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PACKAGE OF PROPOSALS

in connection with the 3 March 2014 decree of the President of the Azerbaijan Republic
on additional measures to develop entrepreneurship

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PACKAGE OF PROPOSALS

PREFACE

This Package of Proposals has been prepared in connection with the 3 March 2014 decree of the President of the Azerbaijan Republic on additional measures to develop entrepreneurship. The Package of Proposals was prepared by the Consortium of Public Associations within the framework of the Small Business Expansion Project of the United States Agency for International Development: 1) The Fund to Support the Development of Entrepreneurship and Market Economy; 2) Centre for Economic Research; 3) Centre to Promote Economic Initiative; 4) Centre to Assist the Development of Small and Medium-Sized Businesses; 5) The Guba Carpet World Association; 6) The Ganja Youth Organization Bridge to the Future. The following are the authors of the Package of Proposals: Azer Mehdiyev, chairman of the Centre to Promote Economic Initiative, Eldar Gojayev, an expert on international commercial law, Ilkin Garayev, president of the Centre to Assist the Development of Small and Medium-Sized Businesses, Gubad Ibadoglu, an expert of the Centre for Economic Research, Rovshan Agayev, deputy chairman of the Centre to Promote Economic Initiatives, and Sabit Bagirov, president of the Fund to Assist the Development of Entrepreneurship and Market Economy. The recommendations included in the Package of Proposals were discussed at four round table discussions held at the National Confederation of Organizations of Entrepreneurs (Employers) of the Azerbaijan Republic in May this year. These round table discussions were attended by representatives of government agencies, entrepreneurs and representatives of associations of entrepreneurs.

1. Amendments to the law in order to reduce procedures and time during the electronic registration of legal persons and physical persons engaged in entrepreneurial activities without creating a legal person (private entrepreneurs) in line with the “one-stop shop” principle.

Currently, electronic registration includes three procedures: 1) Acquisition of an electronic signature. It takes three days and costs 30 AZN; 2) Online registration. It takes three days and is free; 3) Acquisition of a stamp. It takes one day and might cost from 4 to 40 manats depending on the quality of the stamp. Analysis shows that the time spent on the procedures can be reduced with the existing rules. Both the first and second procedure can be reduced to one day. This might require the strengthening of relevant services.

The number of procedures can be reduced only by cancelling the first one. However, this requires changes to the concept of the law “On the electronic signature and the electronic document”, or during electronic registration, the electronic signature can be repealed and other tools can be used.

In general, the model employed in Azerbaijan is very stringent in nature. Such a model has been taken as a basis in Russia. For example, in the United States economic entities are free in the issue of the electronic signature and the electronic document. The European model is also softer than that of Azerbaijan.

Thus, the following are our PROPOSALS:

- 1) The time of online registration should be reduced by one day to two days;
- 2) The electronic signature during online registration should be repealed;
- 3) The substantiality of the concept of the law “On the electronic signature and the electronic document” should be analyzed again.

2. Amendments to the law in order to reduce the existing procedures and times in the field of authorizing construction.

The main legislative act that regulates the authorization of construction is the Town Planning and Construction Code of the Azerbaijan Republic. Under Article 75 of the code, construction work is authorized by a relevant body of the executive authorities. But from the design of any facility to the moment it is put into operation, the customer and the subcontractor are forced to obtain a number of permits and endorsements. For this reason, the 3 March 2014 presidential decree gives a number of government agencies instructions on the acquisition not of a permit for construction, but permits. Analysis shows that the number of procedures for obtaining relevant permits and endorsements is much higher than in other countries. For example, in the annual World Bank report “Doing Business” Azerbaijan’s rating in the indicator concerning the acquisition of a construction permit is not at the desired level. According to this report, an entrepreneur has to go through 28 procedures in order to obtain a permit to build an ordinary warehouse and put it into operation (See Attachment 1). In this case, the loss of time is 212 days and spending on procedures is 14,000 AZN.

These 28 procedures are coordinated with eight government agencies:

- -Six of them with the city executive authorities;

- -Three with JSC Azersu;
- -Two with the Centre for Hygiene and Epidemiology;
- -Eight with the Ministry of Emergencies;
- -Three with the Ministry of Ecology and Natural Resources;
- -Three with the Baku Telephone Communications Production Association;
- -One with the Labour Inspectorate.

Analysis shows that both the number of procedures and the time and expenses can be reduced. If we take into account that the company that prepares the design of a construction facility has a relevant licence and observes all standards and norms while preparing the project, many of the abovementioned procedures appear unnecessary.

Thus, our PROPOSALS are the following:

- 1) The Town Planning and Construction Code of the Azerbaijan Republic must be improved. Norms of authorizing construction should be clarified based on the classification of construction facilities. The link between the code and other legal acts (various rules) should be accurate and clear. The list of construction facilities that do not require a permit should be expanded;
- 2) The procedures of obtaining licences for construction should be based on the classification of facilities and reflected on relevant websites (for example, as a page of the website www.icaazalr.az). When starting the construction of a facility, the entrepreneur should be able to acquire accurate information: what procedures he should go through, what is the time limit for these procedures and what are the duties;
- 3) The number of appeals to the same government agency should be reduced;
- 4) A one-stop shop system should be applied;
- 5) Groundless prices (duties) should be reduced;
- 6) The number of days related to the procedures should be reduced;
- 7) 7) The value of licences issued for designing should be increased. That's to say if a design company has a licence to design a type of a construction facility, the project that has been prepared should not be examined again.

3. The organization of the electronic receipt of documents in the sphere of joining the power grid and making changes to the law in order to reduce procedures, time and expenses.

The main document regulating connection to the power grid is the Rules of Issuing Technical Evaluation for the Purchase of Electric Energy (Power) by Consumers and Connecting to the Power Grid approved by Cabinet of Ministers Resolution No 234 on 27 August 2013. It must be noted that these new rules are much more progressive than the Rules of Using Electric Energy that had been in force since 2005 and have eliminated a number of gaps and shortcomings in legislation. Despite that, analysis shows that it is important to make some changes to the new rules. For example, the World Bank's Doing Business 2014 report shows that connecting an ordinary warehouse to the power grid in our country requires an entrepreneur to go through nine procedures. This process lasts 242 days and costs the entrepreneur 28,000 AZN (See Attachment 2). In order to reduce the number of procedures, the loss of time and expenses, it is necessary to make some changes to the new rules. At the same time, in general there is a need for some institutional reform in the sphere of electricity.

Thus, our PROPOSALS are the following:

- 1) In the field of improving the rules of issuing technical evaluations for consumers to receive electricity (power) and connecting to the power grid:
 - a. Work to connect to the power grid and expenses on the preparation of relevant project documents (if the distance is no more than 200 metres and the required power is no more than 20 kV) should be fully the responsibility of the energy supplying company (relevant changes should be made to Points 2.19 and 2.21 of the Rules);
 - b. With changes to Point 2.13 of the Rules, the issue of the technical evaluation by the energy supplying company should be secured within 10 business days;
 - c. It is expedient to sideline relevant local bodies of the executive authorities from the process of connecting to the power grid both in terms of market economy principles and reducing the number of procedures and loss of time;
 - d. The expediency of a review by the State Energy Supervision Department of the Ministry of Industry and Energy of the Azerbaijan Republic under Point 3.3.1 of the Rules should be examined. Its repeal will serve to reduce the number of procedures;
 - e. The fee for connecting construction facilities to the power grid

(considering the distance from the point of connection to the construction facility) should be repealed (Point 1.10).

- 2) The conduct of drastic reforms in the electricity sector remains topical:
 - a. It is necessary to separate electricity facilities and create a competitive environment;
 - b. Although the law "On Electricity" provides for types of activity related to energy generation, transportation and distribution, it does not say that it is possible to create separate entities as sellers of energy. This gap should be eliminated;
 - c. Provisions regulating the wholesale and retail markets should be added to the law "On Electricity";
 - d. An independent regulator should be created to determine prices (tariffs) in the sphere of energy supplies and to regulate the market of electricity and heating.

4. Amendments to the law in order to reduce the procedures, time and expenses in the sphere of state registration of real estate rights

Our PROPOSALS are the following:

- 1) The process of creating an electronic database should be completed in order to provide online access to land registry information;
- 2) The registration of real estate used for business purposes should be carried out on the "one stop shop" basis;
- 3) An online appointment system should be created to reduce loss of time at the registering authority;
- 4) It is necessary to create an opportunity for online payments;
- 5) It is necessary to reduce the number of documents and procedures required for the registration of small property, which is used for business purposes, is not designed for complex production processes and is related to various services.

5. Enhancement of economic activity that influences the process of issuing credits

Our PROPOSALS are the following:

- 1) A legal basis should be created to ensure the establishment of private credit bureaus operating independently. To this end, it is necessary to expedite the adoption of the law "On private credit bureaus", which regulates the activities of credit bureaus;
- 2) It is necessary to ensure that the preferential credits of the National Fund to Assist Entrepreneurship are used mostly for lending to micro, small and medium-sized businesses. After changes made to the Charter of the NFAE in 2009, the Fund no longer provides loans of up to 10,000 manats, whereas small businesses, which face serious problems in obtaining finances, need precisely loans of below 10,000 manats. Our studies show that in recent years, loans of up to 50,000 manats have accounted only for up to 15 per cent of the fund's assets. More than 80 per cent of the Fund's money is allocated to big businesses (loans of more than 1 million manats). In order to change the situation, relevant changes have to be made to the Fund's charter and rules of using the Fund's assets. At the same time, criteria for micro, small and medium-sized businesses in the country should be reformed by the decision of the Cabinet of Ministers;
- 3) The establishment of specialized sector banks may give a serious impetus to the development of those spheres. The successful experience of foreign countries shows that the establishment of specialized sector banks plays an important role in the development of entrepreneurship in various spheres of the economy (for example, agriculture, construction, etc.) and in increasing entrepreneurs' access to credits. Both state funds, money from foreign funds and investors' funds can take part in forming the capital of such banks. For example, it is especially important to set up an agrarian development bank as soon as possible to finance the agricultural sector in our country and a bank to support export in order to stimulate export;
- 4) It is necessary to speed up the issue of documents that confirm the rights of real estate owners to own their property in regions of the country, small towns and villages. Our studies show that up to 90 per cent of all credits channelled into the country's economy are allocated in the territory of Baku and Absheron. Only 10 per cent of loans fall to the share of regions. One of the most important reasons for this is that people on the ground are facing difficulties in providing a pledge for loans because they have no documents confirming their ownership of their real estate (houses, land plots, gardens, etc.);

- 5) A registry of real estate should be created. It is especially important to create a registry of real estate in order to enhance the mechanism of pledges for small credits. To this end, it is necessary to adopt a law "On guaranteed pledges" and create a special registry of real estate that is not registered by the state and related rights. Specifically, it is necessary to ensure the registration (registry) of productive animals and productive trees in rural areas;
- 6) The registration of non-banking credit organizations should be simplified and the problems they face in their activities should be eliminated. Our studies show that non-banking credit organizations and credit organizations play an important role in allocating loans to agricultural manufacturers, farmers and small businesses in regions and distant villages. Currently, only 2-3 per cent of all loans fall to the share of these organizations. Although up to 30 non-banking credit organizations have received a licence in the country, a small number of them (12) are able to operate normally. If, on the one hand, it is connected with difficulties in the registration of non-banking credit organizations, on the other, it is due to difficulties facing non-banking credit organizations in cooperation with banks;
- 7) A system for the independent assessment of facilities with a pledge. Another problem facing entrepreneurs is that real estate provided as a pledge is evaluated by banks below its real value;
- 8) A fund should be created to insure and guarantee loans allocated for agricultural manufacturers and farmers. One of the most successful experiences of foreign countries is the creation of a fund for insuring and guaranteeing agricultural loans (it operates as an agency in some countries) with the participation of the state in order to insure and guarantee loans aimed at agricultural production. Our country could also benefit from this experience. A relevant legislative base is being formed to this end;
- 9) Opportunities for applying principles of Islamic banking in the country should be increased. There are numerous representatives of the Islamic religion both among businessmen and people who have large capital in the country. These people either do not invest their funds in banks because of their religious views or do not apply to banks for credits despite the fact that they need funds to expand their businesses. In order to use the economic potential of these people, it is necessary to organize banks working on the basis of principles of Islamic banking in the country. To this end, either a separate law should be adopted or relevant changes should be made to banking legislation;
- 10) In districts where credit organizations are not working, post offices should be authorized to accept credit payments. This will expand the opportunities of people living in remote areas to obtain credits and conduct banking transactions.

The implementation of credit payments through post offices will facilitate the work of people, reduce expenses and simplify banks' work with credit customers. For this reason, their participation in credit payments will not create serious problems. In order to conduct credit payments through post offices, it is necessary to make relevant amendments and addenda to the law;

- 11) The system of issuing credits by cards and online payments (services) should be expanded in regions. In recent years, the Internet network has been expanding in all regions of our country, even in remote villages. With such modern technologies, banks could provide credits by cards in rural areas. Customers' reports to banks, credit service payments and payments of debts can be implemented online by cards;
- 12) Reduction of the time of the examination of court cases on problem credits, as well as of the period of the implementation of court decisions. Currently, the shortage of economic courts and judges results in the examination of court cases dragging on for years. It is one of the main problems that concern banks. In many countries of the world, disputes and claims regarding the payment of loans are examined out of court. It would be expedient to benefit from this experience in our country.

6. Improvement of corporate management and protection of investors' interests

Our PROPOSALS are the following:

- 1) A Code of Corporate Management should be adopted;
- 2) A law on cooperation between the state and business should be adopted;
- 3) An ombudsman's institution should be formed to protect investors' rights;
- 4) All shareholders, including minority and foreign shareholders should be treated fairly. All important issues regarding companies, including companies' financial condition, property and information concerning its management should be publicized in time and accurately. Shareholders should be given a chance to get compensation for the violation of their rights;

7. Changes to the law in order to reduce the number of documents, time and expenses required during import and export operations

Our PROPOSALS are the following:

- 1) Certificates of quality and origin that meet international standards for products made by the manufacturer should be presented to the customs authorities in a centralized manner and with the mutual acceptance of standards between countries. Companies should be exempted from the requirement to present such documents while importing those products. In this regard, relevant changes should be made to Point 10 of Resolution No 3 issued by the Cabinet of Ministers of the Azerbaijan Republic on 14 January 2014 on the approval of Rules of Determining the Preferential and Non-Preferential Origin of Products;
- 2) The list of documents envisaged by Subparagraphs 2.5 and 2.4 of the statute on the rules and terms of declaring the customs value of goods brought into the Azerbaijan Republic should be reconsidered and the documents of the legal or physical person that imports the goods, transport and insurance documents, the report on loading or the officially approved calculation of transport expenses, a customs declaration from the sender, packaging sheets and the licence for goods imported in line with the established procedure on the basis of a licence should be removed from the list of documents;
- 3) The methods of determining customs costs envisaged by Point 9.4 of Cabinet of Ministers Resolution No 159 dated 17 December 2003 on changes to Point 2 of the Rules of Applying Customs Evaluations for Goods Imported in and Exported from the Customs Territory of the Azerbaijan Republic approved by 12 January 1998 Resolution No 7 of the Cabinet of Ministers of the Azerbaijan Republic should be reconsidered, and to this end, declarers should be granted in advance free access to pricing information provided by customs authorities. At the same time, there is a proposal under which if it is impossible to use it in identifying the customs value, information about the prices of the same kinds of goods, which is used for determining the customs value of exported goods, should be prepared not by the State Customs Committee, but by the Ministry of Economy and Industry;
- 4) The issue of certificates of origin and quality and codes for exporting local products to the European Union should be handed over to the ASAN service;
- 5) It is necessary to review and take a different approach to tariffs for issuing certificates of origin and compliance;

- 6) It is necessary to ensure access to standards, sanitary-hygienic norms and acts;
- 7) It is necessary to create independent laboratories that will make it possible to conduct quality control analysis and hold training sessions with specialists;
- 8) It is necessary to conduct a business-government dialogue by creating unions or associations of businessmen engaged in foreign trade and involving their representatives;
- 9) It is necessary to prepare a stimulating export package for entrepreneurs who have the potential to place their goods and services on the foreign market and to apply a one-stop shop system.

8. Improvement of the law of the Azerbaijan Republic "On bankruptcy"

The law of the Azerbaijan Republic "On bankruptcy" was adopted on 13 June 1997 (No 326-IQ). So far, some editorial changes that do not have a fundamental nature have been made to the law. We can note that a number of shortcomings that existed before and failed to meet modern requirements with the development of economic relations in the country can be clearly seen in the law "On bankruptcy", which was adopted 17 years ago. As a result, the application of the law is in an unsatisfactory state. Serious changes have to be made to the law. The proposals below are based on recommendations from a number of authoritative international organizations:

- The European Union Convention on Insolvency Proceedings. 23 November 1995.
- The European Union Regulation on Insolvency Proceedings entered into force on May 31, 2002. The Regulation, with 47 articles, contains the framework for cross border insolvency within the European Union.
- UNCITRAL Model Law on Cross-Border Insolvency with Guide to Enactment and Interpretation. 1997.
- World Bank. The Principles and Guidelines for Effective Insolvency and Creditor Rights Systems. April 2001.
- EBRD. Insolvency Office Holder Principles. *EBRD Principles in respect of the qualifications, appointment, conduct, supervision and regulation of office holders in insolvency cases*. June 2007.

Our PROPOSALS are the following:

- 1) The objective of the law, its scope of application, the essence of the process of bankruptcy and its main principles should be reflected in the law;
- 2) The text of the law should fully secure the regulation of the process of bankruptcy (from the beginning to the end);
- 3) In relevant chapters and articles of the law, cases to be regarded as bankruptcy, the process of improvement, declaration of bankruptcy, the beginning of the process of bankruptcy, the completion of the process of bankruptcy, issues such as the results of the completion of this process (including procedural time) should be reformed;
- 4) Applying for the process of bankruptcy is not the right, but the duty (obligation) of the creditor and debtor. For this reason, the law should clearly indicate that this point is an obligation;
- 5) Another innovation and improvement in the law would be the addition of provisions about the application and implementation of a mechanism of regulating the process of bankruptcy if the creditors and debtors settle out of court;
- 6) Although the law (Articles 2, 14, 16, 35) contains general provisions on the process of bankruptcy, there is no mechanism of their specific and effective application and implementation. This gap should be eliminated;
- 7) The law should contain special bankruptcy rules for individual market subjects that have specific features (for example: physical persons, banks, non-banking credit organizations, state enterprises and so on), taking into account their specific features and implications;
- 8) Considering problems in the practice of implementing the law on bankruptcy, it is necessary to take measures to constantly train (involvement in training, specialization) judges and those who publicly promote the procedures and relevant progressive practices existing in the law and run the process.