



MACEDONIA: MOVING IN THE RIGHT DIRECTION

*A Report on Progress and New Priorities
in Commercial Law and Institutional Reform
Since July 2000*

CLIR Assessment
November 2003

Macedonia Corporate Governance & Company Law Project

Mitropolit Teodosij Gologanov, 42A
1000 Skopje, Macedonia
tel: + 389 2 323 1239 ext 108 | fax: + 389 2 323 1040
mobile: +389 70 833 015
www.maccorpgov.com

A USAID-funded project



Table of Contents

Executive Summary	1
Introduction	3
<i>Background on the CLIR Diagnostic</i>	<i>4</i>
<i>The 2003 Macedonia Diagnostic.....</i>	<i>6</i>
Cross-Cutting Themes.....	6
<i>Framework Laws</i>	<i>7</i>
<i>Implementing Institutions.....</i>	<i>10</i>
<i>Supporting Institutions</i>	<i>11</i>
<i>The Market for Reform.....</i>	<i>15</i>
Bankruptcy	18
<i>Overview</i>	<i>18</i>
<i>Legal Framework</i>	<i>18</i>
<i>Implementing Institutions.....</i>	<i>20</i>
<i>Supporting Institutions</i>	<i>22</i>
<i>Market for Reform in Bankruptcy Law</i>	<i>23</i>
Collateral.....	25
<i>Overview</i>	<i>25</i>
<i>Framework Laws</i>	<i>25</i>
<i>Implementing Institutions.....</i>	<i>29</i>
<i>Supporting Institutions</i>	<i>31</i>
<i>Market for Reform</i>	<i>33</i>
Company.....	34
<i>Legal Framework</i>	<i>34</i>
<i>Implementing Institutions.....</i>	<i>38</i>
<i>Supporting Institutions</i>	<i>41</i>
<i>The Market for Company Law Reform.....</i>	<i>44</i>
Competition	46
<i>Overview</i>	<i>46</i>
<i>Legal Framework</i>	<i>46</i>
<i>Implementing Institutions.....</i>	<i>50</i>
<i>Supporting Institutions</i>	<i>52</i>
<i>The Market for Reform in Competition Law.....</i>	<i>53</i>
Contract.....	56
<i>Overview</i>	<i>56</i>
<i>Framework Law</i>	<i>57</i>
<i>Implementing Institutions.....</i>	<i>59</i>
<i>Supporting Institutions</i>	<i>62</i>
<i>Market for Reform</i>	<i>64</i>
Foreign Direct Investment.....	66
<i>Overview</i>	<i>66</i>
<i>Framework Laws</i>	<i>66</i>
<i>Supporting Institutions</i>	<i>70</i>
<i>Market for Reform</i>	<i>72</i>

Trade	74
<i>Overview</i>	74
<i>Framework Laws</i>	75
<i>Implementing Institution</i>	77
<i>Supporting Institutions</i>	78
<i>Market for Reform in Trade</i>	79

	Albania	Armenia	Azerbaijan	Bulgaria	FRY/ Serbia	MACEDONIA		Poland	Romania	Ukraine	Kazakhstan
	2000	2001	2002	2001	2001	2000	2003	1999	1999	1999	1999
BANKRUPTCY	42%	57%	44%	34%	47%	62%	68%	79%	58%	39%	53%
Legal Framework	90%	89%	67%	67%	61%	87%	89%	80%	59%	41%	60%
Implementing Institutions	21%	42%	44%	25%	41%	57%	58%	80%	62%	45%	51%
Supporting Institutions	16%	41%	21%	10%	39%	42%	44%	76%	52%	33%	49%
COLLATERAL	77%	23%	54%	70%	24%	76%	83%	78%	31%	55%	37%
Legal Framework	91%	29%	75%	91%	40%	79%	91%	90%	44%	76%	56%
Implementing Institutions	80%	11%	50%	73%	13%	87%	87%	79%	13%	56%	23%
Supporting Institutions	58%	30%	36%	48%	19%	61%	70%	65%	35%	31%	31%
COMPANY	50%	70%	46%	76%	65%	58%	68%	76%	66%	44%	59%
Legal Framework	75%	90%	56%	87%	80%	76%	80%	70%	53%	39%	53%
Implementing Institutions	54%	69%	46%	68%	57%	45%	62%	76%	73%	52%	67%
Supporting Institutions	21%	51%	35%	72%	59%	52%	61%	82%	70%	42%	58%
COMPETITION	n/a	40%	35%	63%	26%	27%	44%	80%	60%	44%	58%
Legal Framework		66%	71%	93%	40%	57%	71%	82%	66%	55%	64%
Implementing Institutions		22%	22%	37%	15%	6%	35%	81%	62%	42%	64%
Supporting Institutions		33%	13%	59%	23%	18%	27%	76%	51%	37%	46%
CONTRACT	56%	51%	48%	77%	67%	65%	66%	82%	71%	50%	65%
Legal Framework	84%	90%	81%	93%	86%	84%	87%	83%	74%	50%	73%
Implementing Institutions	51%	41%	39%	61%	63%	62%	57%	83%	73%	49%	66%
Supporting Institutions	35%	22%	25%	77%	54%	50%	53%	79%	66%	50%	54%
FDI	n/a	44%	29%	70%	n/a	71%	84%	78%	64%	45%	67%
Legal Framework		73%	52%	77%		88%	93%	87%	96%	89%	83%
Implementing Institutions		15%	12%	81%		62%	82%	82%	58%	18%	68%
Supporting Institutions		44%	22%	52%		64%	78%	66%	38%	28%	50%
TRADE	n/a	44%	27%	40%	n/a	69%	80%	71%	61%	37%	57%
Legal Framework		73%	29%	68%		81%	93%	93%	90%	56%	79%
Implementing Institutions		21%	23%	25%		66%	72%	71%	53%	34%	61%
Supporting Institutions		37%	28%	28%		59%	75%	49%	40%	19%	32%
AVERAGE	56%	49%	41%	62%	46%	61%	70%	78%	59%	45%	57%
Legal Framework	85%	73%	62%	82%	62%	79%	86%	84%	69%	58%	67%
Implementing Institutions	52%	32%	34%	53%	38%	55%	65%	79%	56%	42%	57%
Supporting Institutions	33%	37%	26%	49%	39%	49%	58%	70%	50%	34%	46%

Broad Indicator	Albania	Bosnia	Bulgaria	Croatia	Macedonia	Poland	Romania	Serbia	Slovenia	Turkey
Population (millions) [1]	3.2	4.1	7.9	4.4	2.0	38.6	21.8	10.7	2	69.6
2002 GDP per Capita (\$'000 PPP) [2]	\$3.8	\$6.3	\$6.7	\$8.9	\$6.0	\$9.4	\$5.8	\$2.3	\$17.1	\$5.8
% GDP - Agriculture[3]	33.3	8.0	11.0	9.7	12.1	3.4	13.1	12.2	3.1	15.3
% GDP - Industry	23.5	26.2	24.5	34.2	29.7	33.8	38.1	--	37.6	29.9
% GDP - Services	43.2	37.2	64.5	56.1	58.2	62.8	48.8	--	59.3	54.7
Foreign Aid per Capita [3]	\$85	\$157	\$44	\$26	\$122	\$25	\$29	\$123	\$63	\$2
Corruption Index [4]	2.5	3.3	3.9	3.7	2.3	3.6	2.8	2.3	5.9	3.1
Economic Freedom Index [5]	3.35	3.8	2.85	3.15	3.25	2.9	3.75	4.25	2.85	3.5
Government Effectiveness [6]	-0.47	-0.90	-0.06	0.19	-0.39	0.61	-0.33	-0.73	0.82	0.08
Voice and Accountability	-0.04	-0.25	0.56	0.46	-0.29	1.11	0.38	-0.20	1.10	-0.47
Regulatory Framework	-0.37	-0.93	0.62	0.19	-0.10	0.67	0.04	-0.60	0.81	0.08
Rule of Law	-0.92	-0.88	0.05	0.11	-0.41	0.39	-0.12	-0.95	1.09	0.00

[1] The World Bank: www.worldbank.org/data/countrydata/countrydata.html Figures are from 2002 and are in current US\$. This footnote applies to the Population, GDP per capita, %GDP-Agriculture, %GDP-Industry, %GDP-Services.

[2] The Economist, 2004 World in Figures

[3] The World Bank [<http://www.worldbank.org/data/countrydata/countrydata.html>]

[4] Transparency International www.transparency.org/cpi/2002/cpi2002.en.html

[5] 2003 Index of Economic Freedom, The Heritage Foundation (<http://www.heritage.org/research/features/index/>). Scale: 1-1.95, free; 2-2.95, mostly free; 3-3.95, mostly not free; 4-5, repressed.

[6] The World Bank http://info.worldbank.org/governance/kz2002/mc_chart.asp Governance indicators are measured in unit ranging from about -2.5 to 2.5, with higher values corresponding to better governance outcomes. This footnote applies to the Government Effectiveness, Voice and Accountability, Regulatory Framework and Rule of Law Ratings.

EXECUTIVE SUMMARY

Macedonia is moving forward in its efforts to improve the environment for commercial activity. The progress has come from a combination of political will, technical assistance, and private sector responses to changing circumstances and opportunity. While there is still work to be done, the advances made in the past three years are significant.

Since independence, Macedonia has been undergoing tremendous transition at every level, including law. In 2000, the United States Agency for International Development conducted an assessment to understand the status of commercial legal and institutional reform (CLIR) in order to provide assistance more effectively. The first diagnostic showed a mixed record of success in commercial laws and rather poor performance by institutions. This autumn, a second assessment has been conducted to determine progress and identify priorities for further assistance. The results clearly show that Macedonia has improved its CLIR environment in accordance with international standards. It is also clear that the assistance provided in legislation and institutional support has been effective in producing the desired results.

The CLIR diagnostic methodology measures seven areas of essential commercial laws across three dimensions of implementation while also examining the social dynamics involved in achieving progress and overcoming constraints. The areas of law examined are: bankruptcy, collateral, company, competition, foreign direct investment (FDI) and trade. The examination focuses on existing laws and regulations (Framework Laws), the government institutions responsible for implementing those laws (Implementing Institutions), and the civil society and private sector organizations that are essential for the system to function effectively (Supporting Institutions), providing quantitative scores for each area. The scores are based on hundreds of questions regarding compliance with emerging international standards in each area. In addition, the methodology examines the various forces supporting or undermining reform efforts, including cultural, social, and economic factors that bear upon the results desired.

In all areas, Macedonia has shown significant progress. The scores for Framework Laws demonstrate a 7% overall improvement, with the greatest improvements in collateral, competition and trade. Implementing Institutions did even better, with a 10% overall increase. If low scores for courts (bankruptcy and contract) are eliminated along with the low score for collateral registry (because it already has a very high score), the average improvement in Implementing Institutions goes to 18%, with the greatest improvements in competition (29%) and FDI (20%). Supporting Institutions also fared well, with an average advance of 9%. The greatest change was in the Customs Agency, which was described by respondents as a difference of “night and day.”

In terms of overall success, the Collateral Registry continues to stand out, as it did in the prior assessment. It received very high scores in law (91%) and implementation (87%),

and had good scores for Supporting Institutions (70%). The more important indicator, however, came from interviews with banks that are using the system. One bank noted that the Collateral Law system enabled them to increase lending in Macedonia and increase investment in the bank from abroad. In other words, this aspect of the commercial regime is promoting economic growth and development, which is the sole reason for undertaking investment in this registry system.

Additional work is still needed. Although most of the laws are actually quite good, implementation still lags. The greatest weakness is in courts, which actually *declined* in perceived quality since 2000. This finding is in keeping with problems noted in the *FIAS Report on Administrative Barriers* and the *Programme for Stimulating Investment and Attracting Foreign Investment* by the Ministry of Economy. Moreover, members of the Macedonian Business Lawyers' Association identified court reform as their number one priority in a survey of problems encountered by these legal professionals.

Another significant finding was that the existing laws – and thus the overall investment environment – are threatened by the system for adopting and amending laws. Macedonia, like its neighbors, has historically used the “classic model” of legislative process in which a few technical experts draft laws or amendments before they are passed, with little or no public debate or discussion. Thereafter, implementation is usually quite slow, if it occurs at all. Under this non-democratic model, it is possible for special interests to undercut reforms by changing laws in the wrong direction. For example, the bankruptcy law, which received a high score of 87%, is currently being proposed for amendments that will completely undercut the purpose of the law, with inevitable negative economic impact.

Several Ministries have shown a positive tendency to use a democratic model, in which there is extensive input in and discussion with the private sector in order to create laws that will facilitate economic development. For example, the Ministry of Economy, working with USAID's Corporate Governance and Company Law Project, is holding a series of roundtable discussions around the country on proposed changes to the company law. Interested end users have been able to provide extremely valuable input to the process to avoid future problems. At the same time, the process has ensured shared commitment for the reforms, education about the new system, and increased likelihood of lasting implementation. Unfortunately, such enlightened lawmaking is voluntary, not mandatory, under current regulations; a better system needs to be adopted for all lawmaking.

Perhaps the most important implication of the assessment is that the investments made by various donors over the past three years are paying off in the commercial legal environment. Necessary changes in the rules of commercial activity are being made, which affect the attractiveness of Macedonia as an investment destination. While it is true that additional work is needed in a number of areas, it is important to note that donor assistance can be quite effective in achieving those needed reforms.

INTRODUCTION

In 2000, the United States Agency for International Development (USAID) conducted a diagnostic assessment of the commercial law and institutional reform (CLIR) environment for Macedonia. The assessment was performed to assist the USAID Mission in Skopje in setting priorities for technical assistance. It was also part of a series of assessments that started in 1999 and continue today, and thus provided comparative information on Macedonia's CLIR performance with respect to similarly situated countries.

In 2003, USAID updated the original assessment to determine whether there had been any significant progress in reforms, and to identify continuing needs and priorities for additional assistance. As detailed below, the 2003 Assessment shows that Macedonia has succeeded in upgrading its commercial legal and institutional environment in accordance with international standards. The study also highlighted ongoing needs, primarily with respect to improving institutional performance.

Comparative CLIR Scores Since 1999

	Albania	Armenia	Azerbaijan	Bulgaria	FRY/ Serbia	MACEDONIA		Poland	Romania	Ukraine	Kazakhstan
	2000	2001	2002	2001	2001	2000	2003	1999	1999	1999	1999
Bankruptcy	42%	57%	44%	34%	47%	62%	68%	79%	58%	39%	53%
Collateral	77%	23%	54%	70%	24%	76%	83%	78%	31%	55%	37%
Company	50%	70%	46%	76%	65%	58%	68%	76%	66%	44%	59%
Competition	n/a	40%	35%	63%	26%	27%	44%	80%	60%	44%	58%
Contract	56%	51%	48%	77%	67%	65%	66%	82%	71%	50%	65%
FDI	n/a	44%	29%	70%	n/a	71%	84%	78%	64%	45%	67%
Trade	n/a	44%	27%	40%	n/a	69%	80%	71%	61%	37%	57%
<i>Average</i>	56%	49%	41%	62%	46%	61%	70%	78%	59%	45%	57%

As can be seen in the comparative table, Macedonia raised its overall score from 61 to 70 (on a scale of 100), bringing it into second place out of eleven countries. Some of the individual areas of law were even more significant: Competition went from one of the poorest performers, worse than Azerbaijan, to mid level, moving up 14 points. In Collateral, FDI and Trade, Macedonia now tops the list. These changes indicate improvement in the business climate with respect to establishing investor-friendly ground rules for trade and investment.¹

Weaknesses identified are just as important as the successes. Two areas stand out. First, the courts continue to be a problem in application of law and enforcement of commercial obligations. Delays, lack of specialization, insufficient judicial education and the lack of effective enforcement mechanisms continue to plague the private sector

¹ While significant, these comparative improvements should be balanced by the recognition that many of the other countries surveyed have probably also improved their performance in the past few years. Even so, this does not diminish the importance of Macedonia's successful efforts to stabilize and improve its commercial climate.

and diminish respect for courts and law. On occasion, misuse of biased courts against foreign investors has hurt existing and potential investment by sending the wrong message to the foreign investment community. The problem affects domestic investors as well, because they must manage the risk of non-enforceability through higher prices and more cautious investment. Changes are taking place in the courts, but the importance of reform cannot be overstated: all progress in law ultimately relies on the ability of the commercial sector to enforce its rights through a sound, predictable and transparent court system. Much more work is needed.

Second, the system for passing and amending legislation is flawed. The Law on legislation permits public debate and input on legislation, but does not require it. Consequently, most laws are passed with minimal if any public input. Frequently, the private sector discovers a new law is being considered only after it has been passed. Due to the goodwill of a number of officials involved in lawmaking as well as some well designed donor support, a number of important laws are being vetted effectively prior to passage. Successes from using this democratic approach may provide a window of opportunity to amend the system itself for better law and policy work.

Background on the CLIR Diagnostic

The CLIR diagnostic methodology was created by USAID to address frustrations from earlier legal reform efforts that produced disappointing results. Beginning in 1989, USAID and a number of other donors began investing substantial amounts to assist transition countries move to a market-oriented commercial structure. At first, much of the focus was on laws, but the new laws seldom seemed to be implemented. New investments were then made in the government institutions in charge of implementing laws, such as courts, anti-monopoly agencies, and investment promotion organizations. Still, the impact on implementation did not achieve expectations.

In 1998, USAID began developing a wider approach to commercial law reform, looking at the entire system needed for effective change and implementation. This included the civil society components such as bar associations, business associations, notaries, banking organizations and the numerous other groups normally involved in a democratic system of reform. In addition, they focused more carefully on the “market for reform” or social dynamics affecting the ability of reformers to achieve their goals. Using an institutional economic approach, they developed analytical tools for identifying weaknesses and strengths on the supply side of the equation (government’s ability to produce thoughtful policy and well drafted law) along with the demand side (the needs of the private sector to achieve economic development and growth).

This analytical approaches were then captured by a series of questions designed to explore the essential aspects of each dimension of the commercial legal system. For Framework Laws (those laws that define a certain area, such as bankruptcy), the questions allow legal specialists to grade the existing law in light of emerging

international standards relevant to the region (for example, European standards in a civil law country). Second, the diagnostic examines the structure and performance of the Implementing Institutions responsible for each area. Another section looks at the existence, capability, and involvement of various private sector associations, NGOs and even subsidiary government agencies (such as the Customs Agency) to determine their ability to provide input, support and implementation of commercial reforms. Finally – and perhaps foremost – the methodology examines the Market for Reform to determine the manner in which vested interests, political will, and even basic economic understanding may affect the ability of the country to achieve market-oriented reforms

Each area of law is examined along these four dimensions using a combination of qualitative and quantitative tools. The starting point is often an examination of published laws and policies, local scholarly articles, and other high level documentation and analyses. Knowing that the “law in the books” is not always the same as the way those laws are applied, a diagnostic team will spend extensive time interviewing stakeholders from all areas of the commercial and official community, including ministry officials, lawyers, judges, businesses, foreign investors, bankers, court clerks and numerous others to confirm and validate information received while also identifying conflicting information and common themes and impressions. This work is reduced to a set of scores based on hundreds of questions and, more importantly, to a written analysis of the areas covered.

A caveat on the scores is necessary. The primary purpose of the scoring tool is to ensure integrity and discipline in a highly qualitative process, not to provide a scientific, statistically “correct” grade. The written analysis is much more important than the numerical one. Even so, experience has now shown that the scores effectively capture the actual status of the CLIR environment, and thus have comparative value within these limits. The Macedonian experience is illustrative. Improvements or reverses of scores between 2000 and 2003 indicate the dynamic change that is taking place, and further indicate the positive nature of the general changes, while identifying continuing systemic weaknesses. They are not scientifically accurate, however, in capturing the exact amount of change or impact. For example, a single clause in the 2002 bankruptcy amendments put extremely important limits on timing for submission of claims, with tremendous positive impact on management of bankruptcy cases. The statistical impact is less than a one-point change. The question, however, identified this important element and highlighted it in the earlier assessment as a needed reform.

Finally, it should be remembered that the purpose of the CLIR diagnostic assessment is to identify strengths and weaknesses in the commercial environment in order for USAID missions to better allocate their technical assistance resources for priority impact. Narrative findings, supported by scores, provide strategic input for these purposes.

The 2003 Macedonia Diagnostic

One of the tasks of the USAID's Corporate Governance and Company Law Project is to update the CLIR assessment carried out in July 2000. There are two principle reasons for this. First, the new assessment is needed to identify ongoing areas in which reform is needed and resources can be focused. Second, the Mission wanted to determine whether technical assistance by various donors over the past three years was having any measurable impact. As this report shows, both objectives have been achieved: new and ongoing assistance needs have been identified, and a number of assistance projects have clearly helped Macedonia to improve the commercial legal environment. Both of these themes are addressed throughout the report.

The 2003 Assessment was carried out by a team of legal specialists from the CG&CL project being implemented by Deloitte Touche Tohmatsu. These specialists, assisted by interns, conducted the assessment over a period of five weeks, starting in early October. The team analyzed laws, reports, and assessments (such as the FIAS Administrative Barriers

Macedonia 2003 CLIR Assessment Team	
Wade Channell	Collateral, FDI, Trade
Darrell Brown	Company, Competition
Marija Ignatova-Gjoseva	Bankruptcy, Contract
Samir Latif	Company
Vesna Mirkoska	Research, Analysis, Logistics
Ana Soselevska	Legal Research
Ivana Janeska	Graphics
Marijan Mihajlov	Survey of Business Lawyers

Assessment of 2003) to provide the foundation for the more qualitative information. With this background, they interviewed government officials, business leaders, business and professional associations, lawyers, judges, foreign investors, and foreign donor organizations. They also conducted a survey of commercial lawyers and analyzed other surveys conducted by the CG&CL Project and other projects within the context of the CLIR project. The results were presented at a meeting of USAID implementers on November 8, 2003 in order vet the findings, obtain feedback, and better formulate this report.

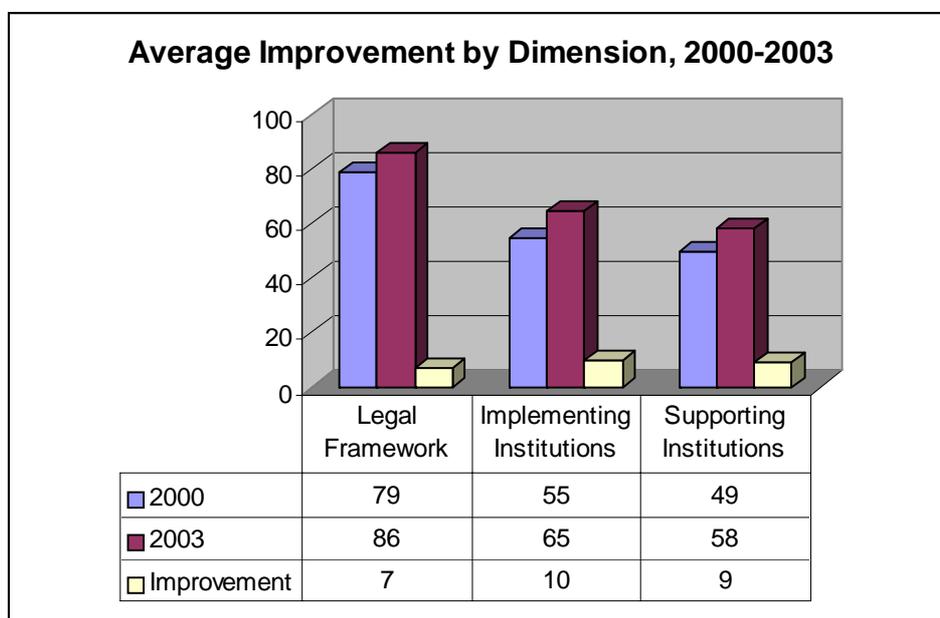
CROSS-CUTTING THEMES

Comparisons of findings in the seven specific areas of law leads to identification of common themes and issues that cut across the narrow fields being examined. These are examined here by dimension, and, where useful, re-emphasized in the separate chapters. In some cases, the cross-cutting issues are much more important than the findings on a specific law, because they tend to involve systemic problems, which, if addressed, would have a positive impact on all areas. It is often difficult, however, to

create stand-alone assistance on broad areas such as the need for better education. Consequently, this report seeks to connect the broad themes to specific areas in which the problem can be addressed through project assistance within a more clearly focused intervention.

Framework Laws

For the most part, the commercial laws of Macedonia are adequate to support the development of business, trade and investment and the economic development of the country. Most of the laws have been drafted based on modern European models, although not necessarily adjusted well to the post-Yugoslav reality of Macedonia. As the scores indicate, they have been improved significantly over the past three years.



Two significant problems exist, however, with respect to the mechanisms for changing law. First, there is not currently a well-established system for those who know the law best to initiate modifications. Most legal drafting initiatives are comprehensive projects to examine a large body of law (the Code of Civil Procedure, for example) on the basis of a perceived need for a major overhaul. In reality, many of the needs – especially now – are refinements of a few specific provisions that have not worked out in practice. Unfortunately, these simple modifications are often ignored until a multi-year analysis of the entire body of law can be carried out. Moreover, when smaller modifications are introduced, they are often recommended by theoreticians, not practitioners, and are often not what is needed. For example, the 2002 amendments to the Bankruptcy Law were rather simple, but wrong; fortunately, an influential practitioner was able to redirect the changes. Unfortunately, there is not an effective system for such practitioners to initiate such changes on a regular, formal basis.

Second, the Law on Legislative Process is flawed. Although it allows the Working Groups responsible for drafting to obtain whatever input they deem necessary, it does not mandate any public notice or any public input. A number of the improvements in the past three years incorporated programs of public notice and input, but they were prompted by donor support or by the good intentions of the individuals responsible. Such individuals are regularly replaced in the current political climate, so it is not possible to build upon their good intentions. It is, however, possible to use recent successes and the goodwill they engender to seek for a permanent change in the legislative process.

The problem is that good laws, without a good process, provide little stability for the investor in Macedonia. Laws can be changed without notice, including the laws underlying assumptions of investors. Bad laws can be improved regularly and incrementally with a good process and provide security to the economy in two ways. First, a deliberative process provides ample warning to the commercial actors that a change will take place over a long term (usually more than a year), so that they can adjust for new conditions and opportunities. Second, it allows the stakeholders to have a say in the nature of the change, so that they can actually participate in reforms rather than being victims of someone else's changes.

An important case in point is the current attempt to change the bankruptcy law. Unknown to most of the legal community, a working group was formed to revise the bankruptcy law. The group has not been open to the public nor their work to public comment. Announcements of intended changes included a stripping of the essential priority requirements and an excessive increase in employee protection during liquidation. The changes appear to be fueled by ideological and economic misunderstanding of the nature and purpose of bankruptcy. It is entirely possible under the current system for these changes to be submitted to Parliament and passed without further discussion. In that case, virtually all progress in bankruptcy and collateral will be substantially undermined, with very negative impact on credit and investment. With the proper mandatory process in place, such proposals would be subject to input and advocacy from those who understand the real needs in bankruptcy and the economy.

At the same time, the CG&CL Project is introducing a democratic model of lawmaking intended to bring about agreement and implementation, not just another new law. The CG&CL team has worked closely with the Working Group to ensure extensive input from experts and practitioners in company law, and is now holding extensive meetings throughout the country to obtain further input from the business and legal community while educating them extensively about the nature of the upcoming changes. The approach has been extremely well received by all involved, and is resulting in a high level of consensus as well as training in democratic lawmaking. There is no guarantee, however, that such a process will be used again, because it is not mandatory.

One of the highest priorities for legal reform is, therefore, a reform of the existing *Rules of Procedure of the Assembly of the Republic of Macedonia* to include mandatory public notice and comment provisions. As part of such a program, it will also be necessary to provide technical assistance to Ministries and the Parliament in democratic lawmaking practices and economic analysis of legislative changes. In addition, the nascent private sector business and professional associations will need assistance in responding to such changes, as there is little if any history of their involvement. Indeed, most do not expect a role, much less attempt to have one. This can be done in the context of a project for reforming specific laws in order to provide context to the very specific work that needs to be done.

The number of laws that still need amendment is substantial. As shown in Annex 2, USAID's WTO Project has identified 80 laws with impact on WTO accession and compliance that are in need of revision. The CG&CL project has also identified a number of ancillary laws and regulations that do not currently meet the needs of the business community in the area of corporate law and governance. These include laws on business associations; the law on arbitration and other forms of alternative dispute resolution; the law on administrative procedure; regulations governing the electronic entry of data and data transmission between government agencies related to business registrations and the proposed "one stop shop system"; revisions to the Law on the Central Registry; introduction of new laws governing credit bureaus, collection agencies, and appraisers; and a review of bankruptcy law to name a few. An expanded list of laws subject to drafting, review or revision can be found in Annex 3.

It should also be noted that laws are only one part of the gap. Many laws call for implementing regulations to take them from general to specific application, and many of those regulations do not exist. Within each project there is the need for developing such regulations to provide a complete package, as well as training for drafters of regulations. The current capacity for such work is insufficient to meet present or future needs.

Access to laws is another issue, but one that can easily be addressed. It is only recently that representatives of the Official Gazette presented lawyers with the opportunity to subscribe to the official gazette online. A subscription package was unveiled to attendees of the Fall MBLA conference. However, during interviews conducted as part of the CLIR review, lawyers were unaware of the availability of such a service. Legal professionals complained that it is unnecessarily difficult to know when laws are published and to obtain copies. The Ministry of Economy is currently working on a website for translated laws as a service to foreign investors, but the greatest need is for a modern system of electronic publication that has broad usage by local professionals at reasonable prices. The recent initiative of Official Gazette is a positive sign that there is a move to respond to the demands of practitioners.

Implementing Institutions

Implementing Institutions, in general, have improved over the past three years, with the exception of the courts. These changes have generally been in response to donor assistance and insistence, although there are instances of changes led and managed primarily by Macedonian officials. Recent clean up of the Customs Agency has been enthusiastically applauded by the private sector, who see it as evidence of political will in that particular area. Some also see the changes as a response to private sector needs and requirements of economic development. Likewise, there is a great deal of satisfaction with the ongoing efficient operations of the Central Registry. In other areas, however, the private sector still holds a low opinion of government services and the attitude in providing those services.

The courts provide a particularly intractable problem because all legal improvements eventually depend upon the courts to enforce them. It is not clear whether performance has actually deteriorated over the past three years or whether public opinion has just become harsher, but in any event there has been no perceived improvement. Current projects are underway to improve administration and judicial education, but additional, separate work is needed to address problems of enforcement. Otherwise, investments in decision-making will simply flounder on the shoals of unenforceability. This is further covered below in *Contracts: Implementing Institutions*.

There is a great deal of demand currently for the reinstatement of specialized courts with specialized jurisdiction and specialized judges. Macedonia had a separate system of commercial courts until 1996, but, unlike most other former Yugoslav republics, they eliminated that branch in favor of a system of courts with general jurisdiction. There has been some attempt at specialization through separate divisions for commercial matters in Skopje and a few other larger cities, but practitioners complain that it is not working because judges are still required to work on other types of cases. The loss in specialization has paralleled a loss in respect for the judiciary with regard to commercial matters.

Most participants – including judges – found that the judiciary needs increased training in various areas of law to perform their functions more effectively. One judge expressly noted that most judges did not understand the last changes to the company law, and received no training. There is a clear demand for very practical teaching materials (including forms, checklists, case studies and the like) on each new area of law being developed. This need could be met from within each project responsible for such changes and woven into the project design and deliverables. A general “judicial education” project may be too broadly focused to capture all the needs and such specific, incremental additions will meet a great need as laws change.

Frustration with the courts has led to an opportunity. Businesses regularly either give up or seek ways to bypass the courts. While foreign investors can sometimes find relief

through foreign arbitration, local disputes have no such outlets. There is a strong demand for alternative dispute resolution to settle commercial disagreements, but little legal or institutional framework to provide it. A study on this issue has been undertaken by FSVC, and is expected shortly. It should provide the foundation for creating an ADR project or project component within existing projects, and should be considered very carefully.

Supporting Institutions

The growth of Supporting Institutions in Macedonia provides a useful look at the interplay of market forces and donor assistance. Scores have improved by nine points in the past three years, led by two developments: the appearance and growth of bilateral chambers of commerce and the donor-assisted growth of various organizations. At the same time, there has been little improvement in the independently-funded Chamber of Economy or the oft-assisted Macedonian Bar Association.

There are a number of reasonably strong and effective Supporting Institutions. The **Macedonian Business Lawyers Association** is the oldest, and has made a relatively successful transition from its Yugoslavian origins to its current independent status. Funding is earned through sale of publications and subscriptions to magazines and journals covering legal topics. Members do not pay annual dues – yet – in part because of economics (low pay of judges, in-house counsel, lawyers and notaries) and in part because of history (no experience with dues-based organizations.) The MBLA has a series of sub-committees that track legal changes and even advocate change on occasion. Although a recipient of donor assistance at times – primarily through using the MBLA as a paid partner in various reform initiatives – it can survive without additional assistance. However, this assistance has been important in achieving sustainability. There is room for growth still in self-regulation of members in areas of business and legal ethics, and in advocacy. The MBLA leadership finds that it is still difficult to get the attention of government through any official channels when they wish to provide input on law or policy. Working with MBLA on legal reform projects may help them gain a more secure place at the bargaining table.

The **Macedonia Bankruptcy Association** is a product of donor assistance, and a successful one. Built in great part through USAID funding, the Association was started by bankruptcy professionals, including lawyers, judges, and trustees after returning from a study tour of these professionals to the US. The Association has assisted in the development of bankruptcy law and practice, and even helped to establish the licensing exam and requirements for bankruptcy trustees. It also serves as the primary donor counterpart for provision of training courses and continuing legal education in this field. Such training has provided much of the funding that the Association still depends on for vibrancy. It appears to be a few years away from full financial self-sufficiency, but is otherwise a significant success.

The **Macedonian Bankruptcy Trustees Association** is not as strong as it has been. Once part of the Macedonian Bankruptcy Association, the trustees were encouraged to create their own association because of their unique needs and interests. With outside support, they founded an association to represent the licensed trustees (currently 137) and the practice of bankruptcy administration. The MBTA has offered a number of courses, worked on trustee licensing issues and supplies its members with forms and checklists related to the bankruptcy process. Several members complain that the current leadership is not functioning effectively, concentrating more on study tours and other trips abroad and less on member needs. This is not unusual in transition societies, where the principle historical model of government is authoritarian with little practice of accountability. The next development phase for this organization may need to focus on service provision, otherwise the members may simply abandon the MBTA. Donors can assist in this by requiring services as a pre-requisite to assistance, and by assisting only through provision of services to members with no junkets for leaders.

The **Macedonian Bar Association** (MBA) is independently funded through mandatory payments by all practicing attorneys. Members expect the MBA to provide various services in terms of legal training, advocacy and professional development and are generally disappointed with the results. A number of lawyers noted that leadership issues define effectiveness, with the MBA's success being highly dependent upon changes in leadership; they would like to see service institutionalized so that quality would not fluctuate so much based on the personality of a given individual. This is not unusual for mandatory-fee organizations and is a common complaint throughout the region. The incentive structure simply does not encourage service provision, because dues must be paid without regard to quality. The existence of voluntary organizations like the MBLA and Macedonian Bankruptcy Association provides some competition, but even so, the competition is for prestige, not membership. The overriding perception is that the current MBA leadership caters to a small clique of lawyers closely allied with the executive at the expense of the members at large.

The **Macedonia Judges Association** also has a mixed record at the moment. Like the MBTA, it has been fortified through substantial assistance from the donor community, and has been successful up to a point by providing training, some publications, and some advocacy services for its members. Association leadership is quite pleased with the success, but judges are not as impressed. A judge sitting only a few doors from the MJA office at the Skopje court was completely unaware of the MJA activities and disappointed with communication. In addition, judges feel that the annual training sessions are a waste of time for the most part, because they tend to be limited to theoretical presentations by professors on new laws. Judges are asking for specific, practical training with useful forms and materials, but complain that they must develop them on their own, without sufficient (if any) help from the MJA. While the conflicting views do not permit a definitive assessment of the actual status of MJA services, it is clear that the Association is not communicating effectively with its membership, at the

very least. The principle problem seems to be a lack of service-oriented management skills, something missing in most Macedonian organizations. Through the MJA, a Centre for Continuing Education has been established that formalizes the continuing education initiatives. However, the future success of the Centre will depend on the practical content of the courses offered and the effectiveness of communication to the membership respecting the timing, types of and eligibility to attend the courses.

The **Macedonian Competitiveness Council** is the newest player in town. Created by USAID's Macedonian Competitiveness Activity (MCA) as an institutional leader of and counterpart for competitiveness work, it is a very high profile organization of respected and important business leaders. Expectations for the Council are very high, but it is too soon to determine how they are performing. A number of stakeholders see the Council as an important voice of advocacy for an improved commercial environment, and there is institutional interest from the various bi-lateral chambers of commerce in working with them toward that end.

The **American Chamber of Commerce (AmCham) in Macedonia** is an independent association of businesses with an interest in US/Macedonian business and trade. During the 2000 Assessment, AmCham was not yet functioning. Since then, it has grown significantly, with approximately 150 members who pay dues to fund the organization. Additional funding comes through payment for various events and donations from members. AmCham has produced position papers on investment issues and intervened directly at times on behalf of members. It has become respected by other bilateral chambers and could be a significant resource for the MCA project and for public education and implementation campaigns aimed at the business community.

The **Deutsch-Mazedonische Wirtschaftsvereinigung (DMWV)** and the **International Council of Investors (ICI)** are other positive examples of bilateral and international business associations making a difference. The DMWV is supported by Germany and focuses primarily on the SME sector in bi-lateral trade and investment with Germany. As such, the organization has an excellent network of businesses that can provide input into the policy and law making processes if permitted. The ICI has a large Greek constituency, but is not intended as a Greek bi-lateral chamber. Instead, the ICI is seeking to work more as a federation for the various international investors and their separate association and is actively involved in policy advocacy and intervention with the government. All of these organizations are hampered, however, by the existing law on business associations, which allows only individual members instead of corporate membership. Although it is possible to work around the restrictions, it is not useful. The associations are interested in working on a new law.

The **Macedonian Chamber of Economy** is under well-deserved attack. Founded as part of the Yugoslav government's system for controlling business, it only recently had a meaningful service mandate, which it has generally failed to fulfill. Business people complain that the MCE is crowding out effective organizations. The Chamber is

funded through mandatory taxes on business and salaries without regard to the quality of services provided. Recently, the government decided to end this mandatory tax on business activity and remove the fees, cutting up the MCE and reformulating it into several smaller, focused agencies that are to be run as voluntary membership organizations, dependent on their ability to provide services as the basis for funding and membership. The MCE has challenged the change as unconstitutional, thus delaying the end of its reign of inefficiency. There is not currently a model of successful conversion of such an agency into a successful state-funded service provider in the transition world, and the decision to convert it into a self-funded organization deserves support. The agencies that emerge may need support in management, organizational, and association skills if they are to survive and succeed.

Bankers' associations are often drivers of change in all areas of commercial law in developing and transition countries. For Macedonia, this has not yet been the case. Despite various attempts by several donors, the past three years have seen little progress in creating a viable association. In early November, however, it was announced that a new Bankers' Association had been formed. Success, this time, may depend on the growth of commercial banks and commercial banking to replace the relational, non-commercial institutions established as banks under the Yugoslav system. Many of the existing banks were started to service state needs and the needs of those connected to the state based on state guarantees, not on creditworthiness or commercial capacity to repay the loans. Consequently, it is not surprising that most of the banks have not been interested in exposing their non-performing loans and outmoded practices through association with other banks in the same situation. However, there are now a number of foreign investors and even a new foreign bank (ProCredit) that are operating in accordance with international standards and recognize the need for a concerted effort for reform and protection through an association.

The **Macedonian Business Resource Center**, noted in the previous assessment, no longer exists. MBRC received substantial funding and technical assistance from donors, especially USAID, and performed admirably in providing training, market research and other business services. Once direct funding stopped, the Center folded. For those who feel that the purpose of the assistance was to establish the Center, its closing can only be seen as a failure. This is a mistake. The Center has produced two viable, smaller consulting firms from the former employees of MBRC. Other employees who left prior to closure have started other ventures or found employment in which they now use their skills on an ongoing, self-sustaining basis. Likewise, the Center helped to train a cadre of business people in a number of essential skills that they continue to use in Macedonia. The fate of the MBRC suggests a reassessment of how success is measured: the function of projects is not necessarily to create institutions, but to enable individuals to build their own. If that is the goal, then the MBRC appears to have been a success.

Aside from a few organizations, NGOs and other associations are not yet highly developed on a self-sustaining basis in Macedonia. Most need assistance in

management skills and basic training on how to provide services for their members. There is considerable interest in management training among private sector stakeholders, which suggests there may be market demand for either a training institute or consulting services in this area.

Professional education received poor reviews from most stakeholders, at least at the university level. Analytical education that could result in effective critique of the state's performance was undermined under Tito and replaced with highly theoretical approaches not intended for application. Although times and approaches have changed, the legacy lives on and still depresses the overall educational experience, particularly in law. One of the most egregious problems is the lack of updated curriculum in the areas in which law has changed. This problem is widespread in the region, in part a result of low professorial salaries based on hours in class not hours of preparation. Professors frequently supplement their salaries with consulting, participation in special committees, foreign speaking engagements, and legal drafting, and thus have little time for re-writing curricula to keep up with the rapidly changing legal environment. Legal projects can provide assistance by developing materials and curricula to address legal changes and by working with student organizations to provide seminars on a voluntary basis.

The Market for Reform

The social dynamics of Macedonia are complex and sometimes contradictory. The recent emergence from a controlled economy and authoritarian power structure has not yet led either to a general understanding or the habits of democracy and free markets. The social fabric is marked by a division between the governed and the government. Historically, Macedonians have been subjects more often than citizens, and this is still reflected in expectations and behavior. As one legal professional explained, Macedonians tend to see rulers as imposed, "not my government," and have developed numerous ways of creatively resisting or thwarting government initiatives. The ability to elect officials should eventually have an impact in this regard, but today there is still a strong sense the rulers are someone else's government.

At the same time, the paternalistic approach of Tito's regime undermined the concept and practice of self-sufficiency. The role of the state was to protect the individual – from creditors, from poor products, from all kinds of problems and conflicts handled by the market and private initiative in the West. A trade expert noted the high level of involvement of the state in phytosanitary inspections in order to protect consumers, because consumers have not yet organized effectively to protect themselves. Several business executives complained that the state is not providing sufficient loans for business, completely unaware that this is normally the role of private sector lenders. Many Macedonians interviewed felt that the greatest obstacle to reform or entry into the European Union was mindset, not laws or institutions.

Recent history has created other complications. The conflict in Kosovo and tensions between ethnic Albanians and ethnic Macedonians has received coverage abroad, keeping many potential foreign investors out of the country, if not the region. While the government has tried to repair the ethnic breach through the Ohrid agreements, there is still a prevalent sense of uncertainty about ethnic relationships and stability.

All of these factors affect the demand for reform of the commercial environment, creating both challenges and opportunities. The top-down model of lawmaking and policy development, combined with a historical cultural resistance to imposed government, means that even the best designed policies may not be implemented because they are disconnected from the demand for reform. It also means that most of the laws and policies have not been well designed precisely because they were top-down and imposed. There is very little sense of ownership for most of the changes going on.

Another challenge is that ownership is slow in coming because people do not expect to have input into the process. For years they were literally told: "You don't need to think - we'll do the thinking for you."² Those who chose to protest or resist sometimes paid a high price, thus reinforcing the concept that it is better to stay invisible and find someone else to voice your concerns. Several business executives stated quite frankly that they try not to have anything to do with the government unless they have to because the risks of retribution are too high. Whether retribution is still likely today is not clear, but perceptions remain, and those perceptions influence behavior.

Despite these challenges, there has been remarkable change and reform, at least at the most superficial levels, but also within some of the institutions. Like many transition countries, much of the impetus for reform has emanated from the international community through conditionalities, direct pressure and targeted assistance and funding. Unlike many countries, this outside demand has met local demand from the private sector for the same reforms in many instances. Numerous respondents in the assessment expressed strong gratitude for US and European assistance in pushing market-oriented reforms through the government. They felt that they did not have the mechanisms, training, or even expectation for accomplishing such changes and had to rely on international economic pressures to achieve the reforms.

Unfortunately, such a system of reform is neither sustainable nor healthy in the long-term. It has filled two significant gaps in the short term, but cannot do so indefinitely. These gaps lie both in the public and private sectors. For the public sector, there is no existing, formal, mandatory mechanism for demand-based economic policy development, formulation, or implementation. The government and legislature have not been known for their ability to prioritize, produce cost-benefit analyses, or respond

² Several older Macedonians cited this as a direct quote from the former Yugoslav government, insisting that it was a well known theme of government.

based on private sector need. On the other hand, the private sector has not been able or willing to provide input needed for democratic processes to work effectively. But this is beginning to change.

Donor assistance, foreign investment, and political will of leading reformers have led to successful reforms and to a potential for changing the underlying processes and expectations of commercial stakeholders. Several government entities – most notably the Ministry of Economy – have become remarkably open to private sector need and input and are actively seeking it. The Central Bank recently surveyed banks on changes in certain banking regulations, then changed the regulations to satisfy the demands of the banks. The approach was neither top-down nor theoretical.

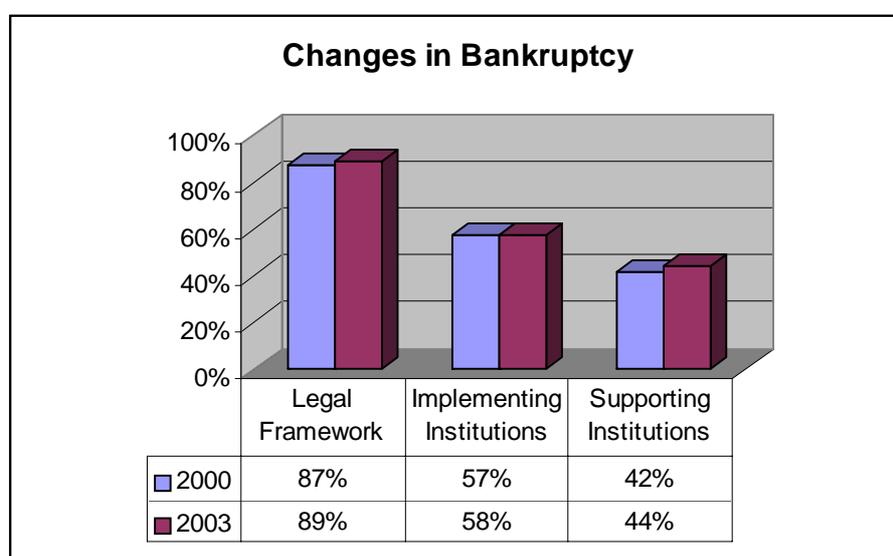
Private sector associations are beginning to grow, with and without outside help. Their ability to articulate and promote national economic development will have a fundamental role to play in holding government accountable for economic and social policies. Ownership habits are being strengthened and introduced through projects such as USAID's Corporate Governance and Company Law (CG&CL) Project, which has a broad approach designed to ensure ownership, responsiveness, and implementation in the formulation, passage and practical adoption of the new company law. This has been coupled with public education and development of teaching materials for all principle stakeholders, utilizing the resources and networks of existing Macedonian organizations. By requiring input from all ethnicities, the process is also encouraging dialogue and collaboration across ethnic lines.

The 2003 Assessment has shown that donor assistance has already had an impact in improving the CLIR environment since 2000. With well designed assistance encompassing public and private sector needs and actors, it is possible to achieve even more.

BANKRUPTCY

Overview

Bankruptcy law and practice are under imminent threat at the time of this writing. Although the law is essentially sound as it stands, there is a move under the Ministry of Finance to re-write the law, with the drafting group led by a professor who appears to have no understanding of the business and economic implications of an effective bankruptcy system. According to one bankruptcy professional, the changes being proposed will set Macedonia back twenty years, hampering access to credit and finance.



This would be a shame, because in other fronts this area has moved forward. The law is generally sound and has been significantly improved in some important areas in the past few years. Bankruptcy trustees are abundant (over abundant, in fact), and are now subject to a reasonable licensing system that establishes relevant baseline qualifications. The Macedonia Bankruptcy Association continues to provide continuing legal education, reform advocacy and other valuable services to the bankruptcy profession. The courts have shown no improvement and even some regression, but projects underway stand a chance of changing the overall level of performance. However, the proposed changes to the law under consideration will nullify all advances in all of these areas.

Intercepting and rerouting the current reform efforts could provide an opportunity for substantial positive impact by engaging the business community in the reform process to address the practical issues of implementation that continue to undermine other advances.

Legal Framework

Recent Changes. As reported in the 2000 Assessment, the Bankruptcy Law is essentially sound. It is based on German and Swiss models (which were based on American bankruptcy law but with adjustments for Europe) and, if implemented, would serve adequately as a means of regulating reorganization and market exit.

In 2001, the Ministry of Finance announced a plan to reform the law. The Macedonian Bankruptcy Association, through one of its prominent members, contacted the Ministry and received permission to participate in the working group, arguing effectively for a different set of changes than were being proposed. Two of these were significant.

First, the new changes imposed a deadline for submission of claims. Previously, new creditors could appear at any time during the course of proceedings, creating substantial disruptions in the distribution of assets. Under the new amendments, creditors who do not meet the deadline for submission of claims lose their rights to the claim within the procedure. This has already begun to bring greater discipline to the proceedings.

A second change is more controversial. The 1998 law permitted the commencement of a claim upon presentation of proof that a debtor was 45 days in arrears. This could be shown through presentation of invoices or other reliable documents. Debtors, however, took advantage of a systemic weakness in the bankruptcy regime in order to disable the process with delays. Upon presentation of invoices, debtors would frequently dispute the claim. This caused the disputed claim to be transferred from the bankruptcy court to a court for commercial claims, and halted the bankruptcy proceeding for as much as two years until the claim could be heard and decided. On the other hand, creditors were using the simple process to enforce payment by bringing suit against solvent debtors who were late in payment or who had refused to pay because of a dispute in order to use the threat of bankruptcy to force the debtor to pay.

In order to stabilize the situation, provisions were enacted in 2002 that required bankruptcy claims to be based upon an executive title – that is, either an unsatisfied court judgment or an executive clause within a notarized contract. Because the terms of such titles are not disputable, debtors are prevented from challenging the basis of the claim in order to delay the bankruptcy proceeding and creditors are prevented from initiating a bankruptcy proceeding in the absence of proof of default. Unfortunately, this has also limited legitimate claims by creditors who are suing on an account instead of a notarized contract, hence it is not an adequate solution.

Changes needed. Although the law is sufficient at present, it is certainly not perfect. As noted, changes are needed in the overall system so that disputes between creditors and debtors are maintained within the bankruptcy proceeding for urgent handling rather than holding the bankruptcy procedure hostage to the schedule of another court.

Second, local professionals who are familiar with international practices feel strongly that the bankruptcy panel should be eliminated in favor of a single judge to preside over the case. This suggestion is based on experience elsewhere, and on dissatisfaction with inefficiencies inherent in the Macedonian three-member panel. Other changes would also be introduced in a properly structured reform project, but these are priorities within the bankruptcy profession at this time.

Changes threatened. Recently, a drafting group was empanelled by the Ministry of Finance to revise the Bankruptcy Law. The group has proposed an elimination of the existing priorities so that secured and unsecured creditors would be equal. In addition, employees would have first priority, with a preemptive right over any claims by commercial creditors, including registered, secured creditors. Proposals also include direct involvement in the procedure by the Ministry of Economy.

The overall tenor of the proposed amendments suggests extreme ignorance of the purpose and function of bankruptcy law in a market-oriented economy. This deficiency appears to be influenced by ideological legacies from the socialist period which sought to maintain a certain level of equality of result, based on a misguided belief that it is unfair for one person (such as a secured creditor) to obtain a better result than another (such as an unsecured creditor), without regard to the circumstances of lending. This attempt at debtor protection would have a serious impact on the entire secured transaction system, and hence on the cost and availability of credit in Macedonia. In short, these changes will create an economic catastrophe in the regional competitive environment. The nature of the proposals suggests that there is a great need for public education – especially among policy makers – about the purpose and impact of bankruptcy law.

Just as troubling as the recommended changes is the approach taken in drafting them. Legal and bankruptcy professionals have unanimously complained that they were not notified of or included in the drafting process. They also are under the impression that no public comment will be solicited or accepted, but that this law will instead be submitted to Parliament without the use of even basic democratic lawmaking processes. Programmatic assistance (including the possible use of sanctions or conditionalities to stop the current process) could dramatically change the outcome of this reform process by ensuring extensive public debate, public education, and stakeholder input to the process.

Implementing Institutions

There are three Implementing Institutions for Bankruptcy: the Ministry of Justice, the courts, and the trustees (or administrators).³ Together they share the responsibility for

³ Trustees are sometimes characterized as Supporting Institutions. Due to the State involvement in licensing and their essential role in implementation, we have characterized them as part of the Implementing Institutions.

effective implementation of bankruptcy law and practice. In Macedonia, this responsibility is not currently being shared effectively.

Ministry of Justice (MOJ). Authority for various aspects of bankruptcy law and practice has been divided within the government, with various statistical and monitoring services under the Ministry of Economy (MOE) and legal and administrative issues under the Ministry of Justice. The MOJ has taken a leadership role by establishing – with USAID assistance – a system for licensing bankruptcy trustees. The work was done in conjunction with the Macedonian Bankruptcy Association and is generally perceived as successful. The MOJ now administers the licensing exam; the bankruptcy profession is generally satisfied with the results.

Currently, the Ministry of Finance is seeking to undermine the bankruptcy system through introduction of surprisingly flawed procedures. The attempted reforms by the MOF in 2001 were also negative, but fortunately were intercepted by an influential judge who redirected the reforms. It is not clear why this Ministry continues to initiate such misguided changes, but it might be helpful to move responsibility to the MOJ.

Reporting and statistics are still problematic, with most court reports poor in quality, not standardized, and, as a result, not very useful. Reporting is not public or transparent. The assessment team was told that statistics on bankruptcy are not available to the general public, but instead require a request from a Member of Parliament. Consequently, the team was unable to obtain any meaningful information on the number of cases being processed.

Courts. The scores for courts continue to show a very low level of effectiveness. Although some improvement was perceived in the ability of courts to respond to violations of bankruptcy law, this was counterbalanced by a perception that overall knowledge of judges has regressed; that is, practitioners today are *less* satisfied with judicial capacity than they were three years ago.

The overall problem of courts is covered in *Contracts: Implementing Institutions* and need not be restated here. It is worth noting, however, that there is substantial interest among judges in creating specialized courts in order to avoid being transferred from the specialized bankruptcy division to some other division after they have developed expertise. Most recommend the re-creation of Commercial Courts, as opposed to the existing Commercial and Bankruptcy *Divisions* within the general courts. Such courts were eliminated in 1996 from Macedonia, but maintained in Croatia and Slovenia, where they are considered to be relatively successful, at least in terms of greater expertise.⁴ Practitioner confidence in the court system continues to be quite low, with numerous complaints about the lack of specialized skills and knowledge even among

⁴ It should be noted that the crisis in enforcement in Croatia has resulted in numerous findings by the International Court in Strasbourg that the lack of enforcement of judgments is a violation of human rights. Macedonian reverence for Croatian solutions should be tempered by a better understanding of the practical problems in implementation.

judges in the specialized divisions. In the past few years, several respected bankruptcy judges have been removed from their positions, transferred to other divisions, or even dismissed from the judiciary, for reasons perceived as political. This has further undermined respect for the system.

There is an expectation that the new changes in the Code of Civil Procedure will help to rectify some of the practical problems affecting bankruptcy cases, especially with respect to delays in proceedings. It seems unlikely that much will be achieved, however, without significant training of both judges and practitioners. Likewise, as already mentioned, it is important to eliminate delays caused currently by removal of disputes. According to judges and lawyers, much of the training needed is not in the legal aspects of bankruptcy, but rather in how to manage and conduct a bankruptcy trial. Problems with legal knowledge are perceived as secondary to a lack of management skills and practices, reflected in unnecessary delays.

It should also be noted that the Macedonian Bankruptcy Association has expressed a need for introduction of mediation and arbitration into bankruptcy claims in order to lower delays, by-pass the courts, and reduce the strain on courts. This subject is further developed below in the discussion of Supporting Institutions.

Trustees. The development of a cadre of competent bankruptcy trustees is a mixed success because supply far outstrips demand for the services. To date, 137 trustees have been licensed by the MOJ based on successful completion of tests related to business and legal subjects. In addition, there has been significant training of trustees over the past few years, primarily through the Macedonian Bankruptcy Association and in part through the Macedonian Bankruptcy Trustees Association. This success is a direct result of long-term programmatic assistance to the trustees by USAID.

The usefulness of the training has been compromised by the dysfunction of the courts. Too few cases are actually moving forward, so that many of the potentially qualified trustees may not get to use their training before they forget most of it.

Supporting Institutions

The Macedonian Bankruptcy Association was established in the late 1990s with assistance from USAID and ABA/CEELI, after a study tour of bankruptcy professionals to the US. The MBkA has been quite successful in leading legal reforms, providing CLE and other training, and providing public information. The Association helped to draft and lobby for the 2002 changes and can be expected to try to head off the current round of revisions under discussion. The Association continues to request assistance in conducting events, in part because the low level of membership fees does not cover expenses effectively. As the bankruptcy courts are repaired, however, demand for services is likely to go up, so that it should be possible to cover the costs of events

through event fees. It may be several years before the local stakeholders can afford to cover the full price of events involving international experts.

The Macedonian Bankruptcy Trustees Association has been less successful. Originally, trustees were members of the MBkA, but were encouraged to form their own association due to their specialized interests. At the outset, there was an enthusiastic response, but perceptions today are that few meaningful services or activities are being offered. Some respondents felt that the leadership was taking advantage of the office for free study tours abroad, but not providing much in return. It is doubtful that many serious changes can take place until the demand for trustee services increases as the problems with courts are fixed. Oversupply of members with undersupply of work is unlikely to provide the necessary foundation for reforming the association.

The Macedonian Judges Association received mixed reviews with regard to bankruptcy issues. On the one hand, the MJA has actively and even spontaneously advocated changes in the law and practice, to the extent that anyone on the drafting committees would listen. Like most other groups, the MJA complains that drafting is left too much in the hand of theoreticians from the law schools and too little grounding in reality and practice. Indeed, one judge characterized this as a monopoly on drafting.

On the other hand, a judge with chambers only a few doors from the Association office had the sense that they were doing very little and had not received information about various activities. In addition, one respondent noted that the training provided by the MJA tended to be theoretical lectures by professors. At the very least, some additional work is needed in information and member services.

The Macedonian Bar Association also received low ratings by all members of the legal profession consulted. The MBA appears to suffer from problems encountered in other post-socialist economies in which the bar association is funded through mandatory fees by all practicing attorneys without regard to performance. In Macedonia, the gap in services is filled by a very active private voluntary association of in-house counsel, notaries, judges and lawyers: the Macedonian Business Lawyers Association. The MBLA receives much higher reviews for publishing legal opinions and magazine articles on bankruptcy issues, providing some legal education, and advocating reforms. Some bankruptcy professionals felt that the MBLA was too close to the government, but there was no serious complaints about performance. Given the choice, the MBLA seems to be a better counterpart for project work than the MBA, although the MBA probably should be included in order to push them toward better services and to keep them from opposing programs that don't involve them.

Market for Reform in Bankruptcy Law

The social dynamics in the bankruptcy field are unusual. There is strong support for change in accordance with international standards from a cadre of judges, lawyers and

trustees with substantial local and international experience. They have worked with various projects in reforming the law and have brought about a number of improvements in both law and practice.

At the same time, there is a countervailing influence being exerted through government that has attempted twice to introduce negative reforms. In recent amendments to the Code of Civil Procedure changes were made by Parliament, without explanation, reducing improvements to enforcement. The current reform effort seeks to establish ministry intervention in bankruptcy proceedings.

Clearly, some of the negative changes come from a poor understanding of the role and function of a bankruptcy system in a market economy. However, some bankruptcy professionals have suggested that there is strong opposition to reform from a "financial oligarchy" with high debts and strong ties to government. It is beyond the scope of the assessment to prove or disprove such assertions, only to note the theory.

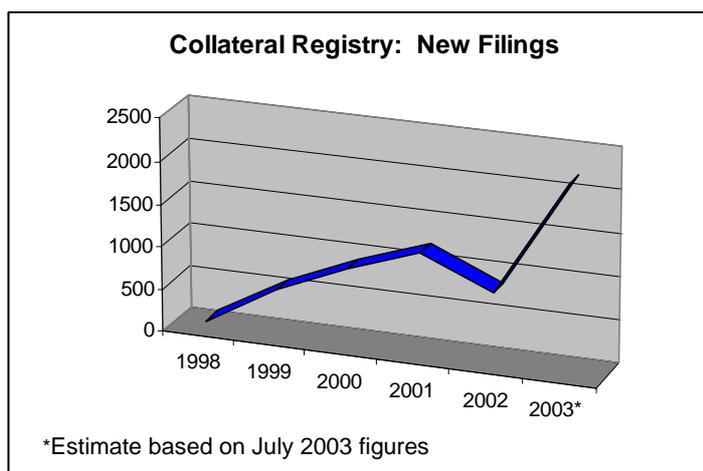
Macedonia also struggles with the political implications of bankruptcy, as do its neighbors. One of the implications of bankruptcy is unemployment as defunct state enterprises are closed down without payment of salaries and social contributions. It is also worth noting that much of the use of bankruptcy to date has been for state lending, not commercial lending. Bankruptcy law is primarily designed to sort out problems of commercial lending based on commercial standards and practices that were not in use when many – if not most – of today's insolvent companies incurred debts through political and relational lending.

COLLATERAL

Overview

The secured transactions regime had already been substantially improved in 2000, with a new law adopted and a new registry established in 1998. Consequently, the scores were relatively high during the prior assessment. In the past three years, improvements have been made at the legal and institutional level, so that Macedonia's collateral registry system has among the strongest ratings of the 11 countries assessed to date in the Europe and Eurasia region. In terms of improvements over the past three years, the legal framework score has moved from 79 to 91, indicating significant improvement.

This can best be seen through the registry's statistics. In the past two years, new filings have almost doubled: from 1200 two years ago to an estimated 2200 this year. During the first six months of 2003, almost €25 million in property has been pledged.



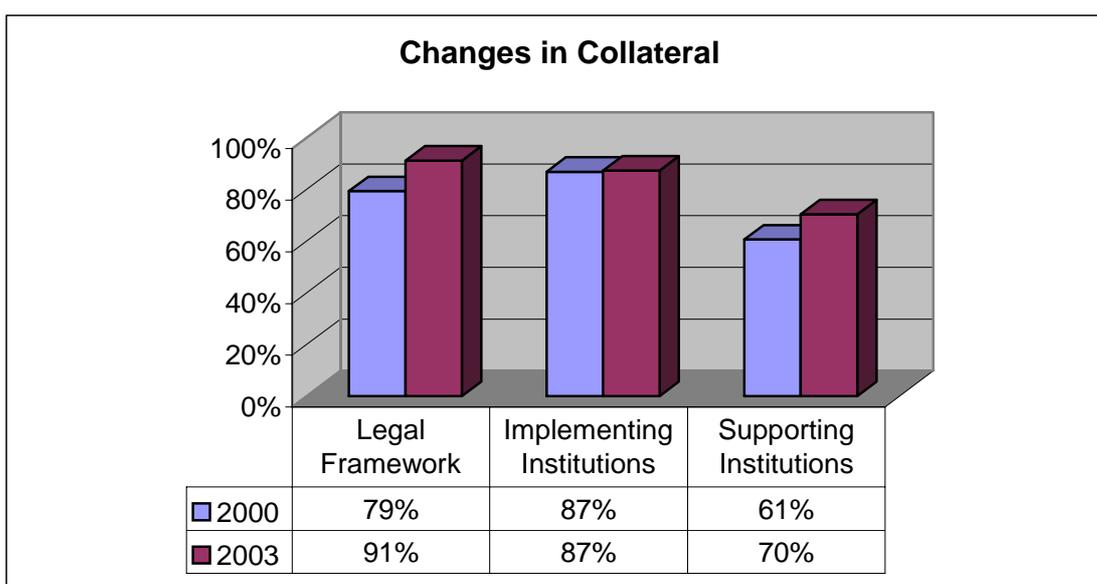
There is still room for improvement, however. Minor amendments are needed in law as are improvements in the overall registry system. One needed change – regarding legality of unregistered pledge agreements – suggests that there is still some misunderstanding of the reason for pledge registration. Lower fees would increase the overall accessibility, especially if Macedonia intends to increase the level of consumer credit and secured financing for SME ventures. Even so, it is safe to say that the system is essentially sound and oriented in all the right directions.

Framework Laws

Law on Contractual Pledges. The 1998 *Law on Pledges of Movable Property and Rights*, although essentially sound, was substantially revised in 2003 to combine pledges on movable and immovable property under one law, the *Law on Contractual Pledges* of January 31, 2003. This approach is not standard, but makes good sense as many of the issues of pledge registration apply equally to all types of non-possessory pledges. The law is well structured, well organized, and effective. It is also an improvement over the prior law, which, although good, lacked a few points.

There are still some missing items in the new law, but not all of them need to be corrected. First, many drafters or legal critics like to see a more detailed list of those

items that can be pledged, such as warehouse receipts, livestock and inventory. The existing law does not expressly name as many items as are found in some laws, but the scope of the law is broad enough to permit such items to be pledged. In fact, banks reported using all of these items as collateral. Several legal professionals noted that the law did not seem to permit the pledge of a business as a going concern. The law would seem to indicate otherwise in Article 12, but the doubts suggest need for clarification by a competent authority – the Supreme Court or a commentator from one of the law faculties.



Of greater potential importance, the law provides that a pledge contract is not legal or binding if not registered. The apparent intent is to ensure that there are no hidden liens and place the burden of registration on the lender as a matter of self-protection. These are certainly worthwhile goals, but the drafters have reached too far. The law would achieve greater impact if the registration created the *priority*, not the *legality* of the underlying pledge agreement; that is, failure to register would result in a loss of priority to any other registered creditors. Lenders who failed to protect themselves would rightly suffer the consequences, but would still have a valid pledge contract subject to the prior claims of registered creditors.

There are several reasons for making this distinction. First, the marginal cost of registration (especially in combination with notarization) is relatively high for low-end consumer loans or small investment loans. Currently, the fees for notarization (about \$50) and registration (also about \$40) are significant as a percentage of total cost on loans under \$5,000. In other countries, where registration provides only priority, not legality, lenders often decide to avoid such expenses for low risk customers and thus can lend on better terms. Second, people make mistakes. Sometimes a lender may inadvertently fail to register the pledge, which should not result in a complete forfeiture of claims, but only in the loss of protection. The purpose of the registry is to protect

lenders and third-party purchasers from hidden priorities. This can be handled just as well through laws that strip priority from unregistered pledges and permit sales to invalidate unregistered interests in the property.

Several stakeholders also noted problems in the area of descriptions. The law permits general or generic descriptions (Article 23), but registry users claim that the registry staff do not. There were complaints that the descriptions required upon registration were too extensive and specific, making it difficult to register an interest on inventory, accounts receivable, an enterprise as a going concern, or even after-acquired property. One stakeholder was even under the misguided impression that only items with serial numbers could be pledged. These problems do not need to be addressed through new legislation, but through better communications between user needs and registry staff. It may be necessary to issue regulations – available both to the registry and the users – more clearly defining the acceptability of descriptions in light of European standards for such descriptions. Unfortunately, there is not yet a viable banking association to act as a counterpart for such work.

The Collateral Law was substantially improved in the new version through expressly providing for self-help (Art. 23), and improved details on the rights of third-party bona fide purchasers (Arts. 36, 37, 50) and responsibility for unauthorized disposal of pledged assets (Arts. 30ff, 50). Only a few stakeholders reported any use of self-help for movable property, which was primarily in the area of automobiles, where a small repossession industry is starting to develop. Those using self-help, however, complained that they would prefer to rely on the police to repossess vehicles, but that the police do not generally wish to exercise that role, leaving them to use repossession agents instead.

Another improvement is the introduction of the possibility of pledge agreements having executive force. Although possible under previous law, the new law more clearly establishes the use of notarized agreements to permit lenders to execute against collateral without a court procedure. This should help to avoid delays inherent in the current court system and to lower the overall burden on the courts, thus improving court performance. The system is still in the trial stages, however, and will probably need refinements as utilization increases.

Leasing Law. The Law on Obligations was previously perceived to be weak in permitting such specialized contracts as leasing, and thus a new law was drafted and adopted. According to stakeholders, leasing actually worked just fine without the law and they did not see the need for it, nor has the situation changed significantly since the passage of the law. As a practical matter, therefore, it is not clear that the new leasing law is a significant improvement in the overall framework of secured transactions, but for newcomers to leasing, a well-defined law creates a more attractive investment environment.

Leasing is a form of secured financing in which ownership remains with the lender during the course of the lease. There are two types of leases, and both are possible under Macedonian law. In financial leases, the contract normally stipulates that the lessor will own the leased asset upon final payment. In operating leases, the lessor generally may buy the asset at market price upon the completion of the lease term, but there is no obligation or expectation of this. The law also requires (Art. 12) that the Lessor register the lease at the Central Registry, thus putting third parties on notice that the object of the lease is encumbered. One stakeholder in the leasing business felt that this was unnecessary, but the opinion was based on self-protection, not protection of third parties. It was clear that there is still misunderstanding about the role of registration.

The Leasing Law also provides for sanctions for various performance failures of lessors and lessee, including fines for lessees who fail to maintain the condition of the goods. This, however, does not necessarily protect the lessor unless the fine is paid to the lessor.

Other Laws. One leasing agency noted several problems related to leases and collateral. First, leases are currently overtaxed because the tax law and tax agents do not recognize that a lease-buyback operation is essentially a financial operation, not a series of sale. In practical terms, this means that transfer taxes and VAT are being charged twice in a lease-buyback operation, instead of only once. In addition, there was a complaint that tax agents do not understand the business side of such transactions or understand financial accounting sufficiently. The result is that they overtax, seek excessive documentation, and, in the end, inspire yet another reason for businesses to keep two sets of books: one that the tax agents can understand and one that represents the financial health of the company.

A more important issue at present is the Bankruptcy Law. This law is currently under review by a working group. It is not clear whether the group has adequately considered the relevance of Bankruptcy Law to the Collateral Law, which are different aspects of the same system of creditor protection. In fact, comments on the proposed changes at the time of this writing indicated that the new draft might strip the priorities among creditors - including secured creditors - to put all creditors on an equal footing once a bankruptcy is declared. This would be disastrous for secured lending in Macedonia and suggests a fundamental lack of understanding among the drafters. Priorities are used to manage and limit risk, thus providing better terms, higher levels of credit, and lower costs. If the Bankruptcy Law is amended as currently suggested, then the improvements in the Collateral Law will be substantially undermined.

Bankruptcy practice has proven problematic in permitting repossession of leased property that is not subject to some form of state registration. That is, it is relatively easy to repossess cars, for which ownership by the leasing company is registered with the motor vehicles registry, but not equipment, where there is no similar ownership

registry. Lease registration should improve this situation in theory, but practitioners note that the problem lies in part with understanding of the bankruptcy trustees.

Lawmaking. The process of revising the framework law received different ratings depending on the stakeholders asked. The drafters felt that they had adequately vetted the new draft with all necessary parties, noting that there were practitioners involved in the committee and that, in a small country such as Macedonia, everyone knows everyone so that all important viewpoints are included. The practitioners and business people (most notably banks and leasing companies), had a very different impression, and clearly stated that they were left out of the drafting and policy process for the collateral law.

In practice, it appears that the working group used a modified “classical model”. The draft was produced by a small working group of professors and practitioners, then sent to the World Bank, EBRD, and perhaps some other specialists for comments. Based on those comments, the drafters revised the law and sent it to Parliament for passage. If there were other opportunities for input, they were not meaningful to the private sector stakeholders.

Although it can be seen that the process produced a technically good law (upgrading it from a score of 79 in 2000 to 91 today), the lack of stakeholder involvement seems to explain the amount of confusion regarding various aspects, including confusion in the law itself over the nature and purpose of a pledge registry system.

Implementing Institutions

The Collateral Registry. The Macedonian Central Registry, and especially the Pledge Registry, have been offered as a model for other countries in the region to adopt and emulate. With 30 offices nationwide (covering all major towns and all regions), a computerized database with national application, and public access (for a fee) to all records, the Registry has earned its excellent reputation.

User satisfaction with the Registry is generally very high. Stakeholders agree that the Registry is accessible and service-oriented. Delays in filing are minimal, with service-while-you-wait the norm. Information retrieval is also satisfactory, with users stating that they are able to get information easily. The website has been developed since last assessment, but during the course of this assessment, it was not functioning.

The most important indicator of whether the registry and law are working effectively is whether lending has increased because of the new system. If information from one bank is indicative, the system is a success. One major bank reports that they have increased their secured lending by \$10 million because of the new system. Moreover, they contended that their capacity to foreign investment in the bank was directly related to the establishment of the collateral lending regime. In other words, the success of the

Registry can be seen in both increased credit availability and increased investment, which is the goal of this area of law. Terms of credit have not yet improved, however, because of other risk factors in the market and the lack of established practice in enforcing secured loans.

The Collateral Registry has consolidated its performance since the 2000 Assessment. The scores have remained even, however, because they were originally very high. (Only the indicators for the courts as an Implementing Institution were low in this section – those too remain unchanged.) This stability is a very positive sign – it is quite common for institutions to lose quality once donor funding has been reduced or withdrawn, and that is not the case here. The Registry is strong.

Strength, however, is not the same as perfection. Two areas stood out as needing improvement. First, those lenders and other stakeholders dealing with SME lending found that the registration was too high, especially when combined with notarial fees for executive documents. The current registration fee (2000 dinars – about \$40 at today's exchange rate) is high compared to fees charged in Albania (less than \$5) and even most U.S. registries (\$10-15).

It is not clear why the costs are this high. One possibility is that the Macedonian system requires a greater number of documents, including the notarized pledge document, corporate documentation, and other papers. More efficient systems register only a simple form giving the basic facts with few or no background documents. This is because the purpose of the system is to put others on notice that someone has a claim against the pledged property. In general, collateral registries do not collect extensive information about the level of debt, the value of the property, or the terms of the contract, all of which change – sometimes rapidly – over time. Collecting and providing more extensive information is more expensive.

There is an upside to this information, however. Registry records provide substantial credit information not currently available from any other source. Lenders are using the registry to check out their debtors more effectively. One banker noted that payment performance on registered debts is better. These results can and should be achievable through introduction of private credit information bureaus, but until that time, the Central Registry is partially filling the gap. The downside, however, is that the high cost of registration increases the cost of SME lending. Coupled with the legal concept that no pledge is legal without registration, pledge financing is being depressed.

Courts. The general public is still highly dissatisfied with the performance of Macedonia's courts in the enforcement of pledge contracts. Although one practitioner noted that it is possible to obtain relatively rapid decisions in simple cases with a motivated judge, there is a general impression that once a claim goes to court, delays will be extensive.

Another problem noted in enforcement relates specifically to real estate transactions. Lenders and practitioners noted that it is extremely difficult to evict occupants of a building if the debtor defaults. Title can sometimes be transferred to the lender, but police will generally not assist with eviction, and numerous delays are possible in the procedures. This is due in part to separate rights of the various family members when the titular owner – normally the husband or father – takes out the mortgage in his own name. Those not named are still subject to protections, so that lenders are increasingly requiring multiple signatures by or on behalf of all other occupants. Eviction laws policies will eventually need to be reconsidered; for now, such practical contractual protections are the best approach to clarifying rights in any given transaction.

It is still too early to see if the self-help provisions of the 2003 Collateral Law will provide any substantial benefits. Much of the enforcement responsibility has been shifted from courts to notaries in rapid, executory actions based on notarized documents. The same approach has met substantial resistance in Croatia, where critics note that the underlying problems – lack of enforcement agents (bailiffs), excessive rights to appeal, and poor auction and sale procedures – are not addressed by shifting responsibility for the problem outside the courts.

Supporting Institutions

1. Notaries. In general, lenders and other practitioners are satisfied with the quantity, quality and prices of notaries. One lender keeps a short-list of high quality notaries available for all transactions requiring notarization, having found that quality of service can vary considerably. As previously noted, stakeholders dealing with SME lending find that fees are relatively high for smaller loans.

The Association of Notaries is not perceived as particularly effective in advancing reforms or refining practice.

2. Enforcement Agents. As also noted in the section on courts, public officials with the authority to assist in seizure or attachment of pledged property are not perceived to be particularly effective. One lender noted that private agents are effective in repossession of automobiles, but found the use of them distasteful, preferring police instead. Once a debtor resists repossession, however, the lender must use state officials, such as the police. They are reportedly unavailable in most situations.

3. Professional Associations. The Macedonian Bar Association has not yet developed any particular specialized committees or other units that can monitor and recommend changes in the collateral law regime. However, two other organizations do provide input or monitor developments. First, the Macedonian Business Lawyers Association (MBLA) is a self-funded group of in-house attorneys, judges, private lawyers and notaries that produce various publications about legal issues, including information on changes in the registered pledge system. They even have a specialized committee on

topics involving property rights, including secured transactions. Although they seek to provide input on legal changes, they feel that they are not given sufficient meaningful opportunity to provide comments or analysis.

The Macedonian Bankruptcy Association also follows some of the trends in secured transactions, as this has a direct impact on bankruptcy practice. The Association works with bankruptcy trustees and can serve as a conduit for public information and training on Collateral Law issues.

4. Credit Information Bureaus and Collection Agencies. Credit information bureaus are an important part of the overall system of accountability in secured lending and enforcement of commercial obligations. They enable lenders to impose both positive and negative consequences for payment behavior while better managing their own risks. Macedonia currently has no such bureau. The Central Bank maintains some negative information on blocked bank accounts, but no positive information on past payment histories or overall credit exposure. The Central Registry provides company information, but it is only as good as the information filed by the companies with the registries. Few banks currently have the internal credit analysis capacity that credit bureaus provide.

Likewise, there appear to be no commercial debt collection agencies. These fulfill an important role in assisting companies with delinquent accounts before the accounts become highly problematic, thus avoiding litigation or repossession. Several companies outlined very good practices that they employ in debt collection, but could identify no outsourcing possibilities for companies that do not have the staff to perform such tasks. This absence weakens the overall enforcement regime for secured transactions.

5. Trade and Special Interest Groups. As noted in the section on cross-cutting themes, few of the groups that might normally play an important role in driving reforms in this area are functioning in an advocacy or educational role. Efforts at forming a Bankers Association have not yet been effective, leaving a substantial gap in one of the most important groups for monitoring and refining this area of lending. Foreign investor groups are increasingly capable of analyzing and providing policy input in this area, but have not yet been engaged to do so. This is partly because those responsible for reforming Collateral Law have not effectively engaged the private sector to collaborate.

6. Universities and Think Tanks. Macedonian law faculties suffer from outdated curricula in the field of secured transactions. Legal professionals generally felt that these schools are in need of substantial updating and reform, including inclusion of somewhat more practical information. Unfortunately, the salary structure is such that it is highly unlikely that any professors will be able to revise the teaching materials unless separately paid to do so. Judges noted that professors provide seminars at annual judges' meetings on new laws, such as the Collateral Law, but that the seminars are

highly theoretical and leave them with no practical information that they can apply in the courtroom.

Many of the legal and practical issues raised in this assessment have very significant economic impact. Currently, there is no regular practice of providing economic cost/benefit or other impact analysis when determining how a law should be drafted or implemented. Macedonia has a need for think tanks and foundations that can provide such information. This permits better lawmaking and better public education when it is necessary to explain changes to the public and various interest groups.

Market for Reform

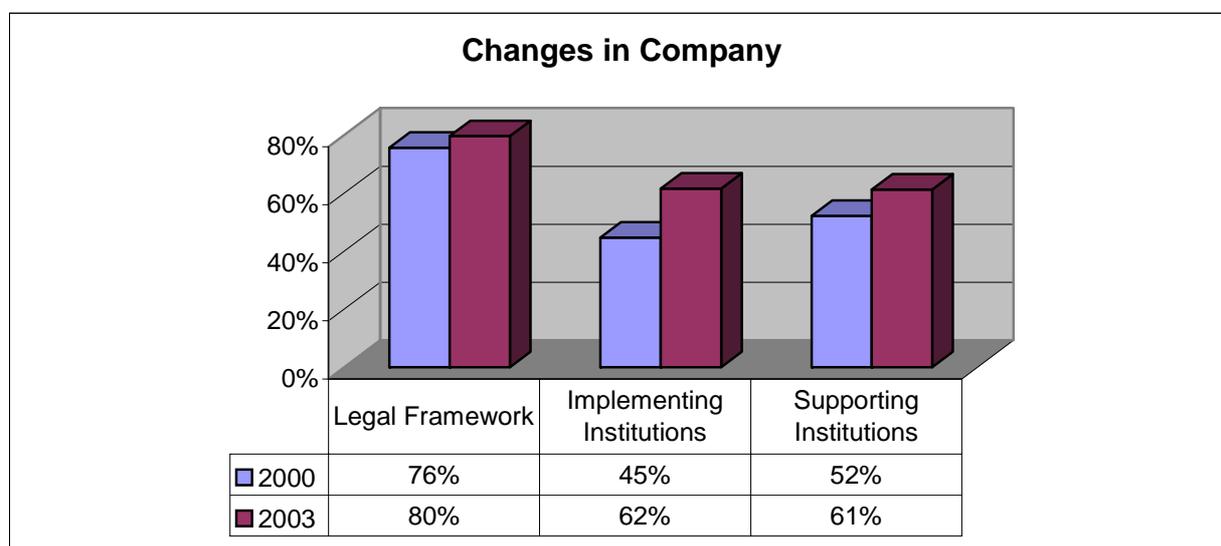
Currently, the overall Collateral Law and Registry system is functioning quite well, resulting in increased lending through secured transactions. There is therefore no particular demand for any significant changes, only for increased use of the system. However, there is some question regarding the level of registry and notary fees and its impact on SME financing. Any changes in this area are most likely to be driven by donor projects, as there does not appear to be any existing institution with capacity to lead such changes on its own.

Demand for increased education in this area is subject to the same constraints and problems noted in the section on Cross-Cutting Themes.

COMPANY

Legal Framework

The GOM has been focused on company law reform over the past three years. The predecessor government established company law reform as one of its top priorities. As a result, a new company law (the “2002 Law”) was enacted on July 1, 2002. The 2002 Law was slated to take effect on January 1, 2003. However, the SDSM-led government that took office late in 2002 decided to postpone its implementation, first to July 2003 and then to December 31, 2003. In the interim, the *Law on Trading Companies* (the “1996 Law”) which was enacted on May 30, 1996 and took effect on July 6, 1996 continued to apply.



ABA/CEELI had provided considerable input into the drafting of the 2002 Law. The ABA/CEELI draft focused on revision to two of the five types of companies covered in the 1996 Law: the limited liability company and the joint stock company.

With respect to limited liability companies, the ABA/CEELI proposals focused on clarifying and expanding the existing provisions of the law. Key changes (as modified in some instances by the final version of the 2002 Law) included:

- Introduction of a definitions section to define terms and state general principles;
- Streamlining of the registration process by eliminating judicial discretion and providing a maximum timeline of 8 days for registration;
- Provision for a separate company agreement to provide for details of its governance, management and intra-shareholder relations;
- Shifting of a number of requirements to default provisions that could be altered by member action. For smaller companies, the default provisions could be relied upon exclusively in the absence of entering into a company agreement;

- Supplementary protection of shareholders and creditor interests by defining a list of prohibited actions and defining what actions require unanimous member consent;
- Expansion of existing provisions. For example, a right of first refusal was inserted for members who wish to sell their interest in the LLC.

The more significant changes were proposed in the joint stock company section of the law. Core proposals can be summarized as follows:

- Improvement in the corporate governance regime including:
 - Expansion of the director's legal duty of care and duty of loyalty to his company;
 - Election of directors only by shareholders;
 - Regular evaluation of director performance;
 - Independent director requirements;
 - More extensive procedural requirements respecting the convening and conducting of shareholder meetings;
 - Restrictions placed on proxies to prevent manager abuse;
 - Clear distinctions between common and preferred stock including, in most instances, a requirement that preferred stock be non-voting;
 - Director authorization for issuing new shares but subject to shareholder-defined restrictions;
- Simplification and streamlining of the registration process including separation of the foundation documents into articles of association (the foundation document) and supporting by-laws, the former of which is filed at registration;
- Increased flexibility in establishing the core provisions of companies but with default provisions if owner discretion is not exercised.

The drafters of the 2002 Law set out to reduce the complexity of the company law in part by reducing the overall size of the legislation. However, the effort to reform the 1996 Law was incomplete. Other entities governed by the 1996 Law (sole proprietorships, general and limited partnerships and limited partnerships by shares) were not reviewed or revised. The general provisions of the 1996 Law were not reconciled with provisions contained in the 2002 Law leading to inconsistent provisions covering similar if not the same issues.

Moreover, the process used to ensure passage of the law was flawed. At the urging of the Minister of Economy, the draft text was assembled and passed through Parliament on an urgent basis within one month. There were no public discussions or critical reviews of the draft law. In the rush to passage, poorly translated provisions were incorporated verbatim, incorrect cross-references within the law were left uncorrected

and certain provisions were inadvertently omitted. Certain law professors, who were typically involved in the drafting of such legislation, were dismissed from the working group to ensure that the aggressive timeline could be met without opposition. While there may have been rigidity on the part of certain “old school” working group participants, the expulsion served to establish a vocal and powerful opposition to the 2002 Law’s implementation.

While the 2002 Law introduced needed changes and was a necessary step forward, there were also detrimental last minute changes incorporated prior to its passage. These included:

- Limiting the access of a single shareholder to information on other shareholders of a company;
- Allowing registration of a company by a notary thereby concealing the identity of the founders of the company.

In addition to these last minute changes, there are a number of issues that require clarification. Although not an exhaustive list, the following examples demonstrate these difficulties:

- **Procedural and Definitional Omissions** - There are numerous areas under the law where further clarification and/or procedures should be set out. For example, no principles are specified as to what constitutes an independent director. Principles for the determination of remuneration for directors are not set out. Procedures are set out for consolidation/splitting of shares, but the vote threshold and what working body of the company has the right to adopt the decision are not specified;
- **Distinguishing Between Small and Large Companies** - All companies appear to be required to have a board. A distinction should be drawn so as to permit a small company to be owner run. The law allows up to 50% of the board to be executive directors. This may have been done in contemplation of small companies where there are not clear lines drawn between ownership and management. However, it would be more effective to lower the percentage of executives on the board, apply the rule to “large companies” and exempt small family run companies from the board requirement;
- **Compliance with EU Directives** - The law prohibits labor or services already performed from being considered as a basis for the payment of shares. Article 7 of EU Company Law Directive 2 prohibits an exchange of shares for *an undertaking to perform work or supply services*. The Directive does not speak to already completed work or services. The prohibition should be tied to undertakings to perform work or services in the future in exchange for shares.
- **Voting Rights of Convertible Preferred Shares** - Convertible preferred shares are provided with voting rights. These shares should not have voting rights until the conversion right is exercised;

- **Exercise of Rights, Transferability and Receipt of Dividends for Shares not Fully Paid** – The law permits the exercise of voting rights, payment of dividends and the transfer of shares that have not been fully paid;
- **Extended liability for in-kind contributions to Charter Capital** - Shareholders who make in-kind contributions to the charter capital of the company are considered liable for 5 years after their contribution. The issue should be whether the contribution is valued properly. A requirement for independent valuation or approval by the regulatory authority is more appropriate than an extended shareholder liability period.
- **Extended Period for the Payment of Dividends** – After dividends are declared, there is no maximum period specified for payment. If a share is transferred, dividends that were declared and not paid prior to the transfer date automatically become the right of the transferee. This should be left to the discretion of the transferor.

Professor Tito Belicanec, Managing Partner of Ernst Young in Skopje and a member of the Law Faculty at Sveti Kiril i Metodij University allied with the Minister of Economy, Ilija Filipovski. With the Minister's support, a group of law professors commenced a re-write of the 1996 Law factoring in changes that had been made as a result of the adopted but not implemented 2002 Law.

Early in 2003, the USAID Corporate Governance and Company Law Project (CGCL) commenced activities. This project had been structured on the assumption that it would assist with the implementation of the 2002 Law. As it came to light that the 2002 Law may never be implemented, USAID, CGCL project members, Professor Belicanec and the Minister met to discuss mutual cooperation. The result of the meeting was the formation of a Drafting Committee in May 2003 comprised of representatives from the Ministry of Economy, Ministry of Finance, the judiciary, Securities Commission, Stock Exchange and the CGCL Project. Shortly after the commencement of committee activities, representatives of the EU Approximation of Trade Laws Project were invited to join the Committee.

A first draft of the 2003 Law was submitted to the Ministry of Economy on July 14, 2003. However, at the request of the CGCL Project, the Drafting Committee was asked to consider promoting one amendment to the 1996 Law on an urgent basis. Article 292 of the 1996 Law permitted shareholders to transfer voting and other rights attaching to their shares to designated representatives. Management of companies used Article 292 to request (some would say order) shareholders (in particular, employee-shareholders) to transfer their rights to management. These shareholder agreements generally locked in the transfer for a period of 5 years. The terms of the agreements varied between companies. The agreement could simply be a transfer of voting rights or it could contain more onerous provisions such as prohibiting the sale or encumbering of the shares for the duration of the agreement. When shareholders attempted to retract the representative designation, court decisions interpreted the agreements to be contracts

that required mutual consent to terminate. Shareholders could not regain their rights and simply had to wait for the expiration of the agreement or the consent of management.

The 2002 Law addressed the issue of shareholder agreements by inserting proxy provisions whereby a designation could be unilaterally retracted at any time. With the delay in implementing the 2002 Law, companies continued to campaign for renewal of the shareholder agreements. The Drafting Committee recommended to the Minister of Economy the adoption of an amendment that would prohibit managers and directors of joint stock companies from signing shareholder agreements with employee/shareholders and prohibit managers and directors from representing shareholders during the General Meeting of Shareholders. The amendment was accepted by the Minister of Economy on July 3, 2003. Parliament approved the amendment on 23 July, 2003.

The July 14th submission of the draft 2003 law to the Ministry did not end the activities of the Drafting Committee. While the Ministry reviewed the law, the Committee continued to meet and revise its contents. The draft law was approved for submission to Parliament in October and now awaits first reading. However, the process of revision continues. This has been an extremely open process. The Ministry of Economy committed to conducting public hearings with all stakeholders. It launched the public debate officially with an introductory meeting held on October 14 at the Holiday Inn in Skopje. No less than 25 separate public events have been planned for the October/November timeframe including meetings with judges, notaries, unions, accountants, bankers, business lawyers, national and regional chambers of commerce and press briefings for journalists. In addition, the Ministry has established a website making the draft law available and providing an opportunity to send written comments from any interested party.

The Government does not anticipate problems with the passage of the 2003 Law prior to year-end with an implementation date of January 1, 2004. Work will continue on the enactment of regulations promoting the "one-stop shop" concept, the movement of the Commercial Register to the Central Registry and amendments to other laws to ensure compliance with the 2003 Law. Central Registry regulations respecting the Commercial Register must be enacted within 30 days of the laws passage while other compliance amendments must be enacted within 60 days of the passage of the law. LLC and JSCs must comply with the 2003 Law by December 31, 2004.

Implementing Institutions

There continues to be considerable criticism of the registration process under the 1996 Law and creeping support for removal of this process from the Registration Courts.⁵ The 2003 Law supports the policies enunciated in the 2002 Law that eliminate judicial

⁵ Under the Law on Courts, three courts are granted jurisdiction for registration – Skopje, Stip and Bitola. These courts retain jurisdiction not only for registration but also to resolve a number of disputes that are specified in the Company Law.

discretion and provide an eight day maximum time for consideration of a registration application.

The CGCL Project conducted a limited survey of the registration courts in 2003 in an effort to benchmark application processing time. Since the files are not stored electronically, representative cases were selected by a manual review of the court files. Surprisingly, the average timeframe for initial registration of LLCs was 7.6 days, already below the contemplated benchmark of 8 days. It is difficult to generalize about JSC registrations since there are few new JSC registrations per year. JSC registration application processing time varied considerably within a small sample with an overall average of 27.4 days. There appears to be substantially greater delay in the processing of amendments compared with initial registrations. The 2003 Law promotes a more streamlined and efficient processing of both initial registrations and amendments since the application process will always be subject to the 8 day limit. Judicial discretion in the review of the documents will be eliminated. Instead, persons who submit an application are liable for its veracity. The Court shall be held liable for the failure accurately to transmit data to the Central Registry that has been filed with the Court.⁶

Aside from changes in the scope of judicial review during the registration process, there may also be timing improvements due to the general modernization of court functions. The European Union has agreed with the Ministry of Justice to provide further funding for the upgrading of court computer systems. The primary objective is to ensure the effective implementation of the Integrated Court Management System (ICIS). To the extent that this improves overall case management, it may also improve the efficiency of the registration process.

In accordance with Article 480 of the 1996 Law, a Commercial Register has been established at the three registration courts. In addition, the Central Registry maintains a Registry of Legal Entities based on information received from the Registration Courts. Registration Court judges continue to assert that there are a number of companies that are registered despite having long ceased activities. The Court records must be vetted and the Commercial Register revised to ensure that it accurately reflects the current status of companies in Macedonia.

The 2003 Law mandates that the Commercial Register will be maintained both electronically and manually. The electronic database will be maintained by the Central Registry based on information provided by the Registration Courts. The Ministry of Justice is required to enact a by-law within 30 days of the passage of the 2003 Law that establishes the electronic Commercial Register within the Central Registry and regulates the method of access and fees that will be charged for data retrieval.⁷ The Commercial Registry will be a public database open for queries from any person.

⁶ Article 417 of the current draft of the 2003 Law.

⁷ Article 479 of the current draft of the 2003 Law.

During the course of discussions respecting registration reform, the Central Registry lobbied to have the company registration process removed from the Courts. The Central Registry has 30 local offices. It has direct data connections with all thirty offices with frame relay and ISDN lines as backup. In the 2003/2004 timeframe, the Registry expects to establish a virtual private network to facilitate electronic filing activities. The Registry maintains connections with all major state authorities for purposes of data exchange including the courts⁸. However, the courts have only recently been provided with computers and continue to maintain key records in a manual form. While the Registry of Legal Entities is a valuable information source, the Commercial Register maintained by the Registration Courts is the authoritative basis for adjudication of company matters. By prescribing the Commercial Register as resident in the Central Registry, the database maintained by the Central Registry will have legal authority as well as practical value. However, if the Ministry is truly committed to implementing a “one stop shop” service that would allow companies to make multiple filings to various government authorities through one central portal, shifting from a court business registration to another venue for registration (such as the Central Registry) appears to be a pre-requisite.⁹

One reason the Judicial Council and the Ministry of Justice resist the removal of business registration from the Courts is that it is a source of court revenue. A new Court Budget Law recently adopted by Parliament may allay their concerns. This law establishes a Court Budget Council (CBC) that will be empowered to prepare the annual budget. The budget will be submitted to the Minister of Finance. If there is no agreement on the budget content, the MoF can override the CBC and submit its own budget to Government. However, despite this, the law establishes the basis upon which the budget must be prepared and therefore lends greater certainty to the appropriation of funds to the judiciary and courts. With greater certainty there may also be a greater willingness to move non-judicial functions away from the courts.

Registration of a company does not automatically result in registration for other government purposes. The consolidation of licensing and registration procedures depends on the concurrence of other Ministries. The Ministry of Economy estimates that at least 78 laws must be amended to accommodate the introduction of a one stop shop system. At this time, registration for tax, customs, statistical and social fund purposes remain separate from the company registration process. Consequently, additional application processes continue to delay the start-up of businesses, and increase the administrative burden and cost of doing business.

⁸ In addition to the Commercial Register, the Central Register maintains the pledge, annual accounts, immovable property, leasing, non-resident foreign investment and foreign investment in Macedonia registers.

⁹ The Ministry of Economy is reluctant to package a shift of registration from the courts with the introduction of the new Company Law because any change in the Law on Courts requires a super-Parliamentary majority for passage. Receiving 2/3 support in Parliament is difficult to achieve when the current Parliamentary majority is reliant on a coalition for its survival.

In 1998, the Foreign Investment Advisory Service (FIAS) of the World Bank conducted an initial examination of the barriers to FDI in the Republic of Macedonia. It was asked to return to commence further research in 2001, this time focusing on administrative barriers faced by investors. Following presentation of the results of this initiative, the Ministry of Economy created a Steering Committee on Removal of Administrative Barriers to Investment. This Committee consisted of both state bodies and private sector representatives. It identified a priority list of administrative issues that includes:

- Company registration
- Labour legislation (work permits and visas)
- Access to land
- Construction permits
- Customs administration¹⁰

Working groups have been established to draft concrete proposals for reform that should facilitate streamlining services offered to businesses by the GOM including the streamlining of registration processes.

For joint stock companies, shares are recorded in the Central Depository in a dematerialized form. The Central Depository compiles the shareholders' record for purposes of providing notice to shareholders and prepares voting lists for the companies' general meetings of shareholders. The Depository has been faced with challenges to the compilation of such lists by shareholders who have attempted to unilaterally retract shareholder agreements. The Depository holds that it cannot render a decision that would affect the relations between parties to a contract. It is only a passive recorder and compiler of information. Based on court decisions wherein the agreements have been defined as contracts, the Depository has refused to reverse nominee shareholder entries. The July 2003 amendment to Article 292 of the 1996 Law will enable the Depository to reverse future designations on the shareholder record. However, the amendment has no retroactive effect. Current nominee shareholder entries will be maintained as is until the expiry of the shareholder agreements unless there is consent to revoke the agreement by both parties. In general, the Central Depository has functioned well and is a valuable source of information on JSCs.

Supporting Institutions

One of the prime supporting organizations on company law matters is the Macedonian Business Lawyers Association (MBLA). It has devoted considerable time to the discussion of company law reform having made it a primary topic of both of its three day semi-annual conferences. These conferences attract business law practitioners, judges, notaries and law professors. Enrollment usually ranges from 500 to 600 attendees. The MBLA has positioned itself as the most effective voice to promote

¹⁰ *Programme for Stimulating Investment and Attracting Foreign Direct Investment, Ministry of Economy, July 30, 2003, p. 13.*

dialogue and policy development in commercial law amongst legal practitioners. In addition to the semi-annual events, the Association publishes a monthly magazine and numerous special purpose publications. It is currently developing a program for small and medium enterprises and is awaiting passage of the 2003 Company Law to embark on a dedicated program of continuing education on the Company Law for its members.

The fall conference staged in late October devoted all three days to commercial issues. Participants commented that it was the most open discussion of a pending law that they have encountered. Members of the drafting committee chaired each session and fielded questions and comments from the floor.

USAID has committed to support the implementation of a new Company Law and the development of corporate governance best practices by funding the three year Corporate Governance and Company Law Project. The CGCL Project has provided technical assistance in the development of the 2003 Law, general public education, support for commercial-oriented NGOs, benchmarking of general awareness and corporate governance practices and is introducing a corporate governance enterprise assistance program.

With the assistance of the Project, the Macedonian Stock Exchange hosted the OECD's unveiling of its White Paper on Corporate Governance in Southeastern Europe. The text of the White Paper was available in Macedonia prior to its official publication by the OECD. The Conference, staged in Skopje on June 11, served to reinforce key corporate governance principles during the initial drafting phase of the 2003 Company Law.

In May 2003, the Project established a Corporate Governance Advisory Committee. The committee consists of representatives of the MBLA, the Central Securities Depository, the Institute of Economics, the Macedonia Stock Exchange, Macedonia Securities and Exchange Commission and project staff of CGCL and the USAID Financial Services Project. A similar Advisory Committee was also established to assist with the development of the corporate governance and company law public relations campaign. The ultimate goal is to establish a permanent sub-committee under the National Entrepreneurship and Competitive Council (NECC). This permanent sub-committee will be mandated to:

- Disseminate the results of the corporate governance survey and develop recommendations for implementation of modern corporate governance principles in Macedonia;
- Conduct public sessions and seminars on corporate governance issues;
- Take a lead role in the development of a Code of Ethics;
- Develop educational materials including a new corporate governance manual;
- Provide industry oversight and validation of certification activities; and

- Provide policy advice to government including the preparation of proposals for the amendment of laws that promote business growth and corporate governance awareness.

In addition to cross-sectoral advisory committees, the MSE and the MSEC have established shareholder rights committees and spokespersons committees.

There is one active shareholder protection organization in Macedonia - Akcioner - which claims to represent 14,000 shareholders. Akcioner has operated on a shoestring budget and at the behest of its founders over the course of its existence. CGCL agreed to assist Akcioner financially, in its acquisition of office space and computers, and strategically, conducting bi-weekly strategy sessions, advising on its internal structure and providing direct assistance in the development of a campaign against shareholder agreements. Akcioner conducted a newspaper flyer campaign with a total distribution of 150,000 in late spring. This campaign alerted shareholders of the importance of resisting management/director pressure to sign agreements that forfeit shareholder rights. It is also exploring opportunities to establish court precedents for the protection of shareholder rights. Akcioner has been actively engaged in shareholder disputes and has initiated investigations into eight privatization cases, of which three investigations have been accepted by the Anticorruption Commission.

In September, the Center for International Private Enterprise (CIPE) confirmed that Akcioner had been granted \$20,000 to further assist it in its ongoing operations. Akcioner is now redefining its mandate, is about to conduct executive elections and is working toward the development of stronger relationships with the Central Depository, the Stock Exchange, the Securities and Exchange Commission and the Association of Certified Auditors. It has recently been invited to become a member of Euroshareholders. There are signs that it is broadening its representation and legitimacy as an SPO.

The Law Faculty at Cyril and Methodius University in Skopje is in the process of revising its commercial law curriculum. It has asked CGCL to assist it in the development of an executive education program, a graduate level commercial law program and undergraduate electives that embody international practice in various areas of commercial law. The first graduate program is targeted to commence in February 2004.

Commercial law reform and shareholder rights have received ongoing coverage in the national print media over the last several months. An average of 13 articles per month has been published in the national media. The primary business journal, Kapital, has covered several issues on corporate governance and company law reform. This coverage has been prompted, in part, by the efforts of CGCL through national and regional press briefings and town hall meetings. CGCL is also financing radio, television and print campaigns on general corporate governance issues.

The Market for Company Law Reform

CGCL recently conducted two surveys: a general awareness survey of the general population and an exhaustive survey of active joint stock companies. Each contained interesting information related to the commercial sector.

The general awareness survey revealed that Macedonians have a very low level of trust in large Macedonian corporations even when compared with certain government offices and agencies.¹¹ Moreover, a majority of respondents consider corruption very commonplace by both public officials and managers of large private corporations (although most respondents consider public officials' corruption as a greater hindrance to the development of Macedonia).

A subset of respondents in the general awareness survey was shareholders in Macedonian companies. These shareholders were asked to identify three of the most important rights they have as shareholders. This was an open-ended question. In other words, the shareholder was not given a list of rights to select from. The respondent had to determine the shareholder rights and self-assess the level of importance of the rights so determined. Of the shareholder group, only 29% were able to mention three rights. The following figure shows the breakdown of responses by type of right.

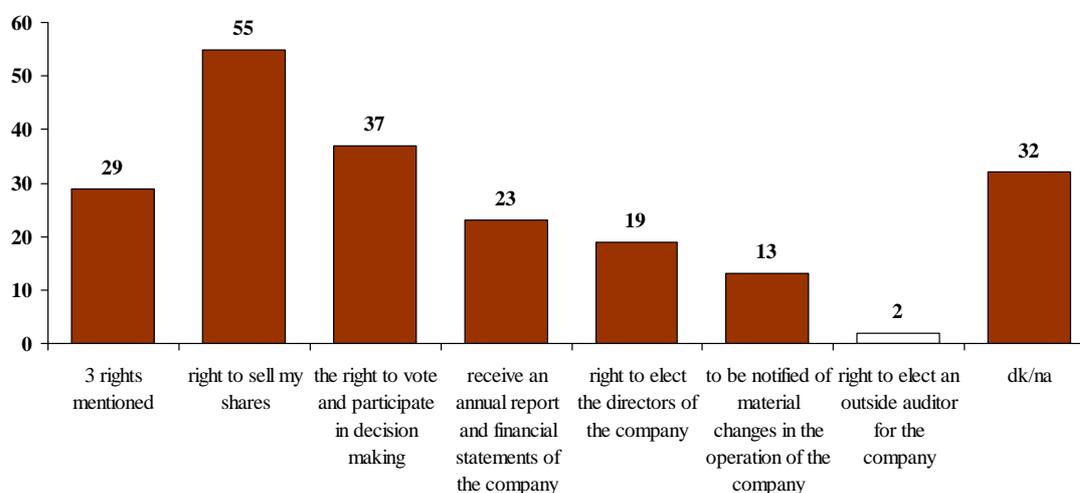


Figure 1 – Shareholders' Awareness of Rights

The low level of shareholder awareness of their rights suggests that they can be easily misled or manipulated. It shows that there is a strong demand for shareholder

¹¹ Respondents were asked to indicate their level of trust in a variety of institutions. Only 38% of respondents indicated that they trusted large Macedonian corporations. This ranked below government institutions such as the Prime Minister's Office and government agencies such as the Pension Fund and Health Funds.

education and also lends support for codification of basic shareholder rights as part of the 2003 Company Law.

The Enterprise Survey was in effect a census of current JSCs given that the survey resulted in a 92% response rate (416 companies). The survey reviewed a number of corporate practices. It was a pleasant surprise to find that many firms followed the correct procedures as dictated by the 1996 Company Law when arriving at certain types of decisions (for example, when amending the company charter, appointing new members to the Board, and changing the charter capital). This shows that the perception of companies' level of adherence to the law may be lower than the actual level of adherence.

There were, however, fewer firms that complied with the procedural requirements respecting appointment of the accountant (only approximately 20% followed the law), determining the annual remuneration of the members of the board of directors and supervisory board and deciding whether to introduce shareholder agreements.

The CGCL survey results¹² can assist in the assessment of demand for technical assistance and reform in the commercial law sector. The registration survey shows that some registration processes appear to be operating more efficiently now than may have been thought (i.e. initial registration of LLCs). The general awareness survey shows that there is desperate need for targeted shareholder education. The Enterprise survey shows that, in a number of areas, companies have complied with legal requirements and are willing to seek help to further upgrade their practices. However, issues fundamental to good corporate governance such as the proper appointment of external auditors, disclosure and proper approval of executive remuneration and, most important, establishment of fair proxy procedures to ensure that shareholders are not disenfranchised remain elusive.

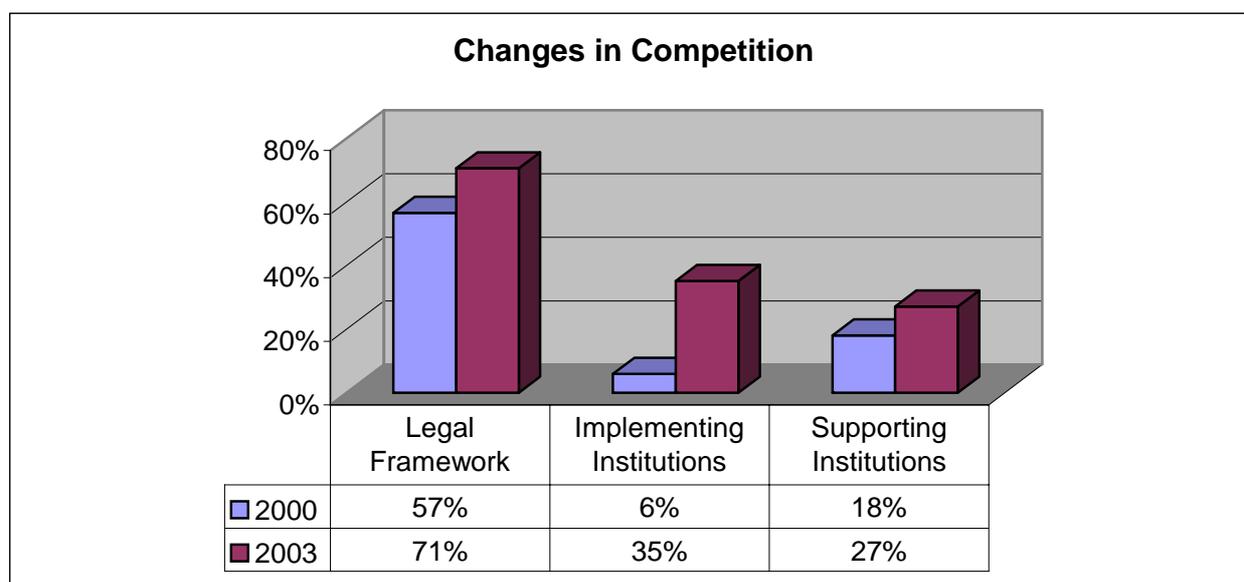
The process used to prepare the 2003 Law can be a model going forward in that it is fully engaging the private sector and allowing sufficient time for review and revision of the draft. The challenge now is to move forward with corresponding amendments that will allow for the introduction of a true one-stop shop for businesses while establishing an effective, targeted public education campaign to assist companies and shareholders understand their new rights and obligations. Both the EU and USAID continue to provide technical assistance to satisfy this demand.

¹² *The ad hoc registration, the general awareness and the enterprise surveys.*

COMPETITION

Overview

Macedonia enacted the *Law against Limiting Competition* (the "Law") on December 15, 1999 (Official Gazette 80/99) with an effective date of April 2000. The Law was amended in 2002 and is currently the subject of a complete re-write.¹³ The push for amendment and rewrite is in part motivated by Macedonia's signing of the Stabilization and Association Agreement with the EU. Macedonia is attempting to harmonize its own competition legislation with the competition legislation of EU countries.



The Law creates a Monopoly Committee and a Monopoly Authority. Since the last diagnostic, the Ministry of Trade has merged with the Ministry of Economy. The Monopoly Authority resides within the Ministry of Economy.

Legal Framework

The Law was written by Professor Galev. It is based on the 5th version of the German Competition Law but the primary source was the Croatian Law. Unfortunately, little thought was given to the particular circumstances of Macedonia. It appears to have been a copy and paste exercise. The Law is complex and contains a host of special exemptions for particular industry categories.

The last diagnostic highlighted a number of substantive flaws in the Law:

- The Law does not contain adequate provisions to address price-fixing, bid rigging, and customer allocation violations;

¹³ The Working Group charged with drafting the new law is comprised of Authority personnel, Professor Goran Koevski (Law Faculty) and Judge N. Lazarov (Stip Registration Court).

- The law provides exemptions from general prohibitions of cartel-like behavior with respect to discounts;
- The law provides no guidance regarding how product or geographic markets are to be determined; and
- The Law requires the Monopoly Authority to seek permission from a judge to apply sanctions.

Serious concerns were also raised respecting the Monopoly Authority's ability to act independent of the Ministry. In particular:

- The Minister is vested with authority to appoint and remove the Director of the Monopoly Authority. This could have a severe dampening effect on the Authority's ability to challenge Ministry policy when such policies undermine the Law.
- Any decision of the Authority is subject to appeal at second instance to the Minister. Consequently, all decisions potentially fall into the political domain.
- The Law provides for decisions to be made unanimously by the three members of the Department for Enactment of Decisions (although in practice all decisions have been approved by the Director).
- Employees of the Authority are State Officials and, as such, are subject to the Law on Administrative Procedure. The salary structure is the same as that of other state officials. The low salary base makes it difficult to attract and maintain quality staff and may promote corrupt practices.
- The eligibility requirements for appointment to the Monopoly Committee appear to have been shaped to ensure participation of academics to the exclusion of other qualified candidates (in particular, to the exclusion of representatives from the business community).

The transparency of a regulatory authority is a key determinant affecting its accountability and credibility in the market place. The Law required the Authority to prepare and publish a bi-annual report intended to overview its activities. In 2002, amendments to the Law removed the requirement to publish the Report and, inadvertently, removed the explicit requirement to publish decisions of the Authority.

Specific types of decisions (i.e. abuse of dominant position and merger) have been published in the Official Gazette. However, only final decisions are published. A final decision is one that survives the 30-day period after its initial rendering by the Authority without having been appealed to the Minister or, if appealed to the Minister, when the Minister renders his decision. There appears to be a serious flaw in the disclosure system. Withholding publication until a final decision is rendered may mean that stakeholders affected by the Authority's decision will not have the opportunity to consider its impact until the second instance appeal has already been exhausted.¹⁴

¹⁴ Named parties would receive notification of the interim decision. However, the nature of competition proceedings may mean that the decision can have broader implications. Stakeholders that are not named will have no access to the decisions until the decisions are final.

The 2002 amendment has muddied the waters further. Despite the inadvertent deletion of the authorization to publish decisions, the Authority ordered the publication of a decision. The decision to publish was challenged. The Court prohibited publication on the basis that the Law provided no authority to publish.¹⁵

With respect to access to decisions, the Authority's policy is regulated by the Law on Administrative procedures. All parties to a case may review the decision.¹⁶ It has been the practice of the Authority to provide the decisions to journalists. However, access is at the discretion of the Authority.

In the fall of 2000, GTZ commenced long-term support for the revision of the Law, provision of technical support to the Authority and support for a public education campaign. A Working Group was formed to redraft the Law. The Working Group used the Slovenian, Croatian, Albanian and Hungarian competition laws as precedents. At this time, the draft law is in its final stages of revision. Through the drafting process, the Working Group has sent the draft law for review and comment by the European Commission and several country competition authorities. The draft is 18 pages in length compared with its 56-page predecessor. The primary objective of the Working Group is to create a law that is understandable, less complex, compliant with EU standards and relevant to Macedonian reality.

If the draft law is adopted in a form close to its current content (as is expected), there will be a number of significant improvements. These include:

- **Clarity in concepts** – The draft law contains a detailed definitions section that clearly defines the various concepts that will be applied by the Commission and the Authority. As was done in the current Law, it also sets out the economic criteria that are to be used to determine the status of certain entities with respect to the determination of dominant position.
- **Advances in Independence** – The appointment process will be moved from the executive branch to Parliament. Both the Monopoly Committee and the Authority will be established by and will report to Parliament. Committee members will be nominated by the executive branch but appointed by Parliament for four year terms. Candidates must have business or scientific backgrounds suitable for the exercise of Committee's functions.
- **Improvements in Decision-Making** – To this point, the Director of the Authority has made all decisions (although the Law stipulates that this is the domain of the Department for Enactment of Decisions). The current proposal is to vest three members of the Authority with decision-making powers. However, unanimity amongst the authorized decision-makers will no longer be required. Cases will be

¹⁵ Article 63 of the Law listed the decisions subject to publication in the Official Gazette. The 2002 amendment was interpreted as removing this obligation.

¹⁶ Article 69 of the Law includes the Complainant, the Government and interested third parties, associations or organizations as eligible parties to a proceeding.

assigned on an individual basis. However, cases will not be randomly assigned. The assignments will be made by the Director.

- **Increased Staffing** – The draft law increases the minimum staff of the Authority to nine persons plus the Director.
- **Removal of Industry-Specific Exemptions** – All industry-specific exemptions have been deleted from the draft law. Instead, provision is made for block exemptions in line with European Union practice. The multiple definitions of cartel types have also been deleted. The public sector and entities owned in whole or in part by the government are not accorded any special treatment.
- **Improved Financing Procedures** – The operations of the Authority have been financed from the general revenue allocated to the Ministry of Economy. The draft law establishes the Authority as an “independent agency” created by and reporting to Parliament. While one can question its characterization as independent, the effect of this change in status is that a separate line item will be established in the Government’s annual budget for the funding requirements of the Authority.
- **Re-insertion of Publication Requirements** - In the draft law, there are different publication requirements depending on the type of case.
 - Abuse of dominant position decisions must be published when the decision becomes final. This continues to mean 30 days after the rendering of the decision provided the decision has not been appealed.
 - The publication of merger decisions also includes a summary of the measures that have been taken to resolve the issue in addition to the decision.
 - A prohibited contract decision contains only the decision.

The general rule is that, when a decision is published, only information on the parties and a short explanation of the case is available. All confidential information is removed.

- **Annual Disclosure** - The Authority must prepare and submit to Parliament an annual report on its activities.
- **Sanctions** - The draft law distinguishes between severe and minor violations of the law. For severe violations, fines can be levied up to 10% of the previous year’s total income. Personal fines may be imposed in amounts ranging from 3,000 to 20,000 Euro. In addition to monetary sanctions, the company and individual can be prohibited from engaging in certain conduct for a specified period. For less severe violations, fines can be levied of up to 1% of the previous year’s total revenue.

While the draft law shows progress, there are still impediments to the effective functioning of the Authority. Three continuing exposures are:

1. Due to constitutional constraints, the Authority is not empowered to apply sanctions to offending companies. This remains the exclusive domain of the court. The Authority can issue orders but, if such orders are not complied with, it has no power to apply fines or other penalties.
2. Staff of the Authority remain state employees and, as such, cannot be paid a competitive salary relative to the nature of work that must be performed.

3. The rules embodied in the Law on Administrative Procedures respecting access to decisions have been incorporated into the draft law. However, there is no unfettered right to review the decisions. The Authority approves access on a case-by-case basis. There is no publicly accessible database of decisions.

Implementing Institutions

The Law against Limiting Competition provides for two related bodies:

1. A Monopoly Committee (quasi-judicial and independent of the government in nature), pursuant to Article 30; and
2. A Monopoly Authority, an “independent organ” established pursuant to Articles 50-52 of the Law. The Monopoly Authority consists of two departments:
 - The Department for Enactment of Decisions; and
 - Department of Analysis & Research.

It is also empowered to establish a register where notifications must be filed and recorded.

The work of the Monopoly Authority is managed by a Director. The Director is appointed and dismissed by the Government of the Republic of Macedonia, on the proposal of the Minister of Economy.

The decisions of the Monopoly authority are made by the Department for Enactment of Decisions. The Department consists of three members. Under the current Law, all decisions must be unanimous. The members of the decision-making department are appointed and dismissed by the Government with a four-year mandate and with the possibility of re-election. At a minimum, an appointee must meet the qualifications necessary for appointment as an appellate level judge. The Director is not a voting member of the Department for Enactment of Decisions.

The Department of Analysis & Research monitors and analyzes market conditions. It is the investigative branch that provides the information upon which the Department for Enactment of Decisions will act. The Analysis and Research Department summarizes aggregate information about the state of competition and market conditions. It also analyses specific sectors, products, etc. To obtain financial and other relevant information from companies, the Department must first obtain court approval.

Progress since 2000. The Authority has been operational since April of 2000. In 2000, GTZ committed to providing long term assistance to the Authority. This was first evidenced by implementing training initiatives. Mr. Hubert Sauter, a German consultant with 15 years of European Commission competition experience, made monthly visits to assist the Authority’s staff upgrade their skills. Actual EU cases were used to train the Authority’s staff in the basic concepts underlying competition law.

The Authority also focused on public education. Four to five public hearings were staged per annum. The objective was to describe basic issues and raise the general level of awareness. In addition to public hearings, targeted workshops and seminars were held for various stakeholders including judges, lawyers and enterprises. With respect to businesses, a primary objective was to raise awareness of the notice requirements under the Law. Many businesses were not (and many still are not) aware of their notice obligations.

The Authority has also cultivated relationships with other monopoly authorities. The United States Federal Trade Commission sponsored an international conference on anti-trust law. Their sponsorship included financing the travel and attendance costs of personnel from other monopoly authorities. The Authority has been in regular contact with EU country competition regulators.

The Authority established its own website (www.mon.upr.gov.mk) in 2001. Unfortunately, likely due to understaffing and a lack of technical support, it has not been kept current as the Authority has moved ahead with its activities.

The Law required the Authority to publish a bi-annual report on its activities. Amendments to the Law passed in 2002 eliminated the requirement to prepare the Report. As a result no Report has been prepared on the Authority's activities since its inception.

Despite low pay and understaffing, the Authority has dealt with a number of cases. Forty-three requests for consideration have been submitted to the Authority and an additional nine inquiries were initiated by the Authority. A number of requests have been denied without a full deliberation usually because the request has been viewed as groundless or the Authority has ruled that it is outside its jurisdiction. During our interview with Authority representatives, they indicated that 19 cases had been fully deliberated.¹⁷ Most cases fall under three general categories: abuse of a dominant position, merger and refusal to deal. The specific categories and frequencies of decisions are as follows:

- Mergers – 7 cases approved, one pending;
- Abuse of Position – 9
- Refusal to Deal – 2
- Vertical Restriction – 1

Of the decisions rendered, there have been nine appeal processes (three at the Supreme Court; five where the Minister denied the appeal; and one where the Minister overruled the Authority and sent the case back to the Authority for a second review).¹⁸

¹⁷ We were subsequently provided with a summary of Authority activities. This summary indicated that requests for consideration were made under the following categories and frequencies: refusal to trade – 2; abuse of dominant position – 26; merger – 6; Vertical Restriction – 2; Other – 16. Note that these are requests as opposed to decisions.

¹⁸ The appeal processes are not mutually exclusive. From the information supplied by the Authority, 8 cases were subject to appeal. One case elicited decisions from the Minister and the Supreme Court; two involved only court deliberation and the remaining five were appeals to the Minister.

From time to time the Authority's actions have attracted significant press attention. When asked to highlight their most significant decisions, staff at the Authority pointed to their decisions against MakTelekom and the public enterprise water supplier. The former case led to an order instructing MakTelekom to permit access to its equipment by another mobile phone supplier. The latter case led to an order to provide water consumers choice in the purchase of water gauges. The water utility had insisted that consumers purchase only gauges supplied by the utility.

Most recently, the Authority ordered a delay in the merger of three local newspapers with German publishing house VAC. In addition, it initiated a misdemeanor procedure against the three local companies involved in the pending merger (LLC Ogledalo, LLC Most, Branko i drugi and LLC Krug) asserting violation of Article 49 of the Law.¹⁹ The misdemeanor proceeding is in respect of the companies' failure to notify the Authority of a past merger involving Ost Holding Company of Vienna.

One of the main obstacles facing the Authority is that the executive power cannot impose sanctions. The Authority will issue an order to stop a particular practice and set a deadline. If the Authority discovers lack of compliance, it will initiate a procedure in court and request the imposition of sanctions as noted in the above example. However, in the opinion of the Authority's employees, the sanctions applied by the court have been significantly lower than the profit earned from the abuse of the dominant position. The Authority would like to see more substantial sanctions applied. The draft law specifies higher amounts of fines and potential prohibitions on activities. But, in the draft law, the Authority must still apply to court to have the sanctions applied.

There are matters still under discussion with respect to the Draft Law. One proposal under consideration is that Parliament establishes two Committees: one to render initial decisions and, if appealed, another Committee to consider the appeal. The executive branch cannot override a Parliamentary decision. If the appeal committee is established by Parliament, the Minister would be precluded from overriding the decision. The appeal committee's decision would be subject to appeal in court only. Another suggestion would be to convene the appeal committee on an *ad hoc* basis using part time committee members. Because the *ad hoc* committee would be a creature of Parliament, it would also preclude Ministerial interference.

In general, the Authority asserts that most of its orders have been complied with. They believe that the new law will represent a significant step forward except with regard to their ability to apply sanctions.

Supporting Institutions

Under the Law, the Monopoly Authority is a part of the Ministry of Economy. The Minister essentially has a veto on Authority activities by virtue of his adjudicative role at second

¹⁹ Article 49 specifies sanctions for failure to comply with a number of provisions in the Law. In this example, the assertion is that the notice of merger required under Article 26 was not provided and should give rise to the imposition of sanctions.

instance. However, there have been encouraging signs of support for the Authority from the Ministry. This is best exemplified by the Minister's support for the Authority's decision in one of the many MakTelekom proceedings.

Another mobile phone supplier wanted access to MakTel equipment. The Authority ordered that access be provided. MakTel appealed the order to the Minister. The Minister upheld the order of the Authority. MakTel complied but concurrent with compliance, launched an appeal to the Supreme Court. The Court overturned the Authority and Minister's ruling.

Staff from the Authority did not comment on the merits of the Court's decision. However, they voiced confidence that the Authority and Ministerial actions were appropriate and within the Law.

The Supreme Court decision may be evidence of the need for more protracted continuing legal education. With the assistance of GTZ, seminars have been held with the MBLA, MBA, chambers of commerce and the Judges' Association. But further coordinated efforts may be needed including instituting a case management program that ensures that competition cases will be placed before judges who are well-trained in the competition field.

The Law Faculty is in the midst of upgrading its graduate and undergraduate curriculum. It has asked CGCL for assistance in the development of graduate, undergraduate and executive training programs. The focus of CGCL assistance will be on company law and corporate governance matters. However, this also provides an opportunity to introduce competition law into the law school curriculum. New and revised courses are intended to be introduced during the 2004 calendar year.

The Market for Reform in Competition Law

The previous diagnostic emphasized that the Government had ignored the EU/Phare Legal Approximation Project's work on a draft competition law when it prepared the Law for submission to Parliament. The rejection of the higher quality European draft was cited as evidence of low demand within the Government for high quality and European compliant legislation.

The Monopoly Authority, with the support of the Ministry of Economy, has played a lead role in working on a new law that better fits the Macedonian market while at the same time complies with European standards. The draft has been accomplished with the full support of the Authority, input from Judge Lazarov and Professor Koevsky as members of the Drafting Committee, and ongoing assistance from GTZ. The expectation is that a new law will be enacted this year.

Although the application of competition law is still a new experience in Macedonia, there are encouraging signs of a growing private sector awareness of the Law and the Authority. In total, 52 requests were dealt with by the Authority over its short lifespan. Only 17 percent of these proceedings were initiated by the Authority. The vast majority of cases have been started at the request of one or more private sector participants.

While there are signs of a growing awareness, there is also evidence of non-compliance and lack of understanding of obligations. The above-mentioned (and still ongoing) review of the merger of three local newspapers is instructive in this regard. When reviewing the merger, the Monopoly Authority became aware of prior mergers involving the local companies and a Viennese holding company. The companies had failed to provide prior notice of the mergers to the Monopoly Authority. The Authority filed an application with Skopje Court 1 to apply sanctions and discussed their action with the press. However, directors of the affected companies claimed that they were unaware that the procedure had been initiated and therefore could not comment to journalists on the process. This may be an anomaly or indicative of a larger communication problem between the Authority and parties to competition law proceedings.

While GTZ has assisted the Authority in the conduct of seminars over the past two years, the introduction of a new law will require further ongoing technical and public education support. GTZ continues to provide assistance. In addition, the European Union is providing support through the auspices of the Approximation of Trade Laws Project. This project will dedicate resources to the public education campaign currently being designed to coincide with the introduction of the new law.

The effectiveness of competition regulation will continue to hinge on the ability of the Authority to effectively communicate and enforce its decisions and maintain an arm's length relationship with government. To this end, the first round of reforms has not fully responded to the challenge. The primary legal constraints to effectiveness remain the Authority's inability to directly apply sanctions and its dependence on government agreement for the upholding of its decisions.

The ability to apply sanctions is not a problem unique to the Authority. Other regulatory authorities, for example, the Tax Authority, face a similar dilemma. Resort to the courts is not always optimal. The international community continues to push for substantial judicial reform.²⁰ Part of the focus of these reforms is to upgrade judicial training, promote more effective case management and redirect disputes to alternative dispute resolution. Certain of the contemplated changes will require super-majority approval in Parliament. There may be a window of opportunity to promote the concept of administrative tribunals with sanctioning power as part of a package of judicial reform amendments. The GOM is reluctant to introduce amendments into a substantive law that require a super-majority for passage. It could jeopardize the passage of the subject law. Consequently, further

²⁰ The U.S. has earmarked about \$15 million and the European Agency for Reconstruction about €7 million for judicial reform. OSCE also has a program to help prosecutors build more effective cases.

improvements to the competition law regulatory framework may depend on effective coordination with the Ministry of Justice during its ongoing consideration of judicial reform.

The other glaring deficiency in current Authority practice is in the communication field. As part of the interview process, we asked the Authority for a synopsis of decisions rendered to date. This had to be manually compiled by members of the Authority. There is no generally accessible database that would allow for broad dissemination of decisions, rules and procedures. As mentioned earlier, a website has been established but it offers little more than a general description of the Authority and summaries of events held two years ago.

The CLIR diagnostic also references natural monopolies as a separate assessment area within the competition framework. The proposed law contains no specific exceptions for natural monopolies. In conducting this assessment, we have focused on the Law and draft law, not on natural monopoly special cases.

There is a drive to privatize current "natural monopolies". As part of its election platform, the SDSM-led government proposed the restructuring of the power utility (ESM). The government has set 2005 as a target for privatizing portions of ESM. The current timetable is to commence restructuring of the energy sector in 2004. Power transmission and distribution activities are to be separated from energy production. The GOM wishes to promote the entrance of foreign investors into the energy production sector through the establishment of new production facilities and possible spin-offs of existing units. The GOM intends to retain government control over transmission and distribution. ESM's management board will decide on the exact terms of the separation.

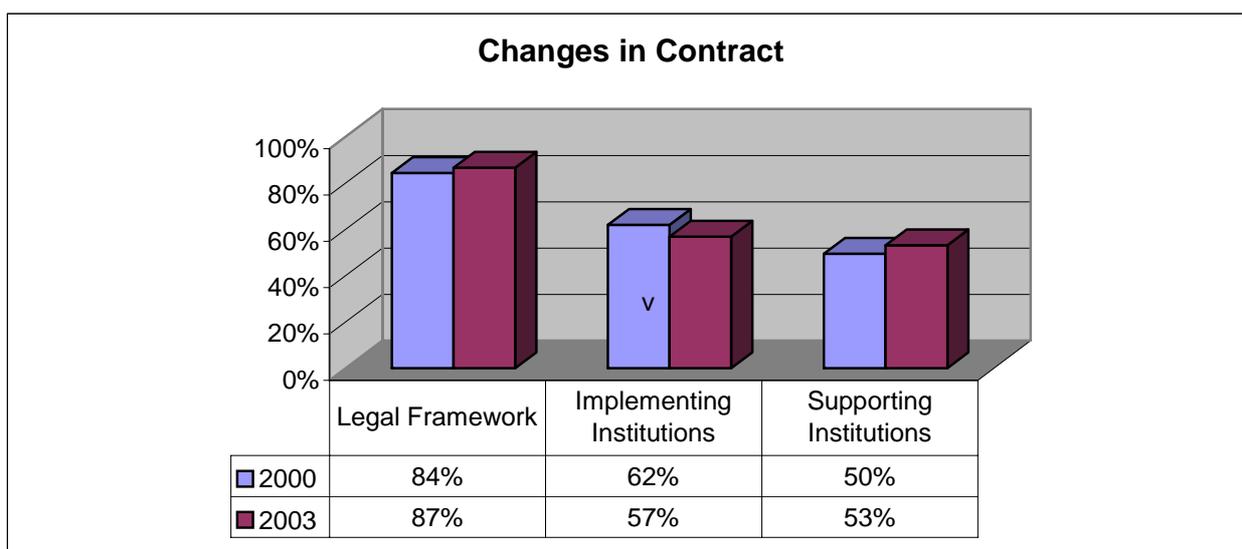
In summary, the current wave of reforms is one step in a multi-step process. The push for further reform likely will be driven by members of the Authority. While there is a creeping awareness of competition matters in the private sector, the most critical flaws impede the actions of the Authority against offenders. As a result, it is the Authority that is most motivated to pursue further change.

CONTRACT

Overview

Macedonian Contract Law was in its fourth year of a revision process at the time of the last assessment. The original Yugoslav 1978 *Law on Obligations* (YLO), amended several times in the 1980s, was generally considered an adequate, efficient contract law, although somewhat overprotective of debtors. In 1996, academic drafters began updating the law again, a process that took five years. The changes were generally positive, but the process of reform showed weaknesses in the democratic methods employed: practitioners and other stakeholders from the legal community felt left out of the process, while the time required suggested a lack of an efficient amendment process.

Although the law was improved somewhat, as shown in the scores, the greatest weakness for the Contract Law regime remains the Implementing Institutions. The



courts have not made significant improvements in the past three years. There is reason to hope for change, however, based on new projects for courts and alternative dispute resolution that are addressing underlying problems. These interventions include a new law on courts that will change the underlying framework for dispute resolution by shifting the burden of production to the parties instead of the judge. This is expected to have far reaching consequences in leaving behind the moribund inquisitorial system of the former Yugoslavia, which has not served commerce well in any of the now independent republics.

One upside of the poor progress in courts has been the increased demand for alternative dispute resolution. There is substantial interest in arbitration and mediation, and some hope that the draft *Law on Arbitration*, which has been in draft for seven years, will soon find its way to the parliament.

Framework Law

The new Macedonian *Law on Obligations* (MLO) was adopted in February 20, 2001. It was published in the Official Gazette of Republic of Macedonia, 18/2001, and became effective as of March 13, 2001. The MLO contains 1141 articles, expanding and replacing the former Yugoslavian Law on Obligations (YLO) by 32 articles.

The drafters of the MLO felt that the YLO was generally compatible with and suitable for the new market conditions and circumstances as well as the new market economy established in the country. Therefore the reform of the law primarily focused on the adjustments of terminology, with some additional upgrading of some provisions to keep pace with developments in the market economy. As a result, the structure of the old law has been retained, but with modifications and a few new solutions.

The declared purpose of the changes in the YLO was: (i) removing the inappropriate terminology and concepts from the former legal and political system; (ii) adapting the new Law to the new economy and market circumstances; (iii) providing more specific and detailed regulation; (iv) incorporating some provisions from other laws in the Law on Obligations for purposes of codification.

The MLO includes five new types of contracts, which have been imported from other laws. Those are the following: Contract for Gift (Donation), Loan for Use Contract,²¹ Partnership Contract, Contract for Distribution of Property during Life, and Contract for a Lifetime Support. The contracts for Distribution of Property during Life and Lifetime Support were originally included in the Inheritance Law, but with the latest changes the legislator decided that because those are contracts, regardless of the substance they are regulating, they should be included in the statute that regulates the contracts.

The main amendment of the YLO was that the principles this law was based upon have been repealed and replaced. The old law was based on socialist principles of property ownership, such as presumptions of state or "social" ownership.²² They have been replaced with the principles of personal ownership and private property.

Some of the most significant changes that were introduced with the MLO were in the area of monetary affairs and interest rates calculations. These include the recognition of currency and indexation clauses to protect against inflation and exchange rate

²¹ The Loan for Use contract covers a situation in which an owner allows the use of property by another party for a certain period of time. Unlike a lease contract, there is no compensation.

²² Social ownership provided for an intangible interest in property by "the people" without effectively defining or translating this interest into practical concepts. As used, the concept permitted extensive state interference in the economy, including individual enterprises, to defend the interests of "the people".

fluctuations. The new law permits the parties to express obligations in foreign currency as well as domestic. If an obligation is expressed in foreign currency, the amount owing in domestic currency will be calculated based on the National Bank's average foreign exchange rate calculated as of the date the obligation has been fulfilled.²³

Indexation was prohibited under the YLO. Article 385 of the MLO permits indexation by allowing the parties to use contractual language linking the amount owed in local currency to a price index, so that creditors can protect themselves against inflation. The indexation must be based upon a price index set by an authorized entity; that is, a governmental authority tasked with indexing prices. The *Law on the National Bank* and the *Law on Banks* prescribe the National Bank and the Bureau of Statistics as competent authorities to establish price indices.

The MLO also reverses debtor protections of the old law with regard to contractual rates of interest. The YLO used to provide "protections" for individuals by distinguishing between rates charged to and by individuals versus rates between entities. Rates for individuals were prescribed by law. Rates for entities were supposed to be regulated, but the regulations were never enacted, leaving a gap in the practice that had to be resolved through a Supreme Court ruling. In either case, rates higher than the prescribed maximums would result in an annulment of the contract, no matter what the market rates might be. The new MLO has eliminated these restrictions and now permits freedom of contract in setting interest rates.

The MLO addresses some other problems related to interest. The purpose of the amendments is to protect debtors and provide certainty when interest rates or terms of payment are not specified in the contract, but the effect will also be positive for creditors by ensuring that they introduce more disciplined contracting behavior by setting the terms more clearly at the outset. The MLO now provides that if an interest rate is not stated in the contract, the rate shall be the discount rate of the National Bank of Macedonia at the time the contract was concluded. If the obligation is in foreign currency, the creditor will receive the lowest rate paid on foreign currency deposits in the place the debt is due, unless otherwise agreed or determined by law. In other words, creditors have strong incentives for specifying the interest rate in the contract to avoid having these rather low rates applied. In addition, if the contract does not specify when interest must be paid, it becomes due at the maturity of the underlying debt, and not before.

Another significant change from the YLO involves default and penalties. The old law did not permit default interest or interest on interest, except in limited cases by financial institutions. The MLO has abandoned these restrictions in favor of permitting parties to set default interest provisions. If they fail to do so, the Law stipulates that the interest rates will be increased if the debtor fails to pay in a timely manner. (Actual regulation

²³ Article 384, Law on Obligations

of default rates is governed by the *Law on the Amount of Default Interest Rates*.) Although most caps on rates are now gone, the MLO does prohibit any interest in a Credit Contract in excess of twice the international financial market rate²⁴ on the currency in question on the date when the monetary obligation becomes due.

Banks are currently providing credit under this new law, with several banks (particularly ProCredit Bank) expanding their loan portfolios significantly, including foreign currency loans backed by their own foreign credit lines. This would suggest that the remaining interest rate cap is not unduly restricting loan activity. However, bankers often use higher interest rates as protection for risky loans – if this rate restriction is too low, they will have to cover the gap with higher fees and collateral requirements.

Implementing Institutions

The Courts. Courts are an Implementing Institution in all areas of law, and the primary Implementing Institution for Contract and Bankruptcy. They have a tremendous impact on the trade and investment environment. Unfortunately, that impact continues to be quite negative.

Scores for courts through all seven areas of this assessment have either stayed even or fallen. In the more extensive review in the Contracts section, scores have actually gone backwards, from a previous score of 62% to a current score of 57%. From a practitioner's point of view, court performance has worsened in the past three years. This may be due to an actual change in performance, but it is also likely an expression of frustration; as conditions have failed to improve, negative impressions have become stronger.

On a somewhat positive side, several practitioners noted that corruption is greater as a perception than a practice. This is quite common in countries in which judges are not consistently required to write defensible, transparent legal opinions justifying their decisions. Unable to critique the reasons for a decision, the losing party will often assume that the judge based the verdict on bribes or favoritism instead of law. Judges who issue opinions are less likely to be accused of corruption, because they can be held accountable for their legal reasoning.

In short, the legal profession and business community are quite dissatisfied with the ability of the courts to resolve commercial disputes in a timely manner with predictable outcomes. There are exceptions to this overriding negative opinion for certain judges who are known for their more professional management and decision-making skills, but not many. On the other side, judges are quite dissatisfied with the performance of lawyers, who are known for their ability to delay proceedings through a wide range of

²⁴ Either the London Interbank Offered Rate (LIBOR) or the European Interbank Offered Rate (EURIBOR).

postponement techniques. Feelings were mixed on whether the judges have a sufficient base of legal knowledge to decide cases, but both judges and lawyers would like to see more education for the judges, especially on new laws. There was also very strong, unanimous support for a proposal to establish separate commercial courts.

While the present performance of courts is poor, the future looks more promising. There are now several court projects underway to improve administration of justice and education of judges. More importantly, recent changes in law can be expected to have a tremendous impact. First, a new *Law on Court Budgets* has been introduced. The law creates a Court Budget Council (CBC). This Council is mandated to establish an annual court budget based on "fiscal policy" and budgets requisitioned from lower courts. The law specifies the items to be included in the budget, including a specific line item for judicial education. The budget is submitted to the Minister of Finance. If the Minister of Finance disagrees with the proposed budget, the Minister has the discretion to submit his own proposal to the Government. Consequently, there is no guarantee that the CBC budget will be adopted. However, the formalization of the budget preparation within the CBC bodes well for better financial management of the courts and will make it more difficult for a reasonable budget proposal to be rejected by the Ministry and GOM. Second, the very nature of the system is being changed from an historically weak inquisitorial model to a stronger adversarial model.²⁵ This second set of changes will shift the burden of evidence and argument to the parties instead of leaving the judge responsible for an endless search for truth that has crippled the capacity of the courts in all of the former Yugoslavia.

Clearly, improved education is needed (and is further addressed below), but the principal complaints from the legal and business communities relate to management. Management systems and skills are badly needed by court administrators as well as judges in order to run the courts in a more professional manner. This is exactly the focus of USAID's Court Modernization Project, which can be expected to have net positive impact as new systems are rolled out through pilot courts to cover the country.

Public education is also needed to correct historical approaches and orientations. The complaints about delays in legal proceedings reflect a change in expectations and role of the judiciary. The system of delays currently in practice developed through an understandable historical process along two unrelated roads that built on each other. First, as noted previously, Macedonians have tended to see government as "someone else's government." Consequently, they have developed various protective devices to limit or avoid the power of the state. This included various delay and obfuscation tactics within the courts, where both judges and lawyers for citizens would try to undercut the state's ability to enforce unpopular policies or decisions. Second, the Government had been the largest single delinquent debtor in the country (and in every

²⁵ This should not be interpreted as adoption of American-style courts, but rather a correction in the weaknesses of a European model that has been modified in Northern Europe but not in the former Yugoslavia. The system will still be essentially European in character.

other former Yugoslav republic), and has encouraged delays to keep from having to pay debts. Together, the legal community has created an impressive array of delaying devices that today are retarding economic growth.

Reconstructing the system to promote economic development will require a change of law (particularly the *Code of Civil Procedure*), an increase in the management ability of judges to enforce deadlines, and a reform of the current legal practices. All of these will require public education, particularly with regard to the negative economic impact of the current system, in order to change expectations (thus raising accountability) and provide a basis for building new practices.

These changes will also require participation by the wider legal community. Unfortunately, the Ministry of Justice has a reputation for continuing with the classical model of legal reform, in which a small group of drafters does the work with little or no stakeholder input, then expects everyone to obey when the law is passed. Judges and lawyers have expressed strong dissatisfaction with their ability to comment upon and assist in drafting. With respect to changes in the *Code of Civil Procedure*, judges and lawyers are the only stakeholder with any practical knowledge of what currently does and does not work. Although scholarly, theoretical guidance is needed in structuring the overall law, practical input is essential in ensuring both ownership and implementation. Due to the importance of these changes for the economic development of Macedonia, the Ministry of Justice should be strongly encouraged to use the law-making model of the CG & CL project.

Judicial education is another area in which reform and investment are needed. As noted, the law now provides for specific budget resources to fund such ongoing education. Moreover, the Government has established a judicial training institute. This will be a substantial improvement over the current practice of providing professorial lectures on new laws at the annual judges' meetings. According to judges, the greatest need is for practical education in new laws, with practical materials that include forms, checklists, and explanations of the situations they commonly face. Judges noted specifically that they would like to have practical training on joint stock companies and other changing legal concepts. They further noted that they prefer not to have professorial lectures, which were critiqued as providing no practical information. The demand for a new style of training and education is very strong.

Finally, it should be noted that enforcement of judgments is also quite weak and may not be adequately addressed by court administration work, which historically has tended to focus on the process of producing judgments, but not the subsequent process of enforcing them. This will require assistance to the bailiff system, as well as reform of the auction and sales systems. Some progress may have been made under the new execution law, which shifted responsibility for simple collections to the notaries, but it is not yet clear whether this will work. In addition, enforcement should not be approached as a judicial problem; the courts are a fundamental component, but the

problem is systemic and involves the private sector as well. Further information is attached in Annex A, *Enforcement of Commercial Obligations: Systemic Solutions beyond Courts*.

To summarize, there has been little positive change in the courts in the past three years, and at least a strong perception of negative change. Many of the problems are being addressed now through programmatic support, so that it should be possible to measure positive change in two or three years. Because of the complexity of the problems involved, however, expectations should be tempered – court reform has proven to be a slow, difficult process throughout the region. Without full engagement of the government, judiciary, bar and business community, changes tend to be even slower.

Alternative Dispute Resolution. There is currently very little use of ADR in Macedonia. The Chamber of Economy offers arbitration through its Arbitral Court, and the Macedonian Business Lawyers Association offers mediation, but neither is used very often. These appear to have been supply-side responses to the need for some way around the existing court system, but they have not yet connected with demand. Partly this is due to lack of public education on the issues, but it also seems to be underutilized because the suppliers have not effectively targeted those likely to use these services. Moreover, arbitration cannot be effectively enforced and is currently available only in cases involving foreigners. As noted below, demand is beginning to coalesce.

There is not currently a law on arbitration. Instead, the law has been in various stages of drafting for over seven years. Completing the law, especially with input from the stakeholders most likely to use the law, would do a great deal to advance use of these dispute resolution tools.

Supporting Institutions

Governmental Entities. As already noted, the Ministry of Justice (which can also be characterized as an Implementing Institution) has a supporting role to play in seeing that laws are changed effectively and appropriately. Currently, however, this is a point of complaint by legal reform professionals. They note that very little public discussion or stakeholder input goes into the process of changing laws under this ministry's jurisdiction. According to one drafter, practitioner input is adequately covered by ensuring that one or two practitioners are in each Working Group, but this formalistic approach is not satisfying the legal community. Greater use of public hearings and organized stakeholder input is needed if the goal is implementation of new laws.

Macedonia has a Judges' Association, but currently it is still considered to be rather weak in providing significant input to the change process. One judge who sits only a few doors from the office of the association was not aware of any of their programs or of any involvement in the various reforms underway. This suggests that the association

could stand to focus on their own outreach and public education skills, because they apparently are not reaching their constituents effectively enough.

The Macedonian Chamber of Economy has an Arbitral Court, but it is decidedly underutilized by the business community, having processed no more than a few dozen arbitrations in the last five years. The ineffectiveness of this institution is in part due to lack of enforcement: arbitral awards are no more likely to be enforced than judgments, so there is not much use in pursuing arbitration if one party is likely not to comply with the award. Arbitration is also poorly understood in the business community, where arbitration between domestic parties has not been permitted. Foreign investors normally include arbitration clauses in their contracts, but opt for foreign venues and foreign enforcement.

Notaries have an important role in ensuring the quality of the documents subject to enforcement. Moreover, the new execution law has established them as actual implementers of the enforcement process. The Notaries Association is responding to this new role by providing some training and development of forms. Overall, however, the notaries themselves are responsible for understanding and applying the law properly. Their role as enforcers is controversial. Notaries now have the mandate to enforce executive titles. However, they do not have the power to obtain the pledged property, which must still be voluntarily turned over or taken with police assistance. Some judges questioned the propriety of notaries serving this role, as it makes them advocates of the creditor in the enforcement process instead of neutral arbiters in the transaction. For now, the law is in place – time will tell whether the system is working.

Professional Associations.

The Macedonian Business Lawyers Association has been involved in the MLO amendments and is also involved in general education of the legal profession through its numerous legal publications and events. MBLA organized discussion groups during the MLO amendment process and provided input to the Working Group. Due to its broad membership – in-house counsel, private lawyers, notaries and judges, it provides one of the only venues for broad exchange of ideas.

The MBLA has also shown substantial interest in ADR. The organization has published rules for mediation and has registered a number of mediators. However, this supply-side activity does not yet seem to have connected efficiently with the demand, as there are few if any cases of mediation being reported. The MBLA would do well to work with business associations in order to more effectively get the message of mediation to the end users – the business community. Many business people do not know that this form of dispute resolution is an option, and their lawyers are often slow to recommend an approach that could mean lower legal fees. This information gap needs to be bridged.

Market for Reform

Demand for reform in the law of contracts is low. For the most part, the private sector is satisfied with the overall content of the MLO, and some practitioners felt that the recent reforms were not particularly significant. The greater demand is for a form of lawmaking that more actively elicits input and feedback from interested stakeholders. This is especially true for the Ministry of Justice, which is known for its commitment to the classic model, at the expense of effectiveness. Not only is the Ministry failing to obtain much needed input, the exclusion of various organizations from the process inspires resistance to implementation.

Court reform, however, is a different matter. Dissatisfaction with the current system is very high. One of the themes repeatedly raised by stakeholders was the need for a specialized court to handle commercial matters. Judges expressed strong interest in a better system of judicial education in order to better understand and apply new laws. This demand should provide fertile ground for effective change under the existing court reform programs as well as strong acceptance of training programs for judges if developed in connection with the various legal reform programs underway.

The dissatisfaction with courts has increased the demand for ADR. The court system does not systematically manage cases. There is no filtering and referral mechanism that could promote alternative methods of dispute resolution. Several stakeholders representing foreign investment groups voiced a desire for mediation services. However, the Arbitration Court within the Chamber of Commerce is perceived as both non-transparent and inefficient. It is not viewed as a viable venue to resolve domestic commercial disputes.

As mentioned earlier, a Mediation Service Center was introduced by the MBLA in 1999. Mediators were trained but no cases were submitted for mediation in part because the necessary legal underpinnings that would support ADR have not been introduced into Macedonian law but also because local businesses have not yet been adequately educated as to the benefits of ADR. The Macedonian Stock Exchange is in the process of establishing an Arbitration Committee to deal with capital market trade disputes between investors and MSE members. No cases have as yet been presented to the Committee. Insurance companies are experimenting with forms of mediation and arbitration as part of their claims settlement procedures but in the absence of an enforceable legal basis. Also, the Judges' Association has taken tentative steps toward the establishment of mediation of petty criminal disputes.

An *ad hoc* committee comprised of donor representatives, members of private law firms, Macedonian NGOs and government officials have been exploring ways to increase and broaden the use of mediation and arbitration in Macedonia. The Ministry of Economy in cooperation with the Ministry of Justice, NGOs and the European Reconstruction Agency intend to prepare a policy paper that will include a draft arbitration law by the

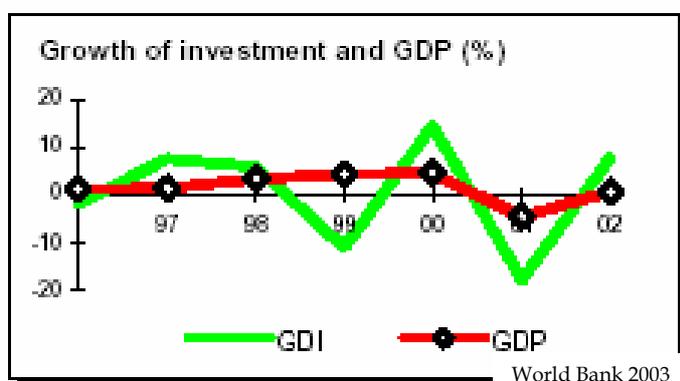
end of March 2004. To increase demand side support for ADR, Southeast Europe Enterprise Development (SEED), a member of the World Bank's International Finance Corporation, has undertaken to launch business education seminars on the value of using mediation to resolve commercial disputes. In addition, the Ministry of Justice is exploring the introduction of formal mechanisms for the diversion of certain types of disputes to mediation. SEED is advocating implementation of a mediation model successfully employed in Slovenia that reportedly reduced the court caseload by 54%.

There may be resistance to increased arbitration by the Chamber of Economy if it is done outside their structure, so it will be important to win their support early for any projects. It would be wiser, however, to work *with* the Chamber than *through* the Chamber, thereby ensuring that other organizations are the driving force in setting up and utilizing services. Some individuals have indicated their unwillingness to participate in any program that will vest exclusively through the Chamber of Economy.

FOREIGN DIRECT INVESTMENT

Overview

Macedonia has sharpened its focus on the reforms in the investment environment at a propitious time. Overall inflows have dropped over the past few years as the privatization process has neared completion, with only a few choice, high value investments left. Policymakers are adjusting to this by fixing their sights on remaining constraints to greenfield investments as well as providing incentives for brownfield investments in existing private sector enterprises. The overall orientation is impressive,



and suggests that policymakers have learned a great deal about what attracts or repels investors; the only issue now is implementation.

The scores for FDI show substantial improvements in both Framework Law and Implementing Institutions. This bears explanation, however. Prior scores for Framework Law were already high (88%). The three-point increase to 91%

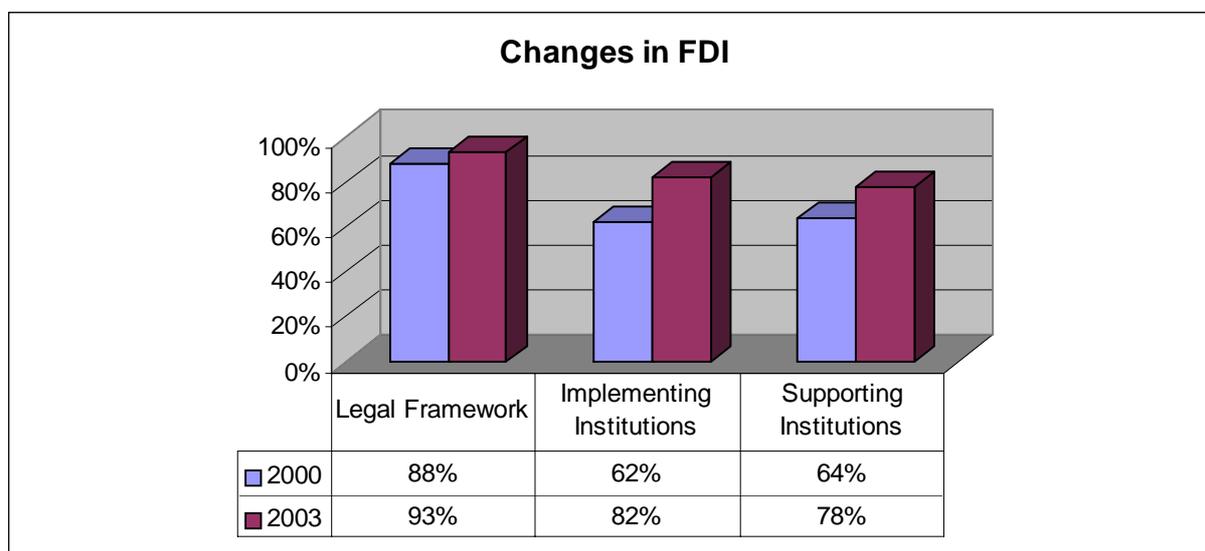
indicates a consolidation of prior efforts as well as improvements. It is not unusual for countries to backslide (as Romania did in 1999 when it reneged on its investment incentives), but Macedonia has held its course and moved forward. Implementing Institutions are not as clear cut. On the one hand, the Ministry of Economy has eliminated the dysfunctional investment unit that has been underperforming since 2000 with an Investment Promotion Agency that is based on an outstanding, investor-oriented analysis and programmatic design. On the other hand, this IPA has not yet been fully established and thus can only be graded on the basis of reasonable expectations. Even so, there is substantial improvement, with Implementing Institutions moving from 62% to 79%.

Supporting Institutions have improved in this area of law more than any other. Most of the upgrading from 64% to 78% is due to improvements in customs administration, growth of private sector business organizations, and the impact of the Macedonia Competitiveness Activity. There is now considerable opportunity to build upon and consolidate these gains.

Framework Laws

Macedonia provides an interesting case study in the ongoing debate among reformers over whether a "Foreign Investment Law" is ever actually needed. Those arguing against investing resources in a specific code note that investors do not particularly care

about the form of the law – one code versus multiple provisions spread across numerous laws – but only whether their concerns are substantively addressed. Those supporting codification believe that by putting all the laws in a single code, the investment environment is more clearly defined, and thus more attractive.



Macedonia's experience would appear to support those emphasizing substance over form. The country has no foreign investment code, yet it receives very high marks for Framework Laws (91%). For those who argue that it is important to have all of the issues affecting foreign investment in one document, Macedonia has met the challenge through its *Programme for Stimulating Investment*²⁶ (the *Investment Programme*) by the Ministry of Economy. In addition, the Ministry has set up a web site with the principle laws and policies available in English for the foreign investment community. In terms of structure, there is no need for any special codification through a foreign investment code.

There were major improvements in scores from the 2000 Assessment in the areas of Investment Treaties and International Conventions, and in Definition of Implementing Institutions. Over the past three years, Macedonia has entered into a number of bilateral investment treaties with the US, EU members and other countries, and has developed programs with the Overseas Private Investment Corporation (OPIC) and the Export/Import Bank (Eximbank) of the United States. Due to the design of the scoring methodology, this had a substantial influence in raising the scores this year. Likewise, the creation of the IPA was very influential in raising scores. In 2000, the Implementing Institution was not defined by law; today, there is a solid program in place for the IPA.

Success in the Framework Laws can be misleading, however. The scoring system gives indicators of the direction in which the regime is headed, but it does not necessarily

²⁶ Programme for Stimulating Investment in the Republic of Macedonia, *Government of the Republic of Macedonia, Ministry of Economy, August 11, 2003.*

mean that investment is likely to increase. There are other issues affecting foreign and domestic investors: market size, competitiveness, administrative barriers, and the performance of the courts in establishing certainty in application of the laws. These cannot be addressed adequately through Framework Laws.

There is an opportunity for establishing greater investor confidence, however. The Ministry of Economy has identified approximately 80 laws in need of amendment. Investors in transition countries are often nervous about extensive or numerous legal changes, because they are generally unable to predict or influence the outcome because of the processes involved. Unpredictable legal changes are often cited as reasons that investors wait to enter a newly independent state or increase their investments already there.

This, fortunately, provides an opportunity. The CG &CL Project and a number of other donor interventions have introduced models for interactive lawmaking, in which the private sector stakeholders actually participate in the development of the law through open discussions, analysis, and active input. This permits them to track changes, predict final versions (within reason), and manage the changes more effectively. If a similar approach could be embraced by the Ministry of Economy and other government stakeholders, these 80 laws (or at least the most important of them) could provide an opportunity for advancing democratic processes that are attractive to investors while ensuring reasonably satisfactory outcomes.

Another area of success in the overall framework is in intellectual property rights. Macedonia is a signatory to all major international IPR conventions and treaties. The legislative framework is undermined, however, by the lack of effective implementation through prosecution for violation of such rights. Despite the occasional public bulldozing of confiscated CDs, enforcement is still weak. Reforming this area will become increasingly important now that IT has been awarded cluster status in the Macedonian Competitiveness Activity: lack of enforcement reduces competitiveness in this field.

Implementing Institutions

In 2000, attempts by the Government to promote investment were unfocused and spread across several ministries and agencies. Over the past three years, this confusion has been substantially reduced, with consolidation of most investment promotion in the Investment Promotion Agency under the Ministry of Economy.

The IPA is still being staffed, formed and implemented. Nevertheless, the team awarded significantly improved scores for several reasons. First, the Government has clarified the roles and responsibilities of those involved in investment promotion through a single, focused entity that did not exist three years ago. This is very significant progress and includes elimination of the Ministry of Development, which

was not well respected in the investment community. Second, investors generally expressed satisfaction with the direction of the new approach. They were cautiously optimistic and enthusiastic, though concerned that political changes in the next election could undermine implementation of the *Investment Programme*. They were also generally satisfied with services currently being provided.

Another reason for high marks in this transitional period is the orientation and performance of the Ministry of Economy. Unlike most programs in transition countries, the *Investment Programme* is remarkably attuned to investor wants and needs with respect to the costs, risks, and revenues in the Macedonian investment climate. In addition, the Ministry is applying lessons learned elsewhere in focusing on all investment, not just foreign investment, and thus is trying to improve the overall investment environment. This will become increasingly important in the post-privatization period, when the greatest benefits are likely to come from increased domestic investment.

The *Investment Programme* is significant also because it reflects input from the private sector. Ministry and private sector representatives reported collaborative efforts and involvement of investors in developing and discussing the program. This bodes well for ongoing implementation and public-private partnership and collaboration.

The IPA has the proper design for providing leadership in addressing constraints and administrative barriers, which still plague the business environment. It is very likely that additional assistance will be needed from the donor community for the next year or two to ensure the IPA properly develops and maintains appropriate customer service and investor orientation standards in its operations. Indeed, ministry officials have openly stated that the IPA needs one or two positions staffed through donor funding in order to attain its goals in the near term. At the very least, ongoing support through collaboration with private sector organizations such as the Competitiveness Council and business associations will be essential to ensure maximum implementation for effectiveness.

The courts also serve as Implementing Institutions for the foreign investment framework because they are charged with interpreting, applying and enforcing the laws affecting investors. There has been much less progress in this area, as discussed elsewhere, but there are some important developments taking place. Foreign and domestic investors unanimously complain of delays and uncertainties in the courts. In courts outside of Skopje, foreigners also complain of higher incidences of unequal treatment in favor of local litigants. Many foreign investors, upon advice of local counsel, will require foreign arbitration clauses in their contracts rather than submitting themselves to the local courts. Not all situations permit this, however. As a result of these factors, there is a growing interest in mediation, arbitration and other forms of alternative dispute resolution in the foreign investment community.

A second weakness in the courts is that judges have been unable to keep up with the numerous changes in the law. Judges complain that the little training currently available is highly theoretical and of little practical use. This suggests an opportunity in legal reform projects to develop practical material for judges whenever a new law is passed. Likewise, it would be worthwhile to find out from investors and their attorneys where they see the weaknesses, then develop materials together with them and the judiciary. The desire for specialized commercial courts noted elsewhere in this report is also high among those dealing with investors.

Supporting Institutions

Government Entities. Foreign investors and others have been very impressed with the progress being made in reform of the customs administration. Various stakeholders noted improvements in the procedures, fee structures, corruption reduction and overall performance. Introduction of random and profiled inspection methods is beginning to replace the previous 100% inspection practices, leading to fewer delays. These reforms are cited as an example of what can be done when there is political will for reform.

The major remaining complaint in this institution is in coordination of inspectors and various agents with the commercial needs of the business community. The business sector complains that land transport is often delayed unnecessarily because the hours of various inspectors are too short: there are no inspectors after 5:00 p.m., even though trucking schedules normally include late night transport. As a result, many shippers experience increased costs and delays when trucks must spend the night at the border. This can be particularly problematic for farm produce during the hotter months, when such delays can cause significant damage to shipments.

Protection of intellectual property rights is still a problem in Macedonia. For industrial property rights, the situation is improving in some ways, but further work is needed. IPR specialists complain that the enforcement agency is under equipped, understaffed, undereducated and under funded for their tasks, and thus underperforming. Prosecution of piracy charges is undermined by very poor preparation of legal documents: the team was shown a complaint that failed to state sufficient facts for even a prima facie claim that the law had been violated, even though such facts existed. To make matters worse, courts are quite weak in interpreting and applying the IPR laws properly, and especially in the matter of preliminary injunctions. Substantial training is needed.

Improvements in this area are coming from private sector efforts. One specialist reported that computer companies are playing a key role in educating the public on the need for legal software and are seeing a growth in sales of legal software. They are supported by a private sector association of IT companies. Microsoft recently obtained an agreement from the Government to legalize all software on Government computers. This has received mixed reviews from the IT community, which has little sympathy for

Microsoft in light of what is perceived as excessively high prices for their products. Even so, this does provide additional public education on piracy issues.

In terms of the overall climate for software development, there were mixed reviews. One company reported that they simply will not attempt to develop off-the-shelf products in Macedonia because of the level of piracy. Another company noted, however, that the Macedonian market is not generally interested in off-the-shelf products, preferring customized applications and service contracts. For these, compliance with licensing agreements has been quite good.

Several IP specialists noted that Macedonia is a net exporter of software developers – that a number of young professionals are regularly emigrating to find better opportunities and salaries in other countries. Clearly, the country is producing good local talent, but will need to make changes in order to attract investment rather than export workers.

Professional Associations. One investor noted a reluctance in the business community to advocate reforms directly with government officials, preferring instead to stay in the shadows while providing their lawyers and accountants with information on change. At this point, however, these two professions do not appear to be providing regular input to policymakers on reform issues with respect to foreign investment concerns. Indeed, there is still resistance at the Bar Association to permitting foreign lawyers to practice in Macedonia. Accountants are generally applying reasonable accounting standards, but do not seem to be serving in a public advocacy role on investment issues.

Trade and Special Interest Groups. Another area of significant growth in the past three years has been in private sector business associations. Although there is still no viable bankers' association yet, a number of groups have appeared. Among these are the American Chamber of Commerce in Macedonia (AmCham), the Macedonian German Chamber of Commerce, and the International Committee of Investors. These organizations have begun providing input to policymakers, but could use additional assistance in enhancing their role and ability in this area. This could come, in part, through better collaboration, for which there seems to be some support. The Competitiveness Council has also begun to appear as an important advocacy group on investment issues and could serve a leadership role among the various associations.

It is fortunate that these groups have developed, because the positive assessment of the official Macedonian Chamber of Commerce in 2000 seems to have been too optimistic. Without exception, foreign and local investors were duly unimpressed with the Chamber, with some noting that the Chamber's moribund performance in regional chambers of commerce stands in the way of private associations doing more effective work with regional counterparts. This view is not unusual in the former Yugoslavia, where the Chambers are funded through mandatory fees and taxes in order to promote their members' (often conflicting and competitive) interests, and have no performance

incentives. It is unlikely that much of the existing Chamber could survive a transition to funding through voluntary payments.

As noted in the section on Collateral Law, credit information and collection services are still insufficient in Macedonia. Foreign investors wishing to check out the credit history of a potential partner will have to be satisfied with reports from the Central Registry. Likewise, the market has not yet responded to the changes in law permitting self-help, so that there is little available in terms of collection services or repossession agents, although the latter do exist.

Market for Reform

The 2000 Assessment reported the following:

The GOM lacks a consultative mechanism to dialogue with the private sector and investors. This represents a potential obstacle to developing investment legislation adequate to support economic growth and increased foreign investment.

Great changes have taken place in the past three years with respect to dialogue. Although the “classical model”²⁷ of lawmaking is still used, the Government is increasingly including private sector input in the policy development and lawmaking processes. In the area of Foreign Direct Investment, it is expected that the new IPA will serve as part of a permanent consultative mechanism, providing input from investors to lawmakers.

The increasing use of dynamic, democratic lawmaking processes has appeared at the same time as several private sector associations have begun to find their role. The various foreign investor associations and bilateral chambers are beginning to fill the historical void.

There is strong demand among investors, and increasingly among potential recipients of foreign investments, for the implementation of the reforms identified in the *Investment Program* of the Ministry of Economy. At the same time, there is concern over the impact of political changes after the next election, with many worried that the current Minister may be replaced, not necessarily with anyone as committed to an investor-friendly reform agenda. This makes it doubly important that work with the private sector continue, so that the pressure to accept input can increase if there is any negative development in the willingness to seek out such input.

With the few exceptions noted in this section, overall demand for change in the Framework Laws and Implementing Institutions is rather low. The legal framework is

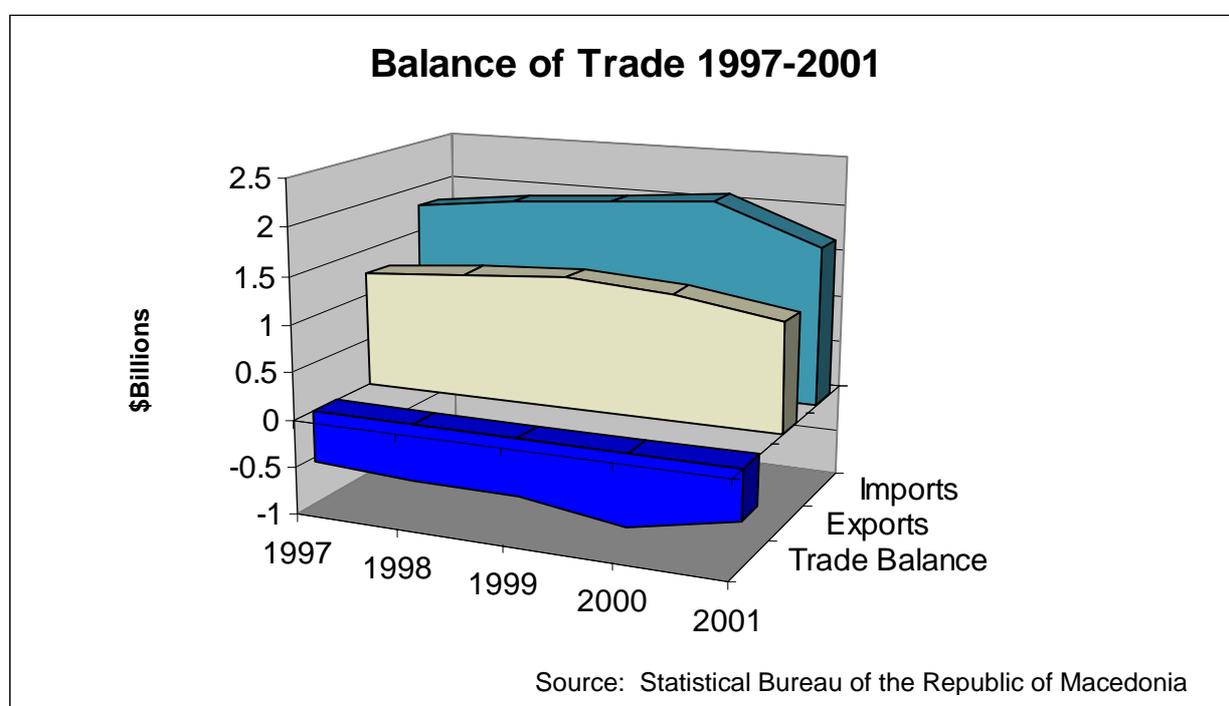
²⁷ The “classical model” normally relies on a few professors to do most or all of the drafting, with no serious input from other stakeholders. The draft is then given to Parliament for passage, which often comes as a surprise to the private sector, there having been no effective notice of the new policy initiative prior to the passage of the law.

generally solid, and the major concerns for investors are not laws, but issues of competitiveness being addressed by the Competitiveness Council.

TRADE

Overview

Macedonia's Trade Law regime is a case study of what can happen when political will and donor support are aligned. The Framework Law scores improved by twelve points, from 81% to 93%, reflecting the serious investment made by local officials and foreign donors in order to gain admission to the World Trade Organization. Due to strong political will, Macedonia agreed to extensive reduction of various protections in the form of tariffs, fees, and quotas, opening the market to increased competition from



the outside. (Some officials still feel that the reductions were too aggressive.)

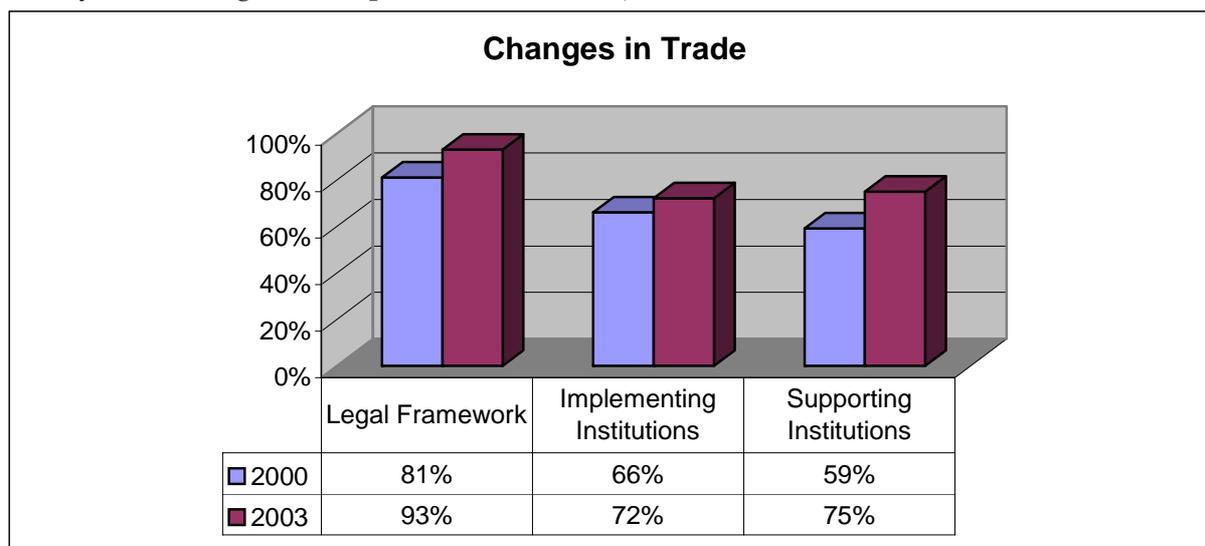
It is still too early to see any economic impact from this new opening. The recent conflicts in Kosovo have negatively affected the economy, with exports falling along with imports. The balance of trade remains negative. WTO accession is part of an overall program of improved trade ties, but it will take some time to see positive results.

Implementation of the recently adopted changes in the trade regime is the next challenge. Numerous stakeholders noted the substantial advances of Macedonia as expressed through WTO commitments, but many also expressed concerns over the ability of the country to keep the commitments. There is likely to be substantial pressure for a return to increased protections if competition from imports increases unemployment.

Framework Laws

Since the 2000 Assessment, Macedonia has become a member of the WTO. In order to accede, the country made numerous commitments and concessions to open the Macedonian market and to regulate trade in line with international standards. Market opening was based on bilateral negotiations with various trading partners. These were based in part on new and existing bilateral investment treaties, including a recently concluded BIT with the United States.

During the negotiations for entry to the WTO, Macedonia agreed to reduce customs and tariff duties, rationalize fees, and eliminate most quotas (except for wheat) and other protections. The textile industry was granted a slower track, with reduction in protections and subsidies scheduled for 2010-12. These changes are significant. In addition, the country has committed itself to liberalization of services in all areas, including legal, financial, transport and education. These commitments will require a number of legal changes as well, as shown in the attached matrix of laws (Annex 2: Survey of Existing and Proposed Trade Laws).²⁸



The legal framework for regulation of trade has been substantially improved, most significantly with regard to customs. Customs fees have been rationalized, eliminating a 1% processing fee in favor of €19 fixed fee. Likewise, practices and performance have been improved, as noted in the Supporting Institution discussion below.

Reduction of licenses is another great success. During the 2000 Assessment, there were numerous licensing requirements for imports and exports, many related to quota requirements. Under the terms of Macedonia's WTO accession, these have been progressively eliminated in three stages since 2001. The only remaining license

²⁸ The Survey was prepared by Booz Allen Hamilton under the USAID Macedonia WTO Project.

requirement – for oil derivatives – is scheduled for elimination by the end of 2003. Although these licensing requirements have improved substantially, the improvements are not reflected in the most recent FIAS report on administrative barriers. The Report found that 37% of the companies interviewed were subject to import/export licenses. Moreover, the report shows no net reduction according to these companies over the past three years. This suggests a lag in implementation of the new regime that should be addressed through inspection of actual practices at the 19 customs posts around the country.

Agricultural export subsidies have also been eliminated, which is a point of contention. Many feel that these subsidies should have been phased out over a longer period due to competitive disadvantages at the present time. (Competitiveness in the lamb industry is currently being addressed by MCA, which, hopefully, will help to overcome the loss of subsidies.)

Tariff quotas have also been restructured from a controversial rate system with arbitrary distribution to a system of auctions and first-come-first-served approach to applications. This has been part of an effort to combat corruption, which is perceived to be working.

As noted above in the discussion of Foreign Direct Investment, the legal regime for protection of intellectual property rights has been sufficient, if enforced. Only minor changes have been made to the laws. Macedonia is a member of WIPO and a signatory to the TRIPS agreement, among others, which together provide adequate legal protection in theory, as long as the laws are enforced. Enforcement, however, continues to be a significant problem, with insufficient staffing, equipment and funding for the enforcement services. (See discussion under Foreign Direct Investment: Supporting Institutions.) Within the courts, IPR enforcement is plagued by delays in the court system. IPR experts, however, felt that the legal knowledge of the judges was adequate but their performance could be improved, especially with regard to issuance of preliminary injunctions. This will require specialized training.

Inspection of imports continues to be high, although it is much improved from the past 100% level. In many countries, quality control is left in part to consumer protection groups and market forces, with consumers effectively protecting themselves from poor quality by rejecting the goods or lodging complaints with appropriate agencies. In Macedonia, protection has always been a role of government (in theory, at least), and the private sector has not yet picked up this role. It is likely that the government will continue to maintain a high level of involvement until NGOs and private sector groups begin to exercise this function more effectively.

Overall, the improvements in the legal framework for Trade are remarkable. The private sector has complained, however, that they were not included effectively in the various WTO negotiations. There appear to be two reasons for this. First, the

Government's aggressive commitment to accession, plus the lack of any regular history of policy interaction with the private sector, left little room for private sector input. Second, and just as important, the private sector has not been effectively organized to provide input. This has changed somewhat over the past three years, but during the course of WTO negotiations, there was very little capacity for dialogue with the government.

Provisions covering anti-dumping and countervailing duties were adopted in the Law on Trade of 2002, and are consistent with the WTO, using the exact language of the WTO agreements. These areas still need regulation, however, as the framework level is quite general and serves more as a notice and commitment than any concrete basis for implementation. Procedures and institutional mechanisms are still needed for enforcement. The Ministry of Economy, which is responsible for this law, has said that they may remove the anti-dumping provisions because Macedonia has no resources to carry out the complicated investigations required to prosecute actions in this area. While perhaps not the ideal solution, it is significant that the MOE would rather remove an unenforceable provision than lower respect for the law by keeping it on the books with no ability to enforce it.

Implementing Institution

The primary Implementing Institution for Trade Law over the past three years has been the Ministry of Economy, which, at the time of the last assessment, had recently been restructured to absorb the Ministry of Trade and eliminate several other agencies that were not working effectively. The MOE has received considerable praise for its effectiveness and private-sector orientation in addressing the problems of Trade Law. On the other hand, business groups have complained that they were dissatisfied with the level of inclusion in the actual process of negotiation. Even so, the overall impression is one of process.

The MOE continues to solidify the gains made in the law by working on implementation. The commitments made to attain accession will require significant, long-term effort. The USAID WTO project is providing much needed technical assistance in numerous areas of WTO compliance, in part because the MOE does not have sufficient resources internally to address the many areas of change. In fact, Ministry representatives clearly stated during interviews that additional ongoing support was needed.

Private sector stakeholders were hopeful that gains made in the past few years will hold when changes in top personnel are made. Political will has been exercised effectively in cleaning up the Customs Agency by replacing the director with an effective reformer and bringing greater transparency, discipline, and customer-service orientation to the conduct of business. As noted under *FDI: Supporting Institutions*, the changes in this agency have been heralded as among the most important in any government entity. In

fact, the reforms have been unusually successful. Internal reformers and stakeholders will be monitoring any changes under the recent cabinet reshuffling. If such monitoring can help to hold the course, then sustainable change has taken place. If not, it may be necessary to rethink project assistance and focus again on accountability mechanisms, such as institutional change and support for watchdog mechanisms.

As noted above, the MOE does not have the resources currently to develop the regulations, procedures and mechanisms for dealing with anti-dumping and countervailing duty issues. Although the law provides for these protections, practice is quite the opposite, leaving a gap in implementation that is unlikely to be filled for a number of years.

Supporting Institutions

Several institutions overlap different areas of law, such as the Customs Agency and Intellectual Property Agency. These have already been covered under the chapter on Foreign Direct Investment and bear no further discussion here. Others – such as business associations – have specific trade aspects that merit additional coverage.

The past three years has seen growth in international business associations, such as the various bi-lateral chambers of commerce (AmCham and the German Chamber), as well as the International Council of Investors.²⁹ Some of these organizations have grown with little or no project assistance to respectable voices for private sector interests. They are actively following changes in the trade regime and lobbying government on behalf of their members. Much of the lobbying is still relationship based; that is, it depends on someone in the organization knowing someone in government and using that relationship to push for changes, sometimes quite effectively. As Macedonian democracy matures, it will be necessary to formalize advocacy in accordance with international standards of transparency, and these organizations have the basic structure and membership necessary to serve as a foundation for professional, formal advocacy. Many of them will need support, especially those with primarily Macedonian membership.

One of the principle areas of concern among investors was the problem of quality controls and standards. Macedonia is still weak in knowing and applying ISO standards, so that numerous stakeholders expressly mentioned the need for assistance in this area – both for inspectorates to monitor and businesses to produce in accordance with international standards. The MCA project has potential for introducing ISO controls into the export clusters under their work in cheese and lamb. Such interventions could possibly be leveraged to provide assistance on a self-sustaining national basis for other industries.

²⁹ The ICI has a strong Greek membership, but also hopes increasingly to serve as a multi-national foreign investors organization. Currently, it is unable to have the other bi-lateral chambers as members because of constraints in the business associations law that restricts organizations to individual memberships.

Market for Reform in Trade

Accession to the WTO changed the dynamics and focus of trade reforms, providing impetus and direction to ongoing reform. This was a result of strong political will that utilized technical assistance effectively to achieve accession. Political will for compliance will also need to be strong, because implementation of the reforms will require long-term, consistent effort to bring about the changes promised.

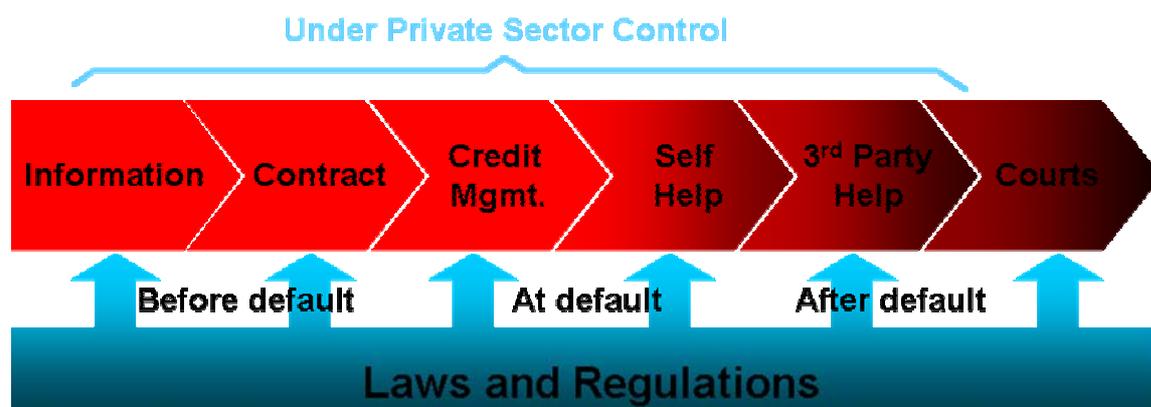
Many Macedonians believe that the concessions and commitments to enter the WTO framework were too generous at this point in Macedonia's economic and political development. There is much concern over lost jobs in various sectors as reduced tariffs lead to a drop in import prices and subsequent shift in market shares to imported goods. Some worry that this will be used politically to press for a more protectionist approach, once again underlining the need for the installation of deliberative lawmaking processes to rationalize the course of change.

Counterbalancing some of the pressure for protection, however, is the ongoing desire to attain EU membership. While requirements for joining the EU are certainly different than WTO membership, there are numerous areas in which the two converge, so that this incentive can be used to maintain gains achieved in the past few years. From the private sector side, EU harmonization is an important rallying point for advocating ongoing implementation and modernization of the trade regime.

Annex 1

Enforcement of Commercial Obligations: Systemic Solutions beyond Courts

Problems in the enforcement of commercial obligations are often addressed solely as an issue of malfunctioning courts in need of reform through government intervention. While court enforcement is surely essential in the foundation of a healthy commercial environment, problems and solutions begin well before courts get involved. In fact, most of the issues are controlled or at least influenced heavily by the private sector.



Enforcement solutions begin before the problems arise, through the use of **credit information** to determine the creditworthiness of a potential debtor. Those who prudently extend credit for goods, services, or loans will use a system for verifying creditworthiness through credit information bureaus and reference checks to avoid taking on unnecessary credit risk without proper protection. This also creates a system of accountability for debtors, who quickly find that poor performance affects their ongoing ability to obtain credit on good terms, if at all. In Macedonia, at least one bank has found that public registration of collateral contracts is already improving payment behavior, because these filings are being used as a form of credit information.

Once the potential debtor has passed scrutiny, creditors should protect themselves through the use of proven, enforceable **contracts**. For standard transactions, it is possible to use pre-printed, proven forms that include all necessary information, including adequate identification of the parties, of the amount to be paid, the date of each payment, interest (if any), collateral (if any) and *penalties* for non-compliance. If local law permits, these penalties can include repossession of property through self-help, accelerated interest payments, attachment of bank accounts and other recourse that does not require court intervention. Courts are full of claims based on poorly drafted, unclear and sometimes unenforceable contracts, situations that are completely avoidable. Most Macedonian banks are currently protecting themselves adequately, but many business people try to save money by drafting their own contracts without lawyers or forms. These practices undercut enforcement.

Once the contract is in force, creditors have an obligation to use reasonable systems of **credit management** to identify and respond to payment problems before they become payment crises. The creditor should track payment due dates and be aware whether payment has been made in order to contact a delinquent debtor immediately. Delays in seeking payment decrease the likelihood of full enforcement and reinforce poor payment patterns. (Debt management – minding amounts due to creditors – is also important, and can avoid penalties and problems in paying debts.)

Despite the best protections, sometimes debtors simply do not pay. When this happens, creditors can utilize **self help** to enforce their rights. First, the creditor should employ aggressive collection procedures through letters, phone calls, and even personal visits to the debtor. If permitted by the contract or law, the creditor can also repossess and sell pledged property, attach bank accounts, or enforce third-party guarantees. Macedonia is beginning to experiment with this on a legal basis (thuggery is still common in criminal and some gray-market enforcement), but stakeholders are not yet comfortable with this approach. Public dialogue would be useful in establishing acceptable self-help approaches.

When these means fail, or when a company prefers to outsource, **third-party help** is needed. This can involve the use of collection agencies, lawyers, and even alternative dispute resolution mechanisms such as mediation and arbitration, depending on the severity and complexity of the issues. If it becomes clear that the debtor will not be able to pay, it is also sometimes appropriate to write off the debt instead of wasting more time and money on fruitless pursuit. (This is another form of self help.)

Eventually, it may be necessary to go to **court**, but this does not end the creditor's involvement. Creditors should manage their lawyers for results, setting strategy, obtaining regular progress reports, and determining the level of aggressiveness instead of meekly assuming the case is out of their hands. This is particularly necessary in jurisdictions like Macedonia where lawyers permit or pursue excessive delays. Likewise, the private sector should monitor the courts and advocate for reform where necessary to ensure that those officials in charge of performance understand the impact of poor performance on the economy.

Reforms of the court system are ultimately the responsibility of government. This includes court administration (reduction of unnecessary delays and costs), quality of judicial decision-making, and enforcement of final judgments. Enforcement entails the performance of bailiffs (or similar court officers), police (to assist bailiffs), evaluators and auctioneers to ensure prompt conversion of judgments to cash proceeds based on market-oriented techniques.

Implications for Macedonia

Programmatically, enforcement of commercial obligations can be approached on a systematic basis or by component. In Macedonia, a systematic basis is justified because of the need for improvements at most stages in the process. Currently, there is little credit information available, variable quality in contracting and credit management, and uncertain use of self-help. The collateral pledge system can serve as a foundation for improvement of credit information and enforcement, especially through expansion into filing of judgment liens against property. (Expansion will depend in part on lower fees, however.) Likewise, it can be a foundation for risk management as commercial creditors outside of the banking industry discover and utilize secured credit for their transactions.

Commercial credit collection services are not yet available in Macedonia, but a number of stakeholders have expressed interest in this service. These should be developed in collaboration with consumer protection organizations – especially international groups - to avoid abuses that have already been recognized and prohibited elsewhere. A market also seems to exist both for outsourcing and for management consulting to teach improved in-house techniques. There is high demand for ADR and for court reform. Targetted together, it is possible to have a significant positive impact over the short and long terms while also creating a climate for encouraging a culture of accountability, driven by private sector demand for change and provision of services, and complemented by work in and with the public sector.

Schematically, the requirements for change are as follows:

Mechanism	Primary stakeholders	Public interventions or reforms needed
Credit Information	Banks, credit information providers, registries, business associations, leasing companies, consumer credit companies (including credit cards)	Reduction of registration fees; computerization of court dockets; internet access to registry and court records; possible change in law of defamation to exclude negative credit reports; opinion from Supreme Court on legality of consumer credit contracts in which consumers permit sharing of information among creditors
Contracting	Lawyers associations, business associations, law schools, business schools	None
Credit Management	Management consultants, business schools, software sellers and developers, business associations, creditor associations, accountants	None
Self-Help and Third-Party Help: <i>Collection</i>	Management consultants, business schools, consumer organizations	Analyze existing law for appropriate rights, limitations on techniques, and sanctions for abuse
Self-Help and Third-Party Help: <i>Repossession</i>	Management consultants, SROs (to monitor and disseminate best practices), private auctioneers	Analyze existing law for appropriate rights, limitations on techniques, and sanctions for abuse

Third-Party Help: ADR	Trade, business and specialized associations (insurance, banking, construction, unions, etc.), bar associations	Laws recognizing validity of private sector ADR; court enforcement of arbitral awards
Courts: Litigation Management	Management consultants, business associations, bar associations	None: private sector is responsible for managing their legal professionals
Courts: Judiciary & Administration	Watchdog NGOs, media, bar associations, legal publishers, judges associations, clerks associations	Extensive reform needed in court administration and judicial education; prosecution for corruption needed to ensure broad compliance
Courts: Bailiffs	Bailiffs, judges associations, bar associations, police	Further analysis of law and procedure of enforcement system, with significant reforms likely
Courts: Auction	Auctioneers, appraisers, bailiffs, bar association, accountants, business associations	Further analysis of law and procedure of enforcement system, with significant reforms likely

Annex 2: Survey of Existing and Proposed Trade Laws

Introductory Note

The Survey of Existing and Proposed Trade Laws (hereinafter: Survey) is one of the specific deliverables contained in the Performance Work Statement of the USAID Macedonia WTO Project (hereinafter: Project) for the period of July 1 - November 30, 2003. Its purpose is to identify and enumerate laws and regulations that produce a certain degree of impact on trade, regardless of whether these pieces of legislation require immediate legislative attention in order to comply with the WTO rules or not. In other words, the Survey is an attempt to compile a list of the most important trade related laws explaining in a separate column for each of them the needs for reform and the intentions of the Government in that regard. Generally, there are three categories of laws included in the survey: legislation that needs immediate changes in order to comply with the WTO rules and/or specific commitments undertaken in the course of the Macedonian WTO accession, legislation that requires further review and investigation and legislation considered to be fully consistent with the WTO rules. The latter category was included in the survey for reasons of completeness and practicality. Namely, further (possible) changes of this legislation and its implementation in practice may result in introduction of WTO inconsistent measures and the government authorities must be aware of it.

As already mentioned, this Survey does not list all trade related laws and regulations, for the simple reason of avoiding a long and complicated document that would make it difficult for the users to focus on the crucial and most urgent and vulnerable items. The selection was made taking the following criteria into consideration: 1) Impact on trade of a certain law/regulation, 2) Its relation with the WTO rules and commitments, 3) Interest about particular trade area or a law/regulation of the WTO Members during the Macedonian WTO accession process, 4) Ongoing WTO negotiations on specific issues important for Macedonia, 5) Possible assistance of the Project in the future.

The Survey is prepared in a table format, which is considered to be the best format for this type of document. The intention was to prepare a relatively short, concise, clear and “clean” document that gives a better picture of the legal environment for trade in Macedonia.

The listing of the legislation is partially based on the classification contained in the accession documents, since the number of laws covered by this Survey does not require detailed classification of trade areas covered by all of the WTO Agreements. Hence, the Survey contains only five classification headings: General, Trade in Goods, Trade in Services, Intellectual Property and Bilateral Cooperation.

The first column of the Survey contains the official titles of the laws and regulations. Please note that this is not always the case where a new law or regulation is to be enacted and the official title of the law is still not finally determined, and in the case of bilateral agreements where entries are modified in order to avoid repetition of the wording contained in the official titles of these documents. This column also contains references to the respective numbers of the Official Gazette where the legislation in question is published. This is done for the purpose of easier identification and retrieval of a particular law/regulation and its amendments.

The second column gives an information about the coverage of the particular law/regulation. The wording is based on the content of a particular law/legislation having on mind the WTO trade areas and issues covered.

The third column contains information on the existence of an English language translation. This is done for the purpose of identifying translations available for the purpose of: 1) possible foreign expertise where such translation can be used, 2) its submission to the WTO, and 3) Project's translation priorities. The entry "Yes" in this column covers the situations where the text of the particular law is translated into English, but does not necessarily mean that the translation includes all the amendments.

The fourth column identifies which Government ministry or agency is responsible for the drafting of the respective law/regulation and/or its amendments, as well as its implementation.

The fifth column contains information on the status of the legislation process for a particular law/regulation. The information is presented in a concise manner, without elaborating in great details the legislation activities. An emphasis is put on the basic information about the current plans for immediate and/or future legislative action without further explanation of the details. The information contained in this column is generally based on information provided from the relevant Government agencies in charge of particular law/regulation and on the Program for Approximation of the National Legislation to the Legislation of the European Union (2003). In cases where the information gathered from these two sources differ (just few), only the information "from the field" (i.e. from the responsible government official) is included.

Given its nature and content, as well as the dynamic legislative reforms currently taking place in Macedonia, this document will need to be updated on a regular basis.

This Survey is intended to represent a basis for the process of determination of the specific deliverables of the WTO Project, including the preparation of a legislative matrix of actions. For this purpose, it should be viewed in conjunction with the WTO Compliance Requirement Matrix that has already been prepared by the Project.

	Law/ Regulation (Official Gazette number)	Coverage	English Translation	Responsible Agency	Status of the Law/Regulation
<u>GENERAL</u>					
1.	Law on Foreign Trade (45/02, 31/03)	Definition and terms of conduct of the foreign trade, and import and export safeguard measures.	Yes	MOEcon	This Law will be abolished with the enactment of the new Law on Trade (see item 2) that will regulate issues of foreign trade as well.
2.	Law on Trade (23/95, 30/95, 43/95, 23/99, 43/99, 6/02, 38/03)	Conditions and practices of conducting trade.	Yes	MOEcon	Draft of the new Law on Trade in existence. First reading by the Parliament completed. Planned to be enacted by the end of 2003.
3.	Law on Trade Companies (28/96, 7/97, 21/98, 37/98, 63/98, 39/99, 81/99, 37/2000, 50/2001)	Establishment and operation of the trade companies.	Yes	MOEcon	Will cease to apply on December 31, 2003.
4.	Law on Trade Companies (58/02, 88/02, 98/02, 42/03)	Establishment and operation of the trade companies.	Yes	MOEcon	In force from January 1, 2004. Draft of new Law submitted to the Government for approval.
5.	Law on Market Inspection (35/97, 23/99)	Competence, authority and organization of the State Market Inspectorate.	Yes	MOEcon MOF	Based on a Government Conclusion, a drafting of a new law, to cover all types of inspection, is planned. No dates for start of the drafting process or for enactment determined. The drafting will be organized and supervised by the Ministry of Justice.
6.	Law on Stock Reserves (47/87, 13/93)	Governing strategic reserves.	No	MOF	New Law planned to be enacted. Drafting in process.
7.	Law on Free Economic Zones	Conditions and the manner of establishment, operation and termination of the free economic	Yes	MOEcon	Planned to be amended by the end of 2003.

	Law/ Regulation (Official Gazette number)	Coverage	English Translation	Responsible Agency	Status of the Law/Regulation
	(56/99, 6/02)	zones.			
8.	Law on Government Procurement (26/98)	Manner and procedure of carrying out public procurements for beneficiaries and individual beneficiaries of the funds of the Budget of the Republic of Macedonia, the budgets of the local self-government, the republic and municipality non-budgetary funds, as well as of the public procurements of agencies and public institutions, other bodies and organizations, enterprises and companies established or owned by the State.	Yes	MOF	New law planned to be enacted by the end of 2003.
9.	Law on Concessions (25/02)	Manner and conditions under which state properties of general interest may be given for use with an approval (concession).	Yes	MOEcon	No changes planned.
10.	Law against Unfair Competition (80/99)	Natural and legal persons acting or executing against the fair business custom and principles of consciousness and honesty for the purpose of competition while conducting a business venture.	Yes	MOEcon	No changes planned.
11.	Law against Limiting Competition (80/99, 29/02)	Establishes rules on competition, monopoly contracts and monopoly decisions, enterprises that dominate on the market, limiting competition and unequal treatment, regulates the establishment of the Monopoly Authority, procedures.	Yes	MOEcon	Planned to be amended by the end of 2003.
12.	Law on Consumer Protection (63/2000, 4/02)	Conditions and ways of consumers' protection, the rights and commitments of the consumer protection organizations, public administration's tasks.	Yes	MOEcon	Draft of the new Law in existence. First reading by the Parliament completed. Planned to be enacted by the end of 2003.
13.	Law on Foreign Exchange Operations (34/01, 49/01, 103/01, 54/02, 32/03)	Definition of foreign exchange transactions, foreign exchange supervision and control.	Yes	MOF	No changes planned.
14.	Value Added Tax Law (44/99, 59/99, 86/99, 11/2000, 93/2000, 8/01)	Definition, calculation and collection of VAT.	Yes	MOF	No changes planned.

	Law/ Regulation (Official Gazette number)	Coverage	English Translation	Responsible Agency	Status of the Law/Regulation
15.	Law on Excise Taxes (32/2001, 50/2001, 52/01, 45/02, 98/02, 24/03)	Rules and procedures for excise taxes charged on certain products.	Yes	MOF	No changes planned.
16.	Law on Investment Funds (9/2000)	Conditions for establishment and control of the operation of investment funds and investment fund management companies.	Yes	MOF	Planned to be amended by the end of 2003.
17.	Law on Ownership and Other Real Rights (18/01)	Ownership rights of domestic and foreign natural and legal persons, state and self-government.	Yes	MOJ	No changes planned.
18.	Law on Construction Land (53/01, 97/01, 59/02, 80/02, 4/03)	Rights and obligations with regard to the construction land.	Yes	MOTC	Planned to be amended by the end 2003.
19.	Law on Organization and Operation of State Administration Bodies (58/2000, 44/02)	Organization, authorities and operation of the state administration bodies.	Yes	MOJ	Amendments in process of preparation.
20.	Law on State Aid (24/03)	Procedure and supervision of allocation and use of the state aid.	Yes	MOEcon	In force from January 1, 2004. Regulations being drafted.
<u>TRADE IN GOODS</u>					
21.	Customs Law (21/98, 26/98, 63/98, 25/2000, 109/2000, 31/01, 4/02, 55/02, 42/03)	The customs procedure, the rights and obligations of the participants in the customs procedure, as well as the scope, the manner of operation and the organizational setting of the Customs Administration.	Yes	MOF CA	Planned to be amended by the end of 2003.
22.	Customs Tariff Law (23/03)	Determination of the customs duties for goods imported in the customs area of the Republic of Macedonia.	Yes	MOF CA	The Customs Tariff is being changed annually for further harmonization of the nomenclature and to implement the gradual tariff reductions stipulated in the course of the WTO accession.

	Law/ Regulation (Official Gazette number)	Coverage	English Translation	Responsible Agency	Status of the Law/Regulation
23.	Decision on the Procedure for Allocating Goods Under Tariff Quotas (29/03, 59/03)	Procedure for allocating goods under tariff quotas pertaining to preferential imports under free trade agreements, the Interim Agreement for Trade and Trade Matters with the European Communities and the Protocol for the Accession of the Republic of Macedonia to the World Trade Organization.	Yes	MOEcon	No changes planned.
24.	Regulation Governing Payment of Fee for Customs Services Rendered (102/01, 6/02, 37/02, 78/02, 98/02, 47/03)	Provides for a fee of 19 Euro per customs declaration for customs services rendered.	Yes	MOF CA	No changes planned.
25.	Regulation on Implementation of the Provisions of the Customs Code Concerning Valuation of Goods for Customs Purposes (60/02)	Prescribes the special rules and procedures for customs valuation during customs clearance of imported goods.	Yes	MOF CA	No changes planned.
26.	Regulation on Criteria for Determination and Manner of Proving the Origin of Goods (26/2000)	Prescribes the criteria for determination and manner of proving the origin of goods, when the determination of origin of goods is needed for the purpose of: (1) Applying the customs tariff; and (2) Applying other measures for regulation of specific areas related to trade in goods.	Yes	MOF CA	No changes planned.
27.	Law on Standardization (54/02)	Principles of the Macedonian national standardization, the status of the Institute for Standardization, its scope of activities, membership and funding, the preparation, adoption and publication of the Macedonian national standards and their application.	Yes	MOEcon	No changes planned.
28.	Law on Metrology (55/02)	Regulates the metrological system in the Republic of Macedonia, the competencies of the Bureau for Metrology, legal measurement units and standards, measuring instruments' placement on the market,	Yes	MOEcon	No changes planned.

	Law/ Regulation (Official Gazette number)	Coverage	English Translation	Responsible Agency	Status of the Law/Regulation
		usage, verification and their conformity assessment, metrological supervision of quantities and marks on pre-packed products.			
29.	Law on Accreditation (54/02)	The establishment, organization and operation of the Macedonian Institute for Accreditation (as a public institution conducting the activities and responsibilities of a national accreditation service), the accreditation procedure, and the supervision of the fulfillment of the accreditation requirements.	Yes	MOEcon	No changes planned.
30.	Law on Prescribing Technical Requirements for Products and Conformity Assessment (55/02)	The method of prescribing the technical requirements that the products should meet before they are placed on the market, the procedures for conformity assessment of products, the validity of certificates and marks of conformity of foreign origin.	Yes	MOEcon	No changes planned.
31.	Law on Safety of Foodstuffs and Products and Materials Coming into Contact with Foodstuffs (54/02)	The conditions to ensure safety of food and products and materials coming into contact with foodstuffs, food production and trade, and the rights and obligations of natural and legal persons dealing in food production or trade.	Yes	MOH	Regulations on food safety planned to be enacted by the end of 2003.
32.	Law on Medications, Remedial Medicines, Medical Devices (21/98)	Production and protection of medications, medicines, pharmaceutical products and devices.	Yes	MOH	No changes planned.
33.	Law on Seeds and Seedling Materials, Recognition, Approval and Protection of Species (41/00)	Sanitary and phytosanitary protection related to seeds and seedling materials.	No	MOAFWE	Planned to be amended by the end of 2003.
34.	Law on Plant Protection (25/98, 6/2000)	Protection of plants against diseases, pests and weeds, the plant health control on the internal market and in cross-border trade; the production, trade and use of plant protection products, equipment and measures for prevention of the harmful effects on human and animal health from	Yes	MOAFWE	Planned to be amended in 2007.

	Law/ Regulation (Official Gazette number)	Coverage	English Translation	Responsible Agency	Status of the Law/Regulation
		using the plant protection products, and protection the environment and nature.			
35.	Decision on Determining Border Posts for Importation, Exportation and Transit of Plants, Plant Products and Plant Protection Chemicals (34/2000)	Determination of border posts for health control of the plants and plant products and control of the chemicals for plant protection.	Yes	MOAFWE	No changes planned.
36.	Law on Veterinary Health (28/98)	Health protection of the animals from diseases; protection from contagious diseases which are transmitted from animals to people; veterinary sanitary prevention and control; veterinary protection and improvement of the environment and nature; the minimum obligatory scope of health protection of animals from diseases; fees and expenditures for animal health protection; organization and execution of the veterinary practice.	Yes	MOAFWE	New Law on Veterinary is planned to be enacted in 2007.
37.	Law on Agricultural Land (25/98, 18/99)	Acquisition and use of agricultural land.	No	MOAFWE	No changes planned.
38.	Law on Agricultural Activity (11/02, 7/03)	Regulates the conditions and the manner of performing an agricultural activity.	Yes	MOAFWE	No changes planned.
39.	Law on the Quality Control of the Agricultural and Food Products in the Foreign Trade Circulation (5/98, 13/99)	The manner of performing quality control of certain agricultural and food products and processed products thereof in the foreign trade circulation.	Yes	MOAFWE MOH	No changes planned.
<u>TRADE IN SERVICES</u>					
40.	Law on Movement and Residence of Aliens	Right to entry, issuance of visas and temporary and permanent residence of foreigners.	Yes	MOIA	No changes planned.

	Law/ Regulation (Official Gazette number)	Coverage	English Translation	Responsible Agency	Status of the Law/Regulation
	(36/92, 66/92, 26/93, 45/02)				
41.	Law on the Bar (59/02, 92/02, 10/03, 34/03)	Supply of legal services by the bar to natural and legal persons, the organization of the bar, conditions for supplying services, suspension and rights and obligations of attorneys-at-law.	Yes	MOJ	Planned to be amended.
42.	Law on Audit (5/97, 27/2000, 31/01, 30/02, 61/02)	Terms, conditions and manner of providing auditing services.	Yes	MOF	Planned to be amended in 2003.
43.	Law on Postal Services (5/02, 59/02)	Conditions for providing postal services in the domestic and international postal traffic, the provision of access for every customer to the universal postal service, introduction of competition in the performance of the postal services, the relationships between the customers and the providers of the postal services.	Yes	MOTC	No amendments planned. Regulations on technical aspects in process of drafting. Regulation on issuance of licenses planned to be adopted by the end of 2003.
44.	Law on Telecommunications (3/96, 17/98, 28/2000, 57/01 4/02, 88/02)	Conditions and the manner for performing the activity in the field of communication, construction, maintenance and the use of the telecommunication network and devices, the relationship between the provider and the user of the telecommunication services, competition in the field of communication, provision of universal services, granting concession and performance of the telecommunication services, use and control of radio frequency spectrum, production, import, sale, use and control of radio frequency spectra, production, import, sale, use and maintenance of radio stations.	Yes	MOTC	Draft amendments prepared. Planned to be enacted by the end of 2003.
45.	Law on Broadcasting (20/97)	Conditions and manner of performing the broadcasting activity	Yes	MOTC	Amendments (or completely new law) planned to be enacted by the end of 2003.
46.	Law on Construction of Investment Buildings (15 /90, 11/91, 11/94, 18/99, 25 /99, 88/02)	Conditions and manner of construction of investment buildings.	Yes	MOTC	Draft of the new Law in existence. First reading by the Parliament completed. Planned to be enacted by the end of 2003.

	Law/ Regulation (Official Gazette number)	Coverage	English Translation	Responsible Agency	Status of the Law/Regulation
47.	Law on Spatial and Urban Planning (4/96, 8/96, 70/96, 5/97, 28/97, 18/99, 76/99)	Conditions and manner of providing spatial and urban planning services.	Yes	MOTC MOE	Planned to be amended by the end of 2003.
48.	Law on Higher Education (64/2000, 1/02, 15/03, 49/03)	Regulates the system of higher education.	No	MOEdu	Planned to be amended by 2005.
49.	New Law on Recognition of Professional Qualifications (Higher Education)	Rules and procedures of recognition of professional qualifications in higher education.	No	MOEdu	Planned to be enacted by 2005.
50.	Law on Communal Works (45/97, 5/99, 23/99, 52/01, 45/02)	Conditions and manner of providing communal services.	Yes	MOE	No changes planned.
51.	Law on Insurance Supervision (27/02, 84/02, 98/02)	Conditions for performing the activities of life and non-life insurance and reinsurance, insurance brokering activities, incorporation, operation, supervision and termination of activities of insurance and reinsurance trade undertakings, insurance brokerages and the National Insurance Bureau.	Yes	MOF	No changes planned. Regulations pertaining to this Law planned to be enacted by the end of 2003.
52.	New Law on Compulsory Insurance in Traffic	Manner and procedure of compulsory insurance in traffic.	No	MOF	Planned to be enacted in the first half of 2004.
53.	Law on the National Bank of the Republic of Macedonia (3/02, 51/03)	Organization and operations of the National Bank of the Republic of Macedonia.	Yes	MOF NBRM	No changes planned.
54.	Banking Law (63/2000, 103/2000, 37/02, 41/02, 51/03)	Foundation, operation, supervision and termination of banks.	Yes	MOF	No changes planned.
55.	New Law on Saving Institutions	Establishment of rules on the operation of saving institutions.	No	MOF	Planned to be enacted by the end of 2003. Drafting process started.
56.	New Law on Transfer of Money	Establishment of rules and procedures for the transfer of money.	No	MOF	Planned to be enacted by the end of 2003. Drafting process expected to start soon.

	Law/ Regulation (Official Gazette number)	Coverage	English Translation	Responsible Agency	Status of the Law/Regulation
57.	Securities Law (63/2000, 103/2000, 34/2001, 4/02, 34/02, 37/02, 31/03)	The Law determines the types of securities, the manner of and conditions for issuance, trading and registration, identification and settlement of transactions in securities, manner and conditions for establishment and operation of the long-term securities market and the Central Securities Depository, as well as the status and powers of the Securities Exchange Commission.	Yes	MOF	No changes planned.
58.	New Law on Air Transport	Conditions and methods of transportation of passengers and goods in the internal and international air transport.	No	MOTC ACAT	Draft prepared. Planned to be enacted in 2004.
59.	Law on Road Transport 63/95, 15/97, 29/98, 7/99, 34/2000)	Conditions and methods of transportation of passengers and goods in the internal and international road transport.	Yes	MOTC	New Law on Road Transport is undergoing second reading at the Parliament. Planned to be enacted by the end of 2003.
60.	Law on Macedonian Railways (9/98)	Conditions and methods of transportation of passengers and goods in the internal and international railway transport.	No	MOTC	Draft of a new law prepared. Planned to be enacted by the end of 2003.
61.	Law on Catering and Tourism (23/95, 33/2000, 48/01, 20/02, 25/02, 48/02, 38/03)	The conditions and manner of performing catering and tourism services.	Yes	MOEcon	Drafts of new separate laws on catering and tourism have been prepared and went through the first reading at the Parliament.
62.	Law on Health Protection (17/97, 9/2000, 41/02)	Establishing the system of health protection, supply of health and health related services.	No	MOH	Amendments planned to be enacted by the end of 2003.
<u>INTELLECTUAL PROPERTY</u>					
63.	Law on Industrial Property (42/93)	Acquisition, exercise and protection of industrial property rights.	Yes	IPPO	Will cease to apply on December 31, 2003.
64.	Law on Industrial Property (47/02, 42/03)	Acquisition, exercise and protection of industrial property rights.	Yes	IPPO	In force from January 1, 2004. New amendments being drafted. Expected to be enacted by the end of 2003.

	Law/ Regulation (Official Gazette number)	Coverage	English Translation	Responsible Agency	Status of the Law/Regulation
65.	New Regulations on: Appellation of Origin; Trademark; Industrial Design; and Patent	Technical aspects of the industrial property rights.	No	IPPO	New Regulations planned to be enacted by the end of 2003. Drafting in process.
66.	Law on Copyright and Related Rights (47/96, 3/98, 98/02)	The right of authors, implementation and protection of copyright and related rights.	Yes	MOC	New amendments planned to be prepared by November 2003. Drafting group established. Initial draft prepared. EU expert expected to assist in the drafting from late September. Amendments expected to be enacted in spring 2004.
67.	New Law on Customs Measures for Protection of Intellectual Property Rights	Introduction of new customs measures for the purpose of protection of intellectual property rights.	No	MOF CA MOC IPPO	Government Decision establishes an obligation for the preparation of such law. No draft in existence.
68.	Criminal Code (selected articles) (37/96, 80/99, 48/01, 4/02, 16/02, 43/03)	Criminal aspects of the intellectual property protection.	Yes (only selected articles translated)	MOJ	Amendments passed the first reading of the Parliament and planned to be enacted by the end of 2003.
<u>BILATERAL COOPERATION</u>					
69.	Free Trade Agreement with the Republic of Slovenia (48/96, 100/02)	Free trade agreement.	Yes	MOEcon	No changes planned.
70.	Free Trade Agreement with the Federal Republic of Yugoslavia (59/96)	Free trade agreement.	Yes	MOEcon	No changes planned.
71.	Free Trade Agreement with the Republic of Croatia	Free trade agreement.	Yes	MOEcon	No changes planned.

	Law/ Regulation (Official Gazette number)	Coverage	English Translation	Responsible Agency	Status of the Law/Regulation
	(28/97, 51/02, 100/02)				
72.	Free Trade Agreement with the Republic of Turkey (83/99)	Free trade agreement.	Yes	MOEcon	Changes being negotiated by the expert group. Planned to be introduced in November 2003.
73.	Free Trade Agreement with the Republic of Bulgaria (83/99, 100/02)	Free trade agreement.	Yes	MOEcon	No changes planned.
74.	Free Trade Agreement with Ukraine (83/99)	Free trade agreement.	Yes	MOEcon	No changes planned.
75.	Stabilization and Association Agreement with the European Union (28/01)	Establishment of an association between European Union and Macedonia, including a free trade area.	Yes	MOFA	Not yet in force. Ratification of Finland and Belgium not completed.
76.	Interim Trade Agreement (39/01)	Part of the Stabilization and Association Agreement regulating trade relations between the parties. It started to implement in 2001.	Yes	MOEcon	Negotiations on agriculture in process.
77.	Free Trade Agreement with the EFTA Countries (89/01)	Free trade agreement.	Yes	MOEcon	Proposed changes in front of the Parliament for adoption.
78.	Free Trade Agreement with the Republic of Albania (47/02)	Free trade agreement.	Yes	MOEcon	No changes planned.
79.	Free Trade Agreement with Bosnia and Herzegovina (45/02)	Free trade agreement.	Yes	MOEcon	No changes planned.
80.	Free Trade Agreement with Romania (52/03)	Free trade agreement.	Yes	MOEcon	No changes planned.

Abbreviations and Acronyms used in the table:

ACAT – Administration for Civil Air Transportation

CA – Customs Administration

IPPO – Industrial Property Protection Office

MOAFWE – Ministry of Agriculture, Forestry and Water Economy

MOC – Ministry of Culture

MOE – Ministry of Environment and Spatial Planning

MOEcon – Ministry of Economy

MOEdu – Ministry of Education and Science

MOF – Ministry of Finance

MOFA – Ministry of Foreign Affairs

MOH – Ministry of Health

MOIA – Ministry of Internal Affairs

MOLSP – Ministry of Labor and Social Policy

MOTC – Ministry of Transport and Communications

NBRM – National Bank of the Republic of Macedonia

Annex 3 – Commercial Law Reform List

The CGCL Project has been mandated to compile a list of laws subject to review and possible revision as part of a broad-based commercial law reform. The list has been compiled, in part, as a result of *Company Law* drafting activities but also as a result of feedback obtained from contributors to the CLIR assessment, CGCL surveys, public hearings and roundtables. The fact that a law has been included in the list does not necessarily mean that the CGCL Project will be the prime contributor to review, policy development and drafting. The laws cover a broad range of subjects, some of which are in the domain of other USAID and other donor projects.

Laws Subject to Review as a Direct Result of Company Law Reform

- ***Securities Law*** – A drafting committee has been formed to revise the current *Securities Law*. Prime USAID input into the reform process will be spearheaded by the Financial Sector Project. During their review, the final text of the new *Company Law* will be reviewed to ensure that the securities legislation and the *Company Law* do not conflict. Where necessary Central Depository rules and regulations will be revised as part of the securities legislation review.
- ***Law on Obligations*** – The *Company Law* has been drafted to operate in accordance with the provisions of the *Law on Obligations*. The *Law on Obligations* is the central law governing commercial transactions in Macedonia. While its prime coverage relates to the rules respecting contracts, the Law covers a number of areas that are also dealt with in other laws including the draft *Company Law*. For example, both the *Company Law* and the *Law on Obligations* address issues of representation, agency, partnership, guarantees, assignment and limitation periods. Both laws must be carefully reviewed to ensure that the laws are complementary. In addition, the *Law on Obligations* also covers such diverse topics as pledge, securities, leasing, franchising and licensing. Aside from a compliance review with respect to the *Company Law*, the *Law on Obligations* will be reviewed as CGCL addresses other topics of a more general commercial nature following the passage of the draft *Company Law*.
- ***Law on Central Registry*** – Under the draft *Company Law*, the Minister of Justice must adopt an act within 60 days of the passage of the Law that sets forth the procedure for manual and electronic registration of companies including the form and content of the forms required for registration in the Commercial Register; the format of the electronic records; the manner of communication between the court and the Central Register; the electronic management of the Commercial Register; the format, rules and procedures including access rules respecting the electronic Commercial Register; and the creation of any databases necessary to facilitate the establishment of a one-stop-shop system.
- ***Labor Law*** – The *Labor Law* has yet to be overhauled to reflect the new market realities in Macedonia. Under the *Labor Law* employees are entitled to share in the earnings of the company¹. A similar provision is contained in the *Constitution*. However, there are no details with respect to how the profit

¹ Article 69

sharing must take place. Arguably, it should be set out in the collective agreement. However, unions argue that there is a mandatory entitlement to a profit distribution. In the absence of a clear provision, there is the danger that a court may decide that employees have an absolute right to share ownership and dividend distributions. The draft *Company Law* provides for the optional establishment of employee share ownership funds. There is no mandatory requirement for a profit distribution to employees. The *Company Law*, *Labor Law* and the *Constitution* must be reconciled in a manner that protects shareholder interests. A clear distinction must be drawn between minimum employment standards and shareholder entitlement.

- ***Laws on Value Added Tax/Profit Tax Law/Personal Income Tax Law*** – The draft *Company Law* stipulates the minimum financial reporting requirements. These reporting requirements must be complementary to the tax reporting requirements. The Ministry of Finance together with the USAID Financial Sector Project has provided an ongoing review during the *Company Law* drafting process to ensure that consistency is maintained between the accounting and tax reporting requirements. However, other issues may trigger a further review. For example, partnerships are taxed at the company level where in many countries partnerships are a flow-through vehicle where income tax is levied on the partnership proceeds at an individual partner level on a *pro rata* basis. If this is the agreed objective, the relevant tax laws must be reviewed and revised accordingly. The draft *Company Law* also mandates the implementation of a one stop shop system by the end of 2004. To do so, coordination of registration requirements and transfer of data protocols must be established between the Tax Authority and the Central Registry. A review of tax laws and regulations will be undertaken within 90 days of the passage of the *Company Law*.
- ***Law on Statistics/Law on National Classification of Activities*** – Companies must register with the Bureau of Statistics as part of the company registration process. Steps have been taken in the draft *Company Law* to simplify the information that must be provided by a company registering or amending its registration. For example, the scope of operations registration will be at a summary level to avoid the filing of laundry lists of approved activities. As part of the move to a one stop system, registration and transfer of information will have to be coordinated between the registration courts, the Central Registry and the Bureau of Statistics. Within 90 days of the enactment of the *Company Law*, regulations must be written that establishes the forms, procedures and data exchange protocols to facilitate a single registration procedure for all business related registrations.
- ***Laws regulating licenses*** – A complex array of business licensing requirements may apply to a particular business depending on its intended scope of activities. The Ministry of Economy is committed to reviewing all business license requirements as part of its commitment to move to a one stop shop licensing and registration system. Regulations must be written that will facilitate (to the extent possible) a single registration venue with the transfer of licensing information to the respective government departments responsible for the issuance of the particular license. It will not be possible to fully integrate this process as some licensing requirements are too specialized and complicated to be incorporated into a streamlined procedure. The Ministry of Economy must assess what licensing requirements may be streamlined and

then coordinate with the relevant Ministries to facilitate the establishment of common procedures, communication and data transfer protocols.

- ***Law on Courts*** – The *Law on Courts* establishes the Stip, Bitola and Skopje courts as the only authorized registration courts in the country. To expand the list of registration courts or to move registration responsibilities outside the court system requires an amendment to the *Law on Courts*. Any amendment to the *Law on Courts* requires Parliamentary approval by a supermajority. The current version of the *Company Law* avoids having to amend the *Law on Courts*. It limits the judge’s discretion when reviewing registration applications and requires the registration courts to transfer the data necessary to the Central Registry to enable the Registry to establish an electronic commercial register. Discussions are still underway as to the viability of having the offices of the Central Registry serve as the recipient of registration applications. A compromise may be to stipulate a transition period. Upon the expiry of the transition period, the registration function may be moved from the courts to the Central Registry. The *Law on Courts* will have to be amended to implement such a strategy.
- ***Law on Appraisers*** – The draft *Company Law* requires a company to obtain an independent appraisal in respect of any share purchase made using non-monetary contributions. The appraisal must be conducted using generally accepted international appraisal standards. There is no law prescribing the minimum appraisal standards nor is there an effective self-governing association of appraisers that can be relied upon to license appraisers and monitor adherence to international standards by licensed appraisers. The drafting committee anticipates that a law on appraisal will be enacted to support the appraisal requirements prescribed in the Law.
- ***Regulations for the Commercial Register*** – Under the current draft *Company Law*, the registration courts retain responsibility for the maintenance of the commercial register. The Central Registry is mandated to implement the electronic copy of the register but the law defines the electronic database with legal validity (in other words, the electronic database is defined as a valid and enforceable commercial register). The *Law* states that a unified, national register is to be created. This is in contrast to the current system where each registration court maintains its own manual register. Regulations must be written that clearly define the fields, format, method of entry and amendment, data query, data transfer, communication protocols between the courts, standards for entry of existing records, rules for resolving conflicts and missing data, data transfer protocols between the courts and the Central Registry, etc. Consequently, a new set of commercial register regulations must be enacted that deal with the unification of current data and the entry of new registrations and amendments.
- ***Regulations for Registration Forms*** – The interface between the courts and their clients – the businesses seeking registration – must be redesigned to facilitate both manual and electronic registration. This requires a review and revision of all existing registration forms.
- ***Criminal Law/Code of Criminal Proceedings*** – The Drafting Committee has coordinated its efforts with the working group that is preparing changes to the *Criminal Code*. These changes provide for additional penalties against executives of companies who have violated provisions of the *Company Law*. As well, the changes contemplated place criminal liability on the legal entity

and provide measures to trace and recover the proceeds of criminal activity between companies. To the extent necessary, we will review the *Criminal Code* to ensure that the changes discussed will, in fact, be incorporated.

Laws Subject to Review to Promote General Commercial Development

- ***Credit Bureau Law*** – Access to credit is an ongoing problem for Macedonian businesses, in part, because businesses are not well schooled in the art of preparing loan applications but also due to the high cost of borrowing. The cost of loans increase when there is no gauge to measure a business's track record in honoring its credit commitments. Macedonia needs private sector credit bureaus. However, these bureaus must be held accountable, adhering to strict data, data verification and procedural guarantees while at the same time serving the need to monitor and disseminate information on credit payment practices. A law should be drafted that specifies minimum credit bureau standards.
- ***Law on Collection Agencies*** – Businesses are not always well-suited to monitor and collect their receivables. In developed economies, businesses establish standards for receivables collection including when accounts will be outsourced for collection. Collection agencies can participate in collection prior to initiating legal default proceedings and can assist in the enforcement process and default proceedings have been initiated. Standards on such agencies should be established in Macedonia.
- ***Bankruptcy Law*** – The bankruptcy law is currently under review following an attempt to introduce negative changes without proper public consultation. The Financial Sector Project is the prime provider of technical assistance during this review. Apparent attempts to strip away priority rights of secured lenders and increase employee rights on dissolution could have seriously hampered creditor rights and dissolution procedures.
- ***Law on Central Registry*** – The Law is slated for revision in accordance with the *Company Law* reform. However, there are other issues which should be addressed. The costs of registering a small loan are too high. The Central Registry should consider lowering the fee from its current level of approximately \$40 USD. Overall, the combined costs of notarizing (approx. \$50 USD) plus registering can operate as a significant disincentive to providing micro-financing.
- ***Law on Contractual Pledge*** – This law was adopted on January 31, 2003. While for the most part sound, it has one serious flaw. It deems a pledge that has not been registered as not legal and binding. A more appropriate provision would be for an unregistered pledge to rank lower in priority to pledges that are registered. However, it should not be deemed illegal. At the least, this anomaly should be corrected.
- ***Law on Enforcement Procedures*** – The Court Modernization Project has been monitoring progress in the preparation of execution procedure reforms. In the Fall of 2003 a basic platform was proposed that would amount to less judicial involvement, greater independence for enforcement agents, improved public records and reductions in objections, appeals and interruption of procedures. The *Collateral Law* permits the use of self-help although there does not appear to have been a large move in that direction by creditors. It is essential to create a private execution option, create professional standards for

public and private enforcement officers, minimum debtor right standards, liability for misconduct in the execution process, clearly enumerated but not excessive categories of execution exemptions, performance incentives payable to the enforcement agent, standardized procedures and minimized interruptions to enforcement through court appeal. There are particular problems related to enforcement of real estate obligations. Current eviction laws exempt specified family members despite the default by the holder of title. There must be changes in eviction laws so that lenders can exercise their right to seize the property when default has occurred. In the absence of clear rights of seizure, the mortgage lending market will be inhibited.

- ***Law on Legislative Procedure*** – There is no formalized process of providing an economic cost/benefit or other impact analysis when submitting a draft law for Parliamentary consideration. More importantly, the degree to which public consultation will occur for a given law appears to be at the discretion of the body that proposes the law. While not purely a commercial law issue, consideration should be given to introducing a mandatory public consultation process as part of the law-making activities. The Ministry of Economy has identified the need to institutionalize a structured dialogue with the business community on existing legislation, policy development and preparation of draft laws. It has committed to formalizing a process that will provide for a minimum of a one month consultation period prior to moving forward with draft laws or regulations. However, this policy should be implemented government-wide. As well, there should be a built-in consultation process as part of the Parliamentary Committees’ consideration of draft laws.
- ***Law on General Administrative Procedure/Law on Administrative Disputes*** – The current rules respecting administrative procedure has the potential to politicize any administrative process. Appeal at second instance is ministerial. Consequently, the independence of any administrative tribunal or administrative process can be jeopardized by simply appealing to the Minister. For example, the Monopoly Authority’s decisions can be appealed to the Minister of Economy. As well, officials acting under administrative procedures are state officials. Establishment of competent administrative tribunals will be hampered since the salary structure is capped at non-competitive rates. The current state of administrative procedure has provided fodder for those opposed to moving company registration from the courts. The argument is that the court procedure is clearly set out and not subject to politicization. CGCL has argued to have a transition period embodied in the *Company Law* that will allow for amendment to the *Law on Administrative Procedure* and the eventual transfer of all company registration responsibilities to the Central Registry. If accepted, one of our top priorities will be to support changes in the *Law* that will allow for the de-politicization of administrative procedures.
- ***Constitutional Amendments*** – Due to constitutional constraints, administrative authorities are not empowered to apply sanctions to offending individuals or companies. This undermines authority in the tribunal (for example, the Monopoly Authority cannot impose sanctions) and creates inefficiencies in administrative procedure. An additional problem that has a direct impact on shareholder rights is the inability to engage in class action law suits. Without this capability, shareholders who challenge a company in court, for example, on a share buy-out arising from opposition to a fundamental change, may be paid a different amount for their shares than

shareholders in the same position but who did not participate in the court process. There should be a mechanism available whereby a court decision can be applied across a shareholder group without each shareholder having to be a party to the court challenge.

- ***Law on Financial Leasing*** – The CLIR review showed that stakeholders are generally satisfied with the leasing legislation. Dissatisfaction was expressed with respect to the Tax Authority and tax laws. Leases are currently overtaxed because the tax law and tax agents do not recognize that a lease-buyback operation is essentially a financial operation, not a series of sales. In practical terms, this means that transfer taxes and VAT are being charged twice in a lease-buyback operation, instead of only once. In addition, there was a complaint that tax agents do not understand the business side of such transactions or understand financial accounting sufficiently to effect accurate assessments. The result is that they overtax and seek excessive documentation. Leasing is a fundamental sector of a healthy economy. CGCL may conduct a further assessment of the laws and the procedures currently in place to determine whether further reforms, training and education are warranted.
- ***Law on Mediation and Arbitration*** - The Ministry of Economy in cooperation with the Ministry of Justice, NGOs and the European Reconstruction Agency intend to prepare a policy paper that will include a draft arbitration law by the end of March 2004. To increase demand side support for ADR, Southeast Europe Enterprise Development (SEED), a member of the World Bank's International Finance Corporation, has undertaken to launch business education seminars on the value of using mediation to resolve commercial disputes. In addition, the Ministry of Justice is exploring the introduction of formal mechanisms for the diversion of certain types of disputes to mediation. SEED is advocating implementation of a mediation model successfully employed in Slovenia that reportedly reduced the court caseload by 54%. CGCL will review the March 2004 draft arbitration law. In addition, activities will be coordinated amongst donors and Macedonian representatives to ensure that minimum standard mediation procedures are developed. The extent of CGCL participation in the development of these standards has yet to be determined.
- ***Law on Courts*** – Aside from amendments needed to support changes in the company registration process, CGCL will conduct an assessment of commercial adjudication. The objective is to determine whether a move back to a specialized commercial court is warranted or maintenance of a general court with streaming of commercial cases to particular judges would suffice. The assessment will also target commercial law training of judges that would be appropriate under either of the above options. If the Ministry of Justice were to decide to revert back to specialization, the *Law on Courts* would have to be amended to accommodate the re-organization.
- ***Law on Civil Procedure*** – The Court Modernization Project is working with the Ministry of Justice to assist it in developing case management models. One approach is to target certain profile cases for mediation early in the case proceeding. To engrain this practice, amendments may be required to the *Law on Civil Procedure*. In addition to the introduction of case management techniques, there is also a move to eliminate structural inefficiencies in the system. The very nature of the system is being changed from an historically

weak inquisitorial model to a stronger adversarial model. This will shift the burden of evidence and argument to the parties instead of leaving the judge responsible to search for evidence. Currently, there is no basis for a default judgment. If a party fails to attend a hearing, the normal course is simply to reschedule. Consequently, an offending party can delay proceedings endlessly. Revisions to the civil procedure rules will introduce default judgments so that non-cooperative parties to a proceeding will fail to attend at their own risk – not at the expense of the other parties. Businesses must have confidence that, in the event of a commercial dispute, courts can be relied upon to adjudicate in a fair, impartial and efficient manner. The inability of the court system to resolve commercial disputes operates as a significant deterrent to increased investment in Macedonia. CGCL does not anticipate having direct involvement in the reform of the civil procedure rules. It is expected that the Court Modernization Project will continue to be the prime technical assistance provider.

- **Trade Law** – CGCL has not reviewed the draft *Trade Law*. This is the domain of USAID’s WTO project. However, there may be certain areas where coordination will be necessary. For example, the concept of “small scope commercial activity” has been inserted into the draft *Company Law*. This is intended to apply to small income entrepreneurs. These persons would not register as businesses. Instead, they would register in their respective municipalities and would not be required to maintain trade books. It appears that the same persons are required to maintain trade books under the draft *Trade Law*. As well, the UNDP is providing assistance to the Ministry of Economy on the legalization of small traders engaged in the textile, food products and other street vending sales. The proposal is to open local registration offices where certificates would be issued to such street vendors. New regulations will define the extent of such vendors’ tax liability. There is potential overlap in the development of these programs. Regulations must also be developed to support provisions introduced into the *Law on Trade* in 2002 covering anti-dumping and countervailing duties.
- **Industrial Property Rights** – Protection of intellectual property rights requires specialization in the courts. Because of the unique nature of the problem, it is sometimes necessary to take urgent, preventive action such as the issuance of interim injunctions, seizure of goods pending a full hearing of the issue, extended authorization for repeated seizures of goods pending a full hearing of individual cases, etc. There must be amendments to the *Code of Criminal Proceedings* and the *Law on Litigation Proceedings* to allow for preventive actions within the judicial process. Further, judges, businesses and NGOs require training on rights and obligations under the law and the function of the Bureau for the Protection of Industrial Property.
- **Law on Insurance Supervision** – The GOM has recognized the need for further improvement in the supervision of insurance companies. The World Bank is currently providing assistance on drafting amendments to the *Law on Insurance Supervision* aimed at providing more efficient, adequate and timely measures for preventing under funding of liabilities and illegal operations by insurance companies. Local businesses will contract for insurance coverage if insurance is offered at reasonable rates for the protection of commercial and other risks but only if the businesses can be confident that insurers stand on a solid financial ground and have an established a record of processing claims

on an appropriate basis and within a reasonable timeframe. In turn, insurance companies that generate increased premium revenue may also have more funds available for future institutional investing. CGCL does not anticipate providing technical support in the insurance sector. But the project recognizes the need for adequate supervision of insurers and protection of policyholders and its potential impact on the development of commercial markets.