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17

Reducing Administrative Barriers to Investment

Lessons Learned

Scott Jacobs
Jacqueline Coolidge

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14 Emery, Spence, Jr., Wells, Jr., and Buehrer, *Administrative Barriers to Foreign Investment: Reducing Red Tape in Africa*

15 Wells, Jr., Allen, Morisset, and Pirnia, *Using Tax Incentives to Compete for Foreign Investment: Are They Worth the Costs?*

16 Morisset and Andrews-Johnson, *The Effectiveness of Promotion Agencies at Attracting Foreign Direct Investment*

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TABLE OF CONTENTS

BOXES

FIGURES

PREFACE

The quality of the investment climate has become a topic of interest to developing and transition countries that are trying to increase economic growth rates and alleviate poverty. Although there are many components to the investment climate, including the quality of worker skills, the strength and independence of the judiciary, the depth and sophistication of financial markets, and the availability of infrastructure, improvements in these areas require long-term investments and are often subject only to the indirect influence of governments.

By contrast, governments have direct and immediate control over the regulatory environment facing businesses, and can make improvements in this area relatively quickly and cheaply. Empirical evidence in favor of this proposition can be found in the World Bank Group publications *Doing Business* (2004 and 2005) and the *2005 World Development Report: A Better Investment Climate for Everyone*. In particular, administrative barriers to investment, which deter both foreign direct investment and the formalization of small domestic firms, can be removed or mitigated with some political will, sound policy advice, and possibly some technical assistance.

Since its establishment by the International Finance Corporation (IFC) in 1985, the Foreign Investment Advisory Service (FIAS), now a joint service of the IFC and the World Bank Group, has conducted more than 600 advisory assignments in 130 countries. Through this process, FIAS has learned much about the nature of policy and regulatory impediments to foreign and domestic investment in many parts of the developing and transition world. FIAS, in partnership with its colleagues in the IFC and the World Bank and such external donors as the United States Agency for International Development, has carried out 82 projects to identify and remove administrative barriers to investment in 47 countries since 1996, mostly in Africa and Eastern Europe but more recently also in Asia, Latin America, and the Middle East.

FIAS's work in the area of administrative barriers was the subject of an independent, external review in 2004, which found that, for the most part, such projects have been quite effective at improving the investment climate of client countries. This publication provides the "lessons learned" from FIAS's efforts in this area—lessons that can be put to use in almost all countries. Such reforms reduce both the costs and risks facing firms, and thereby improve their competitiveness in the global market. This in turn both encourages new investment and allows for more efficient production, contributing to expansion of employment opportunities and ultimately to the alleviation of poverty.

ACKNOWLEDGMENTS

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ACRONYMS

APEC	Asia-Pacific Economic Cooperation
ARCS	Administrative and Regulatory Cost Survey
BITs	bilateral investment treaties
BPAR	Bureau of Public Administration Reform
CIS	Commonwealth of Independent States
EU	European Union
FDI	foreign direct investment
FIAS	Foreign Investment Advisory Service
GATS	General Agreement on Trade in Services
GDP	gross domestic product
IAC	Investor Advisory Council
IFC	International Finance Corporation
IPAs	investment promotion agencies
IT	information technology
LDA	Latvian Development Agency
OECD	Organisation for Economic Co-operation and Development
OIRA	Office of Information and Regulatory Affairs
Phare	*Pologne, Hongrie Assistance à la Reconstruction Economique*
PRA	Paperwork Reduction Act
RIA	regulatory impact assessment
SMEs	small and medium enterprises
USAID	United States Agency for International Development
VAT	value-added tax
WTO	World Trade Organization
YOIKK	Coordination Council for the Improvement of the Investment Climate

EXECUTIVE SUMMARY

Few problems are more universal than government red tape. From Bangkok to Cape Town to New York, businesses around the world complain about the costs, delays, uncertainties, and corruption linked to thickets of administrative procedures and formalities.

Although these visible costs of complying with red tape are high, they are only the smaller part of the picture. The most costly effect of administrative procedures is their ability to raise barriers to market entry for new businesses, investors, products, and services.[1] Investors are among those hardest hit. The Foreign Investment Advisory Service (FIAS) has described the paradox: countries fight for investment, but "when someone has finally made the decision to invest, he then is subjected to some of the worst treatment imaginable."[2] Such barriers to entry condemn millions of entrepreneurs to the informal or gray economies, reduce investment and trade across borders, and diminish competition that would increase consumer welfare and household income in poor countries.

Administrative burdens on businesses are notoriously difficult to reduce. Many extant procedures are necessary to carry out legitimate public policies. But where procedures are no longer needed or can be organized more efficiently, governments often resist reform because of administrative opposition, cultures of intervention, and relationships with private interest groups. Through hard work and good organization, however, some developing countries have made progress in organizing reform programs to reduce administrative burdens and barriers, and their successes appear to share some common approaches.

This report assesses the lessons learned in a decade of work by FIAS to help developing-country governments improve their investment climates by removing administrative barriers to investment. Such improvement has involved conducting diagnostic studies, designing solutions, developing mechanisms for public–private consultation, and implementing difficult reform programs. The final section of the report identifies these seven good practices for organizing and sustaining programs of reform:

Good Practice 1:
Adopt a multiyear time horizon for implementation.

Good Practice 2:
Give reform oversight and management authority to a body that cuts across the whole of government.

Good Practice 3:
Actively manage and obtain resources for the reform process.

Good Practice 4:
Ensure that the reform process actively involves the responsible ministries.

Good Practice 5:
Carry out an ongoing business–government dialogue.

Good Practice 6:
Institutionalize the monitoring of results.

Good Practice 7:
Work with expert international bodies that are knowledgeable about good practices used in countries facing similar problems.

A growing number of studies and international benchmarks have documented the seriousness of the administrative barrier problem in reducing private sector growth. In many countries since the 1990s the market economy has become increasingly important as an engine of development and poverty reduction. This historic transition to market-led growth has focused attention on the hidden costs of administrative formalities.

1. This effect was the subject of a pioneering book by Hernando de Soto, 1989, *The Other Path: The Invisible Revolution in the Third World*.
2. FIAS 1999.

Where gains expected from macroeconomic stabilization, lower tariffs, and privatization were sometimes slow to materialize, one reason was the constraints to growth found in the microeconomy at the level of decisions made by individual companies, entrepreneurs, and investors to take risks, innovate, invest, and expand. This critical phase of development is precisely where poor administrative procedures produce four kinds of negative effects:

1. Their day-to-day compliance costs increase transaction costs for businesses.
2. Their higher levels of uncertainty, risk, and corruption increase capital costs.
3. They make it difficult to define and enforce property rights.
4. They weaken competition by reducing market entry.

The barriers faced by private companies, particularly in developing countries, are daunting. Here are some recent findings about these barriers:

- FIAS notes that starting a business in a developing country may require an investor to comply with as many as 53 different procedures that may consume 443 days and cost approximately US$6,000 (often more than 10 times the annual income of the average citizen in that country).[3]
- The World Bank's *Doing Business 2005* report (www.doingbusiness.org) points out that businesses in the poorest developing countries face three times the administrative costs and nearly twice as many bureaucratic procedures and delays as their counterparts in industrial countries. In effect, the countries that most need entrepreneurs to create jobs and boost growth—the poorest countries—put the most obstacles in their way.
- Trade facilitation is essential to expanding trade under the World Trade Organization (WTO) Doha Round, but importers and exporters still face high barriers at the border. As early as 1994, the United Nations Conference on Trade and Development (UNCTAD) estimated that the average customs transaction involved 20–30 different parties, 40 documents, 200 data elements, and at least one rekeying of 60–70 percent of the data. UNCTAD stated in 2003 that governments had a long way to go in simplifying the processing of business-to-business, business-to-government, and government-to-government transactions.
- Businesses in industrial countries also face high red-tape costs. Based on figures generated by the Organisation for Economic Co-operation and Development (OECD), total government red tape in Europe costs more than 3 percent of European gross domestic product (GDP) each year, or more than the annual value-added of Europe's agriculture, forestry, and fishing sectors combined. More recent estimates place the annual cost of red tape in Europe even higher—as much as 340 billion Euro, or almost 7 percent of European GDP.[4]

3. FIAS 2004, p. 18.
4. Government of the Netherlands 2004.

I. ADMINISTRATIVE BARRIERS TO INVESTMENT

Administrative formalities take an infinite variety of forms, and it is impossible to develop a generic definition. To add to the confusion, the terms *administrative formalities, administrative barriers,* and *administrative procedures* are used interchangeably.

Most programs aimed at reducing administrative burdens focus on the procedures that implement substantive policies. Although the policies may be good, their implementation can go very wrong if procedures are unclear, onerous, or unpredictable. In that sense, administrative formalities are a subset of government regulation, which means that good regulation principles can be applied to administrative formalities. That is the approach increasingly taken in burden-reduction programs.

Defining the scope of a reform program to reduce administrative formalities should be done pragmatically, based on priorities in a particular country. Some countries have taken a comprehensive approach across the whole of government, but most are approaching the problem from the more targeted viewpoints of investors, small and medium enterprises, the informal sector, or priority export sectors.

The typical administrative barriers project taken up by the Foreign Investment Advisory Service (FIAS) examines both the steps an investor goes through to start a new business and several of the most routine interactions between a business and government agencies during normal business operations. That is, FIAS works with governments to reduce both the barriers to market entry that may increase the capital needed for any given investment, and the operating costs that lower the return on capital. These procedures are categorized as follows:

- *Start-up procedures:* immigration procedures for foreign investors; registration procedures for both domestic and foreign investors (including company registration, tax registration, social funds, and statistical registration); antimonopoly clearance (if applicable); and a sample of sectoral business licenses (for example, transport or construction)
- *Locating procedures:* key aspects of site development, including land allocation and registration, site development, building permits, utility connections, inspections, and occupancy permits
- *Operating procedures:* reporting requirements related to tax administration, import/export procedures, foreign exchange procedures, product certification, labor regulations, and government inspections.

Taking a broader approach, the Organisation for Economic Co-operation and Development (OECD) specifically classifies administrative formalities as a category of government regulation. In the OECD view, administrative regulations are information requirements enabling governments to exercise and implement other (substantive) policy functions, including monitoring compliance with such regulations. Administrative regulations can impose both direct and indirect costs. Direct administrative compliance costs include time and money spent on the formalities and paperwork necessary to comply with regulations. Indirect or dynamic costs arise when administrative regulations reduce enterprises' productivity and ability to innovate—for example, by hampering business management, distorting resource allocation, or discouraging market entry.

II. CURRENT REFORM EFFORTS

Recognizing that countries would grow faster if administrative procedures were more efficient, FIAS (later joined by the World Trade Organization [WTO], the OECD, the World Bank, and other organizations) launched initiatives a decade ago against the corrupting, distorting, resource-sapping administrative jungle that discourages market entrants and plagues business operations. Since 1995 FIAS has worked to reduce administrative barriers to investment in more than 60 countries and subnational jurisdictions, in addition to its other substantial work to improve the investment climate (see box 1).

The reform movement has spread remarkably quickly. Today, almost all industrial countries and dozens of emerging markets and developing economies have created programs specifically aimed at reducing administrative barriers to entry and administrative burdens on businesses. From customs services and inspections to land transactions and business registration, reforms are under way to improve the efficiency and transparency of administrative procedures. These reforms take a very wide variety of forms, including public sector reforms and reengineering to improve accountability and boost professionalism; eliminating and simplifying formalities; adopting processes such as business consultation to improve transparency; and developing new tools such as eGovernment (see box 7 on page 28).

TIMELINE FOR FIAS'S WORK ON ADMINISTRATIVE BARRIERS

Since 1995 the evolution of the FIAS administrative barriers work has mirrored the changing capacities of developing countries to tackle the administrative barriers problem. What follows is a chronology of that evolution:

- *1995–2000:* Countries knew little about the nature of the administrative barriers problem. The gap to be filled was the development of low-cost, broad diagnostics that countries could use to measure the nature of the problem. In this period FIAS developed and refined its flagship diagnostic report, the "road map," progressively expanding the scope and depth of recommendations.
- *2000–02:* Countries wanted to carry out "self-assessments" and to set priorities among reforms. The demand in this period was for more rigorous measurements of the burdens and costs of poor administrative practices to help countries set priorities and monitor results. During this time FIAS added more tools, such as business surveys and templates, to provide more detail and data to its general diagnostics.
- *2002–04:* Countries understood the problem but had difficulty designing and implementing solutions. Weak implementation capacities were recognized as the constraint on results. The development focus turned to capacity building and institutional reforms, dialogue, and technology transfer. FIAS began responding to more requests for implementation assistance by experimenting with various types of "implementation projects."

Today the need for broad and general diagnostics is diminishing as information about investment climates expands from a variety of sources. Today, unlike 10 years ago, reform usually falters not because countries do not know what to do, but because they lack the skills and capacities to do it.

The demand for work on administrative barriers will increase over the next few years for several reasons. The construction of international trade and investment frameworks supports the focus on administrative barriers because the definition of *trade facilitation* has broadened to include the environment in which trade transactions take place, the transparency and professionalism of cus-

BOX 1: FIAS AND ADMINISTRATIVE BARRIERS

The mission of the Foreign Investment Advisory Service, a joint service of the International Finance Corporation (IFC) and the World Bank, is "to advise developing-country governments on how to attract and retain foreign direct investment and maximize its impact on poverty reduction." Since its founding in 1985, FIAS has advised more than 130 countries on more than 600 projects. FIAS is a tiny agency—mobilizing fewer than 20 analysts and $7.5 million annually, although it leverages substantial additional resources by cofinancing project costs.

FIAS often has been the pioneer, but its work has been supplemented in recent years by many other initiatives. In countries where it is working, FIAS has seen the field become crowded in only a few years. For example, when FIAS began its administrative barriers work in Russia in 2000, there was no similar activity. Today, the European Union (EU) Tacis program, the United States Agency for International Development (USAID) Small and Medium Enterprise (SME) Policy Advocacy program, the Eurasia Foundation, and a growing number of local think tanks are working in the Russian Federation on issues that overlap the administrative barriers agenda.

FIAS assists in reforming administrative barriers in six key ways that help build and sustain the critical mass needed for change:

1. *Diagnosing the scope and nature of the administrative barriers problem*—The clarity of the FIAS mirror held up to the government enables officials to see the high costs and economic impacts produced by what previously seemed to be many annoying but trivial procedures. The FIAS administrative barriers report illustrates the power of a well-designed diagnostic tool in fundamentally changing perceptions. If measuring a problem defines it, FIAS has had great influence in defining what administrative barriers mean.
2. *Responding to on-demand information needs*—FIAS is an information broker, making high-quality information accessible to governments on demand through a flexible variety of means, including holding in-country and regional workshops, building the best-practices database, and providing short-term experts.
3. *Coaching clients on reform strategies and sustainable governance issues*—FIAS helps countries develop better, more sustainable governance capacities. Its recommended reform strategies and capacities, transparency strategies, public–private dialogue, and consultation help create and strengthen capacities for high-quality administrative and regulatory action.
4. *Deploying a skilled cadre of consultants to work during the implementation phase, depending on financial resources*—FIAS makes available specialized consultants to react with the client during the implementation period in the priority areas of reform.
5. *Facilitating the securing of funds and managing financing from other donors.*
6. *Providing project management services, such as monitoring progress and intervening as a neutral and influential voice to maintain reforms, particularly when the government changes*—FIAS's credibility and its ability to project a neutral business voice into high government levels are assets to the reform process if implementation runs into opposition.

toms and regulatory environments, and the harmonization of standards and conformity to international or regional regulations. These factors move the focus of trade facilitation efforts "inside the border" to domestic policies and institutional structures where capacity building can play an important role.[5] The expanded scope of trade facilitation has paralleled the expanding scope of investment facilitation; indeed, the two are

5. Wilson, Mann, and Otsuki 2004.

becoming more closely linked in substance and strategies. For example,

- The WTO Doha Round may not lead to formal commitments on trade and investment facilitation, but it is now widely accepted that reducing barriers to market openness is important if developing countries are to receive increased benefits from the global trading and investment system. The hidden costs of poor administrative procedures are higher in global markets because they impede the movement of goods, services, and capital, and undermine domestic business competitiveness. The Doha Round includes goals aimed at removing nonquantitative and nondiscriminatory structural barriers by developing stronger disciplines on regulatory transparency through the General Agreement on Trade in Services (GATS), and by removing barriers that primarily serve to deny "effective market access," and then binding the resulting liberalization.[6] Both of these "good governance" goals are directly relevant to administrative barriers.
- The Doha Round also has placed unprecedented focus in developing countries on implementation and capacity building for efficient and transparent interactions between the market and the state. The WTO today gives priority to helping developing countries implement existing WTO obligations. Technical assistance and capacity-building initiatives, such as the Integrated Framework, are seen as part of a flexible learning process.
- Bilateral investment treaties (BITs) also provide a foundation for more attention to administrative barriers. Many investment agreements are being struck on a bilateral basis: 82 BITs were concluded by 76 countries in 2002. In Asia and the Pacific, the number of such agreements has increased rapidly—to improve competitiveness, attract more foreign direct investment (FDI), and better meet the challenges emanating from heightened competition. The number of trade and investment agreements has also increased. Many recent trade agreements address investment directly or have indirect implications for investment, a trend conspicuously different from earlier regional and bilateral trade agreements.[7] These agreements act as pressures and mechanisms to reduce administrative barriers in domestic economies.

More fierce competition to attract and retain FDI will also drive national reform programs. Facing diminished FDI inflows, many governments have accelerated the liberalization of FDI regimes. An increasing number of countries, including those in Latin America and the Caribbean, are moving beyond openness to foreign investment to the adoption of more focused and selective targeting and promotion strategies. This involves not merely financial incentives and investment promotion agencies (IPAs), but also the investment environment.[8] Furthermore, countries are more concerned about retaining existing FDI, and foreign investors are acting as pressure groups.

Greater emphasis on stakeholder consultation and transparency also helps reduce administrative barriers. Discussions at the international level have focused mainly on the nature and depth of transparency provisions and the scope of their application, including ways to administer rules and regulations.

6. Key 2003.
7. For example, the Free Trade Area of the Americas, now under negotiation, could expand market access, promoting efficiency-seeking FDI. In Africa, progress toward the creation of functioning free trade and investment areas has been slow, although several (mostly subregional) agreements have been concluded. The Africa Growth and Opportunity Act (not a free trade agreement but a unilateral preference scheme) holds some promise for the expansion of trade and investment in the region. See UNCTAD 2003.
8. Ibid.

III. BASIS OF APPROPRIATE ADMINISTRATIVE PROCEDURES

GOOD GOVERNANCE

Administrative procedures are not inherently undesirable. Modern governments could not function without using administrative procedures to collect information, such as tax returns, and regulate market activities as necessary to implement public policies. In fact, all over the world the number of administrative procedures seems to be increasing as governments require more information for their activities and as they regulate more stringently to control risks to safety, health, and the environment.[9] Administrative regulations also can create benefits for enterprises by setting market frameworks in which commercial transactions can take place in a pro-competitive and low-cost environment.

The challenge of reform is to enable both governments and markets to perform well. Government formalities that are unneeded or are damaging in a market economy should be eliminated, but deregulation is not the guiding principle of reforms to administrative formalities. Administrative barriers to investment are sometimes inadvertent results of poor government, sometimes unfortunate but accepted results of good government, and sometimes strategic attempts by organized interest groups to block market entry. When administrative procedures are legitimate interventions by governments to pursue public policy goals, the issue is how these procedures should be carried out so that they do not represent an excessive burden on private investors. This is a "good governance" agenda, rather than a simplistic deregulatory or small-state agenda.

Good government in this context means government that is able to carry out its public policy functions efficiently, transparently, and consistently in line with principles of open and competitive markets. The international emphasis now placed on capacity building for good governance is essential to improving administrative practices. One of the Millennium Development Goals, for example, is to develop an "open trading and financial system that is rule-based, predictable and non-discriminatory" through good governance, development, and poverty reduction.[10] The FIAS emphasis on the role of good governance, the rule of law, and anticorruption is in the mainstream of good governance and regulatory quality strategies that are increasingly being adopted worldwide.

Why are poor administrative formalities so universal? It seems odd that governments claim to want foreign investment but actually hinder it through administrative barriers. The reason for the paradox is partly that governments try to achieve many objectives at the same time, and partly that developing countries in transition from planned economies suffer from the legacies of over-control resulting from earlier state-led development strategies. But the more enduring reason is that administrative barriers fall into that class of fragmented, institutional, and cross-cutting issues that governments are the least capable of tackling:

- Unlike spending through fiscal budgets, there is no accounting system for the hidden costs of administrative procedures. Therefore, governments tend to treat the business costs of responding to government demands and of waiting for decisions as a free good, with zero opportunity cost.
- The most common cause of governance failure is lack of coordination across multiple jurisdictions. Such a structural issue in this case leads to excessive and overlapping demands on businesses.
- The political economy of policies in which benefits are concentrated but costs are widely dispersed is difficult to reverse. Administrative formalities generate

9. The OECD has coined the expression *regulatory inflation* to refer to the continual increase in the number and complexity of regulations, as well as their rate of change.
10. See http://www.developmentgoals.org/About_the_goals.htm.

rents for many interests—for lawyers who sell services to help businesses; for civil servants who sell favors, such as faster processing; and for incumbent producers who want to reduce entry. Every administrative barrier is fiercely guarded by stakeholders and, in fighting them, politicians can expend vast political resources to realize little political gain.

These problems of incentives, information, and structure are exceedingly difficult to address in a sustainable way. They require much more than marginal changes to a few procedures. Developing countries face a triple legacy of (1) numerous interventions into business decisions from previous state-led economic models, (2) poor institutional capacities to implement reforms, and (3) weak reform and corrective mechanisms to remedy problems. The resulting overly complex, multilayered, arbitrary, and interventionist administrative and regulatory environments make it almost impossible to create a transparent and predictable business environment. Sustainable changes require institutional reforms to the state. FIAS has remarked that governments will have to shift their mindsets in terms of scope and approach in order to win FDI in an increasingly competitive global market.[11]

Capacity building is also needed to correct some of the reasons for administrative barriers; for example, weak coordination and cooperation across jurisdictions (inside ministries, across ministries, and across levels of government), poor policy analysis capacities, fragmented implementation of reforms because of overlaps and gaps in institutional coverage, poor coordination and institutional incentives, and lack of government ownership and commitment to donor-driven projects. Fragmentation of reform efforts among donors is almost as common; in fact, donors often compound fragmentation by encouraging single-mission reform institutions.

COMMITMENT TO AN ENVIRONMENT THAT ENABLES PRIVATE SECTOR DEVELOPMENT

Reducing administrative barriers is a subset of the wider set of reforms needed to create an enabling environment for domestic markets to function. Like reform of administrative procedures, economic development increasingly will be fought at the microeconomic level, sector by sector. Because work on administrative barriers aims to change the incentives underlying commercial decisions in the market, it is explicitly market based, aiming at bottom-up, sustainable growth. It stands in welcome contrast to the investment incentives, trade zones, and other top-down supports for investment projects that are common in developing countries. Governments must be committed to private sector–led growth if they are to be successful in reducing their administrative burdens.

How important are administrative barriers within the broad agenda to enable private sector development? A growing pool of studies and comparative indicators suggests that they are more crucial than many think for both static and dynamic performance. The dynamic impacts are hard to measure, but evidence is mounting that reducing regulatory and administrative barriers to market entry has significant economywide effects, including accelerating multifactor productivity growth across the economy, reducing the cost of capital by reducing regulatory risk, boosting innovation, increasing the national savings rate, contributing to poverty reduction, and complementing competition policy.[12]

COSTS OF ADMINISTRATIVE BURDENS

Many studies have positively correlated administrative burdens with poor economic and governance practices. The field of empirical growth literature has developed

11. FIAS 2004, p. 7.
12. For example, see Nicoletti and Scarpetta 2003; Bolaky and Freund 2004.

substantially over the past two decades, drawing on larger and richer databases and exploiting better econometric tools to explain cross-country differences in growth performance. Many of these studies correlate the level of administrative and other regulatory costs with corruption, SME formation, competition, and trade and investment openness.[13]

The World Bank's *Doing Business 2005* report reached several conclusions about the costs and impacts of regulatory and administrative burdens. In administrative costs alone, there is a threefold difference between poor and rich nations. The number of administrative procedures and the delays associated with them are twice as high in poor countries. Chad, for example, requires 19 procedures to register a new business, compared with 2 procedures in Australia. In the Congo, it takes 155 days to register a business. In addition, businesses in poor nations have less than half the property-rights protection available to businesses in rich countries. In Angola, it takes more than three years to enforce a contract.

These kinds of heavy regulation and weak property rights exclude the poor—especially women and younger people—from doing business. The report found that investment climate reforms can help create job opportunities for women and young people, encourage businesses to move into the formal economy, and promote growth.[14] FIAS has reported that reducing administrative barriers creates opportunities for those who have traditionally been excluded from the market, whether they are foreigners or the poor. SMEs—both medium-scale and small-scale entrepreneurs operating on the fringe of the formal market—are particularly hard-hit by a high-cost regulatory environment, and are likely to be important beneficiaries of these reforms.

The significance of administrative barriers in shaping trade flows is hard to estimate, but today these costs seem to be more important than border tariffs:

- The Economic Committee of the Asia-Pacific Economic Cooperation (APEC) estimated in 2000 that measures to reduce transaction costs of cross-border trade could generate economic gains of 0.26 percent of total real regional gross domestic product (GDP), or about US$45 billion, almost double the expected gains from tariff liberalization, and that the savings in import prices would be between 1 percent and 2 percent of import prices for developing countries in the region.[15]
- In 2002 the OECD reviewed available literature on the costs of trade formalities and found "important information gaps" in this area. It reported that estimates of trade transaction costs range from 2 percent to 15 percent of the trade transaction value. By contrast, the WTO has estimated that the post-Uruguay Round weighted average tariff of developed countries on industrial goods excluding petroleum is 3.8 percent.[16]
- Guasch and Spiller argued that monopoly port service providers and inefficient regulation of port operations give rise to implicit tariffs of 5 percent to 25 percent on exports in Latin America.[17]

Investment flows also are affected by administrative burdens. FIAS acknowledges that "administrative barriers to

13. See Jacobs 2003.
14. *Doing Business in 2005: Removing Obstacles to Growth* bases its conclusions on assessments of seven sets of business-environment indicators: starting a business, hiring and firing workers, enforcing contracts, getting credit, closing a business, registering property, and protecting investors.
15. Data from the 12th APEC Ministerial Meeting, November 12–13, 2000; 8th APEC Economic Leaders Meeting, November 15–16, 2000, media background notes. See http://www.wto.org/english/thewto_e/minist_e/min01_e/brief_e/brief15_e.htm.
16. OECD 2001.
17. Guasch and Spiller 1999.

BOX 2: BENCHMARKING ADMINISTRATIVE BURDENS AND BARRIERS

Particularly since 2000, a global industry has been built around administrative barriers to investment as a part of investment, competitiveness, and business climate research. Benchmarking and diagnostics have proliferated from public and private sources. The appendix to this volume contains a partial list of current investment climate resources. Among the 26 sources listed there are numerous global benchmarking studies and regional and sectoral assessments of varying quality.

In the World Bank's Private Sector Development department, work on investment climates has grown with the Investment Climate Assessments and the Doing Business indicators:

- **The Investment Climate Survey, now covering almost 60 countries, uses a sample of businesses to collect information on inspections, bribes, labor, customs, and tax regulations.**
- **Doing Business uses information from intermediaries to describe fundamental aspects of a firm's life cycle, although the coverage of Doing Business is still too limited to make it useful in prioritizing business problems. In 2004 it focused on five topics: starting a business, hiring and firing, enforcing contracts, getting credit, and closing a business. In 2005 Doing Business introduced three new topics: registering property, dealing with licenses and inspections, and protecting investors. In 2006 other topics will be added: trading across borders, improving law and order, and paying taxes. Doing Business relies on a very limited data set to characterize countries, and this reliance has produced wide variations in cost estimates compared with other indicators. But the Doing Business data sources are being expanded to cover more intermediaries in each country.**

investment are often secondary" factors for investors, but argues that their reform can be fast and symbolic, sending a positive signal to investors and making a tangible improvement to the investment climate.[18] Administrative barriers can be decisive for investment decisions on location that occur at the margin. Because they immediately affect the bottom line and project timing, lower costs of entry and production may have disproportionate effects, even if investment decisions are based primarily on other factors (see box 2). A 2002 FIAS study of 32 countries estimated that each reduction of 10 percent in the average costs of administration procedures affecting investors would increase FDI flows by 5 percent.[19]

18. See the FIAS Web site: http://www.ifc.org/fias.
19. Morisset and Lumenganeso 2002.

IV. DIAGNOSTICS AND SOLUTIONS ARE PAYING OFF

A range of approaches to reduce the burdens of administrative procedures is under way in developing and industrial countries alike. Much can be learned from these efforts. They demonstrate that despite some claims that reducing administrative burdens is simple and fast, it is neither. The problem is vast, and sustainable change requires not only marginal reforms to procedures but also new institutional capacities and a shift by the public administration from a culture of control to a culture of client services. Indeed, the quality of public administration is part of the larger issue of the rule of law. Because principles of legality and clarity can be undermined at any stage of the administrative system, administrative barriers cannot be viewed in isolation.

It is necessary to put anecdotes of success in perspective. There is little evidence that, overall, administrative barriers are shrinking. Whereas the relative positions of countries are changing as reform proceeds, no business survey in any country shows that net administrative burdens are falling. In the 2003 corruption index from Transparency International, 9 out of 10 developing countries still scored less than 5 against a clean score of 10, indicating medium to high levels of corruption. After a decade of work, the industrial countries also are struggling just to slow the growth of administrative burdens, rather than shrinking overall burdens. Most governments still do not understand either the problem or the solutions enough to mount an effective attack. A recent OECD report on the fight against red tape in industrial countries found that "governments seldom have a detailed understanding of the extent of the total administrative burdens imposed on businesses, citizens, and government itself nor of the cost-efficiency of many of the administrative simplification tools applied."[20] These conclusions are even more readily applicable to developing countries.

PROGRESS IN RESOLVING ADMINISTRATIVE BURDENS

The next 10 years could be very different, however, in light of the progress that has been made in diagnosing and resolving administrative barriers. Advances in diagnostics, such as the FIAS pioneering road map studies and the more recent comparative indicators, have made it possible to consolidate a wide range of problems into a manageable package of reforms—that is, to develop a coherent reform agenda. Setting priorities is key to the best use of weak reform capacities in many developing countries. FIAS work in 60 countries sheds light on the most pressing reform priorities (figure 1). The six economywide issues most often raised by FIAS as posing barriers to investors in developing countries are, in descending order,

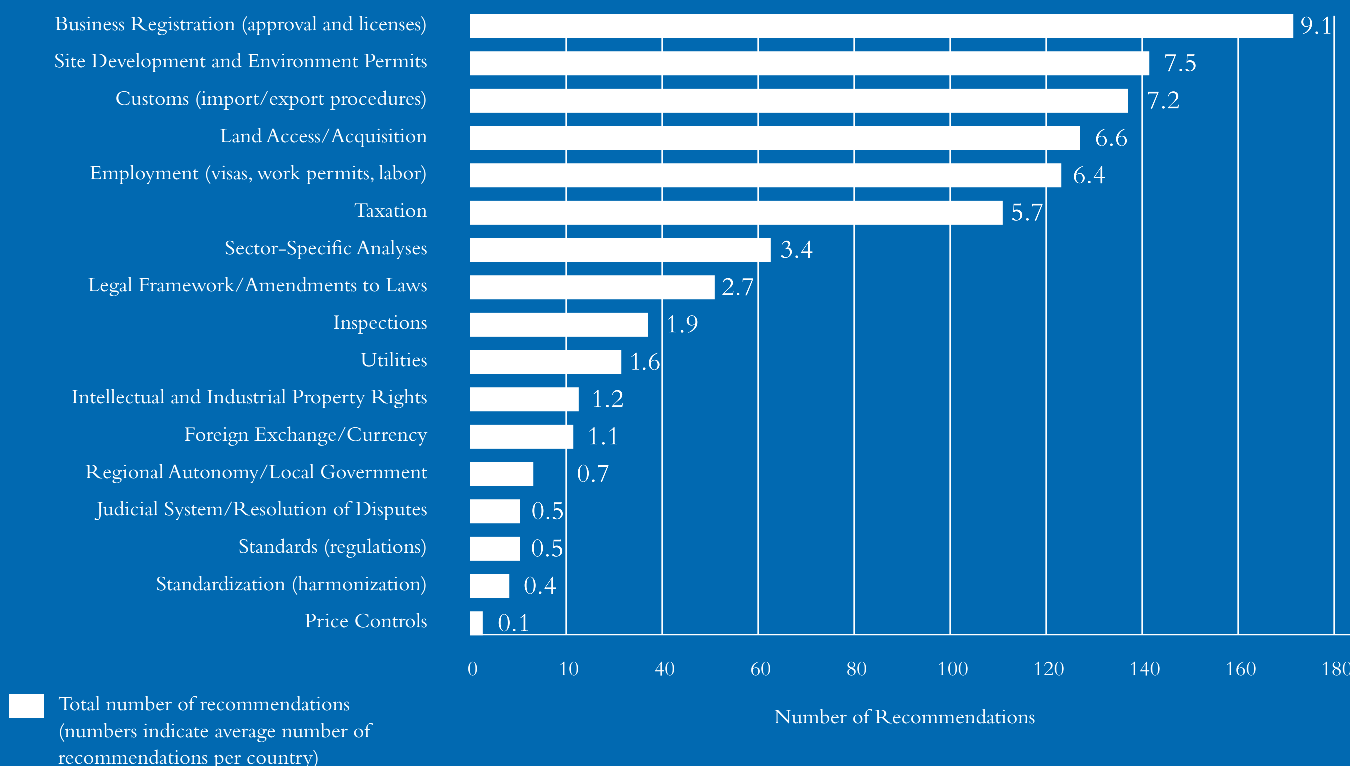
- business registration
- site development, including environmental permits
- customs
- access to land
- employment procedures
- tax administration.

These issues are similar to those examined by the Doing Business reports and the Investment Climate Assessments of the World Bank. They can be considered the core of the administrative burdens problem in developing countries. An administrative barrier–reduction program should start with an examination of these six issues.

Every country, however, will have its unique problems that may merit special attention, such as administrative costs in export-oriented sectors. For example, another emerging issue in the FIAS work is the quality and efficiency of inspections, a phase of the administrative

20. OECD 2003, p. 9.

FIGURE 1: TOTAL AND AVERAGE NUMBER OF FIAS RECOMMENDATIONS PER COUNTRY, BY TOPIC



Source: FIAS Project Impact Monitoring System Database.

process that is highly vulnerable to corruption because of a lack of transparency, accountability, and due process, and an overlap among government agencies.

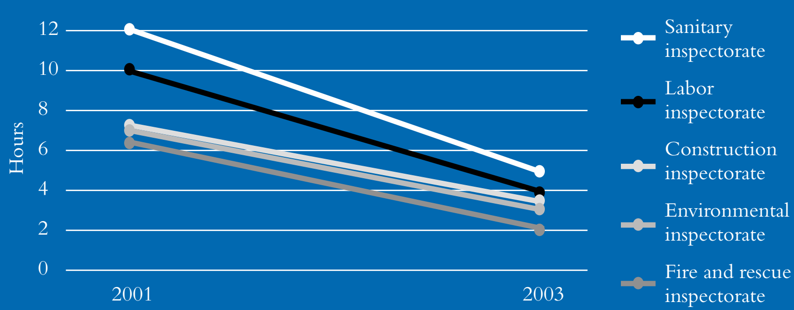
There is no doubt that countries around the globe are moving forward with reforms today on a broad front. The *Doing Business 2005* report noted that it became easier for entrepreneurs to launch a new business in 35 countries last year. Some countries consolidated and streamlined procedures required to register companies. On average, during 2003–04, the top 10 starting-a-business reformers cut procedures by 26 percent, decreased time by 41 percent, reduced cost by 56 percent, and lowered the minimum capital requirement by 8 percent.[21]

FIAS PROJECT CONCLUSIONS

A recent review of the FIAS work on administrative barriers concluded that within three to five years after the FIAS diagnostics were completed, FIAS client countries had launched action to implement, on average, 20–30 reforms, or 50 percent of the FIAS recommenda-

21. *Doing Business in 2005: Removing Obstacles to Growth.*

FIGURE 2: DURATION OF INSPECTIONS IN LATVIA, 2001–03



Source: FIAS Case Study: Inspectorate Reform in Latvia, 1999–2003.

tions. Each of those countries had finalized legal action to implement, on average, a dozen reforms, or 20 percent of the recommendations. Many of these actions are significant, ranging from constraining the discretion of inspectors, to better coordinating company registration, to providing more transparent construction approval procedures. Selected examples include

- preparation of a subnational guide for construction-related procedures in Croatia
- clear appeals procedures for development applications that have been turned down by local authorities in Croatia
- removal of duplication between the tax registry and business registry in Latvia
- requirement of visit reports from inspectors in Latvia
- institution of a single business identification number for company registration in Russia
- clarification of rules for value-added tax (VAT) within the Commonwealth of Independent States (CIS) to avoid double taxation
- improvement of the land cadastre in Senegal
- increase in the number of judges assigned to the commercial court in Uganda.

These reforms would not have occurred without substantial investments by governments in designing reforms, working for the necessary level of consensus, and enlisting parliaments in the reforms. Both rising awareness of the hidden costs of administrative barriers and pressures such as international competitiveness are changing the political economies that long have paralyzed the capacities of many countries to address these issues.

The reactions to FIAS recommendations suggest that a multiyear time horizon is needed for reform to work. Of the 20 percent of FIAS recommendations that were fully implemented, a little more than 2 percent were implemented in the first year after the FIAS report was issued; approximately 6 percent were implemented in the second year; and approximately 11 percent were implemented in the third year or after. Start-up takes time. This suggests that monitoring mechanisms likewise should stretch over a three- to four-year period.

Despite the number of reforms, quantitative evidence of impacts on business costs following administrative barriers reform is extremely limited.[22] Anecdotal information about the effectiveness of solutions is expanding, although much of this information should not be generalized. Such evidence suggests that when reform works, the payoffs can be significant and can appear quickly. Consider the following examples:

- A high-quality assessment of inspections reforms was carried out in Latvia, backed up by pre- and post-reform survey data (see box 3 and figure 2). The Lat-

22. This is partly because the marginal impact of administrative procedures on investment decisions is unclear, partly because the contribution of the costs of the procedures that are reformed to total administrative costs on investors is unknown, and partly because the implementation of reforms is poorly documented and hence results in terms of lower costs are usually unknown. We would have to know the answers to all three questions to assess quantitatively how reforms actually affect business costs.

BOX 3: INSPECTION REFORMS IN LATVIA

Diagnostic: In 1999 FIAS found that the Latvian inspection system subjected investors to inconsistent and discretionary implementation of laws and regulations, the imposition of unclear fines and sanctions, and ineffective appeal procedures, among other administrative barriers.

Solution Design: FIAS developed an action plan for identifying and implementing new laws, regulations, and practices regarding inspectorate reform, including

- systematic identification of problems
- structured stakeholders' dialogue on reform priorities and an action plan
- implementation of the action plan by policymakers
- continuing reform process monitoring.

Implementation: The Latvian response was highly organized. The government formed a working group in 1999 to address many of the FIAS recommendations, among other reforms. The working group submitted an action plan to the government, which designated the Bureau of Public Administration Reform (BPAR) as the institution responsible for the implementation of inspection reform. Specifically, BPAR was charged with the task of writing a unified "instruction" to standardize the internal regulations of the various inspectorates to improve consistency and predictability for businesses.

With guidance from FIAS and cofinancing from the EU/Phare program, the government entered into a dialogue with the private sector regarding inspectorate reform. Subsequently, the Latvian government negotiated with the World Bank to include some of the recommendations from the action plan as conditionalities for a new structural adjustment loan.

FIAS worked with the World Bank to help the country develop new regulations to clarify the rights and responsibilities of both inspectors and the people inspected and to develop a training program that encouraged a more "client-oriented" approach to inspections.

In September 2000 the Cabinet of Ministers adopted an Inspectorate Improvement Program involving the BPAR, an Inspectorate Coordination Council, the Latvian Development Agency (LDA), and more advanced inspectorates, with input from the World Bank, the LDA, and the business community. The LDA assumed the role of monitoring and assessing the business environment to gauge progress. The action plan developed by the country with FIAS guidance has become a living document, continually incorporating the new items to be implemented and tracking those that have been completed.

Impact: Latvia was designated as "CC BEST" (Candidate Country—Business Environment Simplification Task Force) by the European Commission's director general of enterprise, citing Latvia as a positive example for other EU candidate countries. In 2003 FIAS produced a follow-up study, which documented, among other things, these improvements:

- decreased burden of inspections and associated bribes, and constant or improved inspection quality (Critically, the overall public health and workplace safety situation did not seem to deteriorate as a result of reductions in the frequency and duration of on-site inspections; rather, better risk targeting seemed to maintain or improve safety levels.)
- significant progress in enterprise registration, tax administration, customs and border crossing, real estate, and expatriate residency.
- successful implementation of 91 of 106 tasks in the action plan by December 31, 2003.

vian case study shows impressive results in a difficult reform area.

- The *Doing Business 2005* report estimated that an improvement in the ease of doing business from the bottom to the top quartile of countries is associated with an additional 2.2 percentage points in annual economic growth.
- An indication of the payoff comes from Turkey and France, each of which saw new business registration increase by 18 percent after the governments reduced the time and cost of starting a business last year.
- Between 2003 and 2004, Ethiopia witnessed a jump of 48 percent in business registrations after simplifying its entry procedures.
- Slovakia's reform of collateral regulation helped increase by 10 percent the flow of bank loans to the private sector.

V. EFFECTIVE ORGANIZATION: A VITAL STARTING POINT FOR REFORM

Good data about the results of reforms are scarce, but reformers now have access to more and better information about how developing countries are organizing their reforms of administrative barriers. Effective organization of the reform process so as to build consensus and institutionalize change seems to be a good predictor of success. Many developing countries suffer from institutional weaknesses, lack of political commitment, and active hostility to change by inside interests. As a result, the reform process has often run into trouble, faltered, slowed down, and in some cases stopped completely.

Government activities to discuss and design reforms should be seen in the wider context of changing the political economy inside the country, releasing reform energies, and reinforcing a growing consensus about market reform. If reforms of administrative barriers are stimulating these kinds of changes, they are helping governments overcome governance bottlenecks, such as the ability of "insider" groups to stop the consideration of options contrary to their interests. The reform process is not just a means to an end, but is itself a part of the process of changing the reform capacities and political economy of a government. For example,

- Reforms can start a process of negotiations between the government and other actors, such as business interests.
- Reforms can change the political balance by bringing in objective parties, such as international organizations, that balance or referee vested interests.
- The reform process can transfer knowledge throughout the policy structure that changes how it sees and reacts to future issues.
- The reform process can change the attitudes of political actors and influence the domestic debate about reform policies. An action-planning process probably indicates that reformers in the government have been empowered.[23]

To the extent that these impacts occur, the reform process reinforces the pro-market consensus in client countries. This view of the importance of the reform process parallels the views in a recent assessment of the impacts of World Bank development assistance:

"The most successful development assistance will have effects that reverberate far beyond the confines of the project itself, either because the ideas in the project are replicated elsewhere, or because the intervention has helped institutionalize new approaches. . . . aid's largest impacts will come through such demonstration effects and institution-building."[24]

The government responses to the FIAS recommendations, and their reform experiences (which vary in terms of success and sustainability), illustrate how progress was made on a respectable 50 percent of the mostly ambitious recommendations:

- In every country, the FIAS agenda was supported at the ministerial or cabinet level.
- In every country, new institutions were established or existing institutions were given new mandates to pursue the FIAS recommendations.
- In every country, interministerial coordination was developed as part of the process.
- In most countries (including those in which the public and private sectors traditionally viewed each other with suspicion), the private sector was brought into the dialogue and even into the policy-design process in ways that were innovative.

One of the most important impacts of the FIAS reports seems to be the mobilization and stimulation of reform

23. Some of these ideas are developed in an interesting analysis in Boockmann and Dreher (2002).
24. Goldin, Rogers, and Stern 2002.

capacities that were blocked by a lack of information or the paralyzing dynamics of interest-group politics. This is a necessary precondition for reform. As box 4 shows, Turkey made an impressive effort that has produced real results. Senegal, which failed to act in response to a FIAS report prepared in 1999, began to move quickly on the FIAS report of 2002, under the strict direction of a high-level Investor Advisory Council (IAC) that was established with the support of the World Bank and that adopted the FIAS agenda as its own. The investment promotion agency has acted as the secretariat for coordinating the process, but has relied on the political clout of the IAC to push the reforms.

By contrast, the reasons for lack of progress were very similar across the countries: lack of expert and dedicated institutions for implementation, lack of political will and accountability, fierce resistance by insiders, and rampant corruption. FIAS has found that common causes of reform failure include the following:

- There is weak political will in attacking corruption and reducing protection for vested interests.
- Resistance to change within public organizations preserves discretionary power and the opportunity for corruption.
- There is weak leadership and poor coordination in the reform process between initiatives for streamlining administrative procedures. In one country the central unit responsible for overseeing implementation moved among three institutions over the reform period in response to political intrigue among ministers. This caused a decline of support for and participation in the reforms.
- Even when recommendations are adopted and laws are changed, many are not implemented by the responsible ministries. A major reason given by FIAS for lack of implementation was inadequate resources, particularly manpower and technology, in addition to poor organization and bureaucratic resistance.
- Action plans contain no performance measures to ensure that legal revisions achieve expected results.
- Although some procedures were improved, the costs of other procedures actually increased over the reform period so that, on net, private companies are worse off. For example, the time required for an investor to overcome the administrative barriers in Senegal increased from 1999 to 2002 as a result of higher barriers in land access and site development. In Uganda, FIAS survey work found that although some procedures had marginal improvements, the costs of others (such as immigration, business registration, land allocation and registration) had increased. One reason was that Uganda's decentralization process led to proliferation of administrative barriers (such as licensing and fees) at the regional and local levels.
- Ongoing corruption damages the credibility of the government and its policy reforms among private investors.
- Other uncoordinated reforms undermine progress. For example, decentralization in some countries led to proliferation of administrative barriers and incentives for revenue generation at the regional and local levels that increased the burdens of multiple taxes and licensing fees.

Successful reform strategies increasingly recognize that procedures are embedded in institutions, that poor institutions can defeat even the best procedures, and that institutional capacity for diagnosis and correction is the key to sustaining reforms. Reformers can benefit from the increasing attention paid to how institutions affect an economy's attractiveness to FDI inflows and domestic private investment. A growing body of research links institutional success and failure to economic growth and market development over time and across countries. There are several relevant fields of economic literature:

- Empirical growth literature has developed substantially over two decades, drawing on larger and richer databases and exploiting better econometric tools to explain cross-country differences in growth performance.
- The New Institutional Economics theory suggests that governments themselves hold a key to faster growth by adjusting their domestic institutions to reshape incentives among market agents.
- The study of how institutions actually operate has been greatly expanded by a New Comparative Economics theory, which seeks to demonstrate how institutions differ systematically among countries and how these differences have significant consequences for economic and political performance, with a focus on understanding which ones are appropriate in what circumstances.

This body of work has fueled the proliferation of benchmarks, as shown in the appendix to this report, and provides a theoretical basis for work on administrative burdens (for example, in transactions costs).

BOX 4: CUTTING RED TAPE IN TURKEY

Diagnostic: As a result of the June 2001 FIAS report, *Turkey: Administrative Barriers to Investment,* the Turkish government adopted specific targets for administrative streamlining in a range of areas, including investment legislation, taxation and incentives, company registration, customs and standards, intellectual property rights, sectoral licenses, employment, and municipal location issues.

Solution Design: FIAS made recommendations for 32 changes in procedures and laws and for the establishment of an investment council to develop and oversee implementation of an action plan.

Implementation: The government enacted a "Decree on Improving the Investment Climate in Turkey" that set out a three-phase strategy:

1. establishment of the Coordination Council for the Improvement of the Investment Climate (YOIKK)
2. development of an action plan
3. progress monitoring.

YOIKK, with private sector observation and participation, was charged with proposing the legislation to streamline administrative procedures in a range of areas.

Results: YOIKK produced an impressive volume of reform legislation, and 56 percent of those recommendations on the recruitment of foreign personnel, foreign direct investment, company registration, and labor have already been implemented. The council is currently engaged in reforming the areas of sectoral licensing, customs, intellectual and industrial property rights, and land acquisition and site development. The process has been aided, monitored, and supported in an unprecedented way by the participation of the private sector (although the sector's participants note weaknesses, such as lack of transparency in drafting legislation, lack of accountability of technical committees, and lack of monitoring). Business associations are currently monitoring the implementation progress of all FIAS recommendations.

It is increasingly clear that to sustain real gains in reforming administrative barriers, a sustained program of institutional reform must be tailored for each country, often with technical assistance. That is why FIAS has joined the WTO Doha Round and the Millennium Development Goals in emphasizing capacity building. Administrative barriers projects must include a strong capacity-building component aimed at developing the institutional capacity for an ongoing review of the business environment and assigning the responsibility for follow-up and policy recommendations to an appropriately mandated entity, with support from the government and stakeholders in the public and private sectors.

VI. KEY SUCCESS FACTORS FOR REFORM

Reform is a process rooted in the institutions and political economy of the interests at stake. Therefore, the processes of diagnosing, communicating, and engaging with stakeholders are as important to getting results as is the substance of the reform. How do countries manage to overcome institutional and political weaknesses to push ahead with the reform program?

The review of FIAS experiences suggests that countries that gain the most from administrative barrier reforms share key common factors in how they organize and sustain reform in difficult governing environments. Of course, political will is essential, but there also seem to be more operational issues that can be designed into the reform process itself. The success factors seem to be interrelated; that is, more successful governments seem to invest simultaneously in strategies, such as managing the reform program, conducting ongoing public–private dialogue, and monitoring results.

This is not unique to developing countries. Almost all OECD countries have launched multiyear, interministerial programs to reduce administrative burdens. The lessons of these efforts have been synthesized by the OECD.[25] The OECD has concluded that the following three factors are common to multiyear, cross-sectoral regulatory reforms:

1. a reform policy adopted or affirmed at the highest levels of government
2. engines of reform within the administration to drive reform forward, such as dedicated reform units in the cabinet office
3. accountability for results by adoption of clear principles and goals.

Other factors may be necessary but do not in themselves seem to improve the chances of success. Surprisingly, development of an action plan does not seem to predict reform results. Action plans produce nothing if they are not supported by reform strategies and institutions. In addition, there is little evidence that a preexisting critical mass of reformers is necessary to achieve results. Governments can organize themselves fairly quickly if other conditions for reform are present.

SEVEN GOOD PRACTICES

Good Practice 1:

Adopt a multiyear time horizon for implementation

The key to success seems to be sustaining the reform process over three or more years, when results begin to appear. The other success factors discussed below seem to be predictive of sustainability. The most vulnerable period seems to be year 2, when political attention begins to wane and bureaucratic interests take control of the reform process. Surprisingly, actions that do *not* seem to predict sustainability over time include the development of an action plan and the creation of committees or other ad hoc groups with responsibility for implementing the reforms.

Good Practice 2:

Give reform oversight and management authority to a body that cuts across the whole of government

The presence of a high-level official at the center of government or a high-level committee accountable to the center has proved to be a success factor (examples from the Netherlands and the United States are given in box 5). These principles can be seen in countries with more success in reforming. In the Russian oblast of Tomsk, for example, the action plan was overseen by the vice-governor with authority over the whole govern-

25. OECD 2003.

BOX 5: REDUCING ADMINISTRATIVE BARRIERS IN THE NETHERLANDS

The administrative burden for companies in the Netherlands is estimated at 16.4 billion Euros, which equals 3.6 percent of GDP. In the United States, citizens and firms spend $243 billion each year in complying with federal paperwork, or 2.2 percent of GDP. Americans spend 8.1 billion hours each year to comply with administrative procedures—equivalent to more than 4 million full-time American employees working just to collect information, fill out forms, and file records. The burdens in the United States are increasing at unprecedented rates.

Both countries have created programs to control and reduce these burdens—programs that are very different but have some common elements. In both countries they

- operate from the very top of government
- take a governmentwide approach
- involve transparent methods of measuring the burdens
- use public input and consultation to reduce burdens
- attack both new and preexisting burdens
- hold ministers directly accountable for complying with efforts to reduce the burdens.

THE NETHERLANDS

The current Dutch cabinet advocates an extensive program of deregulation and simplification of legislation. It has adopted a target of reducing total administrative costs by 25 percent, or 3 billion Euros, by 2007. According to the government, this reduction should have positive effects on productivity, competitiveness, output, and economic growth. In the long term, GDP will increase by 1.5 percent. Pushing back bureaucracy will free 24,000 workers for redeployment, and employers will be able to respond more swiftly to changing market situations.

The Dutch approach consists of two “building blocks”:

1. *Reducing existing administrative burdens through a simplification program.* Unnecessary regulations will be scrapped and the remaining rules will be tightened where possible, thereby enabling businesses to spend less time and money complying with certain regulations. A package of 130 measures was submitted to and agreed by parliament in June 2004, and a second package will be submitted in 2005.
2. *Prohibiting new administrative burdens by better use of regulatory impact assessments (RIAs) for new laws.* A new questionnaire on administrative costs has been added to national RIA requirements for new legislation. Each new proposal must estimate the administrative cost involved. The ministry must clarify if the least burdensome way of regulation is used. Because the reduction target is a net target, the proposal must show how new administrative barriers will be “paid for” by reducing other burdens. The Dutch Advisory Body for Administrative Burdens will carry out an independent assessment of the potential administrative burdens for new legislation.

Coordination of the cabinet program is in the hands of the Ministry of Finance in collaboration with the Ministry of Economic Affairs. Progress is monitored via the budgetary cycle. The cabinet reports on the progress of implementation in the annual Budget Memorandum. It adopts upper limits for administrative burdens for each ministry, and each minister is held responsible for reducing administrative burdens originating from the ministry. The Dutch government states that “this operation requires the backing of the entire Cabinet. All Ministers have pledged support for these plans.”

The corporate sector, through advisory groups called “Mixed Commissions,” was closely involved in drawing up the inventory of reforms. In October 2003 the Dutch Ministry of Finance started a Web site where entrepreneurs can complain about unnec-

AND THE UNITED STATES

essary and inconvenient information requirements. The ministries of economic affairs and finance are also setting up a "sounding-board" group of employers to monitor government policy on regulations and competitiveness in the wider context.

The Dutch experience provides evidence that large reduction targets can be realized without unacceptable risks. In many instances, red tape is reduced through more effective organization of the public administration, through modern information and communication methods, and through more accountable and transparent information requirements. In addition, compliance rates go up if requirements are more straightforward and less cumbersome.[1]

UNITED STATES

The U.S. government has an enormous appetite for information that must be fed by paperwork filled out by enterprises and citizens. According to a General Accounting Office report in 2003, more than 94 percent of the administrative burdens are imposed to improve compliance with regulations.

Since 1980 the Paperwork Reduction Act (PRA) has required federal agencies to minimize the paperwork burden that they impose on the public. The act sets up a highly centralized and transparent structure to control administrative burdens:

- The act establishes an independent reviewing agency (the Office of Information and Regulatory Affairs, or OIRA) at the highest level of government—in the Office of the President.
- Agencies must estimate the time required to comply with all administrative procedures. They use an accounting method based on "burden hours."
- OIRA must review and approve all administrative burdens (called collections of information) on businesses and citizens. OIRA can disapprove any administrative burden if it finds that the burden (1) does not have practical utility, (2) is not the least burdensome necessary, or (3) duplicates information otherwise available.
- No department or agency can impose administrative burdens without OIRA approval. To protect citizens against illegal procedures, every form and procedure must publish the OIRA approval number, and must tell citizens how much time the procedure is expected to take.
- OIRA approval expires at least every three years, and so every administrative procedure is reviewed periodically.
- OIRA develops an information collection budget that sets annual goals and reports on department and agency progress in reducing burdens during the year. Each agency calculates its total information collection budget by totaling the time required to complete all of its information requests. This budgeting exercise is then used to measure progress toward reduction goals.
- OIRA reports on progress each year to the Congress.

Public comment is an important part of the reviews. Requests for OIRA approval are published in the *Federal Register,* and the public is given 30 days to provide comments.

This process has slowed the growth of new administrative burdens, but burdens are still increasing. The PRA set goals to reduce burdens by 35 percent from 1995 to 2001, but burdens had actually increased by 17 percent by 2002, mainly because of new paperwork prompted by tax requirements. In fact, tax paperwork accounts for more than 80 percent of all administrative burdens imposed by the U.S. federal government.

1. OECD 2003.

Sources: Government of the Netherlands 2004; U.S. GAO 2003.

ment. In Latvia the prime minister operated as the "champion" of the reform effort. Implementation in Turkey suddenly accelerated when oversight of the reform process shifted from a career civil servant to the influential minister of economy. In Senegal a high-level investors advisory group was needed to overcome bureaucratic inertia.

Reforms managed by line ministries or IPAs without clear authority over other ministries seem to slow down and stop in a year or two. Ad hoc committees do not perform well, probably because they are outside the mainstream of the policy process and cannot sustain action over a multiyear program. Nor are ad hoc committees able to follow reforms through the entire implementation process.

Here is a list of the characteristics of an effective central authority guiding the reform process:

- *Has a longer-term agenda and mandate.* Sustainability in focus and influence is key where the policy environment tends to be driven by personalities and where tenure of office is often unpredictable and brief. Ad hoc working groups are inappropriate unless they are stepping stones to a more permanent structure.
- *Has an active interministerial component* to bring in the stakeholders who will have to implement reforms over the course of the project. Top-down instructions to other ministries, such as those given by the ministry of finance, may suffice to set up meetings, but they are not an effective basis for reforms.
- *Is authorized, connected, or accountable for results to the center of government* to strengthen policy coordination and oversight capacities.
- *Has a strong relationship or an active involvement with the private sector,* and includes those parts of the government that are champions of private sector development. Here, too, there seems to be a positive evolution. In Turkey the private sector trade associations played a prominent role in pushing for the reforms by financing the work, by being members of the interministerial implementation group, and through political connections with ministers. In Kenya a private sector group joined the responsible ministry. In Croatia the Presidential Commission on Support of Private Business (whose members included the American Chamber of Commerce, the International Chamber of Commerce, the ministries of finance, economy, and state revenues, and the Tax Payers' Union) played a supporting role in a difficult environment.
- *Is credible to donor organizations on the ground* to improve the chances of longer-term financing and technical support.
- *Commands the resources needed to get the job done,* including a dedicated secretariat with the right skills and financing to move reform forward.

Unsuccessful or Risky Approaches

Two common reform approaches—a champion of reform and the IPA—seem not to perform well, and reliance on them should be avoided unless the government has a strategy to institutionalize longer-term capacities in a more appropriate way.

1. *The champion:* The easiest approach—and the natural tendency of governments—is to find a champion, usually a strong minister who is reform minded, and to place faith in that individual to drive the project forward. This is a tempting but risky strategy. The most frequent explanation for why administrative barrier projects produce few results is that ministers change, or that elections change the government. Getting results requires not only a vocal minister but an institution that is able to promote change, and

commitment to a multiyear program that extends through the planning and implementation phases.

2. *An IPA:* The most common oversight body to fight administrative barriers is the IPA, but the IPA does not seem very effective. Its main strength is its relationship with businesses that understand the problems, but it has several weaknesses. It is not a ministerial-level agency, has no seat on the council of ministers, and is not commonly involved in the policy process. It has little influence on ministries. All of this may explain why, on closer examination, the record of the IPA does not look very promising, particularly for the implementation phase.

Good Practice 3:

Actively manage and obtain resources for the reform process

Active management of the reform program appears to be another signal of success. It seems to be best characterized by a dedicated and accountable secretariat, backed by active political oversight over time.

- In Tomsk several status reports were prepared on the comprehensive action plan as implementation proceeded, and politicians made changes to correct emerging problems (see box 6).
- In Latvia a strong and active layer of "technocrats" maintained continuity as governments changed, provided intellectual input, and handled the details of the reform process.

Good Practice 4:

Ensure that the reform process actively involves the responsible ministries

The nature of the diagnostic process seems to make a difference in the reform receptiveness of the responsible ministries. The key difference appears to be the level of

BOX 6: IMPLEMENTATION ASSISTANCE IN TOMSK OBLAST

One of FIAS's most developed implementation programs is in Russia, where FIAS has assisted several oblasts through their action planning and reform design. In Tomsk oblast, which FIAS considers to be the most effective of the nine oblasts that participated in the project, implementation proceeded in six phases:

1. **November to December 2000: evaluation of administrative barriers in Tomsk.**
2. **November 2001: FIAS report and recommendations for improvement.**
3. **December 2001 to April 2002: elaboration of action plan and identification of baseline monitoring.**
4. **2002: at the request of Tomsk, FIAS provided an assessment of administrative procedures in land property and real estate, which the oblast used as a guideline to develop and implement reforms in land resource management.**
5. **January 2003: the Administrative and Regulatory Cost Survey (ARCS) and new data acquisition from relevant state agencies.**
6. **March 2003: report and detailed recommendations to improve administrative procedures in application for and acquisition of property titles and construction permits by entrepreneurs.**

Source: Oksana V. Kozlovskaya, Deputy Governor of Tomsk Region, economic policy, investment, labor and state property presentation at the FIAS Donors Meeting, Paris, October 2003.

effort made by the government to involve ministries in active discussions about the problems and reforms. Governments that asked the ministries for their input on the diagnostics and solution design seemed to have more success than those that produced top-down reforms that the ministries knew nothing about or with which they did not agree.

Good Practice 5:

Carry out an ongoing business–government dialogue

The intensity and institutionalization of business–government dialogue throughout the reform process seem to be linked to the depth of reform. In many developing countries, there is little or no tradition of constructive dialogue and cooperation between the government and the private sector, but such dialogue changes the political economy by empowering allies of reform, and enlarges the "reform space" by increasing awareness of the scope and depth of the problem.

- In the Tomsk oblast a dialogue between business and government endured as the implementation proceeded.
- In Turkey the business community took a strong role from the very beginning, and intervened when government resolve seemed to falter. Business organizations participated on the committee charged with implementation, and they monitored progress.
- In Latvia a strong, well-organized, and constructive private sector readily contributed to the effort of designing the reforms and cooperated with their implementation and monitoring.
- The beneficial effects of dialogue were missed in some other countries where national business communities reacted positively to being invited to participate in workshops and to draw up action plans but were not included in the implementation phase. In those countries reforms tended to falter halfway through.

There are two main reasons why the involvement of private sector organizations increases the quality and results of these reforms:

1. *Information collection:* Businesses are the only actors that understand the reality of implementation issues and the cumulative impacts of administrative procedures across the ministries. Governments should always meet with business interests in collecting information for administrative barrier diagnostics—for example, through investor workshops—to get a clear understanding of the impediments facing the private sector. In Turkey, for example, FIAS worked closely with industry and investor associations such as YASED and TÜSIAD to provide a "reality check" on how procedures work in practice.
2. *Support for the reform process:* The private sector is, or should be, an important constituency for reform.

Involving the private sector might require capacity building in reform-minded business representatives. The private sector is often too badly organized to sustain attention to the reform agenda. Worse, the most powerful parts of the private sector often are those closest to the public sector, and hence are the least likely to criticize the lack of reform or to support reforms that open markets to new competition. The reform-minded parts of the private sector often are the newer organizations with the fewest skills and the least influence. This neglected stakeholder group is needed during the implementation and monitoring processes.

Good Practice 6:

Institutionalize the monitoring of results

A factor linked to a more successful implementation phase is the institutionalization of monitoring into the reform strategy. There are three main arguments for developing a monitoring strategy:

1. If a government is to be results oriented, it must know more about results. This requires a monitoring strategy.
2. Governments are likely to show more and faster progress if a credible monitoring strategy is in place because reformers are strengthened by accountability and transparency. This is especially important in developing countries that are characterized by unstable political institutions. Monitoring can help sustain attention to a program when a minister or government changes (a frequent cause of program failure).
3. Monitoring will speed up the learning process in governments by clarifying reasons for success and failure.

Governments do not have to do this themselves, and indeed they should not. A more effective and credible approach might be to help develop a private sector monitoring capacity. Private sector representatives could assist in keeping reform on track, assessing the quality of work done, and informing the government of the situation on the ground.

Two of the most successful of the FIAS clients—judged not only in terms of what they have accomplished but also in terms of sustaining the reforms over two years or more—are Latvia and the Tomsk oblast in Russia. In both jurisdictions, the governments conducted a baseline business survey and a follow-up survey to track impacts on the ground.

Good Practice 7:

Work with expert international bodies knowledgeable about good practices used in countries facing similar problems

Success seems related to a longer-term presence of an external, expert body to assist the government in diagnosing problems, designing solutions, and bolstering the efforts of reformers. To identify and find solutions to problems, governments must know more about best practices in a wider range of relevant countries. Access to best practices and cross-country experiences is often accomplished through a relationship with an international organization having cross-country expertise. Governments working with FIAS often request workshops to discuss best practices. Here are some examples (see also box 7 on page 28):

- Latvia, probably the best performer in terms of implementation among the FIAS clients, requested extensive FIAS assistance in developing a monitoring system, institutionalizing dialogue with the private sector, and giving a series of seminars on international best practices in improving "service orientation" in government agencies. FIAS worked with the Latvian government on three back-to-back projects over four years.
- Tomsk had a similar relationship with FIAS, which sent specialists to work closely with the government to include concrete actions, rather than generalities, in the action plan.
- In Turkey FIAS carried out several projects over the period of implementation. These efforts sustained the FIAS presence, while some of the projects fed directly into the implementation process.

BOX 7: GOOD PRACTICES IN OTHER COUNTRIES: eGOVERNMENT SOLUTIONS TO ADMINISTRATIVE BARRIERS

eGovernment, or the use of information technology (IT) to deliver government services, is transforming the administrative procedures of most industrial countries. eGovernment provides many opportunities to improve government administration and transparency. Examples include the extraordinary gains in the quality of customs administration resulting from use of computerized systems, and the advantages of online and paperless business registration. The OECD has noted in its e-book *From Red Tape to Smart Tape* that "administrative simplification is increasingly driven by IT mechanisms."

eGovernment is used less often in developing countries, perhaps because it is believed that these countries have neither the financing nor the expertise to apply eGovernment solutions. However, the costs of IT solutions relative to other solutions are dropping so quickly that such assumptions can be quickly outdated. Some regional and local governments in India have had good success with various eGovernment efforts. Governments might wish to examine good practices in IT solutions in the following areas:

- **one-stop shops (physical as well as electronic)**
- **simplification of permits and licensing procedures (paperless approvals)**
- **time limits for decisionmaking and administrative accountability (for example, tracking applications online)**
- **assistance to small and medium enterprises in implementing regulations (online advice and information)**
- **methods to measure administrative burdens**
- **organizational and structural approaches to administrative simplification (Web-based portals and databases)**
- **public consultation.**

APPENDIX

INVESTMENT CLIMATE INDICATORS: AN INDUSTRY IN ITSELF

The proliferation of investment environment and related indicators in the past few years is remarkable. **Benchmarking** the investment climate means assessing how a country rates against competitors in terms of a wide range of factors that affect investment decisions. These factors include specific aspects of public administration, such as levels of efficiency and corruption in the public administration, the independence and efficiency of the court system, levels of taxation, macroeconomic stability, labor regulation, and capital controls, as well as qualitative factors, such as the perceived readiness of the country to receive foreign direct investment, the willingness of the workforce, and "business-friendliness."

The operational definition as far as the individual investor is concerned may also include many other factors, such as costs, availability of skills and specific services, telecommunications, logistics, technology resources, and access to regional and international markets. Thus, indicators of the investment climate overlap with indicators of competitiveness. Many analyses of world or national competitiveness contain information that directly or indirectly assesses the investment climate. Benchmarking can be carried out by making comparisons with competitor countries, or with what seems to be the "best" country. This has to be done frequently because international change is rapid. But it is not enough to know the country's ranking: the next step is to understand why it is so and how it can be improved. Policy change, perhaps following the policies of the "best" country, is the ultimate purpose of benchmarking the investment climate.

On its Web site (www.ifc.org/fias), FIAS lists several benchmarking resources that are relevant to the investment climate:

- **Doing Business:** The Doing Business indicators are comparable across 155 economies and are mostly comparable over time. They indicate the regulatory costs of business, and can be used to analyze specific regulations that enhance or constrain investment, productivity, and growth. http://www.doingbusiness.org

- **Investment Climate Assessments:** Investment Climate Assessments, a part of the World Bank Group's private sector development strategy, represent an initiative to systematically analyze conditions for private investment and enterprise growth in countries throughout the world. http://www.ifc.org/ifcext/economics.nsf/Content/IC-InvestmentClimate

- **The World Bank's World Business Environment Survey (WEBS):** The survey is a World Bank Group initiative that, in partnership with other institutions, seeks to assess the state of the enabling environment for private enterprise in at least 100 countries, surveying a minimum of 100 firms per country. It provides indicators for assessment and benchmarking. http://www.ifc.org/ifcext/economics.nsf/Content/ic-wbes

- **The World Bank Institute's Worldwide Governance Research Indicators Dataset:** This data set contains composite indicators of six dimensions of governance (voice and accountability, political stability/lack of violence, government effectiveness, regulatory framework, rule of law, and corruption control). Data are available for more than 160 countries. http://www.worldbank.org/wbi/governance/govdata

- **The Heritage Foundation's Index of Economic Freedom:** The index is a practical reference guide to the economies of 161 countries, with detailed information about foreign investment codes, the fiscal burden of government, tariffs, banking regulations, monetary policy, black markets, and more. http://www.heritage.org/research/features/index

- **Transparency International's Corruption Perceptions Index:** This index ranks several countries in terms of the degree to which corruption is perceived to exist among public officials and politicians. http://www.transparency.org/policy_and_research/surveys_indices/cpi

- ***Institutional Investor*'s Country Credit Ratings:** The magazine offers twice-yearly country credit ratings based on survey information provided by leading international banks, money management firms, and economists. www.institutionalinvestor.com

- ***Euromoney*'s Country Risk Rankings:** This is the magazine's twice-yearly country risk rating and ranking. http://euromoney.com/default.asp?page=888&/confidential/awards

- **IMD's World Competitiveness Yearbook:** This annual publication ranks nations' business environments and analyzes their ability to provide an environment in which enterprises can compete. http://www02.imd.ch/wcc/yearbook

- **Global Competitiveness Report:** The World Economic Forum's annual competitive index gives a comprehensive assessment of the several countries' economic performance across different factors.

- **The PRS Group's International Country Risk Guide:** Produced by the PRS Group, the **Guide** provides forecasts and analysis of political, financial, and economic risk for more than 130 countries.

- **A. T. Kearney's FDI Confidence Index:** Conducted by A. T. Kearney, a global management consulting firm, this annual survey tracks the impact of likely political, economic, and regulatory changes on the foreign direct investment intentions and preferences of the leaders of the world's largest corporations.

- **PriceWaterhouseCoopers' Opacity Index:** First published in 2001, this index provides estimates of the adverse effects of opacity on the cost and availability of capital in 35 countries.

- **Standard and Poor's Sovereign Ratings List:** The global provider of independent financial analysis and information has weekly updates on the credit rating of sovereign issuers around the globe.

- **Moody's Sovereign Ratings List:** Moody's provides sovereign ratings for more than 100 nations—nearly every country that participates in the world's capital markets. For each nation, Moody's publishes several different types of ratings to capture divergent risks.

- **The Fraser Institute's Index of Economic Freedom:** The Canada-based institute's Economic Freedom Network Index, which ranks 123 countries, is a joint venture involving 55 research institutes in 55 countries around the world. The core ingredients of economic freedom are defined by personal choice, protection of private property, and freedom of exchange.

- **The Tuck School of Business (Dartmouth College) Emerging Market Access Index:** This index annually ranks the level of access that foreign goods, services, and investment enjoy in 44 emerging economies around the globe.

A growing number of regional, sectoral, and other focused resources contain a wide variety of benchmarks and comparative information on investment climates:

- **Benchmarking FDI Competitiveness in Asia** (MIGA, October 2003) is a report that gives a practical analysis of the investment climate for the electronics and shared services industries in six Asian countries, and is a good example of the use of indicators to make operational comparisons and to draw practical conclusions.

- **India's Investment Climate in an International Perspective** (The Firm Analysis and Competitiveness Survey for India, World Bank, July 2003) is a good example of using indicators relating to different components of the business environment to benchmark a country against potential competitors.

- **Industrial Competitiveness: The Challenge for Pakistan** analyzes the comparative position of Pakistan from a number of points of view, including export and investment performance and conditions for future development. In particular, it compares selected business environment indicators with those from competitor countries.

- **The 2002 Business Environment and Enterprise Performance Survey** (European Bank for Reconstruction and Development, Working Paper 84, November 2003) analyzes the results of an extensive survey of business in selected Eastern Europe and CIS states.

- **Foreign Investment in the Andean Countries** (Center for International Development at Harvard University, Working Paper 85, January 2002) analyzes the performance of the Andean Group of countries in Latin America in attracting foreign direct investment and their varying degrees of performance in improving the business environment.

- **Economic Policy, Institutional Development, and Income Growth: How Arab Countries Compare with Other Developing Countries** (Kiel Institute for World Economics, Working Paper 1183, September 2003) reviews and analyzes the performance of a number of Arab countries with regard to growth and investment. It includes comparisons of social and institutional factors affecting the business environment and the investment climate, together with discussion of their influence on overall performance.

- **Africa Foreign Investor Survey 2003** (UNIDO, Vienna 2003) summarizes the results of a survey of investor experience in a selection of African countries. It provides information on the perceptions and service needs of investors, the importance of different factors in the location process (including for different sectors), and the experience of investors in their dealings with the investment promotion agencies in the different countries.

- **Global Barometer** (http://www.globalbarometer.org) provides information on the results of surveys of the business climate in a number of country groups, including developing countries.

- **GEM 2003 Global Report** (Babson College/London Business School [coordination team host institutions] and Ewing Marion Kauffman Foundation [global sponsor], February 2, 2004). The Global Entrepreneurship Monitor project brings together national teams of researchers and experts from 41 countries, both industrial and developing, to analyze and compare levels of entrepreneurship and its causes. The GEM report for 2003 gives considerable information and comparative analysis on entrepreneurship. The international report is based on national country reports, some of which are available at http://www.gemconsortium.org/category_list.asp

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