors.

Costs
The costs of step 1 are ad hoc costs.
Estimated costs of step 1: $10,000

6.2.8 Credit Line with Preferential Terms

Functioning
As described above, entrepreneurs state that the terms of commercial loans mean that it is not economic to take credit. It is possible to address this problem by giving credit with preferential terms. Such terms may mean, for example, a lower interest rate, or a long grace period. The preferential terms do not necessarily mean that the credit should have a negative real interest rate and, indeed, many of the sources of credit (such as foreign donors) oppose the idea of negative real interest rates because of the fact that they distort the market.

Clearly, any scheme which gives terms better than normal commercial conditions presupposes that the refinancing agency has access to subsidy.

It is however impossible that all SMEs can get this subsidy. On the basis of business activities of SMEs which have to be stimulated to improve the economic development of Poland a selection must be on target groups which can apply for the subsidy. Examples of target sectors could be:

- Manufacturing companies or companies investing in fixed assets
- Medium-sized expanding firms
- SMEs in relatively disadvantaged regions
- SMEs in potential growth regions
- Start up companies
- Companies which create additional employment
- Technical commercialisation
- Export orientated companies.

The subsidy should come from a well-defined separate fund of money, controlled by a specific institution and with clear and public eligibility criteria. The institution controlling the subsidy part of the scheme needs to have effective double check systems for appraisal of the projects to avoid the obvious tendencies towards corruption caused by public subsidy.

At the moment the Ministry of Labour operates a subsidised credit scheme for the unemployed and for small firms which increase employment. Additionally, Germany is setting up such a credit line with a subsidised interest rate through her Kreditanstalt für Wiederaufbau in cooperation with the Polish Development Bank.

Advantages/Disadvantages

Advantages

- Such loans will reduce costs to the SMEs.

Disadvantages

- Even when there is a positive real interest rate, it may be difficult to make the resource renew itself since it is refinanced on less than commercial terms.
- Given the shortage of resources in Poland, the funds should be used to put in place the desperately needed enabling environment. Unless and until that work is fully funded, money should not be diverted to grants or subsidies to individual firms.
- There is an overwhelming experience that the recipients of subsidies tend to be firms with entrepreneurial expertise in getting subsidies, instead of in the business of business. The dream of something for nothing tends to distract entrepreneurs from their real business.
- The fund may locally influence the demand for commercial credits which local banks may not be able to meet.

Implementation steps

1. Analyse the effects of the scheme of the Ministry of Labour to determine the effects of this scheme as well as analysing the problems related to other existing credit lines.
2. Perform a feasibility study on the establishment of the scheme, including conditions and target groups.
3. Approach foreign donors for financing such a scheme.

Actors

The Cabinet of the Minister for Entrepreneurship Promotion and the Bureau for Foreign Assistance should approach foreign donors to finance the activities under 1. and 2.

Time schedule

This action should be started within one year.

Costs

Step 1. and 2. have ad hoc costs estimated at $75,000.
In step 3 no extra costs are involved since these are normal activities of the actors.

7. Information and Counselling

7.1 Elaboration of the Constraints

The constraints in this area can be divided as follows:

7.1.1 *Lack of Business Advice/Counselling/Consultancy*

The business support network is currently insufficiently developed in Poland. For entrepreneurs there are too few places to go for advice and the quality of advice they receive can be very variable. The private sector (commercial consultancy) does not fill the gap since most entrepreneurs cannot afford to pay for such consultancy and the sector is not well enough developed for the market to sort out quality. Currently, organisations which coordinate entrepreneurs (such as Chambers of Commerce and business associations) are weak and therefore the small enterprise sector is not very effective at sharing advice between its members.

7.1.2 *Lack of Information*

Corresponding to the lack of advice, there is a lack of information in selected areas. This includes basic areas of information necessary for good business decisions (markets, financing, technology, SME support organisations, legislation) and also lack of skills amongst entrepreneurs in collecting information and in actual knowledge in key areas (marketing, finance/accounting, management, customer services, quality control). Entrepreneurs additionally complain about lack of information on activities where actions and information tend to be centralised, such as privatisation and foreign trade connections as well as information on foreign assistance schemes. The organisations dealing with such information claim to send the information to regional networks, but clearly communication is still not sufficiently effective. It should be noted that for the entrepreneur, the problem is not just the lack of information - since much information exists somewhere - but the ability to process it into something useful for his business.

7.1.3 *Differing Needs of Different Types of SMEs*

Although the SME sector consists mainly of very small enterprises whose needs for advice and information tend to be very general, we should not ignore the needs of medium sized enterprises, formed either through the growth of small enterprises or as a result of spin-offs from the privatisation process. Such medium-sized enterprises require strategic management training and probably sectoral consultancy services. As a result, the types of institutions which need to be developed for this sector have different characteristics from those developed for start ups or very small enterprises.

7.1.4 *Existing Initiatives*

There are a wide variety of initiatives, both Polish and donor initiated, which act to give advice and information to entrepreneurs and seek to cover the problems outlined above. A list of these initiatives is presented in annex D. Analysis of these initiatives would suggest the following problems:

- Coordination and cooperation between the various networks created by both Polish organisations and by donors is poor.

- Given that SMEs, local authorities, and the various organisations which support business support networks all have few resources, the rate at which the various networks can grow and develop their services is very limited without support from external sources (either the Polish government or through foreign aid). Indeed, without continuing subsidy from some external source, many of these initiatives will cease to exist.

- Most activities are targeted at start-ups and very small enterprises and there is less provision for the needs of medium-sized enterprises.

- Despite a wide geographical spread, there is a large concentration of initiatives in the larger cities and in most cases there are no offices outside the main city of each Voievodship.

7.2 Recommendations

7.2.1 *Introduction*

A number of possible actions to address these constraints are listed in Annex E.

After discussion in the Task Force and in a smaller working group, these actions were prioritised and regrouped. During discussion it was suggested that the following issues should be addressed by any actions to be taken:

- coordination and cooperation between different business support institutions and networks;
- transparency in the allocation of resources, particularly funding, to business support institutions;
- development of effective regional policy;
- availability of future sources of funding for business support;
- development of institutions to address the special needs of medium sized enterprises;
- development of autonomous organisations of businesses and entrepreneurs.

Taking these issues into account, actions are grouped into three areas:

- Actions to improve coordination, cooperation, and the flow of information, both centrally and at a regional level;

- Actions in support of the medium-sized sector;

- Actions in support of autonomous organisations of entrepreneurs.

7.2.2 *Actions to improve Coordination, Cooperation and the Flow of Information*

Such actions need to happen both on a central and a regional level since a large amount of the activity is at the grass roots and emphasises a local aspect, whilst any effective coordination, particularly with foreign donors, needs to have a nationwide element.

a. *Actions at a Central Level: Establishment of an SME Information Centre*

Functioning

A number of the actions which have to be coordinated centrally relate to what should be done in terms of regional policy. Regional policy covers much wider issues than that of SME support, but any allocation of resources to SME support organisations should be done in the context of priority regions and needs. Current indications are that concentration will be made on the most depressed regions which are quite probably not those where there is the greatest potential for SME development. In the absence of any effective governmental regional policy, it is important that there remains some coordination of information between the various business support networks which currently exist and that will be developed in the future.

To address this need, it is proposed that a small SME Information Centre is established with the following specific tasks:

- *Collection and dissemination of information relevant to SMEs* as a core activity including information found within governmental departments such as opportunities resulting from privatisation, information on standards and changes in standards, information on legislation and changes in legislation, information on foreign trade and foreign investment opportunities. Such information should be available to all interested intermediaries dealing with SMEs.

- *Provision of information to foreign donors on projects* which they can fund and, conversely, *information to projects on the availability of foreign assistance.* This activity is *not* one of coordination of donors and donor aid. Instead, the centre will ensure that business support institutions are aware of new initiatives and sources of funding and that the bodies which make decisions on foreign aid are appropriately informed.

- *Support in the elaboration of individual local initiatives* which have relevance across the whole country, for example in promotion of subcontracting of private SMEs to the state owned sector as part of the restructuring process.

In performing such a function, in the medium term the tasks of the centre can be extended to cover the responsibility for:

- *Establishment of centres of excellence in training,* both of business counsellors and of entrepreneurs themselves. Such centres could be established by better coordination of foreign assistance and some form of competition between the many business schools and management training institutes which already exist. Such centres could ensure the maintenance of standards as well as the effective use of strategies related to training trainers. This is important if the knowledge of people trained at high expense by foreign sources is to be retained when they leave the organisations they are trained to work in.

- *Monitoring and evaluation* of individual projects. To start this process it will be necessary to do a comprehensive institutional audit of the existing business support networks.

Within the tasks identified above, the interaction with foreign assistance should be done in close cooperation with the Cabinet of the Minister for Entrepreneurship Promotion and the Bureau for Foreign Assistance, since negotiations on such matters should be done through governmental channels.

Future development of such an centre depends heavily on the development of governmental regional policy, since the centre will have to interact with it. Along with such a policy which would give priorities to regions and a strategy for resource allocation between the regions, the centre could enhance transparency for the projects and better inform policy-makers of the needs of SMEs in individual regions and the needs of business support organisations for support.

Advantages and Disadvantages

This scheme addresses the identified needs for information by intermediaries and the problems of coordination and transparency in the allocation of resources as well as providing the possibility of more efficient use of resources and better information for policy makers.

However, it undoubtedly cannot solve all the problems. Lack of any regional structure and regional policy will limit its effectiveness, whilst its effect on entrepreneurs depends on the effectiveness of individual initiatives at a local level in reaching the true grass roots.

It is possible that some of the functions of the centre could also be performed by better cooperation and coordination between the existing institutions and organisations. As a result, it may prove that no additional quasi-governmental agency at the central level would be of sufficient benefit to justify its high set up and operational costs.

Implementation Steps

Responsibility for the implementation of the new centre should be given to a member of the Cabinet of the Minister for Entrepreneurship Promotion who should be given the task to produce a plan within a short period detailing the costs, responsibilities and funding opportunities for the centre. Production of this plan will involve discussions with donors and interested organisations working in Poland. Clearly, opportunities for funding, particularly from the donor side, may have an influence on the exact nature of the new centre.

When funding is identified and a business plan is produced, establishment of the new centre can be relatively fast, particularly if it is in an institution which already deals with information.

The individual responsible for the project, together with any relevant donor, will then organise a tender between the different organisations which are interested in the project to decide which of the existing organisations should be the host. Criteria for selection should include the experience of the organisation in this field, the possibility to raise funding from other sources, and the degree to which the host organisation already has an information network.

Practical results will only appear in the medium term, since the new centre will have a job of several months after establishment in gathering basic information, identifying and assessing business support institutions across the country, and starting its operation. This task should not be underestimated since there will be a need to create and maintain relationships with a large number of diverse organisations including both individual initiatives and national bodies.

The financial consequences of this action are somewhat difficult to calculate. A rough estimate of the costs for such a centre with real foreign technical assistance come to $650,000 working at full capacity which may be diminished if foreign input is limited.

b. Actions at a Regional Level

Functioning

Although national coordination is poor, at a local level cooperation between different support institutions is growing and this needs to be fostered.

There is general consensus that it is not practical at this time to create a unified network of regional agencies across the country to stimulate this cooperation. Reasons for this include:

- The lack of a clear definition of a "region". Generally the identity of the population and the infrastructure is not congruent with any specific administrative unit.

- The lack of any realistic candidates for this function. The Regional Development Agencies, for example, are a heterogeneous set of organisations with differently defined roles.

- The need to select initiatives on the basis of quality. In the circumstances where many new initiatives have been created, it is important to support those which are actually successful and not just those with the right name.

There are already some initiatives being taken to coordinate regional development, in particular the planned establishment of the Polish Agency for Regional Development which will coordinate the STRUDFR programme as its initial task. In addition, the creation of the SME information centre will help in regional cooperation by informing both donors and projects of the current situation and opportunities, as well as experience elsewhere in the country.

Nonetheless, the following additional actions can be taken to promote regional cooperation and grass roots initiatives:

- ❑ ***Continued support of donor-funded regional initiatives*** and close monitoring of the results. If regional development is to be effective it requires cooperation between different institutions, whilst a source of funding at a regional level will force decisions on which projects should survive where activities overlap.

- ❑ A ***funding allocation for innovative projects at a grass roots level.*** Such funding could come from both government and donors and should be disbursed in a transparent and competitive way. Such projects will have to show that they can raise some part of the costs of the project from their own sources.

- ❑ Similarly, a funding allocation for ***projects which enhance regional cooperation*** between different initiatives.

  These two actions should be coordinated by the Cabinet of the Minister for Entrepreneurship Promotion and run on the basis of a widely advertised open competition between projects. Projects which fail to get assistance can therefore also be identified as candidates for foreign donor assistance and are at least visible for the information centre elaborated above. Assessment of projects should be done by a panel consisting of representatives of several

Ministries as well as the private sector to ensure that the system is seen to be transparent.

- *Support for Voivodship Offices* (and other local authorities) from central government in how to deal with entrepreneurs and how to stimulate cooperation between local initiatives. This would take the form of intensive training of individual officers. This training should also include training of the regional representatives of the Minister for Entrepreneurship Promotion and be performed in cooperation with the Regional Council for Entrepreneurship where this exists.

- *Establishment of a network of telephone help-lines*, both local and national, to advise entrepreneurs on sources of assistance locally and nationally. Local help lines are important if such an initiative is to be effective.

- A *Study on Regional Development* to identify regions where there is the greatest potential for growth in the SME sector and the regions where there are the greatest problems. The study should also identify existing business support institutions and gaps in the institutional network. This could be used as background information for all the above actions in the absence of a regional policy.

- *Support for Coaching of Regional Business Promotion.* A comprehensive concept of regional business promotion which can be implemented successively in all the regions in Poland within five years has been developed. For this purpose Poland is split up in 28 units. A unit consists of approximately 30 towns. The Coaching Programme 'Regional Business Promotion' would consist of three divisions, namely:
  - coaching of Polish companies
  - coaching of Polish consultants
  - coaching of Polish regional business promoters.

  The first two divisions are already implemented in some regions and have shown the first positive, measurable results. The strategy of the coaching approach consists of accompanying the regional business promoters, companies and consultants to success by training, advising and controlling. The tools to reach the success are seminars, practical training on the job assistance by Polish and foreign experts and an efficient controlling system. Business promoters in the third division can include regional development agencies, chambers, business associations, regional banks, etc.. These regional business promoters should deliver various kinds of products such as business contacts, meeting/information days, seminars/workshops, business incubators, development of commercial and industrial areas, etc.. The main customers should be private companies, state owned companies, governmental/ municipal offices and foreign investors and trade customers.

Advantages and Disadvantages

Although these actions can help to improve the environment, it is impossible to force different initiatives to cooperate and to share their experience. In the short term, while much money comes from central sources which are not orientated towards regional coordination, there is a certain incentive for local initiatives to compete with each other for funding. The major factor which will improve the situation will be growth of business support services and recognition of the need for cooperation for practical reasons - as is already beginning to happen in some regions.

Implementation Steps

The steps outlined above are part of an ongoing process and therefore it is difficult to make a clear time schedule for action. It should be noted, as above, that practical results will take a long time, perhaps several years, to appear.

In order to ensure that action is taken, a member of the Cabinet of the Minister for Entrepreneurship Promotion should be given the responsibility for producing an action plan for regional development, including accurate costings, for the above actions. Such a plan should be produced within three months. In terms of specific steps, the following can be noted:

Continued support of donor-funded initiatives
A member of the Cabinet of the Minister for Entrepreneurship Promotion should be given the task of coordination with foreign donors and liaison with the Bureau for Foreign Assistance. It is important that this individual collects information on individual projects from the sources identified by other actions and makes recommendations in the framework of the study on regional development.

In itself this action is within the existing budget of the Minister for Entrepreneurship Promotion.

Funding Allocations for specific types of projects
To allocate funding to projects, a proper assessment Board and procedure should be elaborated by the member of the Cabinet of the Minister for Entrepreneurship Promotion responsible for regional policy. Clearly, the exact criteria depend very heavily on the opportunities for funding this type of activity. It should be noted that a scheme which is very similar in structure is described in the project description of the World Bank's Private Enterprise Development Project and therefore after appropriate negotiation, there is a source of funding which could be available. In trying to establish a fund for the activity a minimum level of activity would require funding for, say, at least 10 projects every year at an average cost of $100,000 making the minimum viable amount $1 million. The Polish government should make a budget allocation for this amount of money in the medium term.

Support for the Voievodship Offices
Before establishing a very large training scheme, a short training needs analysis study of these offices needs to be performed (costing less than $50,000). This could easily be funded by foreign donors. As far as actual training is concerned, it would cost of the order of $200,000 to give two people in each Voievodship a one week training course organised by foreign trainers. Such could be funded by foreign donors.

Establishment of Telephone Help-Lines
This action should be sponsored by the Cabinet of the Minister for Entrepreneurship Promotion but probably the network should be managed by the SME Information Centre outlined above. $100,000 for this project would cover both an initial study and actual implementation in at least a number of regions. An initial study has to be commissioned to determine the best location for such help-lines in the regions and the accurate costs of running such a scheme nationwide.

Study on Regional Development
The study on regional development can be commissioned immediately. Since this is a study that can easily be funded by foreign donors, the individual responsible for the action plan should first approach donors to discover if there is any interest. The cost for such a study should be of the order of $200,000 and should recommend ways of keeping the study updated as well as concrete actions to be taken. The survey should be done as soon as possible in order that it can be used as background information for all of the actions detailed above.

Support for Coaching of Regional Business Promotion
The coaching programme could start in October 1993. Poland would be divided into 28 units. The estimated costs for one unit would be:
capital $ 60,000
annual fixed costs $ 180,000
variable costs $ 660,000
19% overhead costs
The cost of the whole programme of 28 units over 5 years would therefore be more than $20 million. It would be possible to have a reduced programme of a lesser number of units and the costs would be reduced accordingly.

7.2.3 *Actions in Support of the Medium-Sized Sector*

Functioning

It is clear that support for medium-sized enterprises requires different institutions and skills from that for micro-enterprises and entrepreneurs starting new enterprises. In particular, larger enterprises typically require strategic management training and sectoral consultancy as well as professional accounting services.

Although many of the existing initiatives aimed generally at advice to SMEs (such as the Business Support Centres supported by the Cooperation Fund) help medium

sized companies, the main initiative which focuses on this field at present is Polish Business Advisory Services (PBAS). PBAS is supported by many of the major foreign donors and also has Polish government support. PBAS has now established itself both as a service supporting the medium-sized sector and as an agent for the development of an indigenous consultancy sector. It has developed a good reputation, although it still needs to expand its services as the sector which it serves expands.

It is clear that PBAS requires continued support, particularly since in the economic situation and stage of development of the private sector, even medium-sized enterprises cannot afford to pay an economic rate for its services.

Additionally, there are a number of other projects in this area, primarily promoted by foreign donors, such as the "coaching" scheme presented to the Task Force by GTZ. If the GTZ scheme obtains foreign donor support of an adequate nature it could complement regional initiatives such as STRUDER. Any new initiatives should not be set up in competition with the existing ones and there should be agreement, for example, on levels of fees charged to client companies.

In order to make such initiatives more effective, they should have clear access to the information described in the first section, in particular that which is most relevant to the medium sized sector (for example, on technology, technical standards, and foreign trade opportunities).

- It is important for the sector to continue to develop institutions to support medium-sized enterprises, but since foreign aid is likely to be temporary it is recommended that the Polish government develops a strategy to take over funding where this is necessary. Such funding can be at a lower level than at present if the existing initiatives succeed in training a team of Polish consultants to take over from external Western expertise.

Advantages/Disadvantages

Although there is a need for support for the medium-sized sector, in the longer term this should come from the private consultancy sector and there is a danger that subsidised schemes can inhibit the growth of this sector meaning that the Polish government will have to subsidise the existing schemes into the future.

The success or failure of the schemes in this sector depend heavily on the environment and therefore reforms of regulations and availability of finance need to be improved at the same time.

Implementation Steps

The government needs to have some strategy for taking over funding of the various schemes in the future - perhaps in 1-2 years' time. In the current turbulent environment it is difficult to estimate the realistic costs of this, but it could be of the

order of several million dollars a year. In order to help to create such a strategy, which is also true for organisations supporting smaller enterprises, an individual in the Cabinet of the Minister for Entrepreneurship Promotion should be allocated the task of creating a clear plan for funding of business support for the future which can be put forward for incorporation in the budget in future years. This task should be coordinated with the centre outlined above, when this is established.

7.2.4 *Actions in Support of Autonomous Organisations of Entrepreneurs*

Functioning

To develop effective sharing of information between entrepreneurs, a systematic scheme to help develop autonomous structures such as Chambers of Commerce and business and trade associations needs to be developed.

Foreign donors have already given a number of small amounts of technical assistance either to the National Chamber of Commerce or to local Chambers, but this could be made more effective through exchange of information. A natural place for such coordination would be the information centre outlined above. It is important to note that foreign aid has concentrated on the official Chambers and has neglected the development of associations of entrepreneurs and trade associations. This tendency should be rectified if possible.

Most business organisations are weak in the ability to represent and lobby for the interests of their members. Whilst some of this ability can only come by organic growth and political experience, other measures which can be taken to quicken this process include:

- the inclusion of representatives of the business sector in the various bodies connected with policy making, their inclusion being conditional on their effectiveness in representing the sector (encouraging integration of different organisations);

- foreign assistance in making connections with foreign small business associations and learning from their experience.

- foreign assistance in training in the field of lobbying instruments and procedures.

In order to strengthen the Chambers of Commerce and Chambers of Craftsmen themselves, a number of people have suggested that compulsory membership would be useful. Owing to the problems of a strong reaction against this caused by memories of forced membership of communist organisations in the past, it would be necessary to enhance the services given by Chambers of Commerce at the same time, for example by giving them the role of registering businesses and therefore the opportunity to give information. Opinions are divided on this subject and the final result will be determined as part of the political process.

- To help to inform the process of developing the systems of Chambers, it is recommended that a study of the feasibility of using the existing Chamber system for registering business is commissioned.

Advantages/Disadvantages

Although the actions outlined above can have some effect, it is important to realise that truly representative organisations can only grow organically. Even in countries where, for example, Chambers of Commerce have compulsory membership, they have earned this privilege by being truly representative of the sector and offering services to their members. Such a situation will probably take years to achieve.

Implementation Steps

The action to include business representatives in policy making bodies is already discussed above in chapter 3.

Connection with foreign business associations is a matter which foreign donors can effectively facilitate without high costs. A number of such actions are already in progress and should continue. It may be possible for wider overall coordination to be added to this - for example PHARE's assistance to the National Chamber of Commerce or support to Eurochambres (the European Association of National Chambers of Commerce) in training members of Chambers of Commerce. As stated above, such assistance should be enlarged to include associations of entrepreneurs and the establishment of trade associations. The Council for Entrepreneurship should be given responsibility for producing a coordinated plan for using foreign aid in this way which can be submitted to foreign donors.

As a specific action to help the Chambers of Commerce and Craftsmen in the current situation, a survey using foreign expertise and experience should be commissioned to determine the feasibility of using the existing system of Chambers for the purpose of registering businesses and the consequences of this in terms of both financial and other resources. Such a study would cost around $50,000 and could be financed by foreign donors.

8. *Final Remarks*

The report presents a programme of recommendations for action to address constraints identified in the fields of the enabling environment, financing of SMEs and support to SMEs through information and counselling.

These actions are to be taken by the Government, both at central and regional levels, by the business world and the financial sector, as well as by a network of intermediary organisations which include business support centres, development institutions, and projects, many of them supported by a wide range of donors.

The number of actual and potential actors in the field is large and still growing, and so is the number of tasks to be fulfilled. Therefore the question of an optimal organisation of the sector will have to be addressed in more depth and detail than this report has been able to do.

What should be done by whom and where? The objective of such deepened analysis would be to develop an efficient set-up of institutions active in SME support which would be able to respond effectively to the needs of the SME sector but which would at the same time minimise the bureaucratic layers within the sector. As a practical example, additional tasks identified in this report such as the Research and Analysis Unit and the SME Information Centre might be allocated to one of the institutions retained under this set-up, without necessarily creating new ones.

The Task Force would expect this "institutional audit" to take place simultaneously with the further elaboration of the recommendations made in this report, i.e. as soon as the structure, the number, and the volume of actions to be carried out in the sector have been developed in further detail.

Furthermore, it should be stressed once again that the Task Force considered the constraints which the actions address as the most urgent and advised that the actions identified are developed as they are considered to be the most effective and feasible from the political and financial point of view. However, the other obstacles should not be neglected and proper attention should be paid to them when these major obstacles have been solved.

In relation to this, it should be urgently advised both to the Government of Poland and to the donors to strengthen the activities of the Cabinet of the Minister of Entrepreneurship Promotion both with financial and technical means. In addition, it is advised that bilateral and multilateral donors should meet more frequently in order to be adequately informed of each other's activities and to support the strengthening the SME sector in a concerted manner.

Annex 1

DRAFT CONTENTS OF STUDY REPORT

Executive Summary

1. Policy objectives for the SME sector.

2. Picture of the existing situation in the SME sector:

   - trends of SME development since 1990, general, sectoral and regional (appendix: available statistics on SME);

   - existing support institutions and donor funded projects in the SME sector (appendix: list of institutions and projects);

   - banks and other financial institutions relevant for SMEs, donor funded projects in this area (appendix: list of institutions, projects);

   - assessment: results in achieving past and present policy objectives.

3. Main bottlenecks identified for further SME development:

   - legal, regulatory and administrative framework;
   - entrepreneurial and managerial capability;
   - access to modern technology;
   - network of support institutions;
   - finance (interest rates, types of finance available, collaterals, structure of banking system, other financial institutions, etc.). Finance related bottlenecks will be given particular attention in the report.
   - any other relevant bottlenecks.

4. Recommendations on how to overcome the main bottlenecks and major priorities to be addressed by:

   - the Polish Government and the G-24 donor community
   - other donors
   - the financial sectors
   - other support institutions
   - SME sector organizations

   This chapter should also include comments on some recent proposals with regard to existing bottlenecks, such as the "G-24 TA Restructuring Fund".

5. Actions to be taken

In the event that the study report proposes institutional changes and\or the creation of new institutions in the financial sector, it should give terms of reference covering such issues as:

- objectives and scope of work (regional, sectoral)
- ownership\capital structure
- staffing (including recruitment and training)
- operational guidelines.

6. Proposals on monitoring the implementation of the recommendations, the activities of existing and newly planned institutions and the flow of investments into SMEs.

KS\TW 03.02.93

Annex A - Terms of Reference of the Task Force and the Task Force Secretariat

DRAFT TERMS OF REFERENCE

3 February 1993

Task Force for SME Investment

Background

Increased investment by SMEs in profitable projects is seen as a key to economic recovery and development in Poland. Currently, however, SMEs face major obstacles in preparing, financing and implementing profitable investments.

These obstacles include:

- the legal, regulatory and administrative framework for SME operations;
- limited availability of entrepreneurial and managerial capability;
- gaps and overlappings in the network of support institutions in the SME sector;
- an unfavorable macroeconomic climate leading to very high nominal and real interest rates;
- structural weaknesses in the financial sector, very limited scope of funding instruments.

The Polish Government and the donor community have been aware of these problems since the beginning of the transformation process.
Measures taken so far include:

- Restructuring of Government responsibilities for SME promotion (appointment of a Minister for SME promotion, mainly responsible for policy issues);
- a big number of donor supported projects aimed at human resource development through training, business and management advisory services;
- anti-inflationary measures aiming, among other, at a sustained fall in inflation and interest rates.

Task Force Secretariat

The secretariat will carry out the study and write the report along the outline enclosed in annex 1. In doing so, it will extensively interview the task force members, any other institutions and donors active in SME development and finance in Poland, as well as a sample of SMEs. During its work, the secretariat will report fortnightly to the task force, in steering committee meetings. These meetings are open to attendance by interested Polish SME sector representatives and G-24 members.

The secretariat will be managed by the Cabinet of the Minister for Small Business Promotion, assisted by the GEMINI Project, in collaboration with qualified Business Advisory Experts contracted by the EC PHARE programme.

Funding of the Task Force

No remuneration or cost reimbursement will be granted to the members of the task force. Contributions to the secretariat will be made as follows:

- Minister for Small Business Promotion: logistical support such as offices, secretarial services and local transport;
- EC PHARE programme: fees, per diems and international transport for experts.

Time Schedule

10 Feb 93	constitution of the task force
15 Feb 93	steering committee meeting, start of work of the secretariat
1 Mar 93	steering committee meeting
15 Mar 93	steering committee meeting
29 Mar 93	steering committee meeting
9 Apr 93	submission of draft report
14 Apr 93	steering committee meeting (discussion of draft report)
26 Apr 93	submission of final report
30 Apr 93	acceptance of final report by the task force and submission to the Government and the donor community

After discussion of the report with the Government, the task force could either be dissolved or maintained, with the aim to assist the Government in the implementation of the retained recommendations.

KS/TW 03.02.93

Annex B - List of Task Force Members

Polish Side Members	*Representatives*
1. POLISH GOVERNMENT	
Mr. ZBIGNIEW EYSMONT (Co-chairman) Minister - Member of the Council of Ministers	Mr. Tomasz Wąsowicz
Mr. JAN KRZYSZTOF BIELECKI Minister - Member of the Council of Ministers	Mr. Marek Kozak
Mr. JERZY OSIATYŃSKI Minister of Finance	Ms. Helena Góralska
2. POLISH BANKING SECTOR	
Ms. HANNA GRONKIEWICZ-WALTZ President of Polish National Bank	Ms. Janina Kraszewska
Mr. MARIAN KRZAK Union of Polish Banks	Mr. Andrzej Wolski
3. POLISH PRIVATE SECTOR	
Ms. DANUTA PIONTEK Convention of Entrepreneurs, Traders and Agriculture Producers	
Mr. BOGUSŁAW WÓJCIK National Chamber of Commerce Crafts Chamber of Small and Medium Enterprises	
Mr. ZBIGNIEW NIEMCZYCKI Polish Business Round Table	Mr. Jerzy Schön
Mr. MAREK GOLISZEWSKI Business Centre Club	Mr. Witold Michałek
Mr. TADEUSZ MAĆKOWIAK Christian Entrepreneurs' Club	
Ms. ANNA ORĘZIAK Union of Polish Crafts	

G-24 Members	*Representatives*
1. Mr. ALEXANDER DIJCKMEESTER (Co-chairman) Commission of the European Communities	Mr. Klaus Schmidt
2. Mr IAN HUME World Bank	Mr. Mario Reyes-Vidal
3. Mr. WILLIAM R. JOSLIN USAID	
4. Mr. BERND SCHLEGEL The Government of the Federal Republic of Germany	
5. Mr. JOHN HASTINGS European Bank for Reconstruction and Development	

Annex C - Resolution of the Council of Ministers regarding the scope of work of the Minister for Entrepreneurship Promotion

(DAI/GEMINI English Translation of Polish Original)

Resolution No. 139/92

of the COUNCIL OF MINISTERS

dated November 20, 1992

regarding the scope of work of the Minister, Member of Council of Ministers, Zbigniew Eysmont.

The Council of Ministers decides as follows:

§ 1.

The Minister - Member of the Council of Ministers undertakes activities in the field of shaping economic, legal, social and organizational conditions for the promotion of entrepreneurship and the development of small and medium enterprises; supporting inter-departmental activities and the creation of policy in this area.

§ 2.

The duties of the Minister, Member of the Council of Ministers, Zbigniew Eysmont include, specifically:

1) preparing, in cooperation with the appropriate state administration agencies and non-governmental organizations, of a draft of a government program for promotion and support for the development of private entrepreneurship;

2) representing the Government in cooperation and contacts with entrepreneurs and their organizations;

3) informing the appropriate state administration agencies of the opinions, conclusions and expectations of the private entrepreneurs; in order for these to be taken into consideration in the implementation of the social and economic policy of the state;

4) initiating and organizing research concerning the conditions, tendencies and barriers in the development of entrepreneurship; and making evaluations of the current economic and legal system from the standpoint of its influence on economic activity;

5) initiating and preparing, in cooperation with the interested agencies and institutions, projects for programs and legal acts supporting the development of private entrepreneurship;

6) initiating and supporting the activities of the appropriate agencies, institutions and organizations for the development of infrastructure supporting the development of private entrepreneurship and its promotion;

7) cooperating with international organizations and other appropriate institutions in activities supporting the development of private entrepreneurship and its promotion;

8) cooperating with the appropriate state administration agencies and with the Government's Plenipotentiary for European Integration and Foreign Assistance, in order to obtain financial and material resources, both domestic and foreign, designated for the development of private sector, as well as participation in the disposition of these resources;

9) cooperating in the acquisition of foreign technical and financial assistance for the promotion of private entrepreneurship.

§ 3.

1. In the course of performing the tasks defined in art.1 and 2, the Minister, Member of the Council of Ministers, Zbigniew Eysmont shall cooperate with the interested state administration agencies and governmental organizations.

2. The Minister - Member of the Council of Ministers:

   1) comments and consults (makes recommendations) on programs and legislative acts which can have influence on the development of private entrepreneurship;

   2) comments and consults (makes recommndations) activities pertaining to the acquisition of financial and material resources, both domestic and foreign, which serve the promotion and support of private entrepreneurship;

   3) evaluates and consults (makes recommendations) on proposals for allocation and conditions of using domestic and foreign resources designated for the promotion of entrepreneurship and development of private sector;

   4) comments (makes recommendations) on directions and programs of activities relating to the transformation of the economy and its promotion abroad; acquisition of new technologies and the creation of capital and cooperative relations concerning small and medium enterprises.

§ 4.

The state administration agencies and authorities are obliged to cooperate with the Minister, Member of the Council of Ministers, Zbigniew Eysmont in the scope of implementing the duties described in article 2 and 3.

§ 5.

The activities of the Minister - Member of the Council of Ministers Zbigniew Eysmont are supported by the Cabinet of the Minister, which is an organizational unit of the Office of the Council of Ministers.

§ 6.

The resolution becomes effective on the day it is approved.

(original signed on November 20, 1992)
Prime Minister
Hanna Suchocka

Output of the Task Force

The task force will report on the above to the Government of Poland and the G-24 in early 1993. The core of the report will be written by independent consultants (see below: "Task Force Secretariat") and will be discussed and accepted by the task force, in its capacity as a steering committee. A draft outline of the report is enclosed as annex 1.

Composition of the Task Force

The task force will be composed of members representing the Polish Government, banking system and SME sector, as well as of some G-24 representatives.

The Polish representatives (6) will come from:

- Ministry for SME (co-chairman of the task force)
- Ministry of Finance
- Ministry for Foreign Assistance and European Integration
- National Bank of Poland
- Union of Polish Banks
- Entrepreneurs

The G-24 representatives (4) will come from:

- EC Delegation (co-chairman)
- World Bank
- United States of America
- Federal Republic of Germany

G-24 representatives will participate in the task force in their own rights, without committing their governments\headquarters or the G-24 as a whole. Any G-24 member not represented in the task force but wishing to make contributions to the work of the latter will be invited to do so.

With regard to the financial sector, specific measures include:

- the creation of some new institutions (PDB, bise, private sector banks, RDAs);

- TA to the banking sector (both for training and direct management assistance) through PHARE, the IFC twinning programme and others);

- the allocation of lines of credit for SMEs generally intermediated through Polish banks (except for the Polish-American Enterprise Fund).

These measures have proved inadequate in the face of the problems. A large and growing number potential and actual SMEs is unable to overcome the obstacles to profitable investments. On the other hand, huge amounts of foreign grants (mainly for technical assistance) and loans (for channelling finance to SMEs) have remained unspent.

In recognition of these problems, the Government and the donor community have agreed to establish a short-term SME task force.

Task Force General Objective (Mission Statement)

The mission of the task force is to recommend measures aimed at sustainable increase of profitable investments by SMEs.

Task Force Specific Objectives

The task force will analyze all of the above and possible other obstacles to SME investments and recommend appropriate measures.

Specific, but not exclusive, attention will be given to the bottlenecks in the banking system. In this area, the task force will:

- examine the current and future demand on and the capacity of the banking system to channel funds of all kinds to SMEs;

- define the gaps between demand and capacity and make proposals on how to fill these gaps, possibly with the help of technical assistance.

Also with regard to other obstacles, the task force will assess the global needs and delivery capacities of the existing structures and develop recommendations.

A draft outline of the study report is given in Annex 1. The main text of the report should not exceed 50 pages. Ample space will be given to the chapters "recommendations" and "actions to be taken". Theoretical deliberations, descriptions of the past and present situation as well as of the bottlenecks identified and any further background information should be dealt with chiefly in annexes; in the main text, these should appear only to the extent necessary to justify the recommendations. The main text will be preceded by an executive summary of no more than 5 pages.

4. Time schedule (provisional)

10 Feb 93	constitution of the task force
15 Feb 93	steering committee meeting, start of work of the secretariat
1 Mar 93	steering committee meeting
15 Mar 93	steering committee meeting
29 Mar 93	steering committee meeting
9 Apr 93	submission of draft report
15 Apr 93	steering committee meeting (discussion of draft report)
26 Apr 93	submission of final report
30 Apr 93	acceptance of final report by the task force and submission to the Government and the donor community

5. Composition and organization of the secretariat

The secretariat will be managed by the Cabinet of the Minister for Small Business Promotion, assisted by the GEMINI Project, in collaboration with qualified Business Advisory Experts contracted by the EC PHARE Programme (Prof. J. Vianen and an assistant, together about 12 person/weeks, Mr. S. Thompson, about 4 person/weeks and a Polish member, nominated by the Cabinet Office of Minister Eysmont, Mr. Dariusz Stola, for about 8 person/weeks). The Cabinet Office, of Minister Eysmont, with assistance from the GEMINI Project, will provide professional and logistical support such as office space, secretarial services, communication facilities and transport.

Fees, per diems and international transport will be funded by the PHARE Programme, under the Small Technical Assistance Facility.

KS/TW 03.02.93

DRAFT TERMS OF REFERENCE

3 February 1993

Secretariat of

Task Force for SME Investment

1. Background

The Polish Government and the G-24 donor community have established a task force, with the objective of recommending measures aimed at a sustainable increase of profitable investments by SMEs. Specific objectives and other details of the work of the task force have been laid down in the terms of reference for the task force (draft version of 17.12.92). Those terms of reference also give an outline for the work of the secretariat.

2. Objectives

Accordingly, the secretariat will write the report to be submitted, with the approval of the task force, to the Polish Government and the G-24 donor community.

3. Working procedures

In the course of carrying out the study and writing the report, the secretariat will extensively interview the task force members, any other institutions and donors active in SME development and finance in Poland, as well as SME organizations. It will furthermore exploit the existing literature on SME development and finance in Poland.

Based on this analysis, the secretariat will develop draft recommendations aimed at a sustainable increase of profitable investments by SMEs. These recommendations will be submitted to the task force for discussion. The secretariat will consider any comments and changes made to the recommendations by the task force. Possible reservations expressed by individual task force members to recommendations accepted by the task force will be reported in footnotes or annexes to the main report, if this is especially so wished.

The secretariat will report to and seek comments from the task force as a group, in steering committee meetings called fortnightly by the chairmen of the latter.

Annex D - Existing Projects and Institutions Supporting SMEs

We acknowledge considerable help from Polish Business Advisory Services in collecting information used in this section.

1. Types of Support

Support from foreign donors does not come without strings attached. Each donor has its own rules of procedure and eligibility. The following general comments apply:

- The majority of bilateral aid is disbursed on a project by project basis, often including very small projects. As a result, the number of such ongoing projects in this list is relatively small. This does not mean, however, that there are no opportunities for assistance.

- Most bilateral aid is tied to using technical assistance from the donor country. In many cases this means that it is difficult to fund revenue costs relating to Polish employees of a project through foreign assistance.

- In the case of PHARE, although the actual use of the money is not too tightly tied and the funds come as a grant to the Polish government, disbursement is tied to general programmes determined on an annual basis and specific items identified within these programmes are put out to competitive tender where appropriate. PHARE programmes are therefore relatively inflexible when it comes to funding new specific projects. The World Bank operates in a similar way, but the funds come by way of a loan.

The different rules and procedures of different donors can mean that coordination and cofinancing of projects is difficult to achieve.

2. Existing Support Institutions and Donor Funded Projects

Business Support Institutions

There are a wide variety of initiatives, both Polish and donor initiated, which act to give advice and information to entrepreneurs.

a. Polish Initiatives

There are a number of different networks which have been established to give advice and information to entrepreneurs, including:

- Regional Development Agencies. RDAs are autonomous bodies charged with activities connected with regional development, including development of

the private sector. Most are relatively new and are still defining their exact activities. There are RDAs in almost half the Voievodships and they are now trying to establish a national association.

- Economic Foundation of NSZZ "Solidarność". The Foundation has organised a variety of different actions in support of small enterprises including training, advice, and an information bank. The Foundation has 23 regional offices.

- Fundacja Inicjatyw Społeczno-Ekonomicznych (FISE). FISE was set up as an initiative of the Ministry of Labour and Social Affairs and operates through 16 Agencies for Local Initiatives giving basic advice and information. The Agencies have been set up in areas of greatest economic and social need. FISE is closely connected with the bank BISE.

- Chambers of Commerce and of Craftsmen. Chambers exist across the country (although there is a big concentration in the larger towns, particularly Warsaw). Most Chambers are small and weak and in some cases are dominated by State Owned Enterprises.

- Economic Societies. Economic Societies exist across the country promoting economic development. Although they were significant at the point of transition, newer organisations such as local Chambers of Commerce have in many cases taken over their role as far as support of SMEs is concerned.

- Activities within Voievodship Offices. All Voievodship offices have departments dealing with business promotion and information/ consulting points.

- There are a number of other independent initiatives such as the establishment of local incubator projects.

b. Donor-led Initiatives.

It should be noted that a number of the initiatives above, for example FISE, have received foreign aid.

Specific initiatives include:

- Business Support Centres. 16 BSCs have been created through the Cooperation Fund using PHARE assistance. The BSCs give basic advice information and training and are hosted by existing institutions, mostly Chambers of Commerce. The Cooperation Fund also has a number of other initiatives, including the establishment of a national Euro Info Centre Correspondence Centre, giving information on standards and contacts with the European Community, and assistance to the National Chamber of Commerce.

- Polish Business Advisory Services (PBAS). This is an initiative to provide consultancy and support to medium-sized enterprises. The initiative has been set up by the International Finance Corporation and EBRD in association with and with support from a number of other foreign donors and the Polish government. This initiative works on the basis that the recipient enterprises contribute towards the costs. The German organisation GTZ proposes to introduce a similar initiative but without payment by the recipient.

- Regional Management Centres. The UK Know How Fund has established four Regional Management Centres (in Lublin, Łódź, Poznań and Gdańsk) which as well as providing management training also provide advice services to SMEs in their areas.

- STRUDER. This regional development initiative funded by PHARE will include provision for advice and information to the private sector when implementation starts during 1993. In order to support STRUDER, the Polish Agency for Regional Development is being established. This body will have responsibility for coordination of the STRUDER actions.

- USAID has established three Polish-American Small Business Advisory Centres in Warsaw, Gdańsk, and Łódź.

- The Ministry of Labour has a project funded by the World Bank in support of micro-enterprises which includes provision for the establishment of a number of incubator projects across the country.

Schemes for Low Cost Consultancy

There are a variety of schemes to use retired executives or MBAs to help specific enterprises at low cost. These include: USAID (International Executive Service Corps, MBA Enterprise Corps), Canada (Canadian Executive Service Organisation).

Management Training

There are a variety of initiatives to promote management training, since this is an area to which many foreign assistance programmes are ideally suited. Specific initiatives include:

- Management and Business Schools. There are at least 38 such schools in Poland giving a variety of different courses, some relevant to entrepreneurs.

- Regional Management Centres. The UK Know How Fund has established four Regional Management Centres (in Lublin, Łódź, Poznań and Gdańsk) which as well as providing management training also provide advice services to SMEs in their areas.

- Small Business Training Institutes funded by USAID in Białystok, Poznań, and Rzeszów

Many bilateral donors have some form of training exchange programme, typically for targeted sectors and for managers and not necessarily relevant to SMEs. Courses are normally run in the donor country. Countries operating such schemes include: Britain, Sweden, Netherlands, and Denmark.

Policy Advice

USAID has funded the long term *GEMINI* project which provides SME policy advisors attached to the office of the Minister for Entrepreneurship Promotion. To assist legislative reform, USAID has funded the IRIS project (an independent body looking at institutional reform and the informal sector), and RITE (removal of impediments to trade) initiatives, the Rule of Law and Commercial Law projects.

EC-PHARE has allocated funds to policy advice activities, originally scheduled to be with the Ministry of Industry, but the actual use of these funds is still under discussion.

Sectoral Projects

Projects which are related to other sectors also have an impact on SME development. Such sectors include particularly: agriculture, tourism, employment initiatives, technological development.

This applies not only to foreign assistance but also to Polish governmental initiatives. In particular, the Ministry of Labour has a number of schemes related to employment creation and the retraining of the unemployed. These schemes give very small grants or loans to unemployed people who wish to set up their own businesses.

Short Term Assistance from Foreign Donors

As stated above, there are many examples of foreign donors giving short term technical assistance to small projects (for example Swiss government support to SMEs in two specific gminas). There are too many projects to mention individually, but it should be noted that this is a real opportunity for the future.

3. Banks and Other Financial Institutions relevant to SMEs

Banks and Institutions Supporting SMEs

The Polish banking system is structured in the following way:

- National Bank of Poland - the Central Bank
- State-owned banks

- Private banks
  At the moment there are more than 90 private banks active including several with foreign capital. In addition there are extensive number of cooperative banks. The majority of these banks are affiliated in the Food Economy Bank.

Special Institutions
A number of specific institutions have been set up specifically to help the banks help the private sector. These include:

- The Polish American Enterprise Fund (PAEF), set up as a separate fund using the banks only as windows for dealing with clients rather than for credit appraisal. PAEF has also set up a number of other initiatives including an equity fund set up in association with EBRD.

- The Bank for Socio-Economic Initiatives (BISE) set up by the Ministry of Labour with assistance and funding from France and operating in close cooperation with FISE (see above).

- Caresbac Polska. Caresbac Polska is operational since 1991. It is a joint stock company whose shares are held by Caresbac-USA, the Cooperation Fund and the Foundation for development of Polish Agriculture. The aim of the company is to invest in firms with between 15 and 100 employees. In addition to the investment Caresbac provides the firms invested in, with information and advice on all business related subjects. The minimum level of the investment is $ 75,000.

- The Polish Development Bank, set up as an apex bank and responsible for credit lines from the World Bank, the European Investment Bank (EIB) and a number of foreign donors. The PDB also gives loans itself although these are not orientated towards SMEs.

Bank Training

Bank Training is clearly of importance in developing the banking sector. Foreign assistance has been given in various different forms from, for example, EC-PHARE, and the British Know-How Fund. The initiatives listed above have required a substantial amount of bank training to be effective, for example from France in the establishment of BISE.

Sources of Credit

As well as normal bank credit, there are the following schemes of assistance to SMEs:

- Specialist institutions as listed above.

- A credit line denominated in ECUs funded by EC-PHARE managed by the Cooperation Fund

- Loans from EIB and EBRD for larger enterprises. The EIB loans are managed by the Polish Development Bank. The EBRD loans are through a variety of foreign owned banks.

- World Bank loans through the Polish Development Bank. The World Bank also proposes to set up small funds alongside the incubator projects being set up in the programme managed by the Ministry of Labour.

- Small loans to the unemployed who start up businesses funded by the Ministry of Labour through Local Labour Offices.

Sources of Equity

Equity finance is at present an underdeveloped sector, but there are institutions which deal with equity including the Polish American Enterprise Fund, Caresbac Polska, and TISE (associated with BISE). Inevitably these initiatives presently concentrate on larger SMEs and have yet little experience.

The STRUDER programme includes provision for the establishment of regional investment funds.

Western-funded Credit Lines

There are a number of schemes which finance exports from the West to Poland. Such schemes include ones financed by Austria, Denmark, France, Finland, Spain, Norway, Germany, and Switzerland. Such finance is not necessarily very useful to SMEs unless they can avoid the exchange risk by exporting from Poland. Schemes have been agreed but not implemented with a number of other countries, including South Korea.

Nonetheless, there are a number of credit lines which are available for enterprises, typically orientated for a particular sector. Most of the credit lines have not been disbursed very quickly, owing to the conditions and problems in the banking sector. A separate review of these credit lines has been undertaken by a banking task force and its report should be available in due course.

Other Initiatives

Although there has been much speculation about the establishment of guarantee schemes, there is no large scale scheme functioning at present. Under the NBP scheme, 212 guarantees were issued for some 130 billion złoty in 1990-92. Since the guaranteed part of the loan was decreased in mid-1992, no new guarantees were given. The STRUDER programme includes funding for a new guarantee fund.

There are few sources of direct grants outside the STRUDER scheme which will give grants to enterprises receiving loans from accredited banks in specified areas of the country.

There are a number of additional initiatives to support institutions relevant to the financial sector. In particular:

- EC PHARE has a financial sector development programme which, as well as improving the capabilities of the banks through training, seeks to develop the insurance sector, the accounting and auditing sector, and the tax and fiscal administration sector.

- EBRD has initiated a project using a private company to set up a credit rating service.

Annex E - List of Possible Actions

1. Financing

Banking Services

To improve the banking services implies a good infrastructure of payments between banks and this means action to develop banking information technology and the establishment of a clearing house.

In addition, banks have to be informed, advised and trained in working with this new technology. Also personnel of banks have to be trained, for example to be more customer friendly.

Finally, services for foreign transactions, such as provision of letters of credit, are underdeveloped and further action needs to be taken to develop these services.

Credit

The establishment of a central business register could assist banks in gathering information on their clients. Businesses could also use this register to get information on their business partners. There are already a number of concepts developed for the establishment of such a register.

According to normal banking practice, banks ask for collateral when providing loans to private business to diminish their risk. The existing relevant legislation in Poland hampers this process. Regarding legislation it is necessary to:

- speed up of the reform of collateral law including the establishment of an asset/collateral register
- reform the bankruptcy law
- reform the property law

To judge the value of collateral it would be helpful if standard procedures for the valuation of assets/collateral were to be developed whilst in addition a kind of information system on the value of assets and collateral should be set up.

Apart from legislation/regulation and information on collateral also the lack of collateral by SME is mentioned as one of the constraints in lending to private banks. Documentation, reports and interviews suggest that banks will give more credit to private business if there are other institutions to share the risk with. To overcome this problem a guarantee facility can be set up.
Two kind of guarantee facilities can be distinguished, namely:

- a Mutual Guarantee Scheme
- a Loan Guarantee Scheme

At this moment there are several initiatives developed to set up Mutual Guarantee Schemes and Loan a Guarantee Scheme. It would be reasonable to decide that one of the initiatives aimed at setting up a Mutual Guarantee Scheme and one aimed at setting up a Loan Guarantee Scheme will be carried out as pilot projects.

High interest rates form an important constraint for firms for getting loans and consequently for investment. To stimulate investment soft loans could be provided by banks or by specific institutions. The criteria for eligibility of these loans depends on the strategic objectives developed as part of SME policy and could include:

- manufacturing SMEs
- investment in fixed assets
- SMEs in relatively disadvantaged regions
- SMEs in growth potential regions
- start ups

To improve banks in dealing with loans to private business it is necessary that bank personnel are advised and trained on aspects such as:

- assessing creditworthiness and risk evaluation
- loan monitoring
- restructuring loans

Although there are a number of initiatives of donors in this field, the coordination and scope of these initiatives should be improved.

Equity

As described above there is a lack of equity capital. The provision of equity financing by private persons can be stimulated by special tax measures such as:

- tax incentives for private persons investing in private business
- similar treatment of dividends and interest on savings

The number of venture capital institutions is still very limited in Poland. Due to high operational costs and the high risk venture capital firms are not eager to participate in small business. Via schemes participation by venture capital institutions can be improved. Such schemes might include

- tax incentives for venture capital firms investing in SMEs
- guarantee scheme for venture capital firms

A further way of introducing equity is through joint ventures with foreign companies. Such ventures have the added advantage that they introduce management skills and technology to the Polish business. There needs to be further promotion of opportunities for joint ventures.

Other financial institutions

The establishment of leasing, factoring and insurance institutions requires a change in the legislative and regulatory frame work linked with the activities of such institutions.

Other support schemes

Apart from the above mentioned actions which are mainly aimed at the institutions providing financing it also necessary that SME will be informed, advised and trained on different aspects of financing: accounting, filling in application forms and in preparing other required documents, consequences of foreign exchange credits, etc.. In the chapter "Information and counselling" more information is given on the ways in which this can be realised.

The transition to a market economy will inevitably lead to increasing international competition. New technological developments are leading to new and better products and services, to more efficient means of production and to an increasing productivity. To assist SMEs in improving their competitive position, schemes can be developed to assist them in financing activities needed such as:

- soft loans/grants for the financing of technical commercialisation
- soft loans/grants to finance modernisation of the production process

At this moment the economic situation of the domestic market does not leave much room for SME-development, particularly in depressed regions. To grow SMEs, producing goods and services which can be exported, need to export as quickly as possible. In the field of export financing the following actions can be developed:

- soft loans/grants for the financing of export activities
- an institution can be set up for insurance and financing of export activities
- financial support to promote the formation of export consortia consisting of small firms. Support is given for joint export promotion or marketing activities, because in particular these activities are relatively costly for SME to finance on their own. In addition cooperation between firms can improve the exchange of experiences between SME

2. *Information and Counselling*

To address these constraints in the context of existing experience, the following actions have been suggested:

a. To increase the number of local initiatives, some form of central government subsidy scheme open to all local initiatives supporting small enterprise. Such subsidy would be subject to clear criteria of eligibility, for example: a specified maximum amount; at least matching funds from the initiative itself; preference to be given to the establishment of initiatives in relatively disadvantaged areas; no funding for salaries or purchase of property; business plan showing how the initiative can become self-financing. In order

for such a scheme to be effective in the longer term, attention must be given to evaluation of existing projects as well as selection of new ones.

b. To develop standards and knowledge among business counsellors operating in business support organisations, central government coordination of training of such personnel using both Polish and foreign resources. Such coordination could lead to the creation of some form of centre of excellence for such training, ensuring that standards are kept and that training of trainers is effective. There should also be corresponding coordination of training for relevant public agencies, for example the people working in the information points in Voievodship offices.

c. To develop opportunities for relevant training and education for entrepreneurs, similar coordination of training activities in Management and Business Schools (together with any training provided by business support organisations).

d. To increase the quality of private consultants acting for the private sector, some form of national accreditation scheme for such consultants which could be used by other agencies in referring entrepreneurs to private consultants. Possibly a national directory of consultants could be published.

e. To stimulate businesses to use private consultants, the creation of a grant scheme directed at subsidising consultancy costs.

f. To ensure that small businesses can locate sources of assistance, a central government help-line (perhaps with additional regional help-lines) to give information on assistance and to direct entrepreneurs to appropriate institutions. This initiative could include the publication of a directory of sources of foreign assistance.

g. To ensure that information on specific subjects reaches entrepreneurs, coordination of national sources of information so that they use all the local networks of business support institutions identified above. This would require national action in the provision of general business information together with specific information in the fields of technology, export and foreign trade, privatisation issues, regional action on these issues, and also, for example, opportunities for subcontracting. Although this will not necessarily solve the communication problem, it could nonetheless improve the current situation. Any provision of information needs to be coordinated with training of personnel in business support organisations and Voievodship offices in how to deal with queries and how to market information to entrepreneurs.

h. To ensure that the information available centrally is relevant and presented in an appropriate way, a study of the information needs of the SME sector. It

should be noted that the Cooperation Fund has already initiated such a study under the PHARE programme.

i. To develop effective sharing of information between entrepreneurs, a systematic scheme to help develop autonomous structures such as Chambers of Commerce. Foreign donors have already given a number of small amounts of technical assistance either to the National Chamber of Commerce or to local Chambers, but this could be made more effective through coordination.

j. To support the medium-sized enterprise sector, continued support from the Polish government and foreign donors to organisations assisting medium-sized enterprises through consultancy and dissemination of information on, for example, technical standards, sources of finance, and other assistance available.

k. To develop the existing networks of business support agencies, continued support from foreign donors (Business Support Centres, STRUDER, etc). Foreign assistance should pay attention to mechanisms to ensure that over time an indigenous Polish consulting and advice sector will develop itself as a complement to these networks.

Annex F - List of Persons Interviewed by the Task Force Secretariat

Ms. Eve W. Anderson
USAID

Mr. Krystyn Bernatowicz
Ministry of Labor

Minister Jan Krzysztof Bielecki
Minister for European Integration and Foreign Assistance

Ms. Nathalie Bolgert
BISE - Bank of Social and Economic Initiatives

Mr. Radosław Czapski
EC Delegation

Mr. Michael Davenport
British Government Know How Fund

Mr. Ronald A. Dwight
IRIS - Poland Project

Minister Zbigniew Eysmont
Minister for Entrepreneurship Promotion

Mr. David A. Fisher
CARESBAC-Polska S.A.

Mr. Yves Fortin
European Bank for Reconstruction and Development

Mr. Adam Gałczyński
Cabinet of the Minister for Entrepreneurship Promotion

Mr. Andrzej Gerhardt
Cabinet of the Minister for Entrepreneurship Promotion

Ms. Krystyna Gurbiel
Cooperation Fund

Mr. Jerzy Gutkowski
Ministry of Finance

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Mr. Krzysztof Herbst
FISE - Foundation for Social and Economic Initiatives

Mr. Konrad Hryciuk
DAI/GEMINI

Mr. Jacek Jeitmar
SAKK

Mr. Tomasz Jeziorański
BISE - Bank of Social and Economic Initiatives

Mr. William R. Joslin
USAID - U.S. Agency for International Development

Mr. Wojciech Kostrzewa
Polish Development Bank

Mr. Marek Kozak
Office for Undersecretary of State for European Integration and Foreign Assistance

Ms. Janina Kraszewska
National Bank of Poland

Mr. Jan Król
Member of the Parliament

Mr. Waldemar Kuczyński
Unia Demokratyczna

Mr. Marek Kulczycki
Polish-American Enterprise Fund
The Enterprise Credit Corporation

Mr. Andrzej Lewiński
Ministry of Industry and Trade

Mr. Wojciech Lipka
Union of Polish Banks

Mr. Jerzy Loch
Cabinet of the Minister for Entrepreneurship Promotion

Mr. Charles van der Mandele
Polish Business Advisory Service

Annex G - List of Reports and Documents used by the Task Force Secretariat

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Ministry of Industry and Trade
Enterprise Development Center Co.Ltd

Mr. George Metcalfe
DAI/GEMINI

Mr. Witold Michałek
Business Centre Club

Mr. Jerzy Molak
Ministry of Industry and Trade
Small and Medium Enterprises Dept.

Ms. Halina Napiórkowska
Ministry of Finance

Mr. Mart Nugteren
Cooperation Fund

Mr. Tadeusz Olejarz
Ministry of Labour

Ms. Anna Oręziak
Polish Crafts Association

Mr. Janusz Ostaszewski
Ministry of Finance

Mr. Tadeusz Pęczek
DAI/GEMINI

Ms. Danuta Piontek
Convention for Entrepreneurship, Traders and Agriculture Producers

Mr. Witold Radwański
European Bank for Reconstruction and Development

Mr. Mario Reyes-Vidal
World Bank

Mr. Zygmunt Sachnowski
Ministry of Finance

Mr. Bernd Schlegel
Deutsche Ausgleichsbank

Mr Jerzy Sękiewicz
Progress and Business Foundation
Kraków

Mr. Klaus Schmidt
EC Delegation

Mr. Jerzy Schön
Polish Business Round Table

Mr. Charles de Smet
Cooperation Fund

Ms. Justyna Sosnowska
Crafts Chamber of Small and Medium Enterprises

Mr. Tomasz Stawecki
Committee for Civil Law Reform
at the Ministry of Justice

Mr. Janusz Szlanta
Regional Development Agency, Radom

Mr. Kazimierz Ślifierczyk
Ministry of Industry and Trade

Mr. Władysław Świtalski
Association of Economic Advisers
UNI-EXPERT

Ms. Halina Wasilewska-Trenkner
Centralny Urząd Planowania

Mr. Tomasz Wąsowicz
Cabinet of the Minister for Entrepreneurship Promotion

Mr. Jan Wejhert
Polish Business Roundtable

Mr. Andrzej Wolski
Union of Polish Banks

Mr. Bogusław Wójcik
Crafts Chamber of Small and Medium Enterprises

Mr. Mirosław Zieliński
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Komitet Przedsiębiorstw Małych i średnich

Warszawa, dnia 5.09.1991

Stanowisko Prezydium Komitetu Przedsiębiorstw Małych i Srenich K I G wobec polityki rządu w sprawie rozwoju polskiego small businessu. (Małych i średnich Przedsiębiorstw - M S P).
Komitet Przedsiębiorstw Małych i średnich

A view of SMEs 1992. Information on the number of companies and employment, as for December 31, 1992
Cabinet of the Minister for Small Business Promotion
4 March 1993

OECD Economic Surveys.
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Poland 1992

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Warsaw 1992

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Małe i średnie Przedsiębiorstwa w latach 1990-1991
Zakład Badań Statystyczno-Ekonomicznych Głównego Urządu Statystycznego i Polskiej Akademii Nauk.
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