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USAID/EGAT-ILD COOPERATIVE AGREEMENT

N° EEM-A-00-03-00005-00

PROGRESS REPORT

January – April 2004

June, 2004



Instituto Libertad y Democracia

Av. Del Parque Norte 829
Lima 27 – Perú
Telfs.: 225-4131
Fax: 475-9559
E-mail: postmaster@ild.org.pe

18 June 2004

Mr. Timothy Mahoney
Cognizant Technical Officer
EGAT/PR/EMD
1300 Pennsylvania Av. N.W.,
Room 3.08-095, RRB
Washington D.C. – 20523-3800

Subject: USAID/EGAT-ILD Cooperative Agreement # EEM-A-00-03-00005-00

Dear Mr. Mahoney,

Please find attached two hard copies of our Progress Report corresponding to the activities carried out by the ILD throughout January – April 2004.

If you should require any further information, do not hesitate to contact us.

Sincerely,

Humberto Nadal
Administrative & Financial Manager

Enc.: Progress Report January – April 2004
cc.: Ms. Mercedes Eugenia – Program Officer
Office of Procurement

USAID/EGAT-ILD COOPERATIVE AGREEMENT

PROGRESS REPORT

January – April 2004

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I. NARRATIVE REPORT

This report describes the activities carried out between January and April 2004 under Cooperative Agreement No. EEM-A-00-03-00005-00. Details of our activities are given below:

ACTIVITY 1 – Establishing Training Center (s)

Although we spent months of extensive searching in different areas of Lima, and found a locale in Santiago de Surco, we eventually had to discard this option because of the landowner's lack of transparency in the contracting procedures. Therefore, we begun our search anew, and have found a very convenient building in San Isidro —with an area of 1,500 m² and the possibility of future expansion, if needed. Even though the cost is similar to that of the discarded locale, the contractual conditions are much more favorable. The conditioning of these offices is in progress and we plan to move in during the second half of July.

ACTIVITY 2 – Securing On-Going and Future Projects

With respect to our efforts to secure contracts and the corresponding funding for the Diagnosis, Reform Design and/or Implementation Programs, the following is a summary of the country-by-country results.

Egypt

- **ILD has completed the Reform Design stage and presented concrete proposals for reform.**
- **The proposal for both real estate and business reforms was approved unanimously by the Council of Ministers, and hence the Egyptian Prime Minister granted ILD the authority to prepare an action plan to implement this program immediately.**
- **ILD has presented an action plan (see **Annex 1: Action Plan for Pre-Implementation**), which includes the necessary actions to ensure approval of the reforms by Parliament, as well as a strategy to contract with a supplier consortium to help implement the reforms and finance the package.**
- **The reform program proposed by ILD was presented at three conferences and meetings. On Saturday 17 January, the proposal was presented to the Egyptian Prime Minister and Council of Ministers. On 18 January, the day of the main conference, we explained to senior representatives of Egypt's academic and business sectors the characteristics and advantages of the proposed formalization of enterprises and real estate, as well as the economic dimensions of formalization. Finally, on 19 January, we discussed the Implementation Action Plan with the Prime Minister.**

- There is an Egyptian presentation scheduled to take place in Washington DC on 15 June to present the program—for bringing extralegal real estate and businesses in Egypt under the rule of law—to the International Community. High-ranking Egyptian officials, private sector representatives, members of the People Assembly, high-ranking members of the US Administration, will be among the attendants. This presentation is expected to be the launching platform for the implementation of this program.
- For this latter stage of our program, ILD hopes to obtain the assistance of the governments of the USA and Norway, and, of course, from international organizations and private sector companies.
- USAID/Egypt has launched the Request for Proposal N° 263-04-023 for American consulting firms to execute a Financial Service Project (FSP) for Egypt, with the goal of promoting legal and procedural reforms that will allow banks and non-bank financial institutions to effectively use the most important types of secured lending, mortgages, and other forms of secure collateral.

With respect to the latter, ILD has expressed its concern to USAID/Egypt regarding overlapping with our project and pointed out the shortcomings of the RSP.

Haiti

Between the 1996 and 2000, the ILD carried out the Project for the Capitalization of the Assets of the Poor in Haiti, with USAID funding.

In the first phase, the project focused on the Diagnosis of extralegal real estate property, as well as on the Design of Legal Reforms for formalization of real estate assets. In the second phase, both the Diagnosis and the Legal Reforms were expanded to include the necessary reforms for the capitalization of both real estate and small enterprises in Haiti.

Through this Project, the ILD exposed over US\$ 5 billion of dead capital owned by Haiti's poorest. In fact, findings show that 82% of the population holds its real estate assets extralegally and 68% of entrepreneurs operate extralegally.

In addition, the ILD identified the main obstacles generating this extralegality, as well as the common extralegal practices used to substitute legal mechanisms. With all this information, the ILD drew up a Draft Law for the implementation of the "National Program for the Capitalization of the Poor in Haiti".

Both this program and the Draft Law that created it were presented to a Presidential Commission for the Formalization of Property appointed by President Rene Preval (and later ratified by President Jean-Bertrand Aristide), and the corresponding cabinet members.

The last time the results of the Project were officially presented in Haiti was in December 2002. The continuous deterioration of the political situation of the country and the violent acts that went along with this phenomenon, prevented ILD from

continuing the ongoing work of creating the national consensus needed for the approval of the law and the implementation of the Capitalization Program.

After the violent events that ended with the resignation of President Aristide, and the creation of an interim government lead by Prime Minister Gerard Latortue, our Project has renewed interest from the Haitian business sector, the Haitian government itself, and the US Administration.

In March of this year, a Haitian delegation comprised of government and private sector representatives headed by Haiti's Minister of Finance, Henri Bazin, visited the ILD in Lima. As a result, Minister Bazin clearly stated the will of his government to go ahead with the Project, and officially asked the ILD for an Action Plan for the implementation of the "National Program for the Capitalization of the Poor in Haiti".

ILD has prepared a draft Action Plan that will be presented to the Haitian Cabinet in Port Au Prince on June 18, at the request of Prime Minister Latortue. (See the draft of the Action Plan for Pre-Implementation in **Annex 2**.)

Parallel to these events, in order to earn the necessary foreign backing for this plan, the ILD has carried meetings with IDB-MIF representatives, and most recently a complementary meeting with officials of the US State Department, US Treasury Department, and USAID officers in charge of Haiti.

In every case, the re-launching of ILD's Program has been cheerfully received, since it is perceived as a valuable tool in the fight against poverty, at a time in which there are not many ideas on how to help Haiti. Nevertheless, to succeed, we need to secure the total support and the official commitment from the government of Prime Minister Latortue.

With respect to the Reform Design project, the ILD will need a couple of months to update it since it is already over two years old.

Mexico

The grant for the Mexican government to carry out the ILD's Business Reform Program has been approved by the MIF Donor Committee. The ILD had a crucial role in securing this funding, coordinating with both the Mexican government and the US Administration.

What needs to be done now is define the organization within the Mexican government that will contract with the ILD and manage the project, on behalf of the President, outside of the bureaucracy.

The ILD is actively coordinating with the Secretary of Finance and the Presidential Office to help organize the running of the project, as well as to ensure that the Mexican government secures the funds for the real estate component of the proposal.

With respect to the initiation of the project, the Mexican government has decided to bring on the Treasury and Finance Secretaries to participate in the project so that it has the necessary funding, as well as political and governmental support. This means that the project will probably be moved from SEDESOL to a new place, which has yet to be formed. In addition, the project will probably be arranged under a fiduciary agreement. This would isolate it from the bureaucracy and bring it closer to the President. Due to these changes, the signing of the agreement between the Mexican government and the ILD has been somewhat delayed.

As mentioned, a fiduciary agreement, especially designed for this project (financed by the Mexican government), has emerged strongly as the most appropriate mechanism. BANOBRAS (the State bank) has been tasked with the preparation of the agreement. The Mexican government is eager to begin the project as soon as possible.

We have an ILD team ready to start the Project as soon as we sign the agreement with the Mexican government. In the meantime, we continue to collect and update information on Mexico.

Honduras

Upon President Ricardo Maduro's request, Mr. Vicente Williams Agasse, First Vice President of Honduras, has requested the cooperation of the Multilateral Investment Fund (IDB - MIF) to finance the execution of ILD's Reform Design Program. Although the ILD has a work plan to help the government secure the required grant, the MIF has yet to respond.

Tanzania

The ILD proposal submitted to the Government of Tanzania is already being processed by the Norwegian government, who will be providing the necessary funding. As mentioned in our previous report, an ILD team traveled to Tanzania to carry out the initial assessment required to present the ILD program to the Government of Tanzania. In February, an ILD mission led by Manuel Mayorga made a presentation on our proposal to President Mkapa and his entire cabinet. As a result, President Mkapa expressed his full commitment to have the ILD undertake the Diagnose and Institutional Reform Programs in Tanzania.

With regard to financing, since the Norwegian government had expressed its will to help finance this project, the Government of Tanzania sent a letter of application to the Norwegians in March.

This letter is currently being processed by the Norwegian government, and ILD is doing appropriate follow up to speed things up. The grant agreement with the Government of Tanzania, authorizing the hiring of the ILD, will likely be signed in July.

Ghana

President Kufuor's interest in the ILD programs remains strong. His government is in the process of defining who will be in charge of the program, and it continues to work closely with the ILD. We expect the decision to be made in the coming weeks, at which time we will move forward with the discussions of ILD's proposal with the designated political counterpart. Once we have agreed on the terms, we shall submit our proposal officially to President Kufuor's government. The Government of Norway has also expressed its willingness to fund this project.

Nigeria

The ILD proposal to the Nigerian government was discussed with official government counterparts. Once these discussions were finalized, we officially submitted our proposal to the Government of Nigeria. As in the case of Tanzania, the Government of Norway has expressed its intention to provide funding for the project, understanding the strong social and economic impact the ILD's programs will have on Nigeria. The Government of Nigerian is going to submit the proposal to the Norwegian embassy in Nigeria immediately.

Pakistan

Between 17 and 23 February, ILD conducted an initial assessment and an Awareness Building campaign in Pakistan. An ILD mission traveled to Islamabad to carry out intensive research to obtain necessary information to present our program to the government. With the findings in hand, the team led by Hernando de Soto met with President Musharraf, the entire cabinet, and leading army officers. This allowed the ILD to openly discuss its ideas and the application of its program in Pakistan with government officials.

The outcome of these meetings was that President Musharraf asked the ILD to design and implement a Reform Program that will allow the extralegal sector to be incorporated into the legal sector. The ILD is currently designing the requested proposal.

At the same time, the Government of Pakistan is deciding who will manage the project politically on behalf of the President.

Guatemala

In response to the interest expressed by President Oscar Berger's government —through Mr. Harris Whithbeck, High Commissioner for Governmental Reform—, we developed an initial assessment and Awareness Building campaign for Guatemala.

Accordingly, an ILD team visited Guatemala in April, and after a week of intensive research, it prepared a preliminary report, which gave an indication of the root causes of the extralegal sector and clearly showed the enormous stock of dead capital held by the poor of the country. The findings were presented to President Berger and his entire cabinet by Mr. De Soto during a three-hour meeting on 27 April. In addition, the following day, Mr. De Soto spoke at the annual meeting of ENADE (National Gathering of Businessmen), attended by a group of 800

managers from all over the country, to further increase awareness of ILD's assessment. (See **Annex 3** for details.)

As a result of these efforts, President Berger has requested that we submit a proposal to conduct a Diagnosis and the Reform Design in Guatemala. We have submitted our proposal and it has already been approved by the Government of Guatemala. With respect to financing, the Norwegian government has agreed to fund the cost of this project.

Ethiopia

We received an invitation from Prime Minister Meles Zenawi of Ethiopia to visit his country in May. ILD organized an initial assessment and Awareness Building campaign, and an ILD team visited Ethiopia from 19 to 30 May to carry out its initial research and meet with senior government officials.

Mr. de Soto presented the team's findings to the Prime Minister on 27 May, and the Prime Minister subsequently requested a proposal in order to continue discussions with ILD. In addition, the ILD team met with the US Ambassador and the USAID Mission Director to discuss the possibility of obtaining financial support for the project.

(See **Annex 4** for some of the articles published on ILD's Awareness Building efforts in the aforementioned countries.)

ACTIVITY 3 – Awareness Building

Interviews, Presentations, and Conferences

Following with the communication and diffusion of our programs, we have participated in the following:

- USAID Conference: Asset Building for Sustainable Livelihoods, held on Washington DC on 14 January.
- World Economic Forum Annual Meeting, held in Davos, Switzerland between 20 and 25 January.
- The 2004 Albert H. Gordon Lecture, organized by Harvard University, was held in Boston on 19 February.
- Roundtable Congressional Hispanic Caucus, organized by the Mercatus Center at George Mason University. This event was held in Philadelphia on 20 February.
- Conference "Building Dynamic New Prosperity in the Gulf Region through Global Cooperation: Opportunities & Challenges", organized by Zayed University, was held in Abu Dhabi, Arab Emirates between 22 and 23 February.
- The 19th Economics Symposium, organized by Gonzaga University, was held in Spokane, U.S.A., on 22 March.

- Accenture International Utilities and Energy Conference, organized by Accenture, was held in San Diego, USA; between 21 and 24 March.
- 2004 PHARMA International Section Annual Meeting, organized by Pharmaceutical Research and Manufacturers of America, was held in Palm Beach, USA, between 22 and 26 March.
- GSC Partners 2nd Annual CEO's Conference, organized by the GSC Partners, was held in the Bahamas between 28 and 30 March.
- The State of Global Trade, organized by FORBES Magazine, was held in New York on 15 April.
- Annual Conference organized by the University of Monterrey, was held in Monterrey, México, on 19 April.
- Conference "Competitiveness and Sustainable Development", organized by FUNDESA, was held in Guatemala City, Guatemala, on 27 April.

(See **Annex 5** for some of the articles published on these events.)

Awards and Recognition

- The ILD received the **2004 Templeton Freedom Award** from the Atlas Foundation in the category of Free Market Solutions to Poverty. This award is given annually to the best poverty reduction proposals formulated by research institutes around the world. Specifically, the prize is in recognition of our most recent proposal for property formalization in Egypt.
- The **2004 Milton Friedman Prize for Advancing Liberty** given by the Cato Institute every two years has been awarded to Mr. Hernando de Soto. Selected among hundreds of nominees, this is in recognition of Mr. De Soto's contributions to the understanding of freedom and the implementation of reforms to bring freedom to the places where it is most needed.
- Mr. Hernando de Soto was included in *Time* magazine's prestigious **Time 100 list** of the most powerful and influential people in the world. Mr. de Soto was named in the category of "scientists and thinkers", who have "shaped how we see the world and ourselves". He and President Luiz Inácio Lula da Silva of Brazil were the only two Latin Americans on the list. In addition, De Soto and Jeffrey Sachs are the only economists on list.
- Mr. De Soto was deemed one of the most prominent economists of 2003 in the International Monetary Fund's *Finance & Development* magazine. This was in recognition of his innovative theory for converting dead capital owned by the poor into valuable assets, thereby generating wealth and prosperity for all.

(See **Annex 6** for the press releases on these awards.)

Other Dissemination Activities

ILD has found that the information provided on the ILD website not only introduces interested parties to the basic concepts underlying the ILD's work, but it provides additional

information to and reinforces the concepts discussed at awareness building activities. Moreover, our general website statistics show an increase in the number of site visitors from a country where awareness-building activities have been carried out. In this connection, our statistics also show that visits to our site increased markedly after the ILD and Mr. de Soto received the aforementioned prizes and recognition.

With respect to work on our site during this time period, aside from adding pages and or links to information on the prizes received by ILD and Mr. Hernando De Soto, we have added two more versions of Chapter 1 of *The Mystery of Capital*, (Korean and Greek) and will soon be adding the Mongolian version. The book has now been published in 22 countries and is available in 14 languages. Chapter 1 is available on our site in 13 languages, and it will soon be 14 or 15, since the Turkish version is almost ready.

Regarding the number of visitors we have had during this period, overall, hits per month increased from an average of 6,609 visitors —from September 2003 through to the end of December 2003— to 10,347 per month —from January 2004 through to the end of April 2004. Hits per day during this same period increased from 215 to some 345. These figures reflect both the success in ILD general awareness building activities and the publicity received from the aforementioned awards and recognition.

Due to the aforementioned increase in the number of visitors to our site, we have decided to upgrade the entire website in order to allow visitors to obtain more information about our programs. In other words, it will mostly be oriented to serve as an Awareness Tool, especially for by government officials around the globe. We expect to have our redesigned website up by July.

Collaborative Work with other Institutions

- In January 2004, ILD signed an agreement with the **International Republican Institute (IRI)** to promote the adoption of policies for integrating the poor of Latin America into the market economy and for establishing legal property rights over their assets (see **Annex 7** for a copy of the agreement). Accordingly, work is currently being conducted to develop the corresponding work plan, as well as to organize a seminar in Lima for political players of different parties. ILD will be providing trainers and technical consultants to interact with political parties and civil society groups at this seminar.
- On 17 February, the Inter-American Development Bank's **Multilateral Investment Fund** launched a program to promote effective property rights as a tool for development in Latin America and the Caribbean, stressing the importance of property laws in the lives of millions of people who work in the informal sector. For this, the plan is to have the ILD work in partnership with the MIF to implement property-rights programs throughout the aforementioned region.
- Top ILD officials have participated in a series of meetings with members of the **World Bank - African Region**. The purpose of these meetings was to explore areas where work could be conducted together. At a subsequent meeting in Washington DC with World

Bank President James Wolfensohn, both institutions agreed to sign an **Memorandum of Understanding** to undertake joint activities in Africa. The initial scope of the work will be oriented towards **Madagascar, Ghana, and Tanzania**. The aforementioned agreement will be revised in twelve months to identify areas of further cooperation.

- On 12 April, top ILD officials met with a team from the **International Finance Corporation (IFC)** led by Mr. Peter Voycke. During the meeting, we explored the possibility of doing joint work in microfinance and other areas of mutual interest. We have agreed that teams from both institutions will work together to organize a workshop in which the ILD and the IFC will present their work in order to identify specific areas of collaboration. During the first preparatory meetings held in Washington DC on 29 April, many areas of potential collaboration were identified. We are planning the workshop for July in Washington DC to further explore other possibilities of collaborative work.

ACTIVITY 4 – Conducting Training Activities for Strategic/Priority Countries

Training ILD Staff

In close relation to the programs explained in Activity 5 below, our most experienced personnel is updating and fine-tuning all of our procedures in order to be able to produce accurate and useful manuals. These manuals, in turn, will be used to prepare the training material.

With respect to distance training, we have been looking into a program developed by the Francisco Marroquin University of Guatemala that is specifically designed for long distance learning/training. Considering that most —if not all— of our trainees are from abroad, this could be a very useful tool to reduce the stay of our trainees in our Lima headquarters. In addition, the program would be very helpful in new training programs per se.

We are in the process of hiring a training director who will be responsible for running this area of the ILD. Although our most experienced personnel will be directly involved in part of the training, the idea is to standardize the training so that professional teachers can do it in the future.

We calculate that the entire training program should be launched as soon as our new Lima headquarters are operative —approximately this July.

ACTIVITY 5 and 6 – Improving and Adapting Products and Services, and Expanding Delivery Capacity

Adapting ILD Programs (Diagnosis, Reform Design, Implementation) for Massive Use
ILD is currently redesigning its processes and organizational aspects in depth in order to allow it to expand its operations quickly and efficiently. The entire ILD management team

and key personnel, with support from two specialized consulting firms based in Boston (Monitor and Dialogos), are helping to carry out the redesign work.

The work has been divided into 4 major sections:

- 1) Knowledge mapping
- 2) Analysis of ILD's organization, sources of knowledge, and work distribution
- 3) Planning (strategy definition)
- 4) Implementation of action plans

Estimated time for the overall redesign work is approximately 6 months (May through to October). The first stage entails an in-depth knowledge mapping exercise, identifying a number of specific activities to do on 3 key fronts: hiring, contracting and training. We should complete this mapping exercise by mid-June.

The second stage involves the immediate development of the specific activities for hiring, contracting, and training identified above (aimed mainly at defining organizational requirements, developing required requests for proposals, and updating ILD manuals). In parallel, strategic decisions on the 3 key fronts (pace of hiring, initiation of the bidding process, and the training program setup) will be discussed and decided upon. This stage is scheduled to be over by the end of July.

The third stage, scheduled to take approximately until October, consists of the full deployment of the strategies defined above: organizational expansion through hiring roll-out; work outsourced to selected potential/actual contractors; and knowledge transfer through accelerated training courses.

In addition, the top management organizational model should be finally established around specific objectives to ensure optimal performance. Key performance indicators should be obtained periodically thereafter to measure effectiveness of the strategies put in place.

Organizational Structure and New Staffing

In order to manage the challenge that increased demand poses and to respond to our new organizational structure effectively, we have hired three new members to join our Management Committee: a Chief Economist (CE), a Chief Financial and Administrative Officer (CFAO), and a Chief Operations Officer (COO).

We have also hired three new professionals with ample experience in legal reform for our core ILD team as part of the process of rebuilding our structure to meet the increased demand for our programs.

Building a Research Agenda

We held brainstorming sessions and discussions in order to identify and select research projects that would further improve the reforms ILD proposes to our client countries. In

addition, we discussed and identified methodologies to measure the potential economic impact of ILD reforms. The following is a list of the components of the new research agenda:

1. To develop a macroeconomic model to simulate the impact of proposed ILD reforms on the economic growth and welfare of client countries. In order to build this model, we need to gather information from a number of countries with a wide array of variables so as to better capture the potential impact of ILD's proposed reforms.
2. To analyze the impact of ILD reforms to formalize property implemented by the El Salvador Government since 1992. This study includes an analysis of property formalization, as well as a survey to identify their impact at the household level.
3. To identify successful government intervention in the financial market to encourage sustainable credit to newly formalized property titleholders. To identify potential barriers that would obstruct this.
4. To analyze the evolution of the mortgage market in a sample of developed and developing countries to clearly identify the main legal and institutional reforms needed to promote an efficient and active mortgage market.

**ACTION PLAN TO IMPLEMENT
“THE NATIONAL PROGRAM FOR THE CAPITALIZATION OF
THE POOR IN EGYPT”**

(To integrate the extralegal economy into mainstream economic activity)

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III.2 Design and Execute a Communications and Outreach Campaign to Facilitate the Approval of the Draft Law and Obtain Financing

III.3 Identify and Determine Options to Establish and Contract the Execution of the Formalization Processes, as well as the Design, Setting Up, and Operation of the Record Keeping and Information Systems

III.4 Draft a Detailed Implementation Plan, Budget, and Financial Proposal for both PAP and the Capitalization Program

ACTION PLAN TO IMPLEMENT “THE NATIONAL PROGRAM FOR THE CAPITALIZATION OF THE POOR IN EGYPT”

(To integrate the extralegal economy into mainstream economic activity)

I. SUMMARY AND INTRODUCTION

This Action Plan lays out the actions and decisions required to carry out the implementation of the **National Program for the Capitalization of the Poor in Egypt** (the **Capitalization Program**), the primary objective of which is to integrate the extralegal sector into the nation’s mainstream legal economy.

Egypt’s extralegal economy employs 8.2 million people —about 40% of Egypt’s workers— and represents about US\$ 248 billion of assets (businesses and real estate). If this extralegal economy were to be brought under the rule of law, it is estimated that Egypt’s GDP per capita growth rate could almost double five years after the date the proposed reforms have begun to be implemented.

Such impressive growth, however, will always be out of the extralegal sector’s reach for one extremely significant reason: Because its denizens work outside the law, they lack the three basic legal tools that generate wealth: organizational forms to divide labor in house and raise productivity; records as well as standard rights and obligations to contract with unfamiliar parties in Egypt’s expanded market allowing them to specialize further and gain economies of scale; and property rights to capture capital.

Why do so many Egyptians operate and hold their assets outside the law? Two simple reasons: The legal system costs too much for most citizens to enter, and two, some basic institutions are missing. To open a small bakery, for example, takes more than 500 days of navigating bureaucracies and costs the equivalent of 27 months work at a minimum salary; to convert a sandy piece of land into a commercially legal vehicle can take more than 10 years of red tape: to fight off the demolition of an extralegal construction can take up to six years of judicial and administrative battles. Not paying a loan secured by checks in a timely fashion can earn between 6 and 36 months in jail, not to mention the loss of a home and roots in the community. To do business in Egypt, the poor must deal with 56 government agencies, 300 dispersed pieces of legislation, government inspections that are repetitive and overlapping, and no enforceable standard accounting principles.

The GOE can turn this entire situation around by formalizing the most important assets of the poor: their **real estate** and their **businesses** — which is the very purpose of the Capitalization Program.

To launch and carry out the Program successfully, however, two things are necessary: the appointment of a political authority responsible for the Program and an organization to carry it out. The **Prime Minister** has already taken the decision to be the political head responsible for the Program. With respect to the organization, the 5-volume study developed by the Minister of Finance, ECES, and ILD proposes a specialized, independent, and fully empowered body provisionally named the **Public Authority for the Capitalization of the Poor (PAP)**.

PAP would implement the following 4 types of mechanisms contained in the Program:

a) **Mechanisms to facilitate legal entry and exit of businesses:**

- A New Business Public Registry (NBPR) that will administer a unified, simplified, and low-cost system for the incorporation, registration, and licensing of companies and single person businesses¹.
- Limited liability status for single person businesses so that citizens can partition their assets for multiple purposes.
- Low cost procedures to exit the market legally and thereby allow entrepreneurs to quickly begin new businesses and maintain updated registries.

b) **Mechanisms to facilitate the legal operation of businesses:**

- A specific program to improve regulations and simplify legal business procedures.
- Simplified labor and social security procedures.
- A special commission to receive and process complaints and suggestions from citizens, thus ensuring both the correct application of the reforms and continual improvement through feedback mechanisms.
- An easily accessible system of standard accounting principles and rules so that all Egyptian economic agents speak the same language .
- A simplified tax payment regime that can be adopted voluntarily by businesses registered in the NBPR, making it less costly —and more secure and predictable— than operating outside the law.

c) **Mechanisms to promote business expansion:**

- A public Registry of Pledges.
- Simplified procedures to foreclose pledges.
- A service for certifying signatures and protesting documents in order to reduce transaction costs.
- A special judicial system to improve business dispute resolution mechanisms.
- A conciliation and arbitration center as a private alternative for improving business dispute resolution mechanisms.

¹ The objective of the reforms is to spur the formalization of the majority of the extralegal businesses in the country. Nevertheless, for operational reasons, the proposed law stipulates that this new system would be applied only to businesses with less than US\$ 25,000 in capital. This limit should be revised in such a way to allow more firms to be formalized, as the reform process progresses.

- A business information system.

d) Proposed mechanisms to promote **real estate formalization**:

- A comprehensive system for massive formalization.
- A New Real Estate Public Registry (NREPR) that will run a geographically based real folio registration system for defining ownership efficiently.
- Simplified procedures to register real estate assets transactions (e.g. sales, leases, mortgages, and subdivisions, among others).
- Simplified procedures to foreclose mortgages.
- The use of a special judicial system and a conciliation and arbitration center to resolve real estate disputes.

PAP needs to be given all the faculties of *ius imperium* necessary to execute the Capitalization Program. The task of allowing the poor to capitalize their assets and then integrating them into the economy is a revolutionary act that can be accomplished only if the highest levels of decision making in the country are behind it.

Nevertheless, before putting PAP in place and before the implementation of the Capitalization Program can begin, the GOE would need to carry out a number of **pre-implementation tasks**. To that end, we propose **the immediate creation of an Interim Commission for PAP (ICPAP) and the designation of its Chief Executive Officer (CEO)**, who must be a top notch senior professional with the Prime Minister's total support and armed with the executive powers necessary to carry out and concretize the pre-implementation tasks. Primarily:

1. To fine-tune the Draft Law, build consensus for its objectives, and obtain its approval by the pertinent authorities;
2. To design and execute a communications and outreach campaign that would facilitate the approval of the Draft Law as well as the support and funding needed for the implementation of the Program;
3. To identify and determine options to establish and contract the execution of the formalization processes, as well as the design, setting up, and operation of the record keeping and information systems;
4. To draft a detailed implementation plan, along with a budget and a financial proposal, which includes:
 - The procedures to be applied for the implementation of the proposed reforms;
 - The infrastructure required (e.g. technological services, personnel, and facilities); and
 - The promotion and communications activities during the implementation process.

We estimate that these four pre-implementation tasks would take 12 to 18 months to complete.

II THE PUBLIC AUTHORITY FOR THE CAPITALIZATION OF THE POOR (PAP) AND THE INTERIM COMMISSION (ICPAP)

II.1 PAP: A Specialized, Independent, and Fully Empowered Organization to carry out the Capitalization Program

Egypt does not have an organization designed to promote the legal entry, operation, expansion, and exit of enterprises operating extralegally, especially those of the poor. Consequently, the gains in productivity, economies of scale, and the conversion of the assets of the poor into capital remain out of reach. Each of the 56 government entities that affect the economic life of the poor has a separate specific goal, such as collecting taxes, ensuring compliance with health standards, registering property, etc. Not one is charged with changing the *status quo* or seeing economic growth from the point of view of the poor. None of these 56 agencies has the mandate to minimize the prohibitive transaction costs the poor face, to create appropriate legal vehicles for them to organize themselves productively, to give them accessible property rights to obtain credit, investment, and accumulate capital. No single entity within the Egyptian legal system is responsible for making it irresistible for the poor to cross over into the formal sector.

The GOE, therefore, needs to create a specialized, independent, and fully empowered body to spearhead this formalization process: the **Public Authority for the Capitalization of the Poor (PAP)**.

A specialized body: The main task of PAP is to focus fully on the implementation of the Capitalization Program and most of the reform proposals—and nothing else. PAP will have a far-reaching agenda—from overseeing business and real estate formalization, the recording of pledges and mortgages, the reduction of obstacles, regulatory improvement, standardization of rules, the implementation of business information systems to continual research on how the poor can be more quickly and efficiently brought into the legal framework, the *sine qua non* for economic growth.

An independent body: Major reforms tend to stir up vested interests and pernicious old bureaucratic habits, and it is, therefore, necessary to ensure that reformers are protected from defenders of the *status quo* watering down the strong initiatives we are proposing. The ILD's experience in other countries, such as El Salvador and Peru indicates that to avoid having the reforms neutralized, a specialized organization must be created. Independence from existing bureaucracies is crucial—private, such as the Institute for Liberty and Progress (under the tutelage of the First Lady of El Salvador), or public, such as the Commission for the Formalization of Informal Property (under the Minister of Justice, in Peru).

A fully empowered body: Because the task of allowing the poor to capitalize their assets and integrating them into the economy is a revolutionary act that can be accomplished only if the highest levels of decision making in the country are behind it. It is essential that PAP have this kind of political support because it must change the *status quo* and enforce the application of the reforms in governmental bureaucracies that have different agendas and will continually try to neutralize the new measures. In addition, it must be able to quickly and effectively adapt to the changing needs of the reform process.

It is with these three characteristics in mind that PAP is created in the Draft Law² as a Public Authority under the leadership of the Prime Minister. In addition, it will have a Board comprised of three specialists and six Ministers belonging to the public entities whose competencies will be most affected by the reforms or those that will frequently interact with the PAP most frequently (such as, the Minister of Finance, the Minister of Justice, the Minister of Trade and Supply, et al).

The Draft Law empowers PAP with all the faculties of *ius imperium* necessary to execute the Capitalization Program and stipulates that all existing public entities shall participate in the Capitalization Program —under the administrative responsibility of the head of the entity— assisting and providing PAP with the information, documentation, and data necessary to implement the program.

For example, in order to ensure that its objectives are fulfilled, PAP shall be able to issue directives and regulations that must be followed by both private agents and public officials. When the directives must be applied by other government entities, the Prime Minister must personally approve them so that they have greater coercive force. Likewise, the Draft Law grants PAP the authority to directly access the information in the current public registries, as well as to train, evaluate, and dismiss the public officials of other government entities under its competency.

To achieve its objectives without any constraints, PAP shall be governed exclusively by the provisions of its law and be economically and financially autonomous; shall have the flexibility to contract the necessary personnel and services; and shall be empowered to conclude agreements and contracts with national or international specialized institutions.

PAP has been organized in such a way that it is able to respond effectively to the needs of the Capitalization Program. To that end, the Board is the highest political authority of PAP, and the Executive Committee will be the highest managerial authority —formed by PAP's General Director (designated by the Prime Minister), who presides over it, and the Directors of PAP's Directorates.

² The Draft Law was designed and submitted to the Minister of Finance by ECES/ILD in August 2003 and to the Prime Minister in January 2004.

PAP has the following Directorates responsible for putting the proposed reforms into operation:

- The **Directorate of Formalization** whose Director is empowered to manage the Formalization System (for business and real estate assets);
- The **Directorate of Registration** whose Director is empowered to manage the Registration System (including the NBPR, the NREPR, and the Registry of Pledges);
- The **Directorate of Pro Capitalization** whose Director is empowered to participate in the creation of an effective System of Accounting Principles and Rules; as well as to manage the Business Information System; the Regulatory Improvement and Administrative Simplification System; and the Signature Certification and Document Protest Service;
- The **Directorate of New Projects** whose Director is empowered to design and execute projects to implement the complementary reforms needed to consolidate the Capitalization Program; and,
- The **Directorate of Administration** whose Director is empowered to manage matters concerning accounting and budget, as well as the organization and administration of human, material, and financial resources of PAP, and provide support to the Special Judicial System and the Conciliation and Arbitration Center.

II.2 ICPAP: The Interim Commission to carry out the Pre-Implementation Tasks of the Capitalization Program

PAP will only become operational when the GOE has decided on how to implement the Capitalization Program and once the Draft Law has been approved. The GOE will need to take a number of decisions and measures to make this possible, the most important of which will be to establish an **Interim Commission (ICPAP)** with the mandate to execute the pre-implementation tasks needed to carry out the Capitalization Program.

ICPAP, which should be created by way of a Prime Ministerial Decree, shall be the designated interlocutor for the Capitalization Program before the public administration and the private sector. ICPAP will be responsible for carrying out the pre-implementation tasks, as described in Section III below. ICPAP, therefore, should be empowered to contract — with the fewest legal restrictions— the goods, the consultancy and advisory services, as well as all the other professional services required for the pre-implementation tasks. (See Section III for more details.)

ICPAP should have a Chief Executive Officer (CEO) and a staff of 6 to 8 Egyptian upper-level professionals, specializing in:

- Law (registration law, property rights, commercial law, administrative law);
- Economy (economic analysis);
- IT/Systems (registration systems, information databases);
- Surveying and mapping;
- Communications (with good ties to the media and able to design messages specially targeting the extralegal sectors); and,
- Administration of projects and organizations.

ICPAP shall be the base for the executive teams to direct PAP, which will ensure the continuity of the process and that maximum benefits are obtained from the experience gained. Consequently, its CEO must have the full support of the GOE and be empowered to interact with Ministers, members of the People’s Assembly, and upper-level authorities.

ECES/ILD shall provide ICPAP with permanent advisory services and assistance on technical aspects and institutional policies throughout the pre-implementation phase.

ICPAP shall have a specific budget—in the order of an estimated US\$ 800 thousand to US\$ 1 200 thousand per year, according to our experience—to allow it to cover the following *pre-operations costs*³:

- a) Salaries for the Egyptian managerial and technical staff at ICPAP.
- b) ICPAP operating expenses (rental of offices and equipment; expenses for logistics local transportation; and other expenses).
- c) Consultancy services and other similar services.
- d) Expenses to cover costs of the publicity campaign for disseminating information on the benefits of the Capitalization Program, an essential component of the process.

The Prime Minister could also set up an Advisory Committee made up of Ministers of the sectors closely related to the reform so as to help him analyze and evaluate actions and decisions proposed by ICPAP.

III. THE PRE-IMPLEMENTATION TASKS

ICPAP’s pre-implementation tasks include:

III.1 Fine-Tuning the Draft Law, Building Consensus for its Objectives, and Obtaining its Final Approval by the Pertinent Authorities

Having the Draft Law approved is a *sine qua non* for the implementation of the Capitalization Program. Consequently, ICPAP should prepare and execute a strategy to obtain the approval of the law. This strategy should include:

³ This budget estimate does not include ILD consultancy costs.

- Adapting the current Draft Law to the policy definitions of the additional functions and special powers with which PAP and its CEO will need to be granted, as well as to the different options for carrying out the reforms and the provision of infrastructure to be defined by ICPAP.
- Preparing a plan for the approval of the Draft Law, including the legal and economic arguments to build consensus for support ⁴.
- Reviewing and debate the existing Draft Law with the cabinet ministers and their legal advisors so that this will lead to an improved and refined version of the Draft Law to be submitted to the President or/and the People's Assembly for discussion and approval.
- Providing, prior to the presentation of the Draft Law to the People's Assembly, ongoing technical and legal advice to government officials of the relevant entities as well as monitor the policy decisions related to the proposed reform to ensure a proper understanding of the subjects and facilitate the decision process. Whenever necessary, *ad-hoc* presentations will be made to better inform officials about the project's concepts and philosophy.
- Providing, during the presentation and discussion of the Draft Law before the People's Assembly, ongoing legal advice to the members of the People's Assembly. In addition, ICPAP will monitor any modifications to the Draft Law to ensure that the objectives of the Capitalization Program and key articles of the Draft Law are neither diluted nor eliminated.
- Making presentations to political representatives to introduce them to the project concepts and philosophy.
- Carrying out a continuous follow-up of progress made in consensus building for the approval of the proposed reforms.
- Drafting the main regulations of the approved law.

III.2 Design and Execute a Communications and Outreach Campaign to Facilitate the Approval of the Draft Law and Obtain Financing

The objective of this task is to develop a communications strategy to build consensus for the approval of the Draft Law, encourage participation of the extralegal sector and support in the business community and the government sector, and acquiescence among those vested

⁴ The possibility or convenience of following other constitutional means, such as that of the President approving the Draft Law while the People's Assembly is closed for the season or requesting to be granted the power to approve the law.

interests in the *status quo*. The scope of the campaign will be directed at the following sectors:

- Within government: Executive Branch, Legislative Branch, military.
- The public: private sector, public sector, press.
- Foreign relations: international organizations, countries of the region, the world at large.

This task encompasses the preparation of written and graphic material to present and explain the content and benefits of the Draft Law to selected members of civil society and the political sector. This will be done using the study results, the reform proposal, and the impact evaluations reported by ECES/ILD to the GOE throughout the entire project. This campaign will also include a number of workshops and conferences on the subject.

III.3 Identify and Determine Options to Establish and Contract the Execution of the Formalization Processes, as well as the Design, Setting Up, and Operation of the Record Keeping and Information Systems

The implementation of the reforms shall be led by PAP, which shall be directly advised by ECES/ILD. Although PAP will be in charge and will have political control of implementation, it can receive efficient assistance—in different ways—from experts and specialists from the private sector, a fact that should be reflected in the Draft Law and in the implementation plan and budget.

PAP will need to carry out the following basic activities for implementation:

- **Plan and execute the real estate formalization process.** This not only includes designing and putting in motion the operations systems, the fieldwork, the gathering of legal and graphic information (surveying and mapping), the processing of the information collected and the titling of properties, but also drawing up regulations and manuals in addition to recruiting and training personnel.
 - **Plan and execute the business formalization process.** This includes designing and putting in motion the operations systems, the fieldwork, the gathering of legal information, the processing of the information collected, and the formalization of businesses. This also comprises drawing up regulations and manuals, as well as recruiting and training personnel.
 - **Plan, set up, and operate the conflict resolution systems** (both the Special Judicial System and the Conciliation and Arbitration Center). This includes designing and putting in motion the operations systems; having the judges and arbiters assigned; drawing up regulations and manuals, as well as recruiting and training personnel for these systems.
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- **Plan, set up, and operate the new business (NBPR), real estate (NREPR), and pledges public registries.** This includes designing and putting in motion the operations systems and the data bases; developing security mechanisms; carrying out inscriptions and providing the services to the public; drawing up regulations and manuals; recruiting, designating, and training registrars and key personnel.
- **Plan, set up, and operate the business information system.** This includes designing and putting in motion the operations systems; organizing and interconnecting data bases; developing security mechanisms; drawing up regulations and manuals; recruiting, designating, and training key personnel.
- **Plan, set up, and operate the signature certification service.** This includes designing and putting in motion the service; designing and putting in motion the operations systems; developing security mechanisms; drawing up regulations and manuals; recruiting, designating, and training key personnel.
- **Plan, set up, and operate the program for the improvement of regulations and administrative simplification.** This includes organizing the program; developing mechanisms for inter-governmental co-ordinations; designing and putting in motion the operations systems; drawing up regulations and manuals; recruiting and training key personnel, as well as training the public officials from the other government entities forming part of the regulatory improvement program.
- **Plan, set up, and operate the complaint and suggestions program.** This includes organizing the program; developing mechanisms for inter-governmental co-ordinations; designing and putting in motion the operations systems; drawing up regulations and manuals; and recruiting and training key personnel.
- **Plan, set up, and operate the system for the cost-benefit analysis of legislation and drafting of new reforms to reduce the costs of operating formally.** This includes organizing the system; developing mechanisms for inter-governmental co-ordinations; designing and putting in motion the operations systems; drawing up regulations and manuals; and recruiting and training key personnel.
- **Plan, set up, and operate the PAP administrative systems.** This includes developing regulations and the IT support for the organization and its functions, the personnel, the administration of financial resources, among others.

Some of these activities could be carried out directly by PAP or by the private sector. Nevertheless, all the activities contain components that require the **designing, setting up, and operation of infrastructure** (i.e., computer systems, data bases, registries). Since this will involve a high degree of technological specialization, specialized suppliers will have to

be contracted. **Annex 1** shows the different types of suppliers that could provide these services.

In order to prepare for the implementation of these activities as soon as PAP has been created and launched, **ICPAP needs to define the contracting options** to be adopted by PAP for the execution of each of these activities. In fact, the design of some of the components should be contracted out and advanced during this pre-implementation stage.

Some options for implementing these activities would include:

- a) **Directly execute** some or all of these activities by PAP.
- b) **Subcontract out the design** of some of the components of some activities to, **and/or have them put in place by**, local or foreign specialists.
- c) **Privatize or grant in concession to local or foreign specialists** the design, setting up, and operation of some activities.

Whichever option is chosen, ECES/ILD shall act as ICPAP's (and PAP's) principal advisor and, if need be, provide assistance in the drafting of the Terms of Reference (TORs) for contracting, monitoring, and supervising compliance with these and in the quality control of the products.

In addition, there are other services, which, at a later stage, could be provided by other contractors willing to carry these out commercially under different types of financing (such as, charging a percentage for the sale of information or related services). This would reduce the costs of the implementation of the complementary reforms. Some of these services are:

- Identification systems;
- Payments for utility services which would otherwise be stolen or wasted;
- Collection of taxes which would otherwise be unpaid;
- Credit and mortgage applications;
- Personal and business insurance; and
- Collection systems for credit; among others.

III.4 Draft a Detailed Implementation Plan, Budget, and Financial Proposal for both PAP and the Capitalization Program

Before initiating implementation, PAP should have secured the necessary funds from the GOE, multilateral financial institutions, or the national and international private sectors.

To that end, ICPAP must define the criteria and prepare the implementation plan and a budget for both PAP and the Capitalization Program that takes into consideration:

- The procedures to be applied for the implementation of the proposed reforms (see III.3);
- The infrastructure required, such as technological services, personnel, and facilities (see III.3); and
- The promotion and communications activities during the implementation process.⁵ In this case, communications includes the use of different types of media: print, television, and radio to inform the public about the “formalization campaigns” as they are carried out in the different areas of the country. In addition, the communications campaign involves designing and implementing a strategy to forge links with grassroots organizations that will support the formalization process. The latter is important because the participation of these organizations will permit the massive application of the formalization process.

The plan must be drawn up to extend over a period that will allow for the consolidation of the reforms and for fulfilling formalization goals. Ten years is a reasonable time-span, but the time requirements would be evaluated during the execution of the Program.

The contents of the plan will depend on the options selected for carrying out the reforms and the provision of infrastructure. Annex 2 contains a general outline of the information that the plan and budget should have.

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NOTE:

ECES/ILD has organized similar projects in other Third World countries and is therefore totally familiar with the all processes, from field operations to political management, and will be delighted to act as a general “*in-house consultant*” to the GOE, ICPAP and/or PAP, in whatever capacity Egyptian authorities think is convenient.

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⁵ Communications and dissemination are important components of the Capitalization Program, especially during the execution of the real estate and business formalization process. These components are required to promote the integration of the beneficiaries operating outside legal parameters and inside the new legal system. The communications plan also needs to include a periodic and systematic reporting mechanism regarding the Capitalization Program’s progress and benefits, as well as its economic and social impact on the different target groups in Egypt. The plan will also require mechanisms to provide a rapid and adequate response to the criticism received from interest groups affected by the reforms.

ANNEX 1
TECHNOLOGICAL SERVICE PROVIDERS

- The field of surveying and mapping includes companies that provide: comprehensive ground surveying, aerial photography, and mapping services using their in-house capabilities.
- Information Technology companies build the computer software programs (i.e. application programs) to support the automation of the registries systems and subsequently information systems. Such registry automation may also include the capability to display maps (produced by survey and mapping companies) using CAD or GIS that is linked to the registry systems database. There are thousands of large and small IT companies that build application software. Nevertheless, there are no widely recognized property experts.
- Equipment vendors, provide the necessary tools or foundation products used by other companies. While some of this equipment is property related such as surveying instruments, the majority are standard products that are used by and/ or customized by other companies. The different types of equipment vendors are as follows:
 - Hardware vendors. The first group of hardware vendors supplies surveying and mapping equipment such as aerial cameras, GPS receivers, theodolites, etc. The second group are computer hardware vendors who provide equipment such as CPU, disk drives, telecommunications equipment, display screens, etc.
 - Software vendors supply such foundation products as database, operating systems, and networking and telecommunications.
 - Logistical support, particularly with regard to communications equipment, which can be acquired from different sources.
- System integrators are the companies that bring all the technical pieces (hardware, software, communications) together into a total solution that can be effectively used by the client. These services include such activities as installing computers, loading software, establishing networks, coordinating documentation and training, testing and sometimes re-engineering paper flows.

ANNEX 2 IMPLEMENTATION PLAN AND BUDGET CONTENTS

The implementation plan and budget should contain information on the following points:

a) Scope of the Program: This shall be established by taking into account the special elements involved in formalizing extralegal real estate and businesses. The manner in which the activities related to the formalization of these assets progress (such as drafting rules and regulations and procedures, designing and putting in place the different mechanisms), including the criteria to be used in its execution, shall also be contemplated. This will mean identifying and prioritizing the urban areas to be formalized, establishing the scale of formalization activities (local or national), and defining the execution calendar for the entire formalization period.

Real estate and business formalization can be carried out simultaneously when the synergies produced so justify it.

b) Size of the Program: Size (including that of the offices and working areas, amount of equipment and furniture, and number of personnel in the different areas.) will be determined on the basis of the approximate number of houses and businesses to be formalized. When calculating the economic impact that the reforms would have on Egypt, the following were set as reasonable targets for formalization: 61% of all extralegal real estate (7.3 million out of 11.9 million pieces of real estate) over a period of 10 years, and 75% of all extralegal business (1.0 million out of 1.4 million enterprises) over a period of 8 years.

c) Cost of the Program (including facilities equipped for all PAP functions): This will depend directly on the magnitude/scale of the Program, which encompasses:

- **Initial investment.** This includes the cost of initiating operations, which takes into account the buildings, furniture, and equipment required to put in place PAP and its mechanisms, as well as those to set up the Capitalization Program *per se*. Additional investment needed in the future to periodically replace equipment and furniture, and the eventual expansion of PAP and the Program will also need to be considered.
 - **Annual operating costs.** This includes the salaries of the personnel, which will be classified by specialization; expenses for local transportation, electricity, water, and telephone; expenses to cover publicity and dissemination of program information; and logistics and other expenses. Expenses required to cover specialized consultancy services, as well as those arising from activities that are subcontracted, privatized, or given in concession particularly must be taken into account.
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When estimating the economic impact of the reforms on Egypt, reasonable average investment costs were put at US \$ 85 for formalizing real estate and US \$ 38 for formalizing businesses.

d) Infrastructure for PAP and the Capitalization Program: This shall be established by taking into account the special elements involved in the formalization of real estate and businesses. The size of the offices and working areas and of the areas to be designated for user services, as well as that of the areas that personnel working on formalization will require to process and file the corresponding files will need to be contemplated. The types and quantity of equipment required will need to be determined.

e) Equipment and computer system for PAP: A detailed list and description shall be given of the computer equipment, IT support, and software to be used by PAP to administer the Program, which includes the management of the different registries and the rest of the mechanisms to be set up.

f) Personnel for PAP and the Program: A detailed description of the type and number of specialists needed to carry out the different tasks to be handled by PAP and carried out to formalize real estate and business assets shall be provided. This includes a description of the technical teams required to carry out the fieldwork in the areas to be formalized.

**ACTION PLAN TO IMPLEMENT
“THE NATIONAL PROGRAM FOR THE CAPITALIZATION OF
THE POOR IN HAITI”**

(To integrate the extralegal economy into mainstream economic activity)

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III.2 Design and Execute a Communications and Outreach Campaign to Facilitate the Approval of the Draft Law and Obtain Financing

III.3 Identify and Determine Options to Establish and Contract the Execution of the Formalization Processes, as well as the Design, Setting Up, and Operation of the Record Keeping and Information Systems

III.4 Draft a Detailed Implementation Plan, Budget, and Financial Proposal for both ONAC and the Capitalization Program

ACTION PLAN TO IMPLEMENT “THE NATIONAL PROGRAM FOR THE CAPITALIZATION OF THE POOR IN HAITI”

(To integrate the extralegal economy into mainstream economic activity)

I. SUMMARY AND INTRODUCTION

This Action Plan lays out the actions and decisions required to carry out the implementation of the National Program for the Capitalization of the Poor in Haiti” (*Le Programme National de Capitalisation des Actif en Haiti*), the primary objective of which is to integrate the extralegal sector into the nation’s mainstream legal economy.

Haiti’s extralegal economy represents about US\$ 5 billion of assets (businesses and real estate). However, these assets will always be out of the legal sector because they lack the three basic legal tools that generate wealth: organizational forms to divide labor in house and raise productivity; records as well as standard rights and obligations to contract with unfamiliar parties in Haiti’s expanded market allowing them to specialize further and gain economies of scale; and property rights to capture capital.

Why do so many Haitians operate and hold their assets outside the law? Two simple reasons: The legal system costs too much for most citizens to enter; and two, some basic institutions are missing. To open a single-person business, for example, takes more than 62 days of navigating bureaucracies and costs US\$ 565; to convert a piece of land into a commercially legal vehicle can take more than 13 years of red tape. To do business in Haiti, the poor must deal with 45 government agencies, more than 280 dispersed pieces of legislation, government inspections that are repetitive and overlapping.

The GOH can turn this entire situation around by formalizing the most important assets of the poor: their **real estate** and their **businesses** — which is the very purpose of the Capitalization Program.

To launch and carry out the Program successfully, however, two things are necessary: the appointment of a political authority responsible for the Program and an organization to carry it out. With respect to the organization, the 4-volume study developed by ILD and CLED for Haiti’s Presidential Commission proposes a specialized, independent, and fully empowered body provisionally named *L’Office National de Capitalisation (ONAC)*.

ONAC would implement the following 4 types of mechanisms contained in the Program:

a) **Mechanisms to facilitate legal entry of businesses:**

- A New Business Public Registry that will administer a unified, simplified, and low-cost system for the incorporation, registration, and licensing of companies and single person businesses.
- Limited liability status for single-person businesses so that citizens can partition their assets for multiple purposes.

b) **Mechanisms to facilitate the legal operation of businesses:**

- Specific mechanisms to improve regulations and simplify legal business procedures.
- Simplified labor and social security procedures.
- A special commission to receive and process complaints and suggestions from citizens, thus ensuring both the correct application of the reforms and continual improvement through feedback mechanisms.

c) **Mechanisms to promote business expansion:**

- Conciliation and arbitration procedures as a private alternative for improving business dispute resolution mechanisms.
- A business information system.

d) **Proposed mechanisms to promote real estate formalization:**

- A comprehensive system for massive formalization.
- A New Real Estate Public Registry that will run a geographically based real folio registration system for defining ownership efficiently.
- Simplified procedures to register real estate assets transactions (e.g. sales, leases, mortgages, and subdivisions, among others).
- Simplified procedures to foreclose mortgages.
- The use of conciliation and arbitration procedures to resolve real estate disputes.

ONAC needs to be given all the faculties of *ius imperium* necessary to execute the Capitalization Program. The task of allowing the poor to capitalize their assets and then integrating them into the economy is a revolutionary act that can be accomplished only if the highest levels of decision making in the country are behind it.

Nevertheless, before putting ONAC in place and before the implementation of the Capitalization Program can begin, the GOH would need to carry out a number of **pre-implementation tasks**. To that end, we propose the **immediate creation of an Interim Commission for ONAC (ICONAC)** and the **designation of its Chief Executive Officer (CEO)**, who must be a top notch senior professional with the Prime Minister's (or the Minister of Finance's) total support and armed with the executive powers necessary to carry out and concretize the pre-implementation tasks. Primarily:

1. To fine-tune the Draft Law, build consensus for its objectives, and obtain its approval by the pertinent authorities;
2. To design and execute a communications and outreach campaign that would facilitate the approval of the Draft Law as well as the support and funding needed for the implementation of the Program;
3. To identify and determine options to establish and contract the execution of the formalization processes, as well as the design, setting up, and operation of the record keeping and information systems;
4. To draft a detailed implementation plan, along with a budget and a financial proposal, which includes:
 - The procedures to be applied for the implementation of the proposed reforms;
 - The infrastructure required (e.g. technological services, personnel, and facilities); and
 - The promotion and communications activities during the implementation process.

We estimate that these four pre-implementation tasks would take between 9 and 12 months to complete.

II L'OFFICE NATIONAL DE CAPITALISATION (ONAC) AND THE INTERIM COMMISSION (ICONAC)

II.1 ONAC: A Specialized, Independent, and Fully Empowered Organization to carry out the Capitalization Program

Haiti does not have an organization designed to promote the legal entry, operation, and expansion of enterprises operating extralegally, especially those of the poor. Consequently, the gains in productivity, economies of scale, and the conversion of the assets of the poor into capital remain out of reach. Each of the 45 government entities that affect the economic life of the poor has a separate specific goal, such as collecting taxes, ensuring compliance with health standards, registering property, etc. Not one is charged with changing the *status quo* or seeing economic growth from the point of view of the poor. None of these 45 agencies has the mandate to minimize the prohibitive transaction costs the poor face, to create appropriate legal vehicles for them to organize themselves productively, to give them accessible property rights to obtain credit, investment, and accumulate capital. No single entity within the Haitian legal system is responsible for making it irresistible for the poor to cross over into the formal sector.

The GOH, therefore, needs to create a specialized, independent, and fully empowered body to spearhead this formalization process: **L'Office National de Capitalisation (ONAC)**.

A specialized body: The main task of ONAC is to focus fully on the implementation of the Capitalization Program and most of the reform proposals —and nothing else. ONAC will have a far-reaching agenda —from overseeing business and real estate formalization, the recording of mortgages, the reduction of obstacles, regulatory improvement, the implementation of business information systems to continual research on how the poor can be more quickly and efficiently brought into the legal framework, the *sine qua non* for economic growth.

An independent body: Major reforms tend to stir up vested interests and pernicious old bureaucratic habits, and it is, therefore, necessary to ensure that reformers are protected from defenders of the *status quo* watering down the strong initiatives we are proposing. The ILD's experience in other countries, such as El Salvador and Peru indicates that to avoid having the reforms neutralized, a specialized organization must be created. Independence from existing bureaucracies is crucial —such as the Institute for Liberty and Progress (under the tutelage of the President and the First Lady of the Republic of El Salvador), and the Commission for the Formalization of Informal Property (under the Minister of Justice, in Peru).

A fully empowered body: Because the task of allowing the poor to capitalize their assets and integrating them into the economy is a revolutionary act that can be accomplished only if the highest levels of decision making in the country are behind it. It is essential that ONAC have this kind of political support because it must change the *status quo* and enforce the application of the reforms in governmental bureaucracies that have different agendas and will continually try to neutralize the new measures. In addition, it must be able to quickly and effectively adapt to the changing needs of the reform process.

It is with these three characteristics in mind that ONAC is created in the Draft Law as a public authority under the leadership of the Minister of Finance. It will have a Board comprised of a representative of local governments, a representative of public entities and six Ministers belonging to the public entities whose competencies will be most affected by the reforms or those that will frequently interact with the ONAC (such as, the Minister of Finance, the Minister of Justice, the Minister of Trade and Industry, et al).

The Draft Law empowers ONAC with all the faculties of *ius imperium* necessary to execute the Capitalization Program and stipulates that all existing public entities shall participate in the Capitalization Program —under the administrative responsibility of the head of the entity—assisting and providing ONAC with the information, documentation, and data necessary to implement the program.

For example, in order to ensure that its objectives are fulfilled, ONAC shall be able to issue directives and regulations that must be followed by both private agents and public officials. Likewise, the Draft Law grants ONAC the authority to directly access the information in the current public registries, as well as to train, evaluate, and dismiss the public officials of other government entities under its competency.

To achieve its objectives without any constraints, ONAC shall be governed exclusively by the provisions of its law and be economically and financially autonomous; shall have the flexibility to contract the necessary personnel and services; and shall be empowered to conclude agreements and contracts with national or international specialized institutions.

ONAC has been organized in such a way that it is able to respond effectively to the needs of the Capitalization Program. To that end, the Board is the highest political authority of ONAC, and the Executive Committee will be the highest managerial authority — formed by ONAC's General Director, who presides over it, and the Directors of ONAC's Directorates.

ONAC has the following Directorates responsible for putting the proposed reforms into operation:

- The **Directorate of Formalization** whose Director is empowered to manage the Formalization System (for business and real estate assets);
- The **Directorate of Information and Registration** whose Director is empowered to manage the Registration System (including the New Business and Real Estate Public Registries); as well as to manage the Business Information System.
- The **Directorate of New Projects** whose Director is empowered to design and execute projects to implement the complementary reforms needed to consolidate the Capitalization Program; and,
- The **Directorate of Administration** whose Director is empowered to manage matters concerning accounting and budget, as well as the organization and administration of human, material, and financial resources of ONAC, and provide support to the Arbitration Court.

II.2 ICONAC: The Interim Commission to carry out the Pre-Implementation Tasks of the Capitalization Program

ONAC will only become operational when the GOH has decided on how to implement the Capitalization Program and once the Draft Law has been approved. The GOH will need to take a number of decisions and measures to make this possible, the most important of which will be to establish an **Interim Commission (ICONAC)** with the mandate to execute the pre-implementation tasks needed to carry out the Capitalization Program.

ICONAC, which should be created by way of a Prime Minister Decree, shall be the designated interlocutor for the Capitalization Program before the public administration and the private sector. ICONAC will be responsible for carrying out the pre-implementation

tasks, as described in Section III below. ICONAC, therefore, should be empowered to contract —with the fewest legal restrictions— the goods, the consultancy and advisory services, as well as all the other professional services required for the pre-implementation tasks.

ICONAC should have a Chief Executive Officer (CEO) and a staff of 6 to 8 Haitian upper-level professionals, specializing in:

- Law (registration law, property rights, commercial law, administrative law);
- Economy (economic analysis);
- IT/Systems (registration systems, information databases);
- Surveying and mapping;
- Communications (with good ties to the media and able to design messages specially targeting the extralegal sectors); and,
- Administration of projects and organizations.

ICONAC shall be the base for the executive teams to direct ONAC, which will ensure the continuity of the process and that maximum benefits are obtained from the experience gained. Consequently, its CEO must have the full support of the GOH and be empowered to interact with Ministers and upper-level authorities.

ILD shall provide ICONAC with permanent advisory services and assistance on technical aspects and institutional policies throughout the pre-implementation phase.

ICONAC shall have its own budget —in the order of an estimated US\$ 700,000 thousand to US\$ 900,000 thousand, according to our experience— to allow it to cover the following *pre-operations costs*:¹

- a) Salaries for the Haitian managerial and technical staff at ICONAC.
- b) ICONAC operating expenses (rental of offices and equipment; expenses for logistics local transportation; and other expenses).
- c) Consultancy services and other similar services.
- d) Expenses to cover costs of the publicity campaign for disseminating information on the benefits of the Capitalization Program, an essential component of the process.

The Prime Minister could also set up an Advisory Committee made up of Ministers of the sectors closely related to the reform so as to help him analyze and evaluate actions and decisions proposed by ICONAC.

¹ This budget estimate does not include ILD consultancy costs.

III. THE PRE-IMPLEMENTATION TASKS

ICONAC's pre-implementation tasks include:

III.1 Fine-Tuning the Draft Law, Building Consensus for its Objectives, and Obtaining its Final Approval by the Pertinent Authorities

Having the Draft Law approved is a *sine qua non* for the implementation of the Capitalization Program. Consequently, ICONAC should prepare and execute a strategy to obtain the approval of the law. This strategy should include:

- Adapting the current Draft Law to the policy definitions of the additional functions and special powers with which ONAC and its CEO will need to be granted, as well as to the different options for carrying out the reforms and the provision of infrastructure to be defined by ICONAC.
- Preparing a plan for the approval of the Draft Law, including the legal and economic arguments to build consensus for support.
- Reviewing and debate the existing Draft Law with the cabinet ministers and their legal advisors so that this will lead to an improved and refined version of the Draft Law to be submitted to the Prime Minister for discussion and approval. In addition, ICONAC will monitor any modifications to the Draft Law to ensure that the objectives of the Capitalization Program and key articles of the Draft Law are neither diluted nor eliminated. Whenever necessary, *ad-hoc* presentations will be made to better inform officials about the project's concepts and philosophy.
- Making presentations to political representatives to introduce them to the project concepts and philosophy.
- Carrying out a continuous follow-up of progress made in consensus building for the approval of the proposed reforms.
- Drafting the main regulations of the approved law.

III.2 Design and Execute a Communications and Outreach Campaign to Facilitate the Approval of the Draft Law and Obtain Financing

The objective of this task is to develop a communications strategy to build consensus for the approval of the Draft Law, encourage participation of the extralegal sector and support in the business community and the government sector, and acquiescence among those vested

interests in the *status quo*. The scope of the campaign will be directed at the following sectors:

- Within government: Executive Branch, Judiciary Branch.
- The public: private sector, public sector, press.
- Foreign relations: international organizations, countries of the region, the world at large.

This task encompasses the preparation of written and graphic material to present and explain the content and benefits of the Draft Law to selected members of civil society and the political sector. This will be done using the study results, the reform proposal, and the impact evaluations reported by ILD and CLED to the GOH throughout the entire project. This campaign will also include a number of workshops and conferences on the subject.

III.3 Identify and Determine Options to Establish and Contract the Execution of the Formalization Processes, as well as the Design, Setting Up, and Operation of the Record Keeping and Information Systems

The implementation of the reforms shall be led by ONAC, which shall be directly advised by ILD. Although ONAC will be in charge and will have political control of implementation, it can receive efficient assistance—in different ways—from experts and specialists from the private sector, a fact that should be reflected in the Draft Law and in the implementation plan and budget.

ONAC will need to carry out the following basic activities for implementation:

- **Plan and execute the real estate formalization process.** This not only includes designing and putting in motion the operations systems, the fieldwork, the gathering of legal and graphic information (surveying and mapping), the processing of the information collected and the titling of properties, but also drawing up regulations and manuals in addition to recruiting and training personnel.
- **Plan and execute the business formalization process.** This includes designing and putting in motion the operations systems, the fieldwork, the gathering of legal information, the processing of the information collected, and the formalization of businesses. This also comprises drawing up regulations and manuals, as well as recruiting and training personnel.
- **Plan, set up, and operate the conflict resolution systems.** This includes designing and putting in motion the operations systems; having arbiters and conciliators assigned; drawing up regulations and manuals, as well as recruiting and training personnel for these systems.

- **Plan, set up, and operate the New Business and Real Estate Public Registries.** This includes designing and putting in motion the operations systems and the data bases; developing security mechanisms; carrying out inscriptions and providing the services to the public; drawing up regulations and manuals; recruiting, designating, and training registrars and key personnel.
- **Plan, set up, and operate the business information system.** This includes designing and putting in motion the operations systems; organizing and interconnecting data bases; developing security mechanisms; drawing up regulations and manuals; recruiting, designating, and training key personnel.
- **Plan, set up, and operate the complaint and suggestions program.** This includes organizing the program; developing mechanisms for inter-governmental co-ordinations; designing and putting in motion the operations systems; drawing up regulations and manuals; and recruiting and training key personnel.
- **Plan, set up, and operate the system for the cost-benefit analysis of legislation and drafting of new reforms to reduce the costs of operating formally.** This includes organizing the system; developing mechanisms for inter-governmental co-ordinations; designing and putting in motion the operations systems; drawing up regulations and manuals; and recruiting and training key personnel.
- **Plan, set up, and operate the ONAC administrative systems.** This includes developing regulations and the IT support for the organization and its functions, the personnel, the administration of financial resources, among others.

Some of these activities could be carried out directly by ONAC or by the private sector. Nevertheless, all the activities contain components that require the **designing, setting up, and operation of infrastructure** (i.e., computer systems, data bases, registries). Since this will involve a high degree of technological specialization, specialized suppliers will have to be contracted.

In order to prepare for the implementation of these activities as soon as ONAC has been created and launched, **ICONAC needs to define the contracting options** to be adopted by ONAC for the execution of each of these activities. In fact, the design of some of the components should be contracted out and advanced during this pre-implementation stage.

Some options for implementing these activities would include:

- a) **Directly execute** some or all of these activities by ONAC.
- b) **Subcontract out the design** of some of the components of some activities to, **and/or have them put in place by**, local or foreign specialists.

- c) **Privatize or grant in concession to local or foreign specialists the design, setting up, and operation of some activities.**

Whichever option is chosen, ILD shall act as ICONAC's (and ONAC's) principal advisor and, if need be, provide assistance in the drafting of the Terms of Reference (TORs) for contracting, monitoring, and supervising compliance with these and in the quality control of the products.

In addition, there are other services, which, at a later stage, could be provided by other contractors willing to carry these out commercially under different types of financing (such as, charging a percentage for the sale of information or related services). This would reduce the costs of the implementation of the complementary reforms. Some of these services are:

- Identification systems;
- Payments for utility services which would otherwise be stolen or wasted;
- Collection of taxes which would otherwise be unpaid;
- Credit and mortgage applications;
- Personal and business insurance; and
- Collection systems for credit; among others.

III.4 Draft a Detailed Implementation Plan, Budget, and Financial Proposal for both ONAC and the Capitalization Program

Before initiating implementation, ONAC should have secured the necessary funds from the GOH, multilateral financial institutions, or the national and international private sectors.

To that end, ICONAC must define the criteria and prepare the implementation plan and a budget for both ONAC and the Capitalization Program that takes into consideration:

- The procedures to be applied for the implementation of the proposed reforms;
- The infrastructure required, such as technological services, personnel, and facilities; and
- The promotion and communications activities during the implementation process⁽²⁾. In this case, communications includes the use of different types of media: print, television, and radio to inform the public about the "formalization campaigns" as they are carried out

⁽²⁾ Communications and dissemination are important components of the Capitalization Program, especially during the execution of the real estate and business formalization process. These components are required to promote the integration of the beneficiaries operating outside legal parameters and inside the new legal system. The communications plan also needs to include a periodic and systematic reporting mechanism regarding the Capitalization Program's progress and benefits, as well as its economic and social impact on the different target groups in Haiti. The plan will also require mechanisms to provide a rapid and adequate response to the criticism received from interest groups affected by the reforms.

in the different areas of the country. In addition, the communications campaign involves designing and implementing a strategy to forge links with grassroots organizations that will support the formalization process. The latter is important because the participation of these organizations will permit the massive application of the formalization process.

The plan must be drawn up to extend over a period that will allow for the consolidation of the reforms and for fulfilling formalization goals. Some five years is a reasonable time-span, but the time requirements would be evaluated during the execution of the Program.

The contents of the plan will depend on the options selected for carrying out the reforms and the provision of infrastructure.

**TIMETABLE FOR THE PRE-IMPLEMENTATION ACTIVITIES
ICONAC - HAITI**

ACTIVITES	1	2	3	4	5	6	7	8	9	10	11	12
[REDACTED]	1											
	2											
	3											
	4											
	5											
	6											
	7											
	8											
	9											
	10											
	11											
	12											



AWARENESS BUILDING STAGE

**PRELIMINARY DIAGNOSIS OF THE
EXTRALEGAL SECTOR IN GUATEMALA**

May, 2004

**AWARENESS BUILDING STAGE
PRELIMINARY DIAGNOSIS OF THE
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AWARENESS BUILDING STAGE

PRELIMINARY DIAGNOSIS OF THE EXTRALEGAL SECTOR IN GUATEMALA

This document presents the results of the preliminary research carried out by four ILD specialists who visited various localities of the country and interviewed some 50 people in the formal and extralegal sectors during 6 days between 19 and 24 April 2004. *See Table 1 for details about their interviews and visits.*

1. THE MACROECONOMIC PROFILE OF GUATEMALA RELATIVE TO THE POLITICAL, ECONOMIC, AND SOCIAL CONTEXT OF THE COUNTRY

The most critical problems in Guatemala are:

- high levels of poverty (90% in the countryside and 70% in the city);
- a high illiteracy rate (especially in the countryside);
- virtually no growth in per capita income (moderate GDP growth is cancelled out by population growth);
- a high degree of inequality (the richest 10% receive 48% of the national income while the poorest 10% receive only 1%);
- contraband, and
- a low level of tax collection (high levels of evasion).

For more details, see Annex 1 (Principle Characteristics of the Economy in Guatemala).

The poor in Guatemala feel excluded. The government has not responded to the demands of the poor. The Peace Agreements (signed between 1986 and 1996, after 36 years of internal conflict) have not been fully implemented. This is giving rise to widespread social discontent, and is promoting violent land invasions, public demands for the expropriation and redistribution of land among the poor peasants and, in general, violence and crime throughout the country. This climate of insecurity has increased the perception of risk, dissuading investment in the country (private investment, especially foreign, has dropped dramatically). *See Table 2 for additional details on the actors in the current political debate.*

The Government of Guatemala (GOG), aware of these problems, has included the following in the government program it has designed for the remainder of their period of government:

- Resumption of programs for macro and microeconomic growth

- Strengthening of institutions
- Social inclusion of the poor, the indigenous population, and women
- Strengthening democracy
- Achieving environmental sustainability

However, the GOG has not explained how they will fulfill these goals.

2 CURRENT STATUS OF LAND RIGHTS IN GUATEMALA

2.1 The current status of land tenure in the rural areas of Guatemala (**where 60% of the population lives**) is marked by the following factors:

- Historical conflicts between large landowners and poor peasants,
- The attempt to redistribute rural land during the truncated Agrarian Reform carried out by President Arbenz (1952-1954),
- The rise and growth of the guerrillas who started the land invasions in the northern region of the country,
- The land adjudication policies put in place after the unsuccessful Agrarian Reform did not generate legal property, but rather possession, and
- The commitments to grant land to peasants assumed by the government within the framework of the peace agreements clashed with the interests of the large property owners.

Consequently, there are marked disparities in the ownership of land and the concentration of wealth throughout the country:

- The majority of the wealth of the country, as well as the large family-owned and industrial agricultural properties, is concentrated in the southern departments, **which represent 10% of the territory and hold 20% of the population**. It is estimated that two thirds of these properties are in legal order. The remaining third, on the other hand, is extralegal, and is characterized by extralegal land transfers, overlapping boundaries, and errors in registry records, to name a few.
- In contrast, levels of poverty are very high and property rights over land are primarily extralegal in the central and northern departments, **which represent 90% of the territory and holds 80% of the population**. The land in these departments primarily consist of smallholdings and indigenous land, most of which are held extralegally. The ownership of these lands is often under dispute, and in some cases, results in armed confrontations between the legitimate holders and the professional squatters.

2.2 In the cities, current land tenure has been determined by the following factors:

- Continuous migration from villages and small, populated centers to the principle cities of the country since the 1950's (in Guatemala City, for example, the population increased from 1.3 million in 1981 to 2.5 million in 2002);
- Squatting on municipal and state owned land in the main cities, as a result of migration and the deterioration/destruction of the traditional areas of the city (earthquake of 1976);
- Clandestine land development in the outlying areas of principal cities not incorporated into the urbanized areas of these cities;
- The accelerated urbanization of the outlying municipalities (small communities) of the principal cities;
- The inefficiency of public housing programs —which reached only the middle class and had almost no impact on the poorest sectors;
- The massive increase of extralegal transfers and the outdated property registry, both of which result from the taxes and administrative costs that burden legal transfers of property.

3 THE MAGNITUDE OF EXTRALEGALITY IN REAL ESTATE AND BUSINESSES

In general, the absence of an adequate institutional framework has contributed to extralegality in both real estate and business. In real estate, for instance, the absence of viable legal mechanisms for lower income citizens to fulfill their land and housing needs has given rise to a high level of extralegality in this sector. Likewise, in business, onerous legal requirements, and/or the absence of adequate laws force a high percentage of entrepreneurs into the extralegal sector. In particular, entrepreneurs face difficulties in and high costs of remaining legal, tax problems when withdrawing from the market, and the absence of legal mechanisms to gain access to credit and to contract to expand operations are the principle causes of extralegality.

As a result, preliminary estimates indicate that:

- Approximately 90% of urban real estate (or some 2 million houses) can be classified as extralegal (dead capital). See *Table 3, Types of Extralegality and the Magnitude of Dead Capital in Guatemala*.
-

- Approximately **87%** of rural properties (or some 723,000 parcels of individual or collective property) can be classified as extralegal (dead capital) *See: Table 3. Types of Extralegality and the Magnitude of Dead Capital in Guatemala.*
- Approximately **90%** of all enterprises (or some 1,215,000 businesses) can be classified as extralegal (dead capital). This 90% is comprised by all of microenterprises, the majority of small enterprise, and some of the medium enterprises in the country.

In Guatemala, **52%** of the Gross National Product (GNP) is generated by extralegal economic units (compared to **20%** in Chile and **13%** in the United Kingdom)

Value of Dead Capital (For details on the methodology used to make the calculations, see Annexes 2 and 3)

REAL ESTATE	BUSINESS
<ul style="list-style-type: none"> • Urban Dead Capital: US\$ 25 billion • Rural Dead Capital: US\$ 24.5 billion. 	<ul style="list-style-type: none"> • Dead Business Capital: US\$ 6 billion.
OVERALL TOTAL: US\$ 55.5 billion	

**DEAD CAPITAL PER CAPITA IN GUATEMALA IS
US\$ 4,750**

What is the significance of Dead Capital in Guatemala?

US \$ 55.5 billion is:

- 14 times greater than the total portfolio of current loans in the banking system (US\$ 3.8 billion)**
- 19 times greater than the net international monetary reserves of the Bank of Guatemala (US\$ 2.9 billion)**
- 33 times greater than the total assets of the Industrial Bank. (US\$ 1.7 billion)**
- 188 times greater than the total assets of the National Mortgage Credit Bank of Guatemala (CHN) (US\$ 232 million)**
- 239 times greater than the market value of the stock registered in the National Stock Exchange (BVN) (US\$ 232 million)**

4 PROBLEMS IN THE INSTITUTIONAL FRAMEWORK

In this section, institutional problems that impede the formalization of extralegal assets in both real estate and business are described.

4.1 REAL ESTATE

- There is no inventory of lands or a cadastral information system (less than 10% of the total of municipalities in the country are zoned).**
- The property registry, although automated, holds outdated information, is not reliable, is overly centralized (there are only 2 offices to serve the entire country), and is complicated (unnecessary and redundant revisions of titles).**

To register a transaction, one must pay a series of taxes beforehand (single property tax, added value tax in the case of transfers, and registry fees, among others).

For example, the registration of the transfer of a property worth US\$ 10,000 can cost some US\$ 1,000 if one takes into account notary expenses, taxes (IUSI and VAT), registry fees, and other related costs.

- There is no effective system for regularizing titles (massive formalization). The only legal avenue for formalization is the procedure known as adverse possession (*titulación supletoria*).

The regularization of a property takes some 22 years, from the time of possession of the property to when it is fully recognized.

4.2 BUSINESS

Roughly 85% of the 1 million 350 thousand enterprises in Guatemala are organized as single-person enterprises or family operations that legally appear under the name of the head of the family.

Absence of legal mechanisms:

- **These enterprises do not have access to efficient organizational forms.**
 - ❖ They cannot organize or establish themselves as limited liability companies or joint stock companies because of the high costs of remaining in or withdrawing from the market that the country's laws impose on these types of business organizations, costs which are higher than those imposed on single-person enterprises.
 - ❖ They cannot legally differentiate between the ownership of the business assets and the administration of the business.
 - ❖ They do not have a system of limited liability that clearly differentiates between the owner's assets and those of the business.
 - ❖ They cannot issue shares legally to attract investment.
 - ❖ They cannot enter into contracts or guarantee credit to expand activities, acquire more appropriate technology, and renovate assets.
- **These enterprises do not have access to the legal mechanisms that promote efficient expansion/growth:**

- ❖ There are no information systems to provide data on the financial situation and the assets of extralegal enterprises.
- ❖ Accounting information is inexact. The majority of businesses avoid using the accounting system because of its high costs (one needs to hire an accountant in most cases).
- ❖ Contract enforcement is unpredictable. Judicial proceedings take years.

The cost of enforcing a contract is equivalent to 20% of the GNI per capita (in Chile, 15% and in Norway, 10%)

- ❖ They do not have access to bank credit. They can only access other sources of credit (cooperatives, NGOs, and in some cases, money lenders who charge monthly interest rates of 20%) that do not provide enough to cover their needs.
- ❖ They do not use negotiable instruments, such as checks or other commercial instruments of exchange, because they do not believe they can rely on the judicial means available to recuperate their expenditure.
- ❖ For these businesses, judicial foreclosure of a mortgage can take up to 5 years.

Obstacles and costs of starting, operating, and closing a business in the market:

- **Legal access to business:**

The cost of starting up a business is equivalent to 67% of the GNI per capita (in Chile, 12% and in Norway 4%).

- Overall, incorporation and initial administrative registration procedures are not complicated —it takes about 1 month and a half maximum to register at both the Commercial Registry and the Taxpayers Registry. However, difficulties arise in complying with other requirements, such as when the municipality verifies that the construction of the establishment is appropriate for the type of business it is going to carry out, or when sectorial permits are required to initiate operations (as in the case of certain industries having to comply with specific health and environment requirements).

For example, if an entrepreneur wishes to open a small restaurant in the department of Escuintla, he must previously:

- i.) Register the business and obtain a business license at the Commercial Registry;
- ii.) Register with the taxpayers registry at the Superintendency of Tax Administration (SAT);
- iii.) Register employees at the Guatemalan Social Security Institute (IGSS);
- iv.) Apply for an operating license at the corresponding municipality;
- v.) Obtain authorization for handling food from the Ministry of Health;
- vi.) Obtain authorization to install a sound system from the governor;
- vii.) Obtain the license for the sale of alcoholic beverages at the Superintendency of Tax Administration (SAT);
- viii.) Have accounting books authorized, etc.

It could take an entrepreneur at least 6 months to comply with all these requirements and cost him over US\$ 500 if one takes into account the cost of the paperwork (including accountant services and the payment of “tramitadores” —paperwork runners), the time invested, and administrative fees.

- **Institutional obstacles related to operating a business legally:**

- ❖ The tax returns are complex and require the services of an accountant.
- ❖ Entrepreneurs must keep the Guatemalan Social Security Institute informed as to the status of their employees and comply with a number of labor obligations.

- **Withdrawing from the market (closing a business):**

The cost of closing/liquidating a business is equivalent to 18% of the value of the assets of the business being liquidated (in Chile, 18% and in Norway, 1%)

- The procedure for liquidating a business is very long and complicated. One needs to submit up-to-date accounting books and copies of the last receipts, wait for the tax authority to liquidate one’s taxes, and cancel accumulated interest, among others.
- The entrepreneurs interviewed indicate that the procedure can take more than 1 year to complete and that the costs involved are unpredictable. Consequently, the way to withdraw from the market is to wait for an amnesty (the exception becomes the rule).

For more details on the characteristics of the legal and extralegal sectors in Guatemala, see Annex 4.

5 PROJECTED IMPACT OF ILD REFORMS ON THE ECONOMY OF GUATEMALA

The ILD has carried out a preliminary estimate of the impact that some of the proposed reforms will have on economic growth in Guatemala. To carry out this estimate, we used a model designed by professors Gwartney of Florida State University, Lawson of Capital University, and Benson of Florida State University. The model, created to calculate the "Economic Freedom of the World Index" and applied to a sample of several countries, has been adapted to include as indicators the effects of four of the reforms that the ILD proposes: start-up procedures, contract enforcement procedures, liquidation procedures, and the degree of coverage of credit bureaus. The results obtained from the application of this model indicate that if the reforms are 80% successful, GDP per capita in Guatemala will increase between 2.8 and 3.8 percentage points per year. If they are only 60% successful, then the increase of the GDP per capita in Guatemala will be between 2.1 and 2.8 percentage points per year.

See Annex 5 for details of the projected impact of institutional reform in Guatemala.

Table 1
ACTIVITIES OF THE ILD IN GUATEMALA

**Interviews, contacts and visits realized during the week
of 19-24 of April, 2004**

1. Visits and interviews with Public Sector Officers:

- Comisión Presidencial de Reforma del Estado (COPRE).
- Decanato Facultad de Ciencias Económicas de la Universidad de San Carlos.
- Secretaría de Asuntos Agrarios, CONTIERRA.
- Secretaria General, Dirección de Catastro y Dirección de Licencias de Construcción del Municipio de la Ciudad de Guatemala.
- Ministerio de Comunicaciones, Infraestructura y Vivienda (MICIVI).
- Dirección del Registro General de la Propiedad de Guatemala.
- Gobernación del Departamento de Escuintla.
- Gobernación del Departamento de Petén.
- Alcaldía de Flores - Petén

2. Financial Government Institutions:

- Dirección del Banco de Crédito Hipotecario Nacional de Guatemala.

3. Private Sector:

- Federación Nacional de Cooperativas de Viviendas (FENACOVI).
- Confederación de Cooperativas de Guatemala (CONFECOOP).
- Cámara de Comercio de Guatemala.
- FUNDESA.

4. Contacts and interviews with professionals related to property and businesses problems in Guatemala:

- Juzgado de Paz.
- Abogados-Notarios.

5. Contacts with the extralegal sector:

- Interviews with "wisaches" of Guatemala City.
- Neighbors and businessmen in "El Gallito" district (Guatemala City).
- Neighbors and businessmen of Palín.
- Interviews with leaders of people organizations and micro businesses in Escuintla City.
- Interviews with leaders of micro businesses
- Visit to the Municipality of Flores, Department of Peten. Meeting with leaders of community based organizations.
- Neighbors and businessmen in Antigua, Sacatepeques.

6. Private Consultants.

Members of the Research Team of ILD: Luis Aliaga, Susana Lizárraga, Luis Morales-Bayro and Gustavo Marini.

Local Counterpart: Harris Whitbeck, Comisionado Presidencial para la Reforma del Estado, Economist Guillermo Luna (Coordinator and Facilitator).

TABLE 2

ADDITIONAL DETAILS ABOUT MAIN CHARACTERS OF CURRENT POLITICAL DEBATE

- **NOTARIES:** In Guatemala all lawyers can be notaries; it is not an elitist profession as in Peru. According to calculations, there are around 5000 lawyers in activity, of which 3500 perform notary functions, preparing public deeds. Because of the vast number of notaries, they are very accessible.
- **REAL ESTATE PUBLIC REGISTRY:** The registry is considered a very important institution among the legal community. The Chief Justice of the Supreme Court frequently refers to the registry as "el Señorío del Registro", referring to it as an institution worthy of great respect. The current chief of the registry (which is known as Registrar General) has twice served as President of Congress and Minister of State. She is also close friends with President Berger. Although the officials from the REPR are constantly accused of corruption and lack of efficiency, we were recommended to avoid downplaying the importance of the institution.
- **LANDOWNERS AND BUSINESSMEN:** Many private businessmen come from landowning families and the ideas of massive formalization of rural property may cause a negative reaction due to the conflicts that still exist between landowners and indigenous communities that have either invaded their lands and/or demanded an agrarian reform and the reduction and redistribution of their lands among the poor.
- **INDIVIDUAL PROPERTY VS. COLLECTIVE OR COMMUNAL PROPERTY:** Indigenous organizations and NGOs related to them are promoting the idea of communal or cooperative property as the best way to assign and redistribute the land, encouraging the idea of a new agrarian reform. Defending individual property rights will automatically cause opposition from these groups.

However, it is necessary to point out the fact that, according to the 2003 National Agricultural Census, 830 thousand rural plots ("fincas") exist in the country, of which more than 95% are individually worked.

- **RELATIONSHIPS BETWEEN FORMAL AND INFORMAL BUSINESSMEN:** According to journalistic information, a new proposal on fiscal policy has been developed by formal businessmen – since they oppose a government raise of tax rates, they are proposing that a fine or penalty ("Boleta Fiscal") be charged to businessmen who are not registered in the Tax Administration Authority. The scope and extent of the measure is not known, but it appears to be a contribution which charges informal businessmen use of streets for business activities.

The overall view of informality by formal businessmen is a negative one, according to the Chamber of Commerce of Guatemala. They share a traditional approach to the problem, believing that informal businessmen are disloyal competition and should simply be eliminated.

TABLE 3
TYPES OF EXTRALEGALITY AND THE MAGNITUDE OF DEAD CAPITAL IN GUATEMALA

	Category	% of total # of properties	% Dead Capital	% extralegal properties	Causes of Extralegality
URBAN AREA	PROPERTIES OF EXTRALEGAL ORIGIN Invasions and precarious settlements on public and private land	20	100	20	The occupation of the land and the building are illegal. They do not have titles.
	EXTRALEGALIZED PROPERTIES <ul style="list-style-type: none"> ▪ Extralegal subdivisions and land developments in private land. ▪ Properties undertaking procedures to obtain ownership through adverse possession. 	40	100	40	The occupation of the land is legal, but the development and subdivision of the land are illegal. The titles are not registered at the Public Registry.
	REGISTERED PROPERTY <ul style="list-style-type: none"> ▪ Faulty registry records (duplication, errors, etc). ▪ Extralegal transfers of registered properties. ▪ Properties that have obtained adverse possession titles but that have not completed the required 10 years following registration. ▪ Properties in deteriorated areas and hazardous neighborhoods ▪ Untitled homes in government housing projects. 	40	75	30	The information on the registered title is unreliable. The title is not accepted.
	TOTAL URBAN AREA:	100	—	90	
RURAL AREA	EXTRALEGAL SUBDIVISIONS Extralegal subdivision of individually or collectively owned (community, cooperative) agricultural land.	30	100	30	There is no information on these properties in the cadastre or registry.
	INCOMPLETE TITLING Incomplete titling of property adjudicated by the government during the Agrarian Reform carried out by the National Institute for Agrarian Transformation (INTA).	20	100	20	There is no existence of title or the existing titles have not been registered
	LAND DISPUTES AND INVASIONS	10	100	10	Title cannot be accepted dispute has been resolved
	REGISTERED PROPERTY <ul style="list-style-type: none"> ▪ Extralegal transfer of registered property ▪ Properties carrying out adverse possession procedures or with less than 10 years since registration. 	40	68	27	The information on the registered title is unreliable. The title is not accepted.
	TOTAL RURAL AREA:	100	—	87	

ANNEX 1
PRINCIPAL CHARACTERISTICS OF
THE ECONOMY IN GUATEMALA ⁽¹⁾

1. The population of Guatemala is 11.7 million, and grows at a rate of 2.6% per year (the population of Norway increases at a rate of 0.5% and Chile, 1.5%).
2. Close to 60% of the population lives in rural areas (in Norway, 25% and in Chile, 14%).
3. The economically active population (EAP) is 4.4 million (38% of the total population) and approximately 4 million (91%) are working.
4. In Guatemala, 16% of the population has an income of less than US\$ 35 per month (in Chile 9%). Similarly, 37% of the population receives less than US\$ 70 per month (in Chile 9%). These are international indicators of the extreme level of poverty in a country.
5. The poorest 10% receives only 1% of the national income (in Norway this group receive 4% and in Egypt, 4%). The richest 10% receives 48% of national income (in Norway, 22%, and in Egypt, 30%).
6. The Gross National Income (GNI) of Guatemala is US\$ 19.6 billion and the GNI per capita is US\$ 1,680 (the GNI per capita in Norway is US\$ 35,630 and in Chile, US\$ 4,590).
7. The average annual inflation between 1990 and 2001 was 9.7% (in Chile it was 8.3% and in Norway 2.2%).
8. The Gross Domestic Product (GDP) is US\$ 20.5 billion, and between 1990 and 2001 it grew at an average rate of 4.1% per year (in Norway it grew 3.5% and in Chile 6.3%). It is estimated that the GDP of Guatemala will increase 2.6% this year (therefore, the GDP per capita will remain constant) and 3.5% in 2005 (that is, the GDP per capita will grow at least 1% in 2005).
9. The average productivity of a manufacture worker in Guatemala is US\$ 9,235 and is equivalent to 28% of the average productivity in Chile (US\$ 32,977) and at 18% of the average production in Norway (US\$ 51,510).
10. The average productivity of an agricultural worker is US\$ 3,307 and is equivalent to 63% of the average productivity in Chile (US\$ 5,256) and 4% of the average productivity in Norway (US\$ 74,779).
11. Per capita exports in Guatemala are US\$ 211 (in Norway they are US\$ 12,857 and in Chile, US\$ 1,132).
12. The external debt per capita in Guatemala is US\$ 430 (in Peru it is US\$ 1,046 and in Chile, US\$ 2,490).
13. In Guatemala, 52% of the Gross National Income (GNI) is generated by extralegal economic units (20% in Chile and 13% in United Kingdom).
14. The cost of starting up a business is equivalent to 67% of the GNI per capita (in Chile, 12% and in Norway 4%).

⁽¹⁾ Estimates based on World Development Indicators 2003, The World Bank, 2003.

15. The cost of enforcing a contract is equivalent to **20%** of the GNI per capita (in Chile **15%** and in Norway **10%**).
16. The cost of liquidating an enterprise is equivalent to **18%** of the value of the assets of a company in liquidation (in Chile, **18%** and in Norway, **1%**)

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ANNEX 2 ESTIMATE OF DEAD CAPITAL IN GUATEMALA

1. DEAD CAPITAL: REAL ESTATE

a) Urban Dead Capital

- According to National Census XI of the Population and VI of Housing, 2002, there are **2,200,608** houses in Guatemala.
- Estimates show that approximately **90%** of these dwellings (**1,980,547**) are classified as extralegal and are divided into 7 categories:
 - It is estimated that **20%** of the dwellings (**440,122**) are properties of extralegal origin (precarious invaded settlements, without legal title). The estimated average value of these dwellings is **US\$ 5,400**. Therefore, the dwellings in this category have a total value of **US\$ 2.38 billion**.
 - Approximately **40%** of the dwellings (**880,243**) are properties that have become extralegal. The estimated value of each dwelling is **US\$ 13,000**. Hence, the dwellings in this category have a total value of **US\$ 11.4 billion**.
 - It is estimated that **30%** of the dwellings (**660,225**) are registered but with defects. The estimated value of each dwelling is **US\$ 17,000**. Therefore, the dwellings in this category have a total value of **US\$ 11.2 billion**.
- Consequently, the **total value of the dead capital in the 1,980,547 extralegal urban properties is approximately US\$ 25 billion**.

b) Rural Dead Capital

- According to the National Agricultural Census IV, 2004, there are **830,684** rural holdings (*fincas*) in Guatemala.
- It is estimated that some **87%** of these properties (**722,695**) are privately or collectively owned parcels that can be classified as extralegal since they are affected by one of a number of administrative and legal limitations, as well as by *de facto* situations, that generate extralegality.
- The procedure to estimate the value of dead capital accumulated in extralegal rural holdings was as follows:
 - An estimate was made of the value added by agricultural activity (**US\$ 4.714 billion**), which is equivalent to **23%** of the Gross Domestic Product (**US\$ 20.5 billion**).

- It was estimated that **52%** of the value added by agricultural activity is generated by **722,695** extralegal rural holdings. Therefore, the extralegal agricultural value added is **US\$ 2.4 billion**.
- The value of extralegal rural holdings was estimated by calculating the actual value of the flow of extralegal agricultural value added, using a discount rate of **10%** per year.
- Consequently, the value of rural dead capital in the **722,695** extralegal rural holdings is approximately **US\$ 24.5 billion**.

2. DEAD CAPITAL: BUSINESS

- a) The Ministry of Economy estimates indicate that there are **1,350,000** enterprises distributed in the categories of micro, small, and medium enterprises.
- b) It is estimated that **90%** of these enterprises (**1,215,000**) are classifiable as extralegal enterprises and include all of the micro enterprises, the majority of small enterprises, and some of the middle-sized enterprises in the country.
- c) It is estimated that the value of the assets (machinery, furniture, equipment, etc.) of a typical extralegal Guatemalan enterprise is in the order of **US\$ 5,000**.
- d) The total value of the assets of extralegal enterprises, therefore, is **US\$ 6.1 billion**.
- e) Consequently, the value of dead capital in business assets is approximately **US\$ 6 billion**.

3. TOTAL DEAD CAPITAL

The value of dead capital in Guatemala is approximately US\$ 55.5 billion.

Dead capital in urban real estate	US\$ 25,047
Dead capital in rural holdings (<i>fincas</i>)	24,875
Dead capital in business assets	6,000

Therefore, the value of dead capital in Guatemala is US\$ 4,750.

ANNEX 3
RELATIVE IMPORTANCE OF DEAD CAPITAL IN GUATEMALA ⁽¹⁾

The dead capital in active businesses and urban properties in Guatemala (US\$ 55.5 billion) is:

- 14** times greater than the total portfolio of current loans in the banking system (US\$ 3.8 billion).
- 19** times greater than the net international monetary reserves of the Bank of Guatemala (US\$ 2.9 billion).
- 33** times greater than the total assets of the Industrial Bank (US\$ 1.7 billion).
- 188** times than the total assets of the National Mortgage Credit Bank of Guatemala (CHN) (US\$ 232 million)
- 239** times greater than the market value of the stock registered in the National Stock Exchange (BVN) (US\$ 232 million).

**SOME OF THE POSITIVE EFFECTS OF THE FORMALIZATION OF BUSINESS
AND REAL ESTATE ASSETS IN GUATEMALA ⁽²⁾**

- 1. Would increase the market value of formalized properties**
 - a) The average value of a formalized property (US\$ 12,650) would increase US\$ 925.
 - b) Consequently, the total current value of the 1,980,547 extralegal properties (US\$ 25 billion) would increase US\$ 1.8 billion as a result of formalization; this is equivalent to an increase of 7%.

- 2. The owners of formalized properties would have access to bank credit**
 - a) In the first 4 years after formalization, at least 5% of the owners (99,027 proprietors) would secure bank loans averaging US\$ 5,800, using their properties as collateral.
 - b) The total value of the guaranteed loans by formalized properties would ascend, approximately, to US\$ 574 million in the first 4 years of the formalization, which is equivalent to 15% of the total valid credit purse in the Banking System.

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⁽¹⁾ Estimates based on the Bulletin of Financial System Statistics, March 2004, Superintendency of Banks.

⁽²⁾ Estimates based on the results obtained in property formalization in Peru, COFOPRI, April 2004.

ANNEX 4

STUDY OF THE LEGAL AND EXTRALEGAL SECTORS OF GUATEMALA

I. LAND OWNERSHIP IN A POLITICAL AND HISTORICAL CONTEXT

- A. In Guatemala, government attempts to resolve land disputes have consisted of reconciling the interests of the different groups in conflict and in purchasing and adjudicating land through sale to the poorest farmers. No one was ever concerned about defining and protecting existing property rights or promoting its use in a market economy.
- B. The current situation in land tenure in the rural areas of Guatemala (**where 60% of the population resides**) is marked by the following historical events:
- President Arbenz's Agrarian Reform (1952-1954): Attempt to redistribute rural holdings as individual property, which only involved a small percentage of the country's land and only benefited a small group of poor peasants.
 - Coup d'état by President Castillo Armas (1954): Large landowners recuperated the expropriated land with the highest value, and the effects of Arbenz's agrarian reform were checked.
 - New land adjudication policies after Arbenz's attempted Agrarian Reform. These consisted of government purchases of land for their subsequent adjudication by sale to poor peasants (indigenous communities, landless farmers, etc.).

These policies did not generate property titles registered in favor of the peasant beneficiaries, but rather possession. Those awarded land were unable to pay the required price, and therefore, were never able to register the property rights over the adjudicated parcels. These continue to be extralegal.

- Guerrilla movements appear (in the 1960's) and peasants invade large estates. Government used land adjudications for political purposes. It awarded land to party followers to reinforce anti-guerrilla actions, while displacing communities that supported the guerrillas and adjudicating their lands to other indigenous groups to create conflicts between the different ethnic groups.
- Peace Agreements. FONTIERRA, an entity created by the government, negotiated the purchase of land with the respective landowners in order to sell it, individually or collectively, to poor peasant and demobilized guerilla groups with productive projects.

C. As a result of the above, there are large differences in land ownership and the concentration of wealth throughout the country:

- The majority of the wealth of the country, as well as the large family-owned and industrial agricultural properties, is concentrated in the southern departments, **which represent 10% of the territory and hold 20% of the population**. It is estimated that two thirds of these properties are in legal order. The remaining third, on the other hand, is extralegal, and is characterized by extralegal land transfers, overlapping boundaries, and errors in registry records, to name a few.
- In contrast, levels of poverty are very high and property rights over land are primarily extralegal in the central and northern departments, **which represent 90% of the territory and holds 80% of the population**. The land in these departments primarily consist of smallholdings and indigenous land, most of which are held extralegally. The ownership of these lands is often under dispute, and in some cases, results in armed confrontations between the legitimate holders and the professional squatters.

D. **In the cities**, current land tenure has been determined by the following factors:

- Continuous migration from villages and small, populated centers to the principal cities of the country since the 1950's (in Guatemala City, for example, the population increased from 1.3 million in 1981 to 2.5 million in 2002);
- Squatting on municipal and state owned land in the main cities, as a result of migration and the deterioration/destruction of the traditional areas of the city (earthquake of 1976);
- Clandestine land development in the outlying areas of principal cities not incorporated into the urbanized areas of these cities;
- The accelerated urbanization of the outlying municipalities (small communities) of the principal cities;
- The inefficiency of public housing programs —which reached only the middle class and had almost no impact on the poorest sectors;
- The massive increase of extralegal transfers and the outdated property registry, both of which result from the taxes and administrative costs that burden legal transfers of property.

- The public has a negative opinion (distrust) of the registry. A popular joke about the registry says that a property owner has to go to check the registration each week to ensure that his house has not been sold to another person.

C. There is no system for massive formalization of extralegal property:

- The only legal avenue for regularizing extralegally acquired property —possession of land that has not been surveyed and mapped by the cadastre, property acquired through extralegal transfers— in Guatemala is the legal procedure known as **adverse possession** (*titulación supletoria*).
- To regularize property through adverse possession, one must have had the land in his/her possession for 10 years, after which time one must follow a judicial procedure for an additional 2 years. After the judicial proceedings have been completed, the property title can be contest by anyone for up to 10 years after it has been granted.
- **Therefore, in practice, complete and indisputable property rights are only obtained 22 years after acquiring possession** (bankers have confirmed this —they only provide credit 10 years after someone has obtained a title through adverse possession).

III. INSTITUTIONAL PROBLEMS THAT DETERMINE EXTRALEGALITY IN BUSINESSES

Approximately 85% of the 1 million 350 thousand enterprises in Guatemala are organized as single-person enterprises or family operations that legally appear under the name of the head of the family.

A. Absence of legal mechanisms

- **These enterprises do not have access to efficient organizational forms that would allow them to increase productivity through the division of labor:**
 - ❖ They cannot organize or establish themselves as limited liability companies or joint stock companies (S.A. or S.R.L. in Spanish) because of the high costs of remaining in or withdrawing from the market that the country's laws impose on these types of business organizations, costs which are higher than those imposed on single-person enterprises.
 - ❖ They cannot legally differentiate between the ownership of the business assets and the administration of the business.
 - ❖ They do not have a system of limited liability that clearly differentiates between the owner's assets and those of the business.

- ❖ They cannot issue shares legally to attract investment.
- ❖ They cannot enter into contracts or guarantee credit to expand activities, acquire more appropriate technology, and renovate assets.
- **These enterprises do not have access to the legal mechanisms that promote efficient expansion/growth:**

- ❖ There are no information systems to provide data on the financial status and the assets of extralegal enterprises. Despite efforts made by microenterprise associations, existing credit bureaus and registries operate hand in hand with the formal financial system, which only collect information on credit and debt operations of their formal clients.
- ❖ It is impossible to obtain reliable information on the operations of extralegal enterprises. The **accounting system** in Guatemala is complicated and enterprises necessarily require the help of specialized professionals (accountants) to keep their books up to date. Most extralegal enterprises are not up to date in their accounting, or simply have never kept accounting books.

The accounting system forces enterprises to opt for inefficient business organizations. Legal requirements for single-person businesses are less complicated with respect to accounting and tax obligations. As a result, most small family-run enterprises have chosen to be registered legally as single-person enterprises.

- ❖ The outcome of a judicial procedure to enforce a contract, which can take years to complete, is unpredictable. Consequently, most extralegal enterprises forego expanding their activities through business association contracts with other enterprises or seeking credit from third parties outside of their family circles and community.

In Guatemala, the extralegal entrepreneurs interviewed indicated that even **checks or other instruments of exchange**—such as **bills of exchange** or **IOUs**— are not considered reliable. The judicial procedures are so cumbersome that it is difficult to have checks honored or have those who write bad checks detained (there are no prison sentences for debts).

The cost of executing a contract is equivalent to **20%** of the GNI per capita (in Chile, **15%**, and in Norway, **10%**).

- ❖ Most extralegal enterprises do not have access to formal credit. The microfinance specialists interviewed held that 95% of the micro and small enterprises—most of which are extralegal—are excluded from the formal financial system. The alternatives for extralegal enterprises include:
-

- Microfinance banks (such as savings and credit cooperatives, NGOs, Banco Quetzal) that grant loans on a small scale. These are guaranteed using solidarity group principles (*as in the Grameen Bank*).
- Credit extended by moneylenders that operate in areas where extralegal enterprises are concentrated —central markets in the cities— and who provide credit without formal guarantees at a monthly interest rate between 10 and 20 %.
- The system called “Cuchugal”, which is the typical savings and credit association club (also known as *juntas* or *panderos*) organized by groups of people whose activities are related and which allows them to cover a small part of their financial needs.

None of the aforementioned alternatives are able to cover the long and medium term financial needs of these enterprises.

- ❖ The bankers interviewed indicated that, along with the absence of secure property titles and reliable information on enterprises, the delay in the foreclosure of guarantees impedes them from taking the risk of extending mortgage-backed credit to small enterprise owners.

Those interviewed estimate that **the judicial foreclosure of a mortgage can take more than 5 years**. In this type of judicial procedure, the defendants can present the so-called “appeals” against the actions of the judge or the plaintiff. Each of these appeals can delay the conclusion of the proceedings by up to 6 months.

B. Obstacles and costs of starting up (access), operating, and closing a business

- **Problems that impede ACCESS to efficient business organizational forms:**

- ❖ The requirements and costs of legally incorporating a business are not a problem. By law, incorporation only requires that one go to a notary, register in the Commercial Registry and obtain a company and commercial license, register at the taxpayer registry in the Superintendency of Tax Administration (SAT). The legal procedure takes between a month and a month and a half to complete, depending on the complexity of the company contract.
- ❖ The entrepreneurs interviewed opt for extralegality because of the elevated costs of operating legally and the complexity and costs of liquidating a business. In Guatemala, becoming legal means being trapped by the costs and difficulties of the system. Entrepreneurs do not enter because they know that once they are in it is difficult to get out.

- ❖ With regard to the sectorial permits for opening an establishment, entrepreneurs currently do not require a municipal operating license. However, the Office of Construction in the municipality must authorize the opening of the establishment. This requires not only municipal verification, but also obtaining a series of documents and sectorial authorizations, the latter of which involves various public entities depending on the type of activity the entrepreneur wishes to carry out.
- ❖ For example, if an entrepreneur wishes to open a small restaurant in the department of Escuintla, he must previously:
 - i.) Register the business and obtain a business license at the Commercial Registry;
 - ii.) Register with the taxpayers registry at the Superintendency of Tax Administration (SAT);
 - iii.) Register employees at the Guatemalan Social Security Institute (IGSS);
 - iv.) Apply for an operating license at the corresponding municipality;
 - v.) Obtain authorization for handling food from the Ministry of Health;
 - vi.) Obtain authorization to install a sound system from the governor;
 - vii.) Obtain the license for the sale of alcoholic beverages at the Superintendency of Tax Administration (SAT);
 - viii.) Have accounting books authorized, etc.
- ❖ One of the people interviewed explained that compliance with all of these requirements could take an entrepreneur at least 6 months and cost him over US\$ 500, if one takes into account the cost of the paperwork (including accountant services and the payment of “tramitadores” — paperwork runners), the time invested, and administrative fees.
- ❖ The municipal authorities of Guatemala City revealed to us that those enterprises requiring previous authorization from the Ministry of the Environment need to follow a procedure that, depending on the line of business and characteristics of the establishment, can take from 6 months to 2 years to complete before they can continue with the procedures for obtaining the construction license for opening the establishment.

The cost of starting up a business is equivalent to 67% of the GNI per capita (in Chile, 12% and in Norway, 4%).

- **Legal operation of a business:**
 - Operating a business legally is another big problem. Tax returns are complex and require the services of an accountant.

- ❖ Entrepreneurs must keep the Guatemalan Social Security Institute informed as to the status of their employees and comply with a number of labor obligations.
- **Closing a business legally:**
 - ❖ Liquidating a business in Guatemala is very complicated. To liquidate a business, an entrepreneur must cancel the registration with the Superintendency of Tax Administration (SAT), for which one must submit tax returns, have accounting books up to date, and submit copies of the last receipts issued. The tax authority then liquidates pending taxes and imposes fines for any administrative error. In addition, one must cancel administrative registrations at the Guatemalan Social Security Institute (IGSS), as well as pay all pending debts and/or pay a fine for any infraction detected. **The entrepreneurs interviewed indicate that the procedure can take more than 1 year to complete and that the costs involved cannot be predicted.**
 - ❖ Consequently, most entrepreneurs prefer to keep their businesses closed, apparently functioning, and wait for the amnesty (exoneration from paying tax debts and interests) that is periodically decreed by the SAT. The problem with amnesties is that their application depends exclusively on the will of the authorities.

IV GOVERNMENT RESPONSE TO THE PROBLEMS OF EXTRALEGALITY AND PROJECTS UNDER WAY

- There have been no programs for massively formalizing property. The policy has been to work on a case-by-case basis. The Municipality of Guatemala (through the Human Settlements and Housing Office-DAHVI) has formalized a few settlements, but over prolonged periods and as part of their efforts to improve the living standards of the poor.
- Government housing programs have only covered a small percentage of housing needs and have generated extralegality (beneficiaries stopped making payments and did not receive their titles).
- The new National Cadastre law is a current issue in the country. They want to use the international financing available to survey and map the country in its entirety, but the draft law has been held up in Congress for the last 2 years. There is much uncertainty as to the outcome of the debate in Congress: on the one hand, indigenous organizations are arguing for the redistribution of the land through the cadastre, and on the other, large landowners (*finqueros*) want the cadastre to be limited to doing the technical work of gathering information on existing titles.

- The modernization of the Public Registry. Approximately 10 years ago, international companies were contracted to modernize the system. Computer equipment was purchased, and the registry began computerized operations. Last year, however, the entire system crashed and part of the information was lost. This event is still being talked about.
- Local organizations are beginning to design and implement institutional reform and administrative simplification projects. FUNDESA, for example, has two projects on the drawing board (they plan to begin work in a few months); one on competitiveness, and the other on administrative procedures (to simplify paperwork). Their focus is on lowering the costs of remaining legal and increasing the benefits of doing so. Their aim is to propose reforms based on the analysis of the laws and institutions of the country carried out by holding meetings with professionals and micro-entrepreneurs.

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ANNEX 5

PROJECTED IMPACT OF ILD REFORMS ON THE ECONOMY OF GUATEMALA

How can we determine if the measures we propose will have a positive impact on the economy of Guatemala? Most economists agree that an exact quantification is not required to know what the impact will be or to have at least an understanding of the sense of the proposed reforms, especially in complex contexts when numerous variables interlink. Alan Greenspan, Chairman of the Board of Governors of the Federal Reserve System of the United States, recently mentioned that, in spite of the fact that nobody in the country has been able to measure the effects that information technology has had on production, any reasonable economist knows that the effects have been positive. Moreover, any quantification exercise could be very complicated given the number of direct and indirect effects in play.

However, past experience and research demonstrate the positive impact of our reforms. Let us begin with the ILD's positive experience in Peru and El Salvador where similar reform programs were implemented, although of much lesser magnitude than those to be proposed for Guatemala. Between 1982 and 1996, with an investment of US \$17 million from USAID and US \$1.2 million from CIPE, the ILD created a program to bring the poor majority that operated in the extralegal economy —where they were susceptible to recruitment by terrorist organizations— into the formal economy. The results have been adequately documented and show that the poor in Peru obtained US\$ 9.4 billion in net benefits since 1991 until 2002, equivalent to an annual rate of return of 173%, or a cost benefit ratio of US\$ 2.70 for each US\$ 1.00 that USAID and CIPE invested in the ILD. It is important to mention that these figures do not include benefits that are not quantifiable, such as the 28% reduction of child labor in those families that received formal titles.

Historical Support

History too provides information that supports the potential economic benefits of extending a system of formal property rights to rural areas. The results of the reforms in 1946 in Japan designed to provide poor citizens with property titles far exceeded the most optimistic projections: within four years, approximately 50% of the land had been formalized and by 1952, six years after initiating the reforms, farmer income increased by 80%.

Between 1953 and 1963 in Taiwan, newly titled rice farms increased their production by 60% and their owners increased their income by 150%. Similar results were observed in Vietnam where between 1993 and 1998 the government granted property rights for 20 and 50 years for annual and multi-annual harvests, respectively. Annual production increased 3.4% where farmers had these rights, and the overall percentage of the population below the poverty line decreased significantly: from 58% to 37%.

In China, property formalizing carried out between 1980 and 1990 helped to increase gross agricultural product by 86%, and this extraordinary result does not include the benefits of technical reforms, such as the green revolution. More impressively, the per capita income of Chinese farmers over the 10 year period between 1978 and 1988 increased by 192%. Between 1978 and 1984, the total productivity in the agricultural sector increased by 41% for institutional reasons alone, while the productivity growth of the total crop production grew 48% as a result of the change in the property rights regime.

A recent three-year survey in a commune in the Ukraine has shown that the 3 million members who received titles earned an income that is 81% higher than that received by the 3.7 million people who did not have a title. In Russia, only 5% of the agricultural land has been titled (dachas) in favor of its holders over the same period. However, this same 5% produces 50% of Russia's total agricultural output, while the remaining 95% produce the other 50%.

Scholarly Confirmation

Recent academic analyses and statistics support the correlation between property reform and increased prosperity. "The Index of Economic Freedom" compiled by The Heritage Foundation (HF) in Washington and "The Economic Freedom of the World Index" run by The Fraser Institute (FI) in Vancouver, Canada, both provide economic estimates that show that the countries with a higher level of income are precisely those that have reformed their regulations, included their citizens under the rule of law, and have given them property rights—in this regard, very close to what that the ILD proposes. The Fraser and Heritage indices also carry out measurements of the correlation between institutional variables and the level of growth rate of per capita income so as to reconfirm their relevance as explanatory variables. It is important to note that the HF and FI indices lack the precision, scope, and analytical connection to economic development of the institutional components that the ILD usually proposes. If they could incorporate these into the variables underlying the indices, we believe that the HF and FI indices would make an even stronger case in favor of the reforms the ILD is proposing.

University Professors have also begun to recognize the significant role of property rights in economic growth. The Harvard economist Robert Barro, for instance, has put property rights at the center of his research and in his forthcoming book on macroeconomics. A recent World Bank publication, "Doing Business 2004: Understanding Regulation", also adopts the ILD thesis; that is, reasonable and adequate regulations have a positive effect on the growth and well being of a county, whereas excessive and inadequate regulations have a negative effect. According to UCLA's Al Harberger, the excessive cost of doing business is the main variable explaining economic growth. ⁽¹⁾

¹ Arnold C. Harberger, "A Vision of the Growth Process", in *American Economic Review*, Volume 88, Issue 1, March 1998.

Professor Friedrich Schneider's recent work is equally interesting. Schneider has run correlations between the informal sector, which he calls "shadow economy", and the GDP growth rate, finding a significantly negative relationship —high rates of informality are associated with low growth rates, and consequently, reductions in the informal sector are associated with significant increases in the GDP growth rate. (²)

Also of interest are studies done by the McKinsey Global Institute (MGI). Although the McKinsey work differs in focus and is not dedicated to formalizing the extralegal economy, nor does it include most of ILD variables, it does measure the effect that different sectors have on productivity and the effect that these have on economic growth. The MGI studies also measure the effects that institutional reforms geared toward removing obstacles and barriers to productive activity have on a country's economy. After carrying out field work in various countries —which fundamentally focuses on the formal sector of the economy, but explicitly uses ILD concepts— MGI has concluded that in high-income developing countries the final impact that improvement in productivity will have will be a 2 percent increase in a country's GDP. The impact on lower income countries will be even greater, as shown in the case of India where the impact has been calculated to reach 5%.

The Economic Models

Another way to quantify the impact of the proposed reforms is through macroeconomic models. However, these models have several drawbacks.

First, there is no economic model that includes all of the reforms proposed by the ILD. On the whole, the economic models marginally incorporate institutional variables, thereby underestimating their impact on economic growth.

Second, these models are only approximations of the potential impact given that they are based on historical information. However, according to Professor Robert Lucas, when substantial policy changes are brought about in a country — as would be the case in Guatemala if proposed ILD reforms were adopted— the coefficients of the models would be significantly modified.

Third, in connection with the two previous points, a specification problem arises regarding the selection of adequate explanatory variables and their relation with the variable that they are meant to explain.

Fourth, as mentioned by William Easterly (³), a countless number of unforeseeable elements make predicting economic growth difficult; factors which often lead to results that are opposed to those initially foreseen.

² Friedrich Schneider, "Dynamic Effects of the Shadow Economy: An Empirical Approach" Johannes Kepler University Linz, Linz, Oct 2003 Mimeo

³ Easterly William, *The Elusive Quest for Growth*, MIT Press, 2001.

Lastly, there is also great difficulty in gathering data to provide adequate information for these models. According to the experience on extralegality that ILD has gained in the field, the only way to obtain this information is through detailed and extensive fieldwork that is usually not available in developing countries.

Despite these drawbacks, the ILD has carried out a preliminary estimate of the impact that some of the proposed reforms would have on economic growth in Guatemala. To make the estimate, we used the model designed by professors Gwartney of the University of Florida, Lawson of Capital University, and Benson of the State University of Florida. The model, created to calculate the "Economic Freedom of the World Index" and applied to a sample of several countries, has been adapted to include as indicators the effects of four of the reforms that the ILD proposes: start-up procedures, contract enforcement procedures, liquidation procedures, and the degree of coverage of credit bureaus. The results obtained from the application of this model indicate that if the reforms are 80% successful, GDP per capita in Guatemala will increase between 2.8 and 3.8 percentage points per year. If they are only 60% successful, then the increase of the GDP per capita in Guatemala will be between 2.1 and 2.8 percentage points per year.

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Conservative News and Information

Optimism in the midst of despair

Jack Kemp

April 19, 2004

No one can doubt that it's been a tough couple of weeks in Iraq. In spite of repeated attempts by the United States to negotiate a truce with Iraqi insurrectionists, the violence has only intensified. April already has become the most deadly month for U.S. soldiers in Iraq.

One may be tempted at times such as this to get discouraged and to think nothing good is likely to come out of Iraq. But I remain optimistic in the midst of growing despair by some of my friends because I am seeing firsthand how reform and liberalization are occurring in the Arab world, specifically in Jordan, Egypt, Kuwait and the United Arab Emirates. There is no reason that the same process cannot be applied to Iraq and Afghanistan in the fullness of time.

I recently returned from trips to Egypt, Jordan and the UAE, where reform is proceeding apace. Egypt is sending a delegation to the United States in June to discuss with Congress and the Bush administration bold reforms to which the Mubarak government has committed itself in creating private property rights, advancing market reforms and bringing the informal economy above ground, making it formal and vibrant. Peruvian economist Hernando de Soto and Empower America are working together to assist the Egyptian government as it embarks on this adventure in economic reform, and we hope that Egypt can serve as a platform and a model from which similar reforms can spread throughout the Arab and Muslim world.

In Jordan, King Abdullah II is boldly and courageously pushing the envelope on reform. I have seen firsthand what he described in his prescient Wall Street Journal column recently, and I can attest that it is real. In his column, King Abdullah also offered some very profound insights that we in the West should take to heart, especially as they apply to Iraq during these trying times: "Most Arabs agree that reform is vital," King Abdullah wrote, but he also admonished well-wishers in the West that "effective reform must come from within Arab societies. Justified or not, many Arabs do not trust the motives of Western-inspired Arab reform. They look to Islam's own proud tradition of humanistic values, and they believe that Muslim nations are more than able to generate peaceful, democratic regimes."

I am convinced that King Abdullah's wisdom applies not only to democratic and economic reform in general but more specifically - and perhaps even more aptly - to putting down

insurrection, dampening the flames of civil war and organizing a representative government in Iraq virtually from scratch. As the June 30 deadline for returning sovereignty to the Iraqi people approaches, I hope the administration will work closely with other Arab leaders such as King Abdullah and other young leaders in the region as they seek to nurture a new Iraqi government onto its feet.

Islamic civilization made great contributions to science, medicine, architecture and the arts in centuries past, and those contributions occurred when it showed the most tolerance toward religious minorities. It is, therefore, not surprising that Jordan and Egypt, two of the most tolerant Muslim nations, are leading the way toward Arab reform and revival in the 21st century under leaders like King Abdullah and the Mubarak government. Tolerance and liberty are the interlocking pillars of a free society.

Liberty means having the freedom to think and advocate anything you desire and to live your life any way you want, so long as doing so does not encroach on other people's freedom to do the same.

The 21st century can usher in an Islamic renaissance. By erasing the tolerance deficit and showing respect for other religions, Arab democracy and economic development can bloom, freedom can flourish and the full potential of the Arab people can be unleashed to close the development gap with the rest of the world. As Iraqis regain the reigns of sovereignty, they will look to Arab examples for how to build a free and prosperous society. They couldn't do better than heed the words of King Abdullah and apply the work of Hernando de Soto.

News Focus

Raising The Dead

By Jason Ingraham
Photographer Silvia Dogliani, El Comercio

The government has turned to economist Hernando de Soto for ideas about jumpstarting the economy

Culturally driven theories of development have never been very popular in this part of the world. So, it must be refreshing for government officials to hear a leading economist say that while change must come from within, it does not require a cultural overhaul.

Hernando de Soto refuses to blame such things as the absence of a "Protestant work ethic" for the failure of capitalism outside the West. In his popular book, "The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else," the Peruvian national argues that the absence of laws relevant to all segments of society is the real reason why capitalism has let down the non-Western world, particularly the poor. The incongruous relationship between the law and the people has led to an abundance of untapped potential in the form of unregistered businesses and real estate without titles, which de Soto dubs "dead capital."



Photographer Silvia Dogliani

De Soto has seen more than enough dead capital in Egypt since he received an invitation from officials at the Egyptian Center for Economic Studies (ECES) to do a detailed study of the country about four years ago. ECES officials had found great similarities between Egypt and Peru, where de Soto started his groundbreaking work with the Instituto Libertad y Democracia (ILD). The two organizations are now wrapping up a study they hope will convince government officials of the need to pull the informal economy out of the shadows by adopting meaningful reforms.

More than eight million Egyptians are employed in the so-called informal sector, which is more than the number employed by the formal private sector (6.8 million) or the government (5.9 million), according to rough estimates by the ECES. The informal sector is also known as the extralegal sector - not to be confused with illegal - because it exists outside the law. Additionally, the vast majority of real estate, some 12 million properties, is not registered with the government.

All told, de Soto and his Egyptian colleagues estimate that the value of the country's informal assets - including businesses, homes, animals and machines - is more than \$240 billion, which de Soto points out is five times more the amount of foreign direct investment in Egypt since Napoleon Bonaparte and the French gave up Egypt to the British in 1801. They also suggest that most Egyptians do not work in the informal sector to avoid paying taxes. Many would be happy to have their assets protected by the government if not for the time and money it takes to follow the letter of the law, says de Soto.

Egypt is not alone. The accumulation of dead capital has been a worldwide phenomenon. A massive influx of migration from the country to the city has created huge populations working and living outside of the formal sector, as the laws have not adapted to accommodate for them. De Soto first noticed the trend upon returning from Europe to his native home, Peru, in 1980.

"I saw [informal workers] on the sidewalks," de Soto told bt. "I was in the mining business; I saw them as my competition without licenses. I saw them in the amount of taxis that were not recorded or registered. I saw the amount of houses that were not on the map."

Soon after, de Soto founded the ILD and discovered thriving informal sectors in areas as diverse as the Middle East to the former communist states of Eastern Europe. If history is repeated, these countries will be bound by the fact that no country has been able to shed its status as a developing nation without formalization of business and real estate, de Soto argues.

Do as we did, not as we say

The West has largely forgotten how it developed, according to de Soto.

Through research, he believes he has unveiled the preeminence of law in the development of the United States. In the 19th Century, the law had to be modified, albeit begrudgingly, to give squatters on the western frontier land and in mines legitimate claim to their property. The change was revolutionary, de Soto says, and needs to be replicated in areas where capitalism has failed for everyone but the elites.

Without legal title, real estate cannot be turned into collateral to secure a loan. Without access to capital, large segments of the population are powerless to boost a country's productivity, which most economists believe is a central component of development. Formalization also contributes to the division of labor and specialization, says de Soto.

By bringing the informal economy into the mainstream, de Soto believes that the division of labor will increase as companies move out of family living rooms, figuratively speaking in some cases, and greater degrees of specialization become possible as the country attains larger economies of scale.

"You do not have one market economy in Egypt, you have many thousands of fragmented economies," says de Soto.

Each of these economies is governed by its own laws, de Soto says, which is why the government desperately needs to streamline them. Such a process would surely prove difficult, as any revisions to the law would have to hold up across diverse constituencies that have found unique ways of showing ownership of real estate or businesses.

Reform of the legal sector would be much more effective in promoting development than what is prescribed by many social development agencies, de Soto says. Eastern countries now poised to integrate into the European Union, for instance, are not given handouts but are required to overhaul their legal systems.

The EU treats legal reform as the priority in preparation for integration. "And when they look south, they say, 'Let's see what I've got in change in my pockets,'" says de Soto.

On one hand and the other

If formalization is adopted, it will be consumers who spend most of the time digging for change in their pockets. Though its many supporters have largely declared formalization a "win-win" situation, ECES has detailed calculations about winners and losers.

Extralegal entrepreneurs, who outnumber their legal counterparts by more than four to one, have much to gain in the form of increased profits if reforms pass. Workers may take home less pay but would benefit from newly available social insurance programs. ECES also predicts an increase in wages as productivity improves and new employment opportunities as the economy expands. On paper, consumers would have the most to lose as a result of rising prices. However, product quality would likely improve due to better surveillance and inspection.

Stoking some controversy, the government would come out as the indisputable winner if reforms were passed and formalization occurred on a broad level, according to ECES estimates. Conspiracy theorists will undoubtedly see formalization as the government's veiled attempt to boost tax revenues. Members of the local press were keen on this idea when de Soto and his Egyptian colleagues presented their findings at a recent conference.

The government seems sensitive to this fact. So sensitive, says de Soto, that officials "discouraged us from looking at the tax benefit side." The omission is likely to fuel suspicions, however, that taxes are indeed the main motive, signaling deep mistrust of the government in extralegal circles.

Formalization is not to be mistaken as a cure-all for the economy. The most optimistic readings by the ECES suggest that formalization could help the GDP grow 3.7 percent a year. The pessimistic prediction, again by the ECES, is only 0.4 percent.

Central to the proposal of making formalization work is the ability of the government to make a convincing case that it is in the best interest of extralegal firms and property owners to embrace the formal sector - and make sure those benefits are evident every step of the way. Economic incentives are probably the only way the government can win over participants in the informal economy. And there is a lot of money riding on whether the two can come together.



Fact and Comment

Steve Forbes, 02.16.04, 12:00 AM ET

Mideast Miracle?



When it comes to the middle east, the eyes of the world focus mainly on Iraq and on the Israeli-Palestinian conflict. Yet in coming months Egypt will be initiating reforms that should dramatically transform its economy into a wealth-creating, wealth-distributing dynamo that will lead millions of Egyptians into a vibrant, increasingly democratic middle class. The country is set to become an economic miracle rivaling Ireland or Hong Kong. In doing so, Egypt will deal a devastating blow to global terrorism.

The catalyst is something that's prosaic yet absolutely essential for a sustained, innovation-oriented economic takeoff: property rights.

We in America and the rest of the West take our inclusive, easy-to-access property systems for granted. You own land, for instance, and everyone recognizes it. You can readily mortgage it. Want to start a business? The legal requirements are easy. Want to sell bonds or shares or use other capital-raising instruments? The legal structures to do so are open to anyone who can meet standard requirements. Commercial contracts? They're widespread, and the courts are there to enforce them and to adjudicate disputes.

Incredibly, most of the world has no such property rights or common rule-of-law system. Japan didn't until after World War II, when, under General Douglas MacArthur's occupation, it shucked off its medieval social structure and put in place institutions and laws with principles long familiar to Americans. This dramatic change played a critical, oft-overlooked role in Japan's rapid postwar modernization and economic expansion. After all, in the early 1900s Japan's per capita income was less than that of Peru.

After several years of preparation, Egypt is about to commence a Japanese-like makeover of its society, one that will profoundly and positively impact the rest of the Middle East and the developing world. Reforms will create easy access to private property for all Egyptians, including those in city slums. All enterprises will be able to easily turn themselves into legal entities; previously, obtaining a business license had been a costly process that could take nearly two years. Not surprisingly, most Egyptian businesses are extralegal, part of the country's shadow economy.

Most development experts ignore the elephant in the room--the fact that most people in the world operate outside their country's formal legal systems. In Egypt's case, 88% of all



enterprises are extralegal, as is 92% of the country's housing. Egypt and other developing countries do not lack for entrepreneurs; they lack institutions and legal structures that would enable their entrepreneurs to expand and truly flourish. The Peru-based Institute for Liberty and Democracy, which spurred this project and is headed by economist Hernando de Soto, estimates that Egypt's shadow economy has accumulated \$248 billion in assets. But as De Soto notes, "All this activity and all the assets in the extralegal economy are dead capital--assets that cannot be leveraged to obtain credit and investment. To convert all of this dead capital into live capital requires the two cornerstones of a market-based rule of law: legal property rights that cover all of Egypt's assets and good business law for entrepreneurs."

Too often, Western aid programs assume that codifying property rights means documenting existing *formal* properties and businesses; they overlook the fact that most such assets are outside the system--they are *informal*. In the U.S. property laws often *followed* what people did informally. American property law history can be summed up as having turned squatters into pioneers.

The system prevalent in most of the rest of the world is immensely costly. It hampers the ability of businesspeople to expand. There is too little accountability for performance, and this also hobbles growth. When people are brought into the formal economy and legal system, the rule of law takes on real life. People then know who owns what. Losses can be tracked and fraud attacked. Contracts and rules can be enforced. The current informal system effectively excludes most businesspeople from having access to their national economies, not to mention the global economy. In effect, Egypt will be doing what Japan did in the late 1940s--it will be legalizing what's already there.

The massive informal economies in Egypt and elsewhere resoundingly put paid to the hand-wringing conclusion of many Western experts that certain cultures and religions are incompatible with Western-style free enterprise.

The kind of survey Egypt engaged in several years ago to discover what its informal commercial and housing patterns and systems actually were should be replicated in Iraq and other nations. Societies evolve differently, so no one-size-fits-all approach will work. What will work is to legalize, to make transparent the systems that hundreds of millions of businesspeople and homeowners around the world have already created.

Egypt backs plan bring firms into formal economy

By Jonathan Wright

CAIRO, Jan 19 (Reuters) - Peruvian economist Hernando de Soto said on Monday the Egyptian government had accepted his plan to break down financial and bureaucratic barriers which keep much of the country's businesses out of the formal economy. Under current arrangements, about 80 percent of Egyptian businesses operate without licences because they find it too expensive and time-consuming to seek legal recognition. Prime Minister Atef Obeid and his economic ministers have now asked de Soto's think tank to prepare a plan of action setting out practical steps that need to be taken, de Soto told Reuters in an interview. "The plan was accepted. That was on Saturday. Today they affirmed their commitment and said our next task was now to draw up an action plan, which means the immediate details of how we kick this thing off," he added. De Soto, who is known for his advocacy of property rights for the poor, says the Egyptian government could add several percentage points to annual economic growth if it gives the vast informal sector of the economy incentives to go formal. Without formal status, businesses cannot obtain credit, they cannot expand easily, they tend to keep a low profile and they may have to pay bribes to stay in business. A team from de Soto's Peruvian-based think tank, the Institute for Liberty and Democracy, after four years examining the Egyptian informal sector, concluded that administrative changes could transform the economic landscape. It found that it takes an average 200 days of bureaucratic work to open a business, and 549 days to open a bakery. Registration also brings recurrent costs, such as of meeting the government's sanitation regulations.

Under the institute's recommendations, the costs of setting up a business would fall 75 percent and 300 pieces of legislation would be consolidated into one law. Sixty-six government agencies would merge into what de Soto called the one stop-shop "where anyone who wants to get into enterprise has to go to one window". "The average time will go down to an average time of five days — radical," he said. Once businesses go formal, they can use assets to guarantee loans, issue shares, integrate their operations without fear and raise their profile in the market. De Soto's theory is that once the institutional structure is right, most businesses prefer to go formal, even if it means they have to pay more taxes. Egyptian Finance Minister Medhat Hassanein told a news conference after Monday's meeting with Obeid that the government was looking at ways to streamline the process of setting up small businesses and to allow their owners to obtain licences from a single place as quickly as possible. "The government is trying to provide a legal umbrella for this (informal) sector and to simplify the procedures," said Hassanein, who has been working with de Soto on the project. A new law would also make finance and land in new areas available to small businesses, he added.

(Reporting by Jonathan Wright, editing by David Stamp; Cairo bureau
+20-2-578-3290, Reuters messaging: jonathan.wright.reuters.com@reuters.net)

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Egypt on the economic cusp

Jack Kemp ([_____](#)) | [E-mail](#)

January 19, 2004

I just returned from a remarkable conference in Cairo, Egypt, put on jointly by the Egyptian Center for Economic Studies and Instituto Libertad y Democracia. ILD is led by Peruvian economist and Empower America associate Hernando de Soto, whose two books, "The Mystery of Capital" and "The Other Path," are seminal works for understanding and solving world poverty and terrorism in the 21st century.

The conference was the culmination of a joint study by the two organizations in which they developed concrete proposals on how to integrate Egypt's informal sector (what usually is referred to loosely as the "underground economy") into the formal economy. The project was conducted with the support and assistance of Egypt's Finance Ministry and would not have been possible without the personal commitment of Finance Minister H.E. Medhat Hassanein and the Mubarak government.

The particular focus of the ECES/ILD study was on how to bring the extralegal business and real estate sectors above ground and onto the books, thus turning "dead capital" into "live capital." If successful, Egypt will be the first country in the Middle East to make these reforms, and it will set a precedent and serve as an example and template for the whole Arab and Islamic world. At the conclusion of the conference, I invited the leaders to Washington in the spring to help make the case for taking these reforms beyond Egypt into Iraq, Afghanistan and beyond.

In a nutshell, the study concluded that, "Under the coarse mask of extralegal activities lies a mass of talented and hardworking people capable of creating value out of practically nothing who hold the potential for making Egypt a rich and powerful country." Egypt has approximately 1.4 million extralegal entrepreneurs, who comprise 82 percent of Egypt's entire entrepreneurial class.

The extralegal economy employs some 8 million Egyptians, and the value of business and real estate assets in extralegal enterprises totals almost \$30 billion. All told, 92 percent of the Egyptian population holds its private real estate assets extralegally, thus preventing people from leveraging property into capital. In round numbers, this "dead capital" adds up to almost \$250 billion.

In addition, Egyptian taxes, laws, paperwork and regulations thwart entrepreneurial efforts and discourage work, saving and investment. For example, the study found that it takes more than 500 days and costs the equivalent of 27 minimum monthly salaries to open a mere bakery in Egypt. Registration and licensing of a single-person business take an entrepreneur 189 days and 86 administrative steps to complete. An entrepreneur must suffer through more than 10 years of red tape to convert a sandy piece of land into a commercially useful parcel, and up to six years of judicial and administrative battles are required to avoid demolition of a business initiated in an extralegal manner.

Doing business in Egypt subjects the poor to dealing with 56 different government agencies and complying with 300 separate pieces of legislation, all of which lead to "repetitive, redundant and overlapping government inspections." Meanwhile, there are no enforceable accounting principles to standardize business activity and regularize commercial relationships. In short, the study concludes, "because businesses and real assets cannot be organized productively, using the economies of scale that would result from operating in the broad Egyptian market, and because people cannot secure the interests of all parties and be leveraged to guarantee credit and

investments, they are 'dead capital' incapable of initiating surplus production and the increasing productivity in any significant manner."

Just before the Super Bowl in Houston, I will be reporting on the Egypt conference and speaking on the topic dear to my heart - a 21st century Marshall Plan for Central Asia and the Middle East - at the Baker Library of the James A. Baker III Institute of Public Policy at Rice University. The institute's director, Ambassador Edward P. Djerejian, a leading expert on the complex political, security, economic, religious and ethnic issues of the Middle East, has written extensively on how to bring democratic capitalism to this region and how to engage in new diplomacy to the Arab world. I will be sharing with the institute the work of the 21st Century Committee, created and led by Ted Forstmann at Empower America in conjunction with ILD, where we are thinking through how best to create a 21st century Marshall Plan based, in large part, on de Soto's ideas.

Egypt stands on the cusp of an economic revolution. If the reforms proposed by the ECES/ILD study are implemented, it will ignite the most far-reaching economic and social transformations since the Japanese, Korean and Taiwanese economic wonders were created in the aftermath of World War II. If Egypt implements these reforms, it could ignite an economic transformation not only in the Middle East but throughout the entire Arab and Islamic world.

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Posted on Fri, Mar. 05, 2004

One nation under the gun

By [John Heilbrunn](#)
Special to the Star-Telegram

I met Jean-Bertrand Aristide, who fled Haiti the other day, in the spring of 2001. I was in Port-au-Prince for several days on assignment for *The New York Times Magazine*, profiling Hernando de Soto, the Peruvian economist whose obsession with spreading property rights to the poor of the Third World is rightly ranked among the most powerful ideas of our time.

Aristide had asked de Soto to help Haiti. When I interviewed Aristide at the presidential palace, I was struck by how small and soft-spoken he was. It was hard to imagine that this quiet little man was either as charismatic or as abusive to the fledgling democracy he was leading as one heard.

Aristide told me that de Soto's "scientific" approach to economic development fit well with the human dimension he stressed in his own writings. "I know the political will I have," he added. "We can make it happen."

So much for Aristide's career as a pundit. He's got bigger problems now, and so does poor Haiti.

Haiti represents poverty on a scale hard to grasp here. Eighty percent of Haiti's 8 million citizens live on less than a dollar a day. Eighty-five percent are illiterate. Most children suffer from malnutrition. Life expectancy is under 50.

On my visit, I saw naked men urinating in the street. Water doesn't run to Haitians' cement homes or tin shanties; they fill their buckets at a community tap, store what they can in unsanitized underground tanks, and boil the water before drinking or cooking.

Streets in Port-au-Prince were jammed with ragtag vendors hawking old tires, clothes, shoes and motor oil. Gas stations and funeral homes were the only decent structures on view.

To reach one section of town, we took roads so pitted that my tape recorder flew from my hand as we drove and bounced. No wonder street vendors were big on spare parts here, I thought.

A thin, grayish stream ran down the side of the street, carrying effluent from people's washing. Homes stole electricity off the main line through improvised wiring. Flies were everywhere.

Here's how economic life works for ordinary Haitians: A teacher we met explained how he bought his home for \$7,000. The seller didn't have any documents. "How did he know he was buying the right house on the right land?" de Soto asked through a translator.

The teacher knew the area, we were told. He sounded out the neighbors. Then he made up a sales agreement of sorts and had it witnessed by a few respected people on the block -- people who essentially said, "Yes, we recognize this to be so-and-so's house, and now it will be yours."

In a court, of course, this had no value. In the neighborhood, it did.

The locals had recently formed a cooperative that lent money at 2 percent a month. If you needed more than \$1,000, though, it was back to the loan sharks -- and 25 percent a month. "One doesn't want to have to live this way," one man, who dreamed of opening a small food market, told me.

I asked a group of Haitians how they would react if the government said it was launching a big new program to formalize all these property rights. Would you trust them to do it right?

"They never finish what they start," one man answered, "The people who work for the government are just out for themselves."

Brian Dean Curran, the U.S. ambassador at the time, understood.

"The state here is viewed as an agent of exploitation," he told me. "It's not by chance that so much is in the informal sector -- the formal sector is the enemy. You do it on the sly; you stay away from the authorities, work only with your family -- that's how you get around in this country. How do you bridge that cultural gap? The advantages [of de Soto's economic program] are profoundly clear -- but how do you stack that up against 200 years of history?"

Three years later, that's one of the many questions still haunting Haiti. I don't pretend to know the answers, but it's hard not to think that this latest crisis represents another deep failure of Haiti's elite, and of our own.

A decade after we reinstalled Aristide to "save Haitian democracy," we've now eased his exit, and the suffering there continues. And the Marines, confused as before about exactly what their mission is, are back in Port-au-Prince.

Matthew Miller is a senior fellow at the Center for American Progress. www.mattmilleronline.com

Junta de Consejo De Soto arrancará con nueva estructura

MARIELENA VEGA

A un paso del arranque. El gobierno de Vicente Fox tiene programado para mayo oficializar y con ello dar el banderazo de salida a la incorporación del mercado informal a la formalidad, programa que trabajará de la mano de **Hernando de Soto**, presidente del Instituto Libertad y Democracia (ILD).

Se tiene programado que sea durante los primeros días de mayo, cuando se dé a conocer los pormenores de este proyecto, que sin lugar a duda será el más importante del gobierno panista.

Aquí le podemos adelantar que la estructura que elabora un grupo de abogados para arrancar con este programa será más libre, porque la responsabilidad de su aplicación ya no recaerá sólo en la Sedesol, al mando de **Josefina Vázquez Mota**, y se trata de una estructura a la medida de México.

Ahora se hará participe a por lo menos dos secretarías más, se trata de la Secretaría de Hacienda, al mando de **Francisco Gil Díaz**, y de la Secretaría de Economía, que encabeza **Fernando Canales Clariond**, ¡claro!, además de la supervisión de la Presidencia, del área de **Eduardo Sojo**.

Con esta estructura se espera que la aplicación de las normas, reformas o cambios estructurales que vaya dictando **Hernando de Soto** tenga una mayor movilidad, pues estamos hablando de que se tiene proyectado incorporar una economía ilegal a la legalidad equivalente a 315,000 millones de dólares, es decir, una economía equivalente a siete veces el valor de Pemex, al mando de **Raúl Muñoz Leos**.

Además se está analizando la viabilidad de ampliar el equipo mexicano con el cual trabajará **Hernando de Soto**, para que los resultados se vayan viendo antes de que termine el sexenio de **Vicente Fox**, con lo cual, la economía mexicana tendría un mejor desempeño.

Lo cierto es que el peruano recientemente considerado como una de las 100 personas más influyentes del mundo, vino a tierra azteca a poner las cosas en claro, ya que la desincorporación de su equipo mexicano, con la salida de su titular **Juan Carlos Leal Sosa**, le causó más que preocupación.

Y es que, cómo se lo adelantamos en este espacio, el área en México se desintegró hace ya un mes con la salida de éste funcionario, debido a que Sedesol no le estaba dando la importancia que merece al tema, ni respeto los compromisos hechos con **Leal Sosa**.

De ahí que **Hernando de Soto**, quien estuvo unos días en el Distrito Federal, puso en alerta al gobierno mexicano al reunirse con gente muy cercana de presidencia, y con **Eduardo Sojo**, a quienes

además de solicitarles la reincorporación -a su equipo- de Juan Carlos Leal debido a que ya se encuentra capacitado y coordinado en el asunto, preguntó si de verdad el gobierno mexicano tiene interés de sacar adelante este asunto.

Más le vale al gobierno mexicano hacer bien las cosas, porque Hernando de Soto, recientemente obtuvo un financiamiento de 25 millones de dólares -por parte de autoridades estadounidenses- para trabajar con 30 países asiáticos y africanos, así como firmó un par de proyectos más, con Egipto y otro con Rusia. Por lo que el especialista peruano dejó en claro, en esta visita a tierra azteca, que no tiene tiempo para estar jugando o invertirle tiempo a un proyecto que no va en serio.

En fin, se ve muy difícil que Leal Sosa nuevamente sea parte del equipo de Hernando de Soto, pues sabemos que a partir de mayo se sumará a las filas del titular de Profeco, Carlos Arce como su asesor, y no tiene intención de regresar a este proyecto, ¡no por que no le interese, sino porque sus derechos como colaborador en Sedesol, no fueron respetados!, y hoy día, ya tiene nuevos compromisos al interior de la Profeco.

Sin embargo, las autoridades mexicanas ya trabajan en la conformación de un equipo, por igual sólido, incluso este martes 27 de abril, el presidente Vicente Fox, sostendrá una reunión privada con cuatro secretarios de Estado, con la finalidad de ponerle pies y cabeza a la estructura con la que comenzará a trabajar Hernando de Soto, a partir de junio próximo, y poder ver los primeros resultados antes de que termine el sexenio de Fox.

Además los compromisos firmados con el Banco Interamericano de Desarrollo (BID) se mantienen latentes, tan es así que hacia finales del año, este organismo internacional realizará la primera supervisión de los adelantos que lleva el gobierno mexicano. Al final de cuentas, México es el primer país de los lugares Latinoamericanos que le interesan apoyar en su economía, pero quiere ver resultados.

En fin, habrá que seguir muy de cerca este asunto, pues si bien, Hernando de Soto se fue este fin de semana con la idea firme de que el gobierno mexicano está más que dispuesto a trabajar en la incorporación de su economía informal a la legalidad, aún no se da el arranque de salida.

Sin embargo, la forma en la que trabajará Hernando de Soto, se mantiene tal cual se lo comentamos, es decir, que durante los primeros nueve meses de la ejecución se realizará un diagnóstico exhaustivo de las dimensiones y la naturaleza del sector informal. En cuatro ciudades, incluido el Distrito Federal.

A partir del ejercicio de la generalización de los resultados en las cuatro ciudades, a los 12 meses se reformará el marco jurídico que regule el entorno empresarial.

La estrategia debe hacer explícitos los beneficios con la finalidad de crear un consenso para la aprobación de las reformas y apoyo en el mismo proceso de formalización. Para que después se ponga en marcha un paquete de reformas en las cuatro ciudades diagnosticadas, a fin de llevar a cabo las actividades que constituyan una primera etapa nacional.

Junta de Consejo
México bajo la lupa del BID

MARIELENA VEGA

México esta bajo la lupa del BID. El proyecto que arrancará en unos días el gobierno mexicano de la mano de Hernando de Soto, presidente del Instituto Libertad y Democracia (ILD), para incorporar al mercado ilegal a la legalidad, estará más que supervisado por el Banco Interamericano de Desarrollo (BID).

Este proyecto que se oficializará el próximo 26 de marzo durante la reunión del BID que se llevará a cabo en Lima, Perú, dará inicio hasta junio con dos importantes retos: incorporar 315,000 millones de dólares que se calculan representan el mercado ilegal a la legalidad, y demostrar que el proyecto es viable, pues de no ser así, el BID tiene la facultad de suspenderlo y retirar el dinero invertido en cualquier momento.

De acuerdo con el documento "Apoyo al Programa de Incorporación de los Activos Empresariales a la Formalidad", que entregará el viernes la Sedesol al BID, y al que tuvimos acceso, el gobierno mexicano tiene un reto más que importante, pues aunque este proyecto se extenderá hasta el próximo sexenio, los compromisos se asumen desde ahora.

Así que el gobierno de Vicente Fox y en especial la Sedesol, al mando de Josefina Vázquez Mota, tendrá una labor más que importante, ya que será esta dependencia la que le rendirá cuentas al BID cada seis meses para ir supervisando los adelantos, el planteamiento y la viabilidad de este programa. No obstante, el BID contratará a consultores individuales que evalúen el proyecto en la mitad de su desarrollo, y tres meses después de concluir.

Y es que además de que el BID donará al gobierno mexicano 2 millones 600,000 dólares para financiar este proyecto, es decir 50% del costo, utilizará a México como prototipo para definir si otorga una cantidad similar a países como Colombia y Brasil, que también planean incorporar su economía informal a la formalidad.

Cabe aclarar que este dinero que el BID otorgará a México no tiene carácter reembolsable, sin embargo, deberá aportar unos 3 millones de dólares, de los cuales nos adelantaron que 400,500 dólares se buscan obtener en especie. Mientras que del compromiso de contrapartida de Sedesol, se espera que unos 396,000 dólares, provendrán de los gobiernos locales.

El proyecto contempla el diagnóstico del sistema del entorno empresarial; el desarrollo del paquete de propuestas de reforma, y la implementación, esto, en un periodo de dos años y medio, aunque la Sedesol buscará que se reduzcan los plazos. Seguramente el gobierno de Vicente Fox planea dejarlo casi terminado antes de que concluya su sexenio, al final de cuentas sería su más grande logro.

El camino

Entre los pasos de supervisión, la Sedesol debe preparar y presentar ante el BID informes del progreso en los 60 días posteriores al término de cada semestre, y un informe final a los 30 días del desembolso final.

El BID utilizará estos informes para supervisar los progresos y preparar un informe final en los tres meses posteriores al último desembolso. Además, el Banco contratará a consultores individuales para llevar a cabo dos evaluaciones de los trabajos. Se realizará una evaluación intermedia una vez desembolsado el 50% de los recursos.

El documento afirma que la Sedesol deberá presentar ante el BID estados financieros auditados anualmente, además de que en los 90 días posteriores al desembolso final. Y será responsable de la ejecución del proyecto, y Nacional Financiera, actuará como agente financiero.

Así, la Secretaría conformará un grupo de trabajo para la realización técnica y operativa del proyecto. Dicho equipo se compone de abogados, economistas, ingenieros y personal administrativo.

Los oficiales principales del equipo se encuentran en funcionamiento dentro de Sedesol, y ya han recibido capacitación del personal del Instituto Libertad y Derecho (ILD), que encabeza Hernando de Soto, y seguirán recibiendo adiestramiento intensivo durante el proceso de elaboración del propio proyecto.

Sedesol establecerá y será responsable de mantener sistemas contables para el manejo de los recursos y de mantener en archivo toda la documentación comprobatoria de los gastos. Esto, con el fin de poder ofrecer los informes que sean necesarios.

mvega@economista.com.mx

México y el ILD lanzan plan de formalización

Programa liderado por peruano De Soto busca legalizar bienes y activos informales por US\$315,000 millones

● El gobierno de México y el Instituto Libertad y Democracia (ILD), que preside el economista peruano Hernando de Soto, lanzarán un gigantesco programa de formalización de la propiedad que apunta a legalizar bienes y activos informales por aproximadamente US\$315,000 millones.

La semana pasada, el Banco Interamericano de Desarrollo (BID) aprobó un crédito de US\$5 millones para México, con lo que todo quedó listo para iniciar uno de los más ambiciosos programas de formalización de la empresa y la propie-

dad en América Latina.

En la medida de que el proyecto requiere una inversión de US\$10 millones en los primeros dos años, la administración mexicana aportará una cantidad igual a la otorgada por el BID.

Según los primeros estudios realizados por De Soto, México tiene una economía de US\$315 mil millones "como ca-

millones

de personas, seis millones de empresas y 11 millones de inmuebles involucra la economía extralegal azteca.

pital muerto:

Dicha suma indica que no existe una base de datos legal de bienes inmuebles, empresas, transacciones financieras y de las economías alternas.

En los casos donde hay títulos, éstos no entran al mercado. El monto señalado representa además un capital siete veces mayor al de Petróleos Mexicanos y 31 veces el valor total de la inversión extranjera en dicho país. ■





Norway might fund informal economy survey

2004-04-24 07:32:28

By Henry Lyimo

Norway is considering Tanzania's proposal to fund a study of the informal economy in the country that operates outside the official financial system.

The Deputy Head of the Norwegian Embassy, Inge Rydland, told The Guardian in Dar es Salaam that his Embassy was currently examining the proposal from the government for funding the study.

"We have a favourable opinion about the programme, but we have not seen the proposal in detail, Rydland said, adding that the implementation plan of the study was not yet arranged.

The study will be undertaken by a renowned Peruvian development economist, Prof. Hernando de Soto who was invited by the government last year to help turn successes in the macro-economic reforms into a reality for the majority of the population.

The informal economy in Tanzania, a massive employer of millions of people, is estimated to account for over 50 per cent of the country's gross domestic product (GDP).

The potential of the informal economy to the national economy that grows at the rate of 6.2 per cent per annum is largely not known, but analysts say there is great-untapped wealth from the area, which needs to be brought into the formal settings.

The Norway envoy said his country had a positive outlook of the project as a step forward in understanding the contribution of the informal economy to the national economy.

"If Tanzania shall develop quickly, it has to bridge the gap between formal and informal economy and seek to know how big is the latter," Rydland said.

Prof. De Soto is the author of "The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Elsewhere." His economic models attempt to reverse the predicament of the poor people who have no access to credit because of lack of legal property.

Meanwhile, our Correspondent in Mwanza, Emmanuel Chacha, reports that the Norwegian Crown Prince, His Royal Highness Haakon Magnus, has hailed the Tanzanian government for its remarkable efforts in the drive to achieve the Millennium Development Goals.

He made the remarks when he addressed the masses at Hungumalwa, Ilula and Imalilo villages in Kwimba District, Mwanza Region, during his visit to inspect projects implemented under the United Nations Development Programme (UNDP) support. He is UNEP's Goodwill Ambassador.

He said that, the current government's initiatives are an indication that Tanzania can achieve the millennium goals before 2015 as planned.

"There are clear signs that the Tanzanian government is working hard to achieve the Millennium Development Goals. Your country is committed to achieving the goals, and the UNDP is working with your government to make sure you achieve them," he said.

The UNDP Resident Representative and co-ordinator of UN System in Tanzania, John Hendra, praised the Norwegian government for her support to UNDP particularly to the decentralisation programme that is executed in Mwanza Region.

He noted that UNDP and United Nations Capital Development Fund (UNCDF) supported the programme, but last year the fund experienced financial constraints hence failed to continue to fund it, adding that the Norwegian government issued (1.2bn/-) for completion of the programme.

- SOURCE: Guardian



The Boston Globe

Tanzania's street economy is a blessing and a curse

Officials look to curb hawkers' chief livelihood

By Carter Dougherty, Globe Correspondent, 3/21/2004

DAR ES SALAAM, Tanzania -- Kongo Street in this bustling capital boasts some of the most chaotic commerce in the world, in scenes that resemble both free enterprise and guerrilla warfare.

Each day in the narrow, dirty, and crowded alley in a poor district, hawkers on foot plug an endless array of wares, from shoes to rat poison and cashews. Some hound their customers relentlessly, while others coolly let the merchandise do the talking.

But when Tanzanian riot police in drab olive uniforms back their paddy wagon to the top of Kongo Street and begin smacking their black nightsticks into their palms, the peddlers all do the same thing - retreat. A few hours later, they return to what they consider their rightful turf.

"We have to watch the police all the time, and run if they come near," Hamad Silaji, 17, said as he dangled several pressed white T-shirts from both arms.

The hawkers, known in Swahili as "machingas," personify Tanzania's informal economy - the off-the-books commerce that the World Bank believes constitutes 60 percent of the East African nation's true economic activity. With Tanzania's president, Benjamin Mkapa, trying to reform what was once Africa's proudest socialist economy, the machiningas pose a difficult challenge: how to turn an unwieldy black market into a taxpaying, legitimate one.

For three decades after the country's creation in 1964, under founding father Julius Nyerere, Tanzania pursued a version of socialism known as "ujamaa," a Swahili word connoting close familial relations. Nyerere nationalized industries, collectivized agriculture, and promoted free Swahili-language education for all.

Ujamaa generally is credited with welding together a nation of 130 tribes, avoiding the ethnic conflicts that killed untold numbers in neighboring Uganda, Rwanda, and Burundi. But the policy was an economic failure that helped drive Tanzania's per capita income steadily downward, to about \$280 in 2002, according to the World Bank.

Now, Mkapa is pursuing free-market reforms in this nation of 36 million, abandoning the economic legacy of Nyerere, who died in 1999, even as he speaks the former leader's name in reverent tones. Mkapa has made peace with the International Monetary Fund to secure more international aid. Inflation is down from over 30 percent a decade ago to 4.5 percent in 2002, while annual economic growth has been boosted to 6.2 percent. Mkapa also has overseen privatization of hotels, paper mills, and sugar factories.

But knocking the informal sector into shape, which in Tanzania mainly comprises agriculture and the retail trades represented by the machingas, has proved more formidable. Mkapa is a fan of the theories of the Peruvian economist Hernando de Soto, who favors conferring official recognition on the informal sector so that its practitioners enjoy legal protection and access to credit and so that the state can tax them.

In a September speech, during a visit by de Soto to Tanzania, Mkapa called for a "better and legal legitimacy" for people like the machingas.

"What would happen if the entire informal sector in Dar es Salaam were to go on strike?" Mkapa said. "The truth is that if that were to happen, God forbid, much in this city could grind to a halt."

The machingas take their name from a tribe in Tanzania's south known as "chingas." In the 1980s, when socialism was in full gear, they began migrating to Dar es Salaam, a city of 3 million, to work as itinerant peddlers. As they were joined by other Tanzanians, the word "machinga" came to apply to anyone hustling goods on the streets, notably those in the poorer Kariakoo district that includes Kongo Street.

A 2000 crime survey by the United Nations suggested that a quarter of all residents in Dar es Salaam might be engaged in machinga-like commerce.

Eighty percent of them are in their 20s, with almost all having a primary school education. They do business in Tanzania's largest city because they think the opportunities are greater than in rural areas, the report found.

As the burgeoning numbers of machingas made some areas of town nearly impassable, Yusuf Makamba, the capital's regional commissioner, decided late last year to lower the boom. His administration built marketplaces out of rough timber with corrugated metal roofs in another part of town, and issued identity cards to the machingas who agreed to move there. But few machingas did because they said the spot was too distant from their customers.

So Makamba ordered in the riot police, who began scooping up traders from Kongo Street.

"If you were caught, the cops either wanted a bribe [of about \$5] or they would send us to court to pay a fine" of about \$15, said Zola Malilo, 30, who sells baseball caps. Malilo said he was caught twice, and both times family members had to kick in money to get him out of jail.

Machingas said authorities confiscated tons of their wares. The sellers accuse some police officers of reselling the goods or simply keeping them. Frustration boiled over Dec. 14, when a crowd of

machingas overpowered four police officers guarding a warehouse of their merchandise and stoned one of them to death.

But Makamba promised not to forget the attack and pledged to continue his offensive against the machingas, who more than three months later continue a daily cat-and-mouse game with police.

"This kind of business is useless," Makamba fumed in a December speech. "It does not help the trader or improve the national economy."

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Govt making earnest efforts to dent poverty: Shaukat

Monday February 23, 2004 (1537 PST)

ISTANBUL: Federal Minister for Finance & Economic Affairs, Shaukat Aziz has said that Pakistan would not hesitate to follow the economic system of any country to improve the living standard of people and stabilize the economy of the country.

"It is the priority of government to improve the living standard of the masses especially of the low-income and those who are residing in villages of the far flung areas", the Minister said, while addressing a press conference after meeting with renowned economist and founding president of IND of Peru, Hernando de Soto on Monday.



Mr Hernando, who met President Gen Pervez Musharraf for three hours and presented his suggestion, where he also addressed the meeting, chaired by President, was attended by high officials of civil and military bureaucracy, the Minister informed.

Shaukat Aziz said that a framework, in the light of Mr Hernando's law on property, legal and reform of economic, would be

constituted and reforms would be introduced later, which would lead to improve agri and industrial sector and would help in increasing exports.

"Government is making earnest efforts to improve the living standards of masses and to dent the price hiking, unemployment and poverty", Shaukat Aziz said.

Later, replying to question, Mr Hernando said that about 75 per cent of the employees are engaged with the small and medium size industries by borrowing loans in the industrialized countries and developing countries should follow them in this regard.

"Corruption and kickbacks are main hurdles in the progress and development of Pakistan. Officers and people of black market are compelling the masses to indulge in bribery and wrongdoings", Mr Hernando added.

Unavailability of just and fair system forced the laymen to involve financial embezzlement and it is dire need of time to uproot corruption and ensure the justice in the society, he said.

With help of economic reforms in Textile and Furniture industry in Peru, its export targets crossed from \$ 3 billion to \$ 10 per annum, Mr Henando informed.

"Abolition of terrorism and better law and security situation in the country could improve the direct foreign invest", he concluded.

Earlier, speaking in Dera Murad Jamali Finance Minister, Shaukat Aziz has said that all the provinces are being given due share in National Finance Commission (NFC) Award adding that the rights of all the provinces will be protected in the award as the prosperity of provinces is prosperity of Pakistan.

He was talking to the journalists on the eve of inauguration ceremony of National High Way in Dera Allah Yar on Monday.

He maintained that it is shared objective of the President General Pervez Musharraf, Prime Minister, Mir Zafarullah Jamali and the federal cabinet to afford maximum relief to the common man because the prosperity of the country lies in the prosperity of masses.

About Khushali Bank, he said that launching of the Bank in Balochistan will benefit all the people in the province particularly the farming community.

To a question he said that all the four provinces have proper representation in the federation and no province will suffer in the NFC award as far as its rights are concerned.

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Peruvian economist advocates cheaper loans to help SMEs

*** *De Soto could be hired to help SME sector***

Staff Report

ISLAMABAD: The government is likely to hire Hernando De Soto, a Peruvian economist, as a consultant to legalise the titles of lands, properties and businesses in order to make them an additional instrument for obtaining credit and developing the country's Small and Medium Enterprises (SMEs).

Mr De Soto, at the invitation of President Gen Pervez Musharraf, on Monday, delivered a three-hour lecture to a gathering of some 200 people including cabinet members, economists, and civil and military bureaucracy about his experiences in Peru and other economies. The meeting was presided over by the president at his camp office in Rawalpindi. "The president, after reading *The Mystery of Capital*, a book written by Mr De Soto had advised inviting the Peruvian economist to Pakistan, said Finance Minister Shaukat Aziz at a joint news conference with Mr De Soto.

Mr Aziz said the government had already invited a few donor institutions to fund Mr De Soto's project in Pakistan. He said the government wanted to improve the quality of life and provide credit to the common man. Mr De Soto said a major cause of slow progress in developing countries was that people lacked documentary proof of their properties, lands and businesses owned by them and which could be used as a guarantee while applying for credit from financial institutions.

He said most of these properties in developing countries belonged to the middle and low income groups who did not have access to credit because of the lack of legal documents. He said the economy could not grow until such assets were given a legal status.

Mr De Soto said the informal sector was outside the legal system because it was not satisfied with the existing laws, adding if it was assured of fair play and better costs of business, it would gradually transform into the formal sector which would eliminate corruption.

He said even in developed countries like the US, almost 75 percent of employment generation comes from the SME sector because people get loans against their houses, businesses and lands. He said his team would visit various parts of Pakistan to identify the size of the informal and black economy, examine the existing rules and regulations and see how these could be changed for the good of the economy. He said a strong commitment from the president and the prime minister was required to develop a national consensus on such issues.

Pakistan Times

Tuesday February 24, 2004
Muharram 03, 1425

President Musharraf for improved Economic Progress to Common Man

By Rezvan Malick - Pakistan Times Staff Correspondent

RAWALPINDI: President General Pervez Musharraf called Monday for measures to transfer benefits of improved economy to the common man so as to bring about a qualitative change in their lives.

He was talking to Hernando de Soto, a world renowned Peruvian economist and President of leading international think-tank here after attending his lecture on improving the quality of life of common man by empowering the less privileged.

Progress

The President said that while substantial progress had been made during the last four years in stabilizing the economy of Pakistan, there was a need to expedite the transfer of these benefits in order to improve the quality of life of the common man.

Hernando de Soto, who is also the President of The Institute of Liberty and Democracy (ILD) is currently visiting Pakistan at the invitation of President General Pervez Musharraf.

The lecture was attended by the President, Federal Ministers, Services Chiefs, senior civil and military officers.

Lecture

The lecture by Mr de Soto focussed on the latest modes and techniques for transferring the fruits of economic achievements of government to the poor masses and alleviating poverty in the country. The lecture was followed by a question and answer session.

The President thanked Mr do Soto for his thought provoking lecture. He also appreciated his suggestions to accelerate the growth of the construction industry and small and medium enterprises in Pakistan.

Hernando de Soto, has also worked as an economist for GATT (now WTO) and as Governor of Peru's Central Reserve Bank. He is currently working in Asia, the Middle East and Latin America on the practical implementation of the measures for bringing the poor into the economic mainstream. He is also a best-selling author on economic aspects, 'The Mystery of Capital' being his most popular book.



Encuentro Berger-De Soto



El economista peruano y presidente del Instituto Libertad y Democracia, Hernando de Soto, se reunió ayer con el mandatario de Guatemala, Oscar Berger, para abordar los problemas de la legalización de la propiedad, las empresas y la creación de mecanismos de acceso al mercado de los más pobres en el referido país centroamericano.

EFE

Pulso Económico

'Se necesita reformar el Estado'

pulso@sigloxxi.com

'Hay que hacer una reforma del Estado como lo propone el presidente Óscar Berger porque el sistema que existe pone trabas a los más pobres que buscan que se les reconozca el derecho de propiedad', señaló el economista peruano Hernando de Soto, en su discurso acerca de la competitividad del pequeño y mediano empresario, en el marco del II Encuentro Nacional de Empresarios (Enade).



POR LOS POBRES. Hernando de Soto dijo que hay que apoyar la reforma de Estado que impulsa el presidente Berger.

Agregó que obtener el derecho de una propiedad es un proceso que lleva más de 20 años. 'De ahí que no se le puede pedir a la gente que crea en la economía de mercado y que los políticos no logren la reelección de sus partidos'.

Añadió que es difícil desarrollar la pequeña empresa si no existe capital, la base de la economía de mercado, y por ello se debe lograr que todos los sectores estén incluidos en este proceso, incluyendo a los más pobres. De no ser así, se da espacio a una 'serie de populistas y comunistas disfrazados que no creen en el desarrollo del mercado'.

Por aparte, Francisco Flores, presidente de El Salvador, que también participó, habló de los logros de su partido para alcanzar 'un país más seguro'. Dijo que el haber obtenido el 100% de los votos de los municipios pobres en las elecciones pasadas, es muestra del rechazo al populismo.



President Clinton Calls For 'Systematization' For Peace And Humane Globalization

World Economic Forum (Geneva)

PRESS RELEASE

January 21, 2004

Posted to the web January 21, 2004

Davos

To ensure globalization with widespread peace and prosperity, world leaders must work to create mechanisms that can be applied on a large scale to address inequality and other challenges, said former US President William J. Clinton, Founder of the William Jefferson Clinton Foundation, at the opening lunch of the World Economic Forum's Annual Meeting 2004.

"There are lots of wonderful people who are dealing with the rough edges of globalization," Clinton said. "But we do not have the systems the world needs to respond in a comprehensive way."

Hundreds of business, political, religious, academic and civil society leaders are gathered in this Swiss mountain resort for five days of meetings around the theme, "Partnering for Security and Prosperity." They listened as Clinton said that many of globalization's opponents "have got their criticisms right". He added: "There is a broad conflict between the 'haves' and the 'have-nots' to define meaning, identity and rootedness."

Yet Clinton defended moving forward instead of trying to return, in the ungrammatical words of the late US humorist Will Rogers, to "the good old days that never was."

Clinton cited the battle against HIV/AIDS as an example of how "systematization" might work. The former US president described how he and former South African President Nelson Mandela launched a roadshow to ask for more money to combat the disease. "Nelson Mandela and I were out there rattling the cup for more money, and the head of the programme in the Caribbean told me that they wouldn't have the infrastructure to spend the money and that they wouldn't have enough money to buy medicine anyway."

As a result, Clinton said, he changed his focus to helping to build local clinics and bringing down the price of HIV/AIDS medicine. Capacity building at the local level is key to the process, he commented.

Initiatives that deserve to be "systematized", said Clinton, include the Grameen Bank, a community loan programme in India, and a campaign led by Hernando de Soto, President of the Instituto Libertad y Democracia in Peru, to guarantee property rights to the poor. "Soto is probably the most important living economist," said Clinton, "though some people think that the term 'living economist' is an oxymoron."

Clinton also advocated greater global support for politicians who are willing to take big risks to promote democracy, such as Ernesto Zedillo, the former Mexican president who ended one-party rule in his country, and Mikheil Saakashvili, President-elect of Georgia. "Are you just going to pat [Saakashvili] on the back?" Clinton asked participants. "Or can we give him help in some systematic way so that all those other countries of the former Soviet Union want to get in line?"

"Half the people here today deserve medals for their work," said Clinton. "But we 'haves' need to systematize our responses. When you hear about a good thing during these next few days, think about how we can systematize this to scale."

The World Economic Forum is the foremost global community of business, political, intellectual and other leaders of society committed to improving the state of the world.

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GLOBALIZATION:

Breaking Barriers To Participation

The 2004 Albert H. Gordon Lecture By:

HERNANDO DE SOTO

President, Institute for Liberty and Democracy;
Former Principal Advisor, President Fujimori of Peru

John F. Kennedy
School of Government
79 JFK Street
Cambridge, MA 02138
(617) 495-1390

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THURSDAY, FEBRUARY 19, 2004

6:00 PM



■ Hernando de Soto también sostuvo una reunión de trabajo con el staff de ejecutivos de la Casa Blanca.

Hernando de Soto dio conferencia magistral ante comunidad de Harvard

Boston, 19 feb.- El afamado economista peruano Hernando De Soto dio hoy una conferencia magistral ante la comunidad académica de Harvard y público en general, tras haber sostenido en la víspera una reunión de trabajo en Washington con el staff de ejecutivos de la Casa Blanca.

El autor de *El Misterio del Capital* tuvo a su cargo el discurso "Albert H. Gordon Lecture 2004", uno de los eventos académicos más importantes de la Universidad de Harvard, organizado anualmente por la J.F. Kennedy School.

La disertación del peruano duró aproximadamente una hora y al final respondió cortésmente algunas preguntas del público asistente, conformado principalmente por catedráticos y estudiantes.

Después de la conferencia hubo una cena en honor del autor de *El Otro Sendero*, a la

que asistieron maestros, funcionarios y estudiantes de la J.F. Kennedy y de Harvard.

En la víspera, Hernando de Soto sostuvo una reunión de trabajo con el staff de ejecutivos de la Casa Blanca, en la que expuso las propuestas del Instituto Libertad y Democracia (ILD) para superar la pobreza en los países en vías de desarrollo, así como su visión de la realidad de Egipto.

Horas antes, tuvo otra reunión similar con los funcionarios del Banco Mundial (BM) responsables de los países de África, invitado por ese organismo, que está interesado en las propuestas de De Soto, que un día antes fueron puestas en práctica por el Banco Interamericano de Desarrollo (BID).

El BID lanzó el lunes un programa destinado a promover los derechos de propiedad efectiva que permitirá acceder al crédito a los pequeños y microempresarios y a los empresarios informales, en una ceremonia a la que asistió el economista.

Tuesday, March 23, 2004

Business

Capitalism must be taught to others, economist says

Tom Sowa

Staff writer

America's strong legal system and its set of property rights are the DNA needed to help transform economies in the Third World, a noted economist said in Spokane Monday.

"It took until the late 18th and early 19th century before America reached the point where you didn't have the Clint Eastwood situation, where anyone could grab other people's property," said Hernando de Soto.

The United States' strong property rights linked with extensive record-keeping guarantee a society that promotes commercial trust and preservation of capital, de Soto said in a [lunch address at the Spokane Convention Center](#).

"Now you have to figure out a way to teach that to other countries, because the struggling countries aren't learning those lessons easily on their own," he said.

De Soto is this year's Gonzaga University James Jundt Professor of Economics. He is also president of the Institute for Liberty and Democracy, based in his home country of Peru. The institute fosters programs to spur capital formation in Asia, Latin America and the Middle East.

"We have property rights in other (Third World) countries," de Soto said. "But they're not legal like they are in this country. That difference is enormous."

His research, for example, found that more than 80 percent of all homes in Egypt are not titled the way the American system operates, he said. And in Mexico, well over 60 percent of all property is owned off-paper -- meaning not formally recorded or registered in any way.

De Soto's most recent book is "The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else."

The prescription he offers is to not assume that every nation will gradually find capitalism. Focused efforts are needed, especially in key countries like Russia and China, de Soto said. Both those nations have turned toward capitalism, but in neither case is there the necessary legal underpinning to ensure it succeeds, he said.

China has made great strides in the past decade but the changes there have only bettered the lives of 150 million people, he said. "The other 1.1 billion in China are no better off. The big challenge there is to help the rest of those residents see the benefits of fully established property rights. It has to be sooner than later, or there's the risk of a counter-revolution against capitalism (in China)," he said.

Third World governments addressing poverty have to face a key decision, de Soto said: either embrace capitalism and focus on building a full network of legal and democratic institutions; or focus resources on direct programs of jobs, education and social welfare. The first course may take longer but can have larger rewards; the second may be quicker in some respects, but it usually means a slower, managed economy, he said.

"That's at least the debate we want to see those countries move toward," de Soto said.

04/20/04, 10:41 (Hora de México DF)

• **Propiedades son comienzo de economía individual: De Soto**

Monterrey, Nuevo León, México, 20 de abril. Para que los trabajadores mexicanos se integren a la economía formal deben integrarse por ellos mismos, afirmó el economista Hernando de Soto.

Para que los trabajadores mexicanos se integren a la economía formal deben integrarse por ellos mismos, ya que es un hecho que todos quieren pertenecer a este sector sin estar fuera de la ley, afirmó el economista peruano Hernando de Soto, en la Universidad de Monterrey.

El que las personas tengan una propiedad permite igualarlos económicamente, pues cuando se tiene muy claro dónde trabajan es posible identificar a las empresas y hacer una reforma tributaria, hacer responsable a los individuos, aseguró en conferencia de prensa.

"En México los cálculos que hemos investigado para obtener una hipoteca no bajan de 48 meses, y lo que se tiene que hacer es crear un sistema de derecho lo suficientemente económico para que sea accesible a los más pobres.

"Es en ese momento cuando ellos solos se integran a la economía por que es lo que mas les conviene", expresó a los medios de comunicación el ganador del premio Milton Friedman, que le será entregado el 6 de mayo en San Francisco, California, Estados Unidos.

El escritor del libro *El otro sendero* dijo que para que los mexicanos puedan tener una propiedad en México tienen que tener en cuenta cual es costo de constituir una hipoteca para que ésta como garantía genere una nueva empresa.

El también fundador del Instituto de Libertad y Democracia (ILD) en 1980 manifestó que esta propuesta está en los libros que el presidente Vicente Fox usó para contratar a De Soto cuando era Gobernador de Guanajuato.

En México, un 47 por ciento de personas trabaja extralegalmente mientras que una tercera parte navega entre los sectores de economía formal e informal, afirmó el

también activista que ha sido víctima de atentados en su contra por parte del movimiento peruano Sendero Luminoso.

Señaló que cuando el gobierno peruano canceló al ILD sus propuestas de desarrollo por diferencias con el presidente Alberto Fujimori, se volvieron consultores sin fines de lucro para otros países que los comenzaron a llamar, como Rusia, Egipto Etiopía y Nigeria, donde estudian los principales problemas del campo.

De Soto indicó que el derecho es indispensable para crear una economía de estado, y la ausencia de este es lo que lleva a la pobreza, a la incertidumbre, las migraciones y el crimen.

Hernando De Soto visitó la UFM

Guatemala, 26 de abril de 2004

Hernando De Soto, autor de *El misterio del capital: por qué el capitalismo triunfa en Occidente y fracasa en el resto del mundo*; coautor de *El otro sendero*; director del Instituto Libertad y Democracia; y especialista en economías de países en desarrollo, visitó la Universidad Francisco Marroquín.

Durante su recorrido por el campus, estuvo acompañado del rector, Giancarlo Ibárgüen S.; del rector emerito, Manuel F. Ayau; del secretario general, Ricardo Castillo A.; y del director ejecutivo del Instituto Libertad y Democracia, Manuel Mayorga.



Manuel F. Ayau, Hernando De Soto y Giancarlo Ibárgüen S. mientras conversaban con estudiantes en la Biblioteca Ludwig von Mises

La visita, de De Soto incluyó un recorrido por la Biblioteca Ludwig von Mises, por el Centro de Operaciones de Internet, la Escuela de Negocios y el Centro de Recursos Digitales New Media.

El Instituto Libertad y Democracia es una organización privada sin fines de lucro con sede en Lima, Perú. Su misión es apoyar a los países en vías de desarrollo y a los que vienen del sistema soviético en su tránsito a una economía de mercado moderna. Esto la realiza a través de la ayuda a los jefes de Estado para que implementen reformas institucionales capaces de incorporar a la ley y aportar poder a las personas excluidas del mercado legal. El ILD incorpora a esas personas —más de 70% de la población mundial— a la esfera de la ley mediante el acceso a los derechos de propiedad formal y el aporte de herramientas para liberar el capital que vive encerrado en los activos que ellos poseen.

El ILD no solo diseña estrategias y proyectos. También los implementa: ha creado y manejado con éxito sistemas de propiedad legal que ya han trasladado a cientos de miles de negocios e inmuebles de la economía subterránea a los espacios centrales de la economía.

De Soto participó en el Encuentro Nacional de Empresarios organizado por la Fundación para el Desarrollo de Guatemala (Fundesa).

Guatemala, 26 de abril de 2004

Atlas Economic Research Foundation

Bringing Freedom to the World

FOR IMMEDIATE RELEASE
Ziebarth
March 8, 2004

Contact: Elena
703-934-6969

INDEPENDENT INSTITUTES HONORED BY THE TEMPLETON FREEDOM AWARDS PROGRAM

Fairfax, VA – The Atlas Economic Research Foundation today announced the prize and grant recipients for the inaugural year of its *Templeton Freedom Awards Program*. Supported by and named for Sir John Templeton, a pioneer of international investing and philanthropy, the program rewards innovative work of think tanks in countries throughout the world. More than 140 institutes from over 50 countries competed for prizes and award grants within the program.

The *Templeton Freedom Prizes for Excellence in Promoting Liberty* were given in four different categories:

- • **Social Entrepreneurship:** The Liberty Institute (India) received first place in this category for its *Language of Liberty Summer Camp*, where low-income Indian high school students from rural Himalayan villages learn English while discussing the ideas of freedom and liberty. The runner-up in this prize category was the Canadian-based Fraser Institute for its *Children First: School Choice Trust* which provides private school tuition assistance by lottery to elementary school students from disadvantaged families.
- • **Ethics and Values:** The Acton Institute for the Study of Religion and Liberty in Grand Rapids, MI won first place in this category for its extensive body of work on the moral defense of the free market. The runner-up, the Instituto Cultural Ludwig von Mises (Mexico), teaches ethics to key defenders of liberty and security in Mexican society through utilization of an Ethics & Character Formation interactive CD-ROM.
- • **Student Outreach:** The Centre for Civil Society (India) was honored for its *Liberty & Society Seminars*, which give university students a better understanding of society, economy and culture by emphasizing the rule of law, limited government, free trade and competitive markets. The National Center for Policy Analysis (NCPA) in Dallas, TX was the runner-up for *Debate Central*, an online debate resource for high school debaters.
- • **Free Market Solutions to Poverty:** The Instituto Libertad y Democracia (Peru) won first prize in this category for their *Egyptian Property Law Program*, which is reforming Egyptian property law through a focus on state acknowledgement of lawful property ownership. The runner-up, the National Economic Research Institute in China, won for its long-term project, *Promoting Economic Freedom in China*. The project focuses on accurately documenting the

market-oriented reforms in each of China's thirty provinces and proposes policy reform to provincial government officials.

The winning institutes in the four prize categories each receive a \$10,000 prize and the runners-up in each category received \$5,000.

Additionally, Atlas announced 15 winners of *Templeton Freedom Award Grants for Institute Excellence*, which are given to outstanding and promising young think tanks:

Association for Liberal Thinking (Ankara, Turkey)
Centro de Divulgación del Conocimiento Económico (Caracas, Venezuela)
Center for Liberal-Democratic Studies (Belgrade, Serbia & Montenegro)
Centre for Civil Society (New Delhi, India)
Civic Institute (Prague, Czech Republic)
Free Market Foundation (Johannesburg, South Africa)
Fundación Libertad (Rosario, Argentina)
F. A. Hayek Foundation (Bratislava, Slovakia)
Institut Économique de Montréal (Montréal, Canada)
Institute of Economic Affairs – Ghana (Accra, Ghana)
Istituto Bruno Leoni (Torino, Italy)
Instituto Ecuatoriano de Economía Política (Guayaquil, Ecuador)
Instituto Libertad y Desarrollo (Santiago, Chile)
Liberty Institute (New Delhi, India)
Lithuanian Free Market Institute (Vilnius, Lithuania)

Each Award Grant winner receives a general grant of \$10,000 to help them continue their efforts.

Several award-winning institutes will be featured within the program of Atlas's upcoming Liberty Forum, which will be held in Chicago on April 28-29.

The Atlas Economic Research Foundation launched the *Templeton Freedom Awards Program* in September 2003 with a four-year pledge from the John Templeton Foundation, which enables Atlas to award more than \$1,250,000 in prizes and grants.

Since 1981, the Atlas Economic Research Foundation has been the leading international organization for supporting independent think tanks advancing freedom. Atlas works with more than 200 think tanks from 67 countries. More than half of these organizations were assisted in their formative years by Atlas through financial support or advisory services.

For more information, please contact Elena Ziebarth at 703-934-6969.



April 14, 2004

Dangerous Minds: Hernando de Soto

by Gene Healy

Gene Healy is senior editor at the Cato Institute, which awarded this year's Milton Friedman Prize to Hernando de Soto.

On April 1, 2004, Hernando de Soto, the Peruvian economist who has devoted his life to bringing real property rights to the world's poor, became the second winner of the Milton Friedman Prize for Advancing Liberty. That prize is awarded every other year to an individual who has made a significant contribution to advancing human freedom.

The prize is a rare honor, but then de Soto is an extraordinary individual. It's not every economist that finds himself the target of terrorist bombings and assassination attempts. Because of his scholarship and activism on behalf of the world's poor, in the late '80s and early '90s, de Soto was repeatedly targeted by the Marxist terror group, the Shining Path.

It's not hard to understand why Marxist radicals found de Soto's ideas so dangerous. They threatened the monopoly the political left (Marxist and non-Marxist) held over solutions to the problems of the world's poor. For years, statist development experts had sought top-down solutions, operating under the implicit assumption that poor people in the Third World were largely incapable of entrepreneurship. De Soto utterly rejected that patronizing viewpoint, and, beginning in his native Peru, focused on the lack of formal property rights as the source of poverty in poor countries. As an author and an activist, and later as advisor to Peruvian President Alberto Fujimori, de Soto worked to bring impoverished Peruvians out of the shadow economy, and unlock their potential for wealth.

In 1979, after a successful career in business in Europe, a 38-year-old Hernando de Soto returned to a Peru plagued by poverty and Shining Path terrorism. Having made enough money to retire, he could now devote himself full-time to solving the riddle of development: What is it that makes the "North" rich, and the "South" poor? De Soto knew that Peruvians did not lack for entrepreneurial energy. The bustling underground economy of Lima was a testament to that. Nor did they lack property, *per se*. From countryside to urban shantytown, ownership was governed by a system of informally evolved and acknowledged property rights.

But as de Soto explained in his 1987 book *The Other Path*, these *de facto* owners were locked out of the formal, legal economy – and that was the root of the problem. "They have houses but not titles; crops but not deeds; businesses but not statutes of incorporation." And the more de Soto and his fellow researchers at the Institute for Liberty and Democracy investigated, the more they realized that dealing with the Peruvian state to obtain legal recognition of one's assets was maddeningly difficult, if

not impossible. Thus, the poor "do not so much break the law as the law breaks them -- and they opt out of the system."

Lacking formal legal title to their property, the poor are unable to use these assets as collateral. They cannot get bank loans to expand their businesses or improve their properties. Their potential is locked up in what de Soto calls "dead capital." He and his colleagues calculate that the amount of "dead capital" in untitled assets held by the world's poor as "at least \$9.3 trillion" -- a sum that dwarfs the amount of foreign aid given to the developing world since 1945.

The Shining Path is moribund, but de Soto remains. Through books like 2000's *The Mystery of Capital*, and hands-on work with the Institute for Liberty and Democracy in Egypt, Mexico, Haiti, and elsewhere, de Soto has pushed developing-country governments to simplify and streamline the process of granting title. Bringing formal property rights to the poor can bring them out of the sway of leftist demagogues and into the extended order of the modern global economy. "Are we going to make [capitalism] inclusive and start breaking the monopoly of the left on the poor and showing that the system can be geared to them as well?" That's de Soto's challenge, and his life's work.



COMMENT

Free the world's oppressed entrepreneurs

AMITY SHLAES.

5 April 2004

What to do after Fallujah? There is a general feeling that last week's atrocity marks a new low in the Iraq story. The mob that killed, burned and mutilated four US security contractors seemed to be rejecting not only the occupation but also the possibility of the end of conflict.

No wonder that the trade fair that was supposed to open in Baghdad today has been postponed. The likelihood of it — or any other trade fair — taking place now looks remote.

Or maybe it does not. At least not according to Hernando de Soto, the Peruvian economist. Next month Mr de Soto will be awarded the Cato Institute's Milton Friedman Prize for a decades-long effort to challenge the fatalistic view that the developing world is always poor and angry and therefore always tends towards extremism, dictatorship and terror. Mr de Soto foresees instead a future for the developing world of shaded afternoons trading at the electronic souk. This optimism might seem naive. Still, the thoughts that underlie it are worth review. Last week Mr de Soto explained to me how his argument works.

Citizens in most developing regions do not think of themselves as belonging to the private sector, even if they do have a chicken farm or CD-player repair business on the side. The phrase "private sector", to such people, describes a distant plutocratic elite, and that elite is presumed to be allied with imperialists from abroad.

The only source of pride for such people is their tribe (Sunni Fallujah) or their national sovereignty (loyalty to Saddam Hussein). That pride is easily offended. The sight of a US tank rolling by or a Coca-Cola banner unfurling infuriates. Citizens feel that such insults "poke at their sovereignty", as Mr de Soto puts it.

This is a familiar attitude — one often identified by Marxist theorists, in fact. But Mr de Soto next explains how he would change it. For starters, it is important to recognise that the stereotype of the impoverished developing world is wrong. The developing world is not poor. It is, in many cases, rich. A good share of people in Mexico City or even Baghdad actually do have assets — that repair shop, the family chicken farm.

The trouble is that citizens do not always have formal legal claim to those assets; nor do they, in many cases, live under governments that would honour such claims if they could make them. As Mr de Soto

wrote in the first of two books on property, *The Other Path*, many Latin Americans, Asians and Arabs are trapped in black and grey economies. "They have houses but not titles, crops but not deeds; businesses but not statutes of incorporation."

Such "frozen" capital is — needless to say — illiquid: sales are hardly possible without documents. Leveraging such capital or using it as collateral is also a challenge. Securitisation proceeds at a glacial pace; debt and equity markets fail to develop.

Converting a black market to a legal one, or making it possible to open a legal business, would be huge improvements in such circumstances. But the political effect of Mr de Soto's ideas could be even greater. For once the small businessman sees that his work is respected and bankable, he will be less inclined to view outsiders as threats and more inclined to view them as potential business partners. An angry local will become a friendly stakeholder. Now recognising himself as part of that once-distant private sector, he will no longer feel "poked", to use Mr de Soto's term again. What is interesting here is that change starts with nomenclature and law. "Instead of viewing people as unemployed proletarians," says Mr de Soto, "we should view them as oppressed entrepreneurs."

Mr de Soto established his bona fides in Peru from a base at the Institute for Liberty and Democracy two decades ago. Now, however, he is busy plying his theories elsewhere. He recently estimated there was about Dollars 245bn (Pounds 134bn) of frozen or "dead" capital in Egypt; nine out of 10 enterprises, by the ILD estimate, operate outside the law. Change in that part of the world he views as entirely possible. "The majority of Egyptians, ergo the majority of Arabs, are actually a budding entrepreneurial class," he says. He has also discussed his ideas with Hamid Karzai, president of Afghanistan, and Vladimir Putin, Russia's president.

Sceptics will call Mr de Soto's approach dangerous. For what to you may look like justifiable legalisation of your informal claim may to me look like frank expropriation. A lot depends on which government and which claimant we are talking about. After all, every morning at breakfast Robert Mugabe probably tells himself that his resettlement actions were just honest legalisations of ancient Zimbabwean claims.

Then there is the possibility that dithering around with Mr de Soto and the other reformer-consultants of this world may give heads of corrupt, resource-rich states an excuse to postpone other important actions: privatising the national oil company, for example.

Yet another danger lies in assuming that property rights reform alone can transform places such as Libya, Iraq or North Korea. In all such places, political change has to come first. But once it has — as in Iraq and, one can begin to hope, Libya — Mr de Soto's agenda may bring a new and shared prosperity to the most unpromising places. And with that a more reasoned view of the world — even after Fallujah.

Peruvian Economist Awarded Friedman Prize

Thursday April 1, 2004 6:31 am

By MARTIN CRUTSINGER

AP Economics Writer

WASHINGTON (AP) - Noted Peruvian economist Hernando de Soto has become the second winner of the \$500,000 Milton Friedman Prize for Advancing Liberty, the libertarian Cato Institute says.

The prize, named after Nobel Prize-winning economist Milton Friedman, is awarded by the Washington think tank every other year to an individual judged to have made a significant contribution to advancing human freedom.

De Soto, who founded the Lima-based Institute for Liberty and Democracy in 1980, was recognized for his research into the connection between the lack of property rights and poverty in developing countries.

He has received international acclaim for his books, including "The Other Path" in 1986 and "The Mystery of Capital" in 2000, which proposed encouraging growth in developing nations by granting property to the disenfranchised poor.

Cato Institute President Edward Crane praised de Soto for his groundbreaking research. "Everyone talks about helping the world's poor. This is a man who figured out how to do it. His work exemplifies the spirit and practice of liberty," Crane said.

In a statement to be released Thursday by the think tank, de Soto called the award "an enormous honor for me and my associates who worked, and in some cases died, for the cause of liberty."

The prize and its \$500,000 cash award are to be presented to de Soto at a dinner in San Francisco on May 6.

The first winner of the Friedman prize in 2002 was the late British economist Peter Bauer, who taught at Cambridge and the London School of Economics. Bauer argued in his research that development aid provided by rich nations to poor countries was often wasted and did little good.

De Soto was selected as the 2004 prize winner from hundreds of nominations from around the world. The winner was chosen from 10 finalists with the selection made by an international selection committee of nine judges, the institute said.

A --

On the Net:

Friedman Prize: <http://www.cato.org/special/friedman/index.html>

April 1, 2004

Peru's Best Export

Today the Cato Institute will announce that its biennial \$500,000 Milton Friedman Prize for Advancing Liberty goes to Peruvian economist Hernando de Soto. It is a fitting and timely tribute when global troubles so closely mirror the challenges that Mr. de Soto first tackled in his native Peru.

Mr. de Soto founded the Institute for Liberty and Democracy in Lima in 1980 to understand the causes of Peruvian poverty and promote free-market ideas. In the 1986 "The Other Path" - written with colleagues Enrique Ghersi and Mario Ghibellini -- he revolutionized development economics by chronicling the realities of Lima's shantytowns at a time when Shining Path terrorism was burgeoning. Peru's informal economies, it turned out, were already full of enormously capable entrepreneurs. What held them back was burdensome government regulation and a lack of property rights. There was no way for them to move into the formal economy.

Mr. de Soto has since made it his life's work to spread the gospel of property rights in the developing world. His 2000 "The Mystery of Capital" advances the work done in Peru, looking at informal markets in places such as Egypt and the Philippines. The book also traces the evolution of property rights in the U.S., emphasizing the importance of an institutional and legal framework that recognizes and protects the value behind an ownership deed. Without such institutions wealth and creativity remain untapped and growth stagnates.

The job of empowering the world's poor is far from done, especially in Africa and the Arab street. But thanks to Mr. de Soto's efforts, much has been added to our understanding of what is needed to unleash the entrepreneurial spirit that exists in every human society.

April 1, 2004; Page A14

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TIME
ONLINE EDITION



TIME 100
SCIENTISTS & THINKERS

TIME 100/Scientists & Thinkers

Hernando de Soto **Unlocking the Riches of the Poor**

Development schemes for Third World countries rarely benefit the poor, largely because aid is too often squandered by corrupt bureaucracies. That makes fresher, commonsense visions like those of Peruvian economist Hernando de Soto all the more welcome. De Soto has spent years looking deep inside the underground economies where poor people—who make up two-thirds of the world's population—eke out a living. He figures the value of their extralegal property, from cinder-block squatter homes to black-market street-vendor sales, at almost \$10 trillion. De Soto insists that bringing the poor and their assets into the formal economy, which is usually closed to them by oligarchies and epic red tape, would eclipse all previous development efforts.



But how? De Soto, 62, offers a simple solution: give these underground denizens legal title to their homes and businesses. That would grant them access to bank credit and investment capital, much as the property-title revolution of the 18th and 19th centuries enriched Western Europe and North America. A limited experiment in Peru in the 1990s proved the idea had merit when it brought in more than \$1 billion in new tax revenue. Some 30 heads of state, from Egypt to Mexico, have hired de Soto for similar projects. "I think our time has come," says de Soto. "Four billion people exist outside the market, where angry folks like Osama bin Laden followers lurk."

This month de Soto became the second recipient of the Washington-based Cato Institute's \$500,000 Milton Friedman Prize for Advancing Liberty. "Hernando sees strong entrepreneurs among the poor who make do in such horrible circumstances," says Cato's president, Edward Crane. "This is going to grow." And so, it's hoped, will the fortunes of those underground.

—By Tim Padgett

See also cover story of same issue

COLOR PHOTO: PETER CHARLESWORTH FOR TIME

**From their laboratories and university chairs—and sometimes seats of power—
they have shaped how we see the world, and ourselves**

**Edward Witten
Steven Pinker
Eric Lander
Korean Cloners
Paul Ridker
Hernando de Soto
Jeff Sachs
Linus Torvalds
Niall Ferguson
Bernard Lewis**

**Tariq Ramadan
Jürgen Habermas
Samantha Power
Sandra Day O'Connor
Jill Tarter
Julie Gerberding
Joschka Fischer
Bjorn Lomborg
Jong-Wook Lee
Louise Arbour**

De Soto considerado como una de las personalidades del mundo

■ El economista peruano Hernando de Soto se constituyó en una de las personalidades mundiales más destacadas de este año que finaliza, cuyas innovadoras tesis en torno a una economía libre y eficiente son capaces de generar riqueza y prosperidad. De Soto ha sido convocado por gobiernos de más de 25 Estados con ese propósito.

Uno de los reconocimientos más trascendentes para De Soto proviene de la influyente revista *Finance & Development*, órgano oficial del Fondo Monetario Internacional (FMI) que subraya que ha encontrado (De Soto) el "estebón perdido", que permite convertir la riqueza escondida de los pobres en trillones de dólares en bienes fungibles palpables.

ADEPTOS

Ha ganado ya muchos adeptos entre los principales líderes del mundo de la actualidad, desde el ruso Vladimir Putin, el presidente de Tailandia, Thaksin Shinawatra, hasta los presidentes Vicente Fox de México y Hamad Karzai de Afganistán. En julio, De Soto fue designado miembro de la Comisión de Alto Nivel sobre el Sector Privado y Desarrollo de las Naciones Unidas, creada para lograr objetivos de desarrollo del milenio y confrontar los desafíos que enfrenta la humanidad. Con el ex presidente de los EE UU Bill Clinton, participará en el 2004 en el Primer Simposio Económico anual que se realizará en Tokio, diseñado para mejorar las condiciones de la economía mundial.

The same principles that apply to IRI volunteer trainer/observers in the attached Code of Ethics (Attachment B) apply to the Consultant and is made an integral part of this contract.

IRI and Consultant acknowledge that this Agreement contains the entire integrated Agreement between the parties, and supercedes all prior contemporaneous agreements, representations, and understandings. No amendment or modification shall be valid or binding upon the parties unless made in writing and signed by the parties to the Agreement.

The terms of this Agreement shall be interpreted under the laws of the District of Colombia.

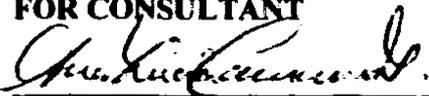
ACCEPTED AND AGREED TO

FOR IRI

George A. Folsom
President and CEO

Date: _____

FOR CONSULTANT



J.2 Manuel Mayorga la Torre
Executive Director

Date: JANUARY 6, 2004

Attachment A

Program Objectives: IRI hopes to promote the adoption of policies that seek to integrate the poor into the market economy and establish legal property rights for the assets of the citizens of the Republic of El Salvador. IRI will promote the implementation of institutional reforms that assure a level playing field and fair rules of the game for those seeking to integrate into the formal economy and establish legal and potentially capital accruing ownership over property.

Contract Responsibilities:

During the period of 12/23/03 through 12/24/04 consultant will be available to:

Travel on assessment and training trips where ILD expertise is relevant. (Maximum three trips).

Coordinate with IRI and the Center for International Private Enterprise (CIPE) in workplan development.

ILD will provide 15 participants with a scholarship to their "Tour of Informality" course in Lima, Peru, to be held in May or June, 2004. This does not include airfare, cost of lodging, taxes, or related expenses.

Provide IRI with trip reports and summary reports of activity throughout the course of this program.

A handwritten signature in black ink, appearing to be the initials 'M' or 'A' followed by a vertical line and a horizontal stroke, located at the bottom right of the page.

INTERNATIONAL REPUBLICAN INSTITUTE
CODE OF ETHICS

The following general principles apply to every officers, directors, contractors and employees of the International Republican Institute (IRI). Where a situation is not covered by the standards set forth below, officers, directors, contractors and employees shall apply these principles in determining whether their conduct is proper. In certain cases arising under this Code of Ethics, circumstances may exist which dictate that IRI's Board of Directors grant an exception to the general policy. Unless such exception has been granted, however, all officers, director, contractor and employee shall conduct themselves in accordance with these principles.

IRI officers, directors, contractors and employees shall not use their positions with IRI for private gain. It is prohibited for officers, directors, contractors or employees of IRI to seek or conduct an IRI mission for his/her own private purposes or for the private purposes of another.

IRI officers, directors, contractors and employees shall not engage in financial transactions using non-public IRI information nor allow the improper use of non-public information to further their own private interests or those of another, whether through advice or recommendation, or by knowing unauthorized disclosures.

IRI officers, directors, contractors and employees shall not use confidential or proprietary information gained in the course of employment for or service on behalf of IRI for private gain.

IRI officers, directors, contractors and employees shall act impartially in carrying out their functions on behalf of IRI and, in carrying out those functions, shall not give preferential treatment to further any private interest.

IRI officers, directors, contractors and employees shall refrain from engaging in activities that conflict with their duties as IRI officers, directors, contractors and employees.

IRI officers, directors, contractors and employees shall not accept any gratuity, gift, or favor that might impair or appear to influence their actions as officers, directors, contractors or employees of IRI.

IRI officers, directors, contractors and employees shall make no unauthorized commitments or promises of any kind purporting to bind IRI.

Only coach travel is authorized for reimbursement by IRI for officers, directors, contractors and employees traveling on IRI business. Wherever possible, travel arrangements should be made far enough in advance to take advantage of advance purchase discounts.



IRI officers, directors, contractors and employees who plan to conduct private business while traveling on an IRI mission must disclose such plans to IRI's Chairman, General Counsel and President in advance of the trip. If a trip is taken for the dual purpose of IRI and private business, transportation, meal, and lodging expenses shall be fairly apportioned between the two business ends conducted so that only those expenses attributable to IRI business are paid for from IRI funds.

IRI officers, directors, contractors and employees shall protect and conserve IRI property and funds and shall not use such property or funds for other than authorized activities.

No IRI officers, directors, contractors or employees may claim payment or accept funds from IRI for any expense for which he has received reimbursement from any other source.

No IRI officers, directors, contractors or employees may use any funds furnished to defray ordinary and necessary expenses incurred in connection with an IRI mission for any purpose other than the purpose for which such funds are furnished.

Any allowance for expenses for an IRI mission not actually used for food, lodging, transportation, and related expenses incurred in connection with that mission shall be returned to IRI promptly upon return from the mission.

IRI officers, directors, contractors and employees shall endeavor to avoid any actions creating the appearance that they are violating these ethical standards. Whether particular circumstances create an appearance that these standards have been violated shall be determined from the perspective of a reasonable person with knowledge of the relevant facts.

IRI officers, directors, contractors and employees shall disclose to IRI's Chairman, General Counsel, and President any circumstances that could be construed as a conflict of interest and should ensure that such conflict does not compromise the interest of IRI.

A violation of this Code of Ethics may be cause for appropriate corrective or disciplinary action by the Executive Committee of the Board.

IRI directors shall recuse themselves from voting on any question properly before the Board in which that director has an actual or apparent pecuniary or personal interest which a reasonable observer could construe as presenting a conflict with the exercise of his or her impartial judgement as a member of the Board.

I have read and will comply with the Code of Ethics as stated above.

Date

JANUARY 6 2004

Signed



ANA LUCIA CAMAROSA ITURZIAGA

Print Name