



**Report on parafiscal charges
in Montenegro**

THE ANALYSIS OF PARAFISCAL BURDENS AT LOCAL LEVEL

**Municipalities Danilovgrad, Bijelo Polje
and Budva - Summary -**

Note

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- Municipalities Danilovgrad, Bijelo Polje and Budva -

SUMMARY

Podgorica, November 2018

Title:

Report on parafiscal charges in Montenegro: **THE ANALYSIS OF PARAFISCAL BURDENS AT LOCAL LEVEL** - Municipalities Danilovgrad, Bijelo Polje and Budva

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Executive Summary

It is common knowledge that productivity determines the limits of development of the standard of living of any country, and modern globalized economy emphasizes the importance of productivity to the utmost limits. National economy productivity is a resultant of many factors, with lower or higher power of impact, with attractiveness of business environment and stimulativeness of business environment for business operations excelling in the power of impact.

Business environment is significantly determined by the conditions present on the macro level reflected in political and legislative environment and on the micro level related to conditions present in terms of this on the local level – level of competence of local self-government.

Economic prosperity is ultimately based on micro level, which is indicative of the fact that in addition to an exceptionally important element in the form of quality of national business environment (macro level) crucial conditions which impact productivity and business operations of an enterprise and thus competitive capability of a country and its overall economy are constituted on the local level.

Business operations of an enterprise imply the necessity to comply with large number of regulations. In addition to the fact that enterprises have to improve their business operations in order to survive on the market and accomplish their business objectives, enterprises have to fulfill diverse regulatory requirements which significantly complicates accomplishing of their objectives and makes business operations more difficult and more expensive. For this reason, the issue of regulation quality becomes crucial and thus the need to analyze the costs of regulation imposed to business sector, that is to small and medium enterprises, is necessary and reasonable.

In that regards the conducted survey focused on three local self-governments (Bijelo Polje, Budva, Danilovgrad) which monitors the state of fiscality/parafiscality through several forms (taxes, fees, membership fees) aimed at providing arguments on the need to change existing view of regulation by political and administrative decision makers. In line with this, presenting the manner and scope of regulation by the state and local self-government authorities – presented in form of adopted regulations, frequency of regulations amending, as well as, by means of identifying their amounts – was primordial manner to prove and indicate the necessity for this change.

Doubtlessly, regulation affects business sector causing primary and secondary effects. Primary effects are reflected in form of costs caused by compliance with legal provisions (administrative costs) while the secondary effects are consequence of primary effects impact on competitiveness capability – as a result of impact of harmonization costs on enterprise competitiveness (higher costs lower effectiveness...).

Societies with unfavorable and burdening regulatory environment, to a greater or lesser degree, instigate small and medium enterprises to business operations in grey zone under the pressure of enterprise survival. On the other hand, stimulative regulatory environment does not emit incentives for such a thing, and in the given context excessive regulations can be viewed, among other, as a strong generator of grey economy.

Significant, permanent and sustainable effects of regulation can be achieved by means of **establishing regulatory policy as efficient means of managing regulatory process**, instead of ad hoc regulatory intervening, one off intervention as well as, unpredictable, frequent and autonomous acting without coordination with the central government.

In respect to this decision makers in Montenegro need to create efficient regulatory framework whose costs shall not be an impediment to businesses and their competitive capability, because economic growth on local and national level depends on this.

Universally applicable tool for improving regulation is **Regulatory Impact Assessment - RIA**, that is Regulation Effect Analysis, which considers and measures the benefits, costs and effects of new or amended regulations. RIA is considered to be a key instrument for improvement of regulatory management process and for improvement of its transparency, and it is necessary to insist on RIA greater and stronger application.

The process of creating stimulative business environment is reflected, primarily, in improving its two structural elements: **regulatory** – legislative framework encouraging business, **administrative** – viewed in simplifying and greater cost-effectiveness of mandatory business procedures.

Aiming at encouraging competitiveness of Montenegrin companies (which is not on the necessary level) regulatory environment and regulatory framework need to be simple, transparent, efficient, effective and cost-effective – created in line with the principle “think small first” – in particular because small and medium enterprises endure disproportionate regulatory burden.

Conclusion

Overall business sector and in particular its most numerous share – small and medium enterprises have a strong need for regulatory environment which is simple and transparent.

Regulations are necessary, since many social objectives could not be accomplished without them. However, when excessively used and in continuous reaching for regulating regulations become sole purpose in itself. Regulations always have to be in correlation with the desired accomplishment, and regulations objective should not be opposed to social objectives. Regulations need to be targeted and effective and should not exceed their specific purpose.

Regulations, besides the fact that they serve objective accomplishment, also have side effects in the form of regulatory burden (regulatory costs), with potentially serious consequences for enterprise sector and social efficiency. This is the reason why the burden of public regulations, in particular for small and medium enterprises, needs to be continuously reduced and this must be the objective of policymakers and decision makers on the national and local level, especially because microeconomic conditions for business operations – conditions on the local level are crucially important for the success of an enterprise.

Significant regulation effects cannot be accomplished by means of ad hoc regulatory interventions, one off and individual interventions, frequent and unpredictable actions, autonomous actions and actions not harmonized with the centre and the like, but by means of establishing regulatory policy as efficient means for managing regulation process. Thus, the regulatory environment needs to be simple and transparent, which means efficient, effective and attached with low costs and created in line with the principle “think small first” – because small and medium enterprises endure disproportionate regulatory burden.

Key characteristics of regulatory environment in Montenegro on the local level are, largely, opposite to the above mentioned: excessive regulations (extremely large number of regulations), large number of parafiscalities, stochasticity in regulation adoption (frequent, unpredictable and autonomously made decisions on the amendment of regulatory elements – parafiscality/fiscality), high levels of parafiscality.

All this together results in form of expensive and complicated, complex and burdening regulatory environment making business operations exceptionally difficult to enterprises and raising their regulatory costs, and the final effect is reflected in undermining their competitive capability.

Taxes are one of two typical parafiscal/fiscal instruments.

The level of taxes should be determined based on costs or value of provided service and not based on other criteria, since this creates opportunity (which is the case in our country) for the level of taxes to significantly exceed the value of provided service for which it is paid. The following should impact the amount of taxes: costs of provided service, benefit from the service, presence of general interest in intensive use of a service, presence of general interest in limiting an action.

Additionally, it is difficult to understand and contradicts the system of taxes, that taxes are paid for something the service is not provided for (possession of specific equipment) and these types of taxes do exist.

In addition to this, regulations related to local municipal and administrative and other taxes in the competence of diverse state authorities and local self-governments need to be aligned in order to improve regulatory framework in respect to this and to resolve the issue of the same taxes for the same affairs and different taxes for the same affairs in uniform manner.

Fees are relatively new form of parafiscality/fiscality whose primary objective should be accomplishing non-fiscal (economic, transportation, infrastructural, urban, environmental...) and not fiscal objectives, which most commonly is not the case with local self-governments in Montenegro. It is clear that fees are in direct conjunction with investments which means that local self-governments highly depend on them, but they are also a factor for stimulating or discouraging investment activities of enterprises. For this reason, their level can be and is of capital value for local self-government itself – in the short term by means of collecting fees, and in the long term through overall social and economic development of local self-government.

Despite their exceptional importance, fee costs are high and they are not in accordance with the value of the service provided by local self-governments. This is exceptionally destimulating and it affects the level of business climate quality on the local level significantly. In that regard, revising of the overall fee policy as the key element of sound management of the regulation process certainly should be conducted.

RECOMMENDATIONS

Taking into account what has been said, we hereby provide the recommendations on how to improve regulatory framework i.e. regulatory environment in local self-governments in Montenegro.

General recommendations

- To integrate the principle of “think small first” – first think about a small (business), systemically into all new business related policies.
- To estimate the impact of new rules to the enterprises and systemically include the option of searching for particular manners for the SME sector.
- To include business sector in decision-making processes related to enterprises and regulation process.
- To ensure transparency in the adoption of regulations.
- To align the system of quasi-taxation in local self-governments.
- The improvement and simplification of regulatory environment should be a permanent task and a key goal of regulatory policy.
- Small and medium-sized enterprises, whenever possible, should be exempted from the existing obligations, while partial or temporary exemption should be strived for, if the full exemption is in contrast with the purpose of the regulations.
- To simplify regulatory obligations for enterprises.
- To introduce common start dates for all new laws, regulations and orders related to enterprises.
- To ensure enough time to small and medium-sized enterprises to adapt to a new regulation.
- To ensure information to enterprises adequately so as to be clear and not causing dilemmas for enterprises.
- To make single locations in local communities where all typical administrative tasks/regulatory obligations may be carried out at one place.
- To provide enterprises with the possibility of interaction with the ministries and take care of them in an organized and systemic manner.
- To revise the amount of fees and consider their reduction.

Specific recommendations

1. The amount of tariffs has to be at least closely aligned with the value of provided service.
 - Administrative tariffs – the amounts of administrative tariffs are disproportional to the services provided and they are different for the same tasks regarding the tariffs for national and local level.
 - Import tariffs are very high (e.g. the Ruling of Veterinary Administration amounts to 100 EUR per supplier and type of good, with 90-day expiration date).
 - Local municipal tariffs are in many cases different per local self-government units, so their alignment is necessary.
2. To abolish quasi-fiscal/fiscal burdens for which no service is provided
 - Municipal tariff for saw mills, reciprocating saws and structural material cutting saw
 - Local municipal tariffs charged for the placement of advertisements, headings, etc. placed by the owners on their business buildings.
3. To eliminate multiple payments of the same levies
 - Enterprises which at one place have several buildings (business building, storeroom, shop and the like) for each building separately pay the fee for the usage of commercial buildings ensuring the access to the same municipal road;
 - the access to municipal road is also paid by the owner of a business space, and, again, the same business space and the same access road are paid by a renting enterprise.

4. The methodology of calculation of membership contribution paid by commercial entities is inadequate and it has the power of a tax, so it should be changed.
5. The introduction of quasi-taxation should be done only by law, not by state administration authorities' bylaws, enactments of local self-governments and other entities performing public powers, since, thus, the issue of their legal validity is opened.
6. The overlapping of fees should be eliminated, which means that the regulations should be harmonized.
7. Each self-government should make the list of quasi-taxations on their territory, which would be an introduction for the creation of the list on the national level.

