Improving the Legal Environment for Business and Investment in Central Asia

PROGRESS REPORT

With the financial support of

OECD

Improving the Legal Environment for Business and Investment in Central Asia

PROGRESS REPORT

OECD
BETTER POLICIES FOR BETTER LIVES

Please cite this publication as:
OECD (2023), *Improving the Legal Environment for Business and Investment in Central Asia: Progress Report*, OECD Publishing, Paris, https://doi.org/10.1787/33a28683-en.

ISBN 978-92-64-51239-9 (print)
ISBN 978-92-64-78853-4 (pdf)
ISBN 978-92-64-72597-3 (HTML)
ISBN 978-92-64-89775-5 (epub)

Photo credits: Cover © Happy_stocker.

Corrigenda to OECD publications may be found on line at: www.oecd.org/about/publishing/corrigenda.htm.

Foreword

In early 2021, the OECD published a report assessing the legal environment for business in Central Asia with targeted recommendations for each of the countries of the region based on a set of reform priorities identified in work with Central Asia governments in 2019-2020. This work has been conducted against the backdrop of multiple shocks with widespread effects on the economies and societies of the region, including the COVID-19 pandemic and Russia's full-scale invasion of Ukraine, reinforcing the need to engage in structural reforms to increase resilience.

Improving the Legal Environment for Business and Investment in Central Asia - Progress Report is a continuation of the work carried out by the Eurasia Division of the OECD's Global Relations and Cooperation Directorate since 2020. The European Union provided financial support for this work through the OECD policy component of its Central Asia Invest programme.

The purpose of the report is to assess progress made by the governments of Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, and Uzbekistan in implementing the recommendations made in 2020. Despite recent reforms across the region, particularly in streamlining legislation and digitalising government services – the business environment in Central Asia remains challenging, largely due to gaps between *de jure* frameworks and *de facto* implementation and an uneven playing field between private firms and State-Owned Enterprises.

The analysis considered the effect of the COVID-19 pandemic and the disruption caused by Russia's war in Ukraine on the ability of the governments to implement the initial recommendations. In particular, the OECD assessment integrates three main dimensions: (i) a measure of implementation progress based on the reforms agreed upon with the government in 2020; (ii) an assessment of the drivers for implementation gaps; and (iii) an assessment of new challenges and priority areas for policy action.

The report comprises an overview section followed by five country-specific chapters. Each chapter presents a detailed analysis of the progress made in each priority area, indicating remaining room for improvements, and providing indicative policy recommendations to further improve the legal environment for business and investment in Central Asia.

Acknowledgements

This report complements and extends the work carried out by the OECD Eurasia Competitiveness Programme (ECP) on assessing the legal environment for business and investment in Central Asia in 2019-2020. The work was realised within the framework of the OECD Central Asia Initiative funded by the European Union (EU).

This report was prepared by the Eurasia Division of the OECD Global Relations and Co-operation Directorate (GRC), under the guidance of Mr William Tompson, Head of the OECD Eurasia Division, and Mr Grégory Lecomte, Head of the Central Asia Unit, and co-ordinated by Ms Céleste Laporte-Talamon, Policy Analyst, OECD Eurasia Division.

The author of this report is Ms Céleste Laporte-Talamon, Policy Analyst, OECD Eurasia Division, with significant contributions from Ms Amélie Schurich-Rey, Policy Analyst and Ms Ryskul Iskakova, Policy Analyst (Staff on Loan) in the same Division. Valuable analytical support was provided by Ms Shamima Oshurbekova, Mr Hugo Brisebard and Mr Daniel Poloyko, Junior Policy Analysts in the OECD Eurasia Division. Ms Anna Chahtahtinsky and Ms Elisa Larrakoetxea, Programme Administrators in the OECD Eurasia Division, provided unfailing administrative and logistical support.

The project would not have been possible without the continuous support of, and dialogue with, representatives of ministries and state agencies, the private sector, business associations, international organisations, non-governmental organisations, and other stakeholders across the countries covered.

In Kazakhstan, the OECD is particularly grateful for the support of the Minister of National Economy, Mr Alibek Kuantyrov; Vice-Minister of National Economy Mr Abzal Abdikarimov; Vice-Minister of Trade and Integration Mr Kairat Torebayev; the Director of the Department of Entrepreneurship Development Policy of the Ministry of National Economy Mr Erik Jambulov, the teams of the Ministry of Justice, the Ministry of Digital Development, Innovations and Aerospace Industry, the State Revenue Committee, Kazakh Invest, the National Chamber of Entrepreneurs of the Republic of Kazakhstan “Atameken”, Astana International Financial Centre (AIFC), the Economic Research Institute, QazIndustry and QazTrade.

In Kyrgyzstan, the OECD is grateful for the support of Deputy Minister of Economy and Commerce of Kyrgyzstan Ms Ainura Usenbekova, the State Tax Service, the Ministry of Justice, the International Business Council and Mr Nurlan Musuraliev, Acting Business Ombudsman at the Business Ombudsman Institute of the Kyrgyz Republic.

In Tajikistan, the OECD is grateful for the leadership of the State Committee for Investment and State Property Management of Tajikistan, the Ministry of Economic Development and Trade, and Mr Maruf Solekhzoda, First Deputy Chairman of the Tax Committee under the Government of Tajikistan.

In Turkmenistan, the work was made possible thanks to contributions from the Ministry of Finance and Economy.

In Uzbekistan, we are grateful to a wide range of partners, notably Mr Shukhrat Vafaev and Mr Rustamkhon Azizov, respectively Director General and Deputy Director General of the Agency for Strategic Reforms under the President of the Republic of Uzbekistan, as well as Mr Ibrahim Karamatov, Lead Consultant in the same Agency, Mr Aleksey Sim, Head of Investment Climate and Ratings Department at the Ministry of Investments, Industry and Trade, Mr Golib Kholjigitov, Head of the Foreign Investors Council under the President of the Republic of Uzbekistan, Mr Umid Azizov, Head of International Tax Relations at the State Tax Committee, the Ministry of Justice, the Customs Committee, the IT Park and the Digital Economy Centre.

The OECD would also like to thank Ms Gulsara Arystankulova, Ambassador of Kazakhstan to France, and Mr Yerzhan Nessibkulov from the Embassy of Kazakhstan in France; Mr Ruslan Bekbolotov, First Secretary of the Embassy of Kyrgyzstan in France; Mr Manuchehr Jobir, former Counsellor at the Embassy of the Republic of Tajikistan in France; Mr Maksat Chariev, Ambassador of Turkmenistan to France; and Mr Jamshid Saydazimov, First Secretary at the Embassy of Uzbekistan in France. The OECD is grateful for the support of its local consultants - Ms Ikbal Yusupova (Uzbekistan), Ms Svetlana Bairamova (Turkmenistan), Mr Bakyt Omurzakov (Kyrgyzstan), and Ms Veronika Grushevskaya (Tajikistan).

The present iteration of the report was greatly improved by the numerous comments received from colleagues within the OECD. We are particularly grateful for the comments and guidance from our reviewers Ms Mariarosa Lunati, Senior Advisor, Middle East Africa Division in the OECD's Global Relations and Co-operation Directorate, Mr Arnault Prêtet, Project Manager from the Governance Reviews and Partnerships Division in the OECD's Public Governance Directorate, and Mr Fernando Mistura, Policy Analyst in the Investment Division of the OECD's Directorate for Financial and Enterprise Affairs.

Finally, this work would not have been possible without continued financial and diplomatic support of the European Union. The OECD is grateful for the EU for their valuable support during working group events of the report in all Central Asian countries. In particular, the OECD would like to thank Mr Kestutis Jankauskas, Ambassador of the EU to Kazakhstan, Ms Marilyn Josefson, Ambassador of the EU to Kyrgyzstan, Mr Raimundas Karoblis, Ambassador of the EU to Tajikistan, Mr Diego Ruiz Alonso, Ambassador of the EU to Turkmenistan, and Ms Charlotte Adriaen, Ambassador of the European Union to Uzbekistan.

Table of contents

FIGURES

TABLES

BOXES

Executive summary

Central Asia has proven relatively resilient to recent shocks

Recent economic shocks, including the COVID-19 pandemic and Russia's large-scale aggression against Ukraine, and their effects, such as closed Chinese borders and the disruptions of global value chains, have affected the economies of Central Asia in a milder way than expected. Despite the region's large economic dependence on its two large neighbours, the five Central Asian states have so far shown great resilience to the economic headwinds: remittances registered record-high figures in 2022, national currencies quickly rebounded to pre-war levels after an initial drop, trade significantly increased and an influx of skilled workers from Russia boosted demand for services and hospitality. However, as the medium-term effects of the sanctions against Russia, the global cost-of-living crisis, and China's economic slowdown have started to unfold, Central Asia faces lingering uncertainty. The aftermath of these developments could also further impede income convergence with OECD and EU economies, which had already started to slow in the aftermath of the global financial crisis. Meeting these challenges requires addressing remaining gaps in the business and investment climate, foregrounding the need for long-term reforms to encourage investment and private sector development.

This report assesses progress made in improving the legal environment for business and investment

This report presents an updated analysis of the work carried out by the OECD in 2019-2020 along several crucial dimensions of the legal environment for a healthy business climate: the legal and regulatory framework for investment; tax regulations; land legislation; registration procedures; contract enforcement and dispute settlement; the operational environment for firms; trade facilitation, expropriation regimes; exit mechanisms; and public-private dialogue. Each priority area identified in each country in the initial report was updated following the monitoring.

Unleashing the potential of private sector development in Central Asia requires the stability and transparency of the legal environment for business as well as improved regulations. The implementation of predictable rules, the creation of a level-playing field between private firms and state-owned enterprises (SOEs) and a competitive environment are cornerstones to encourage companies to invest and grow in the region.

Implementation gaps and interpretation issues remain problematic

Many of the essential components of the business environment mentioned above are already in place at different levels in the region, but legislative gaps, inconsistencies and implementation challenges remain. The report finds that, while great strides have been made in areas such as digitalising government services and streamlining business procedures, governments' efforts to undertake structural reforms have remained uneven and have been further impeded by the impact of external shocks requiring short-term responses. Issues most frequently mentioned by the private sector relate to the uneven implementation of *de jure* provisions, as well as disagreements related to the interpretation of the law, as is often seen, for instance, in tax policy. In addition, the need for the governments to ease the strain on public finances following afore-mentioned shocks has sometimes prevailed over the desire to ease the fiscal burden on firms.

Addressing the gaps highlighted in the report can help the region adapt to unprecedented environmental, social, and economic challenges

Filling the gaps in the legal environment for business will help increase the region's resilience to future shocks. The risks associated with climate change have significantly increased in Central Asia, whilst inflationary pressures have downside effects on purchasing power and social stability. Implementing structural reforms to make the business environment more conducive to entrepreneurship and private sector development could help achieve the overarching goals of energy security, climate resilience and social inclusion and, more generally, unleash sustainable and inclusive growth over the long term. The governments of the region have committed themselves to a wide range of needed structural reforms. Delivering on these commitments will prove daunting but can lay the foundations for more resilient and inclusive economies and societies.

1 Setting the scene

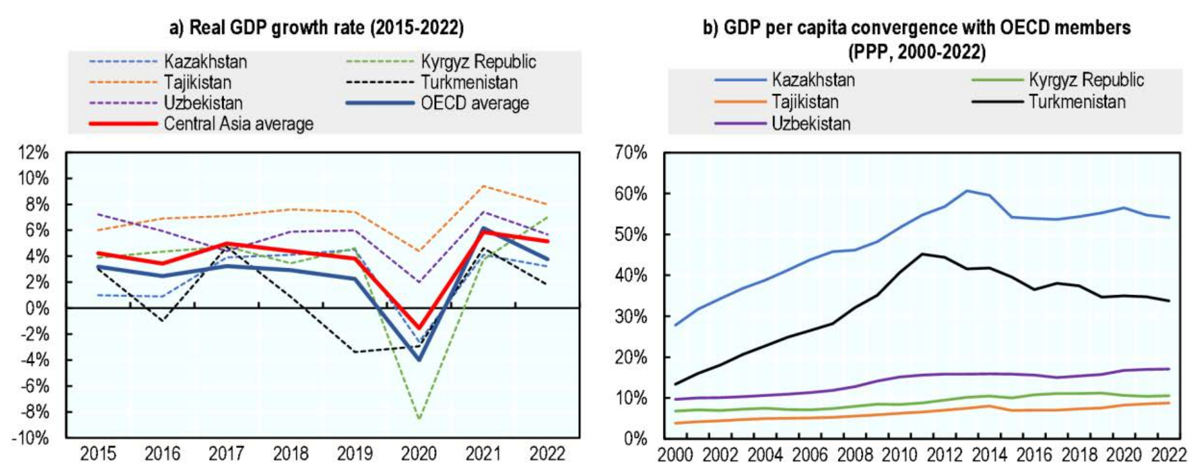
In the recovery path from the COVID-19 pandemic, Central Asia has shown unexpected resilience to the new economic headwinds brought by Russia's invasion of Ukraine. While governments moved rapidly to respond to the shocks of pandemic and war and improved elements of the business environment, structural reforms in the region are advancing more slowly. More effective implementation, heightened public-private dialogue and increased transparency in policymaking could lay the foundations for a more robust and healthy business environment.

The region has not been spared the consecutive economic shocks resulting from the COVID-19 pandemic and the effects of Russia's war in Ukraine

The economic effects of the pandemic exacerbated fundamental structural weaknesses across the countries of Central Asia

The COVID-19 pandemic was arguably the biggest economic shock hitting post-independence Central Asia. Beyond its human toll, the pandemic created both demand and supply shocks. Domestic and external demand fell, production and trade flows were disrupted, and financial conditions tightened (IMF, 2020[1]). Oil exporters like Kazakhstan and Turkmenistan faced the additional shock of plummeting oil prices due to decreased global demand. Economic policy responses consisted of temporary fiscal measures to support vulnerable households and small businesses. Liquidity support, concessional lending to banks and loan repayment deferrals served to support the private sector. However, limited fiscal space and weak transmission mechanisms for monetary policy highlighted the cost of insufficient structural reform efforts across the region, against the backdrop of declining effectiveness of traditional drivers of growth – the export of surplus labour and extractive goods – before the pandemic (OECD, 2021[2]).

Figure 1.1. Economic growth in Central Asia



Note: Panel b) shows countries' GDP per capita (in purchasing power parity) as a share of OECD members' average GDP per capita (PPP).
Source: (IMF, 2023[3])

The economies of Central Asia still managed to recover rather rapidly following the phase-out of lockdowns. Cyclical factors, namely the normalisation of domestic activities, higher commodity prices and recovering remittances, allowed the region to expand again (EBRD, 2021[4]). However, strained public finances and higher debt levels resulting from large stimulus packages and reduced tax collection left the region vulnerable to potential economic shocks. Russia's war in Ukraine, in particular, was expected to have profound negative spill over effects given the region's trade, investment, energy and labour dependence on Russia.

This resilience has not, however, reversed the slowdown in trend rates of growth and convergence with higher income countries, particularly OECD member countries. Having progressed rapidly since 2000, the convergence progress began to decelerate in 2013 (Figure 1.1)**.** Apart from Kazakhstan, all countries of the region remain below the 50% of the OECD average GDP per capita at purchasing-power parity terms (PPP). Resuming income convergence requires policies to facilitate a shift in growth models for the region, by increasing productivity in sectors generating the most employment and expanding the size of the formal sector, where wages and productivity have been growing.

The region has withstood the effects of Russia's war in Ukraine so far, but long-term risks to growth remain

Russia's full-scall invasion of Ukraine in February 2022 did not derail the region's post-COVID recovery. On the contrary, across most of the region, growth was supported by an important boost to consumption driven by government spending, more demand for services, high remittance inflows, and real public sector wage increases (OECD, 2022[5]). The region also experienced a 20% increase in trade with Russia in 2022 (Foreign Affairs, 2023[6]), as it filled the void created by Western firms' withdrawal from the Russian market. It also increased exports to the rest of the world, as Central Asia played a new role of a transit platform between their northern neighbour and Europe and started to diversify trade links. Inflation has gradually slowed down thanks to a decrease in international food and energy prices, restrictive monetary policy, and fiscal reforms (IMF, 2023[7])

However, GDP growth is expected to decelerate to 4.6% in 2023 and 4.2% in 2024 in the Caucasus and Central Asia region, reflecting an attenuation of the initial positive spill overs from the war in Ukraine (IMF, 2023[7]). Remittance inflows are already showing a normalisation of their trend. For instance, remittances in Uzbekistan recorded a 21.2% year-on-year decrease in the first half of 2023 to reach 5.2 billion USD (Central Bank of Uzbekistan, 2023[8]), reflecting a return to the usual level of financial inflows. Agriculture and gold production are expected to soften in Kyrgyzstan, Tajikistan and Uzbekistan (IMF, 2023[7]). Yet, a high degree of uncertainty still weighs on this forecast. On the one hand, a sharper-than-expected contraction of the Russian economy, sustained inflation and climate-related disasters could negatively affect growth. On the other hand, good harvests, trade, and investment diversion, as well as a continued influx of highly skilled migrants and foreign exchange could further boost demand and increase productivity growth in the region (IMF, 2023[9]).

The longer-term outlook is uncertain. China's economic slowdown may hit the region's exports and investment inflows, but deflation could mean a drop in the cost of goods imported into Central Asia and could contribute to decelerating inflation. Looking at the European Union, the impact of clouded economic perspectives could be mitigated by the EU's need to diversify its energy supplies and its increased trade with Central Asia. Central Asia energy and raw material supplies to the EU have already been on the rise since the beginning of Russia's full-scale invasion of Ukraine. Climate change is another concern which requires concerted, regional-level effort to palliate more frequent droughts, extreme weather and energy supply disruptions.

Whilst the economies of the region are expected to continue growing, the current fragmented and volatile context requires governments to accelerate structural reforms in order to support growth and increase resilience. In that regard, achieving the goals of inclusive and resilient economies will require full engagement from the private sector, alongside other structural policies to improve trade facilitation, ramp up diversification, and increase resilience to climate change. Within this context, the OECD has been providing policy advice and support to the region to help the latter advance reforms supporting the development of the private sector, and ultimately of local economies.

The OECD first assessed the legal environment for business and investment in Central Asia in 2020

In 2020, the OECD offered targeted advice to Central Asian governments on improving the legal environment for business

The OECD report on *Improving the Legal Environment for Business and Investment in Central Asia* provided targeted advice and identified priority reforms for the governments of Central Asia to improve the legal environment for business, tailored to the particularities of each economy. The analysis allowed the OECD to both ascertain the key legal and regulatory barriers to private sector development and investment in Central Asia and to disseminate a number of OECD instruments for the first time in the countries of the region.

Box 1.1. Description of the OECD's methodology and assessment of the legal environment for business in Central Asia (2019-2020)

Defining the legal environment for business

Given its multidimensional nature, establishing a common understanding of the legal environment for business is a contentious endeavour. For the Improving the Legal Environment for Business in Central Asia project, the "legal environment" encompasses policy, administrative, regulatory, and other legal areas that govern and affect businesses, investment and operations. Leveraging OECD instruments, such as the Policy Framework for Investment, the SME Policy Index, the Trade Facilitation Indicators, and the OECD FDI Regulatory Restrictiveness Index, the project examined ten dimensions for analysis: the legal and regulatory frameworks for investment; tax regulations; land legislation; registration procedures; contract enforcement and dispute settlement; the operational environment for business; trade facilitation; expropriation regimes; exit mechanisms; and public-private dialogue.

OECD methodology

The 2020 report was built on two complementary components:

- Two questionnaires focused on the ten dimensions noted above were circulated to the governments of participating countries and representatives of the private sector, respectively. The input was collected and analysed by staff at the OECD.
- The OECD organised a series of private- and public-sector consultations. In particular, the project organised a workshop in each of the project countries, as well as roundtable meetings with local and international entrepreneurs in each of the countries and at business associations in Paris, and held bilateral meetings with individual policymakers, entrepreneurs, and investors from or active in the region.

Policy support

On the basis of the data collection and analysis conducted, as well as on consultations with governments and with the private sector, the OECD identified three key reform priorities for each country. These priorities took into account the *de jure* legal environment for business and the *de facto* operational reality for firms, domestic and international. The OECD has been careful to reflect ongoing reform processes in each country, as well as the activities of donors and other international organisations active in the region.

In 2020 and 2021, the OECD worked with the Central Asia governments on the identified reform priorities, continuing the OECD's deepening co-operation with a dynamic region through a series of capacity-building exercises with each country focusing on the priorities identified. In addition, a regional two-day event focussing on contract enforcement was organised in 2020, gathering policymakers from the region, academics and international experts for experience sharing.

Source: (OECD, 2020[10]).

The original report identified significant gaps between* de jure *protections and the* de facto *operational environment for firms

Table 1.1. Top challenges identified in the legal environment for business and investment in Central Asia in 2020

Kazakhstan	Kyrgyzstan	Tajikistan	Turkmenistan	Uzbekistan
Operational environment for firms Implement consistently and thoroughly the new code for entrepreneurs	**Operational environment for firms** Streamline the legal environment for entrepreneurs and small businesses, especially legislation and service delivery	**Legal and regulatory framework for investment** Ensure the implementation of existing laws for investment and entrepreneurial activity, and improve the accessibility of necessary information	**Legal and regulatory framework for investment** Enforce, streamline, and publish all legislation on investment on the Ministry of Justice's legal database to ensure transparency	**Legal and regulatory framework for investment** Ensure proper implementation of the new investment law and remove sectoral restrictions
Legal and regulatory framework for investment Improve dispute settlement for all businesses operating in the country	**Contract enforcement** Ensure transparent fair and efficient contract enforcement for businesses	**Contract enforcement** Improve the enforcement of contracts and arbitral decisions in domestic courts	**Operational environment for firms** Develop a simplified targeted legal framework and support for SMEs and small entrepreneurs	**Operational environment for firms** Streamline and consolidate business-related legislation and licenses for domestic firms and entrepreneurs
Trade facilitation Enhance trade facilitation and improve cooperation between agencies involved in export procedures	**Taxation** Simplify the tax code and tax administration for companies of all sizes	**Taxation** Make tax administration simpler, more consistent and more transparent	**Business registration** Streamline business registration and licensing, and introduce a one-stop-shop	**Taxation** Ensure changes to tax requirements are predictable, and improve tax administration for small firms

Source: (OECD, 2020[10]).

The OECD assessed progress made and new challenges arising in the legal environment for business in Central Asia since 2020

The report finds improvements in the operational environment for business driven by digitalisation, a streamlining of procedures, and adaptation to economic shocks

Efforts to streamline the operational environment have eased the administrative burden on firms

Most countries of the region have made significant progress in digitalising and simplifying the provision of government services. In particular, countries implemented measures to streamline the number of licenses and permits required to operate a business, a welcome step mentioned by interviewees during the fact-finding process (Box 1.2). These efforts have also translated into intensified regional integration, as several countries implemented digital trade and customs procedures. For instance, Kazakhstan introduced an electronic queue system, allowing trucks to register at the desired date and time of the border crossings with China, Turkmenistan, and Uzbekistan (Zakon.kz, 2023[11]). OECD interviewees reported easier border crossing between Kyrgyzstan and Uzbekistan. Intra-regional trade increased by 73.4% between 2018 and 2022, from 5.8 billion USD to 10 billion USD (The Astana Times, 2023[12]).

Governments swiftly reacted in the face of a challenging global economic context

In the face of the COVID-19 context, governments managed to rapidly adapt in a volatile context. Restrictive monetary policies and higher reserve requirements contained inflation and excess liquidity (IMF, 2023[9]). Fiscal policy, benefitting from increased remittances (through increased consumption), focussed on measures to support businesses affected by supply chain disruptions, increased costs, and lockdown, and measures to secure food and energy supplies, ensure price stability and increased agriculture output. The vacuum created by the withdrawal of Western firms from the Russian market created new export opportunities for Central Asian firms (EBRD, 2023[13]). Efforts to diversify trade routes through the Middle and Southern Corridors have helped mitigate to some extent disruptions along the Northern Corridor going through Russia (OECD, 2022[5]).

However, deeper reforms are taking time to materialise

Recent economic disruptions have hindered governments' efforts to advance more profound reforms. The prevalence of the state in the economy and the lack of competitive neutrality remain roadblocks to the creation of a level playing field between state-owned enterprises (SOEs) and the private sector. The investment framework is still challenging, due to perceived risks of indirect expropriation and opaque privatisation and public procurement processes. Strains on public finances have led to undue pressures on businesses to pay taxes early or to wait for long periods to receive VAT returns.

Weak implementation remains a key challenge for firms across the region

An issue already identified in the initial OECD report relates to the implementation of legal provisions. Whilst the formal statutory conditions for businesses may somewhat guarantee the freedom to do business, the *de facto* operational environment remains complicated, changeable, and often opaque. This is demonstrated in the unpredictability of tax systems, and divergences in statutory interpretation. With regards to investment, whilst the framework is quite open, as shown by the region's performance in the OECD's FDI Regulatory Restrictiveness Index, its application remains problematic for foreign investors, which continue to struggle with the challenges of transparency in public procurement, information availability, corruption and the prevalence of the state in the economy through SOEs.

Whilst public-private dialogue has been improving across the region, regulations are subject to frequent changes and the private sector is often given little notice to implement changes. Frequent changes, such as in tax policy, with little time for firms to adapt, result in implementation challenges, risks of noncompliance and fines. The rapidity of changes also poses difficulties for ministries and government agencies to integrate updates into processes and harmonise interpretation. An issue frequently raised by firms relates to the lack of agreement within the public administration on the interpretation of primary and secondary legislation. Firms have often found themselves faced with conflicting instructions from different government agencies and civil servants.

The lack of transparency around decision-making and incentive allocation also creates a roadblock to firms' voluntary compliance with the law. Governments have started to rely on regulatory impact assessment (RIA) to assess the positive and negative effects of proposed and existing regulations and make policymaking evidence based. However, firms have reported that the results of such RIAs are not always integrated into policy and that RIAs are sometimes carried out with predetermined policy objectives, which influence the outcome of the RIAs. This reduces the effectiveness of the exercise and does not encourage compliance, as firms are not convinced of the expected positive effects of conducting RIAs on the operational environment. In addition, the reported existence of sometimes unpublished or unavailable decrees granting favourable conditions to SOEs, such as tax breaks and preferential lending conditions, distorts competition and further discourages compliance with legal provisions.

The 2023 assessment of progress made since 2020 has allowed to update and fine-tune the recommendations for each country of the region

Box 1.2. Description of the OECD methodology for the 2023 monitoring of the legal environment for business and investment in Central Asia

OECD methodology

The monitoring exercise relied on several tools:

- a matrix table of the 2019-2020 recommendations with preliminary desk research to tentatively identify areas of progress in each country of the region;
- a series of written questionnaires circulated to the five governments of Central Asia;
- a series of fact-finding online interviews with private sector and international organisation representatives in the region;
- open access quantitative data;
- in-person working group meetings in each country of the region to discuss the preliminary findings and give the opportunity for government and private stakeholders to complement and/or comment on the analysis.

Note: For further details on the methodology, please refer to Annex A of the report

The table below summarises progress made along the priority reform areas identified in the 2020 report for each of the five countries of the region, before delving into each country's individual assessment. It also provides updated recommendations per country. Going forward, the final chapter of the report suggests revised overarching policy recommendations for the region to lay the foundations for the development of a vibrant and inclusive private sector. Overall, the assessment finds that reforms have been initiated to digitalise public services, facilitate trade, reduce the number of redundant procedures and improve fiscal policy, however, gaps remain in the implementation and interpretation of the text. Tax administration has also been mentioned as particularly problematic by private sector interviewees.

Table 1.2. Overview of reform implementation

Kazakhstan	Kyrgyzstan	Tajikistan	Turkmenistan	Uzbekistan
Operational environment for firms Regulation became more transparent and equitable, but implementation lags behind and complexities remain	**Operational environment for firms** The government's digitalisation efforts have begun to bear fruit, but further streamlining of business-related legislation and predictable enforcement are needed	**Legal and regulatory framework for investment** The investment framework has seen some progress, yet restrictions and uncertainties still need addressing	**Legal and regulatory framework for investment** The government has increased communication about changes in the law, but reform efforts seem to have slowed down due to the COVID-19 pandemic	**Legal and regulatory framework for investment** Significant reforms to increase investor protection rights were undertaken but a lack of transparency remains
Contract enforcement Judicial and dispute resolution reforms have been advanced in priority by the government, but contract enforcement and dispute resolution continue to be perceived as a major challenge for businesses	**Contract enforcement** The judicial system is evolving, but further steps to ensure predictable, fair and effective enforcement of treaties would be preferable	**Contract enforcement** The legal framework for businesses has registered some improvements, dispute resolution mechanisms need strengthening	**Operational environment for firms** The post-pandemic period has provided some relief to businesses, but the business environment remains difficult to navigate	**Operational environment for firms** The streamlining of procedures and legislation has made significant progress, yet the pace of reforms creates implementation challenges, and land and property rights remain an issue

Kazakhstan	Kyrgyzstan	Tajikistan	Turkmenistan	Uzbekistan
Trade facilitation The trade regulatory framework improved, especially with digitalisation and for IP rights, but implementation lags and regulatory barriers to services trade remain	**Taxation** New amendments to the Tax Code aimed at creating conditions to level the playing field for businesses, but tax administration and policy remain complex and unpredictable	**Taxation** Fiscal policy developments have reduced the tax burden on firms; however, tax administration remains the most contentious issue mentioned by firms	**Business registration** The government has revised and simplified some procedures for business registration and licensing, but procedures are still paper-based and cumbersome	**Taxation** Fiscal policy developments have reduced the tax and administrative burden on firms; however, tax administration remains the most contentious issue mentioned by firms

Source: OECD analysis (2023).

References

Central Bank of Uzbekistan (2023), *Приток денежных переводов сократился более чем на 20% — ЦБ*, https://www.spot.uz/ru/2023/07/27/remittances/ (accessed on 31 July 2023). [8]

EBRD (2023), *Regional Economic Prospects: Getting By - High Inflation Weighs on Purchasing Power of Households*, https://www.ebrd.com/rep-may-2023.pdf (accessed on 31 July 2023). [13]

EBRD (2021), "Bittersweet recovery", *Regional Economic Prospects*, https://www.ebrd.com/sites/Satellite?c=Content&cid=1395301907147&d=&pagename=EBRD%2FContent%2FDownloadDocument. [4]

Foreign Affairs (2023), *Is Russia Losing its Grip on Central Asia*, https://www.foreignaffairs.com/china/russia-losing-its-grip-central-asia (accessed on 5 October 2023). [6]

IMF (2023), *Regional Economic Outlook for the Middle East and Central Asia - Building Resilience and Fostering Sustainable Growth*, https://www.imf.org/en/Publications/REO/MECA/Issues/2023/10/12/regional-economic-outlook-mcd-october-2023 (accessed on 13 October 2023). [7]

IMF (2023), *Safeguarding Macroeconomic Stability amid Continued Uncertainty in the Middle East and Central Asia*, https://www.imf.org/en/Publications/REO/MECA/Issues/2023/04/13/regional-economic-outlook-mcd-april-2023 (accessed on 31 July 2023). [9]

IMF (2023), *World Economic Outlook Database, April*, https://www.imf.org/en/Publications/WEO/weo-database/2023/April/download-entire-database. [3]

IMF (2022), "Financial Development and Growth in the Caucasus and Central Asia", *IMF Working Paper*, Vol. 22/134, https://www.imf.org/-/media/Files/Publications/WP/2022/English/wpiea2022134-print-pdf.ashx. [15]

IMF (2020), *COVID-19 Pandemic and the Middle East and Central Asia: Region Facing Dual Shock*, https://www.imf.org/en/Blogs/Articles/2020/03/24/blog-covid-19-pandemic-and-the-middle-east-and-central-asia-region-facing-dual-shock (accessed on 31 July 2023). [1]

OECD (2023), *Insights on the Business Climate in Kazakhstan*. [14]

OECD (2022), *Assessing the impact of the war in Ukraine and the international sanctions against Russia on Central Asia*, https://www.oecd.org/migration/weathering-economic-storms-in-central-asia-83348924-en.htm. [5]

OECD (2021), *Beyond Covid-19: Prospects for Economic Recovery in Central Asia*. [2]

OECD (2020), *Improving the Legal Environment for Business and Investment in Central Asia*, OECD Publishing, https://www.oecd.org/eurasia/Improving-LEB-CA-ENG%2020%20April.pdf. [10]

The Astana Times (2023), *Five Trade Trends in Central Asian Connectivity*, https://astanatimes.com/2023/06/five-trade-trends-in-central-asian-connectivity/ (accessed on 5 October 2023). [12]

Zakon.kz (2023), *New rules: how to book an electronic queue for crossing the state border*, https://www.zakon.kz/pravo/6390366-novye-pravila-kak-zabronirovat-elektronnuyu-ochered-dlya-peresecheniya-gosgranitsy.html (accessed on 1 August 2023). [11]

2 Kazakhstan

Kazakhstan has worked to diversify its economy in post-pandemic recovery. Progress has been made in reforming the legal and regulatory framework for investment, digitalising administrative procedures and services for SMEs, and levelling the playing field with SOEs. However, gaps remain in investment in the non-oil sector and productivity growth, while the regional context might durably weigh on Kazakhstan's growth prospects. The COVID-19 pandemic and Russia's war in Ukraine exacerbated long-standing and structural issues holding back private-sector development, in particular persisting state presence in the economy, inconsistent regulatory enforcement and dispute settlement, and lacking trade facilitation measures.

This chapter assesses progress and remaining challenges for Kazakhstan in implementing reforms to improve the operational environment for business, contract enforcement, and trade facilitation, and concludes with six policy recommendations.

Table 2.1. Summary of priority reform implementation and updated recommendations

2020		2023	
Challenges identified	**Recommendations**	**Implementation assessment**	**Way forward**
Operational environment for firms: Implement consistently and thoroughly the new code for entrepreneurs	➢ Raise public sector capacity on licensing and permits, especially at the local level ➢ Review and rationalise licenses and permits (e.g., environmental permits) ➢ Carry out an impact assessment of the Entrepreneurial Code, online one-stop shop and streamlined licensing procedures and use outcomes as a basis for a public-private dialogue on further steps	➢ Regulation became more transparent and equitable ➢ But implementation lags because of capacity issues, and complexities remain	➢ **Stabilise business regulation with a focus on analysing the impact on SMEs** ➢ **Raise firms' awareness and ability to cope with regulatory changes**
Contract enforcement: Improve dispute settlement for all businesses operating in the country	➢ Further modernise and guarantee the independence of the judicial system ➢ Promote alternative dispute resolution mechanisms, continue to expand capacity based on international arbitration best practices, ensure the independence of ADR	➢ Judicial and dispute resolution reforms have been advanced in priority by the government ➢ But contract enforcement and dispute resolution continue to be perceived as a major challenge for businesses	➢ **Keep improving the quality of the court system by monitoring the implementation of judicial reforms** ➢ **Improve domestic businesses' awareness of and access to available dispute resolution tools** ➢ **Set up an effective institutional framework for intellectual property rights enforcement**
Trade facilitation: Improve co-ordination of internal and external customs agencies	➢ Improve horizontal co-ordination across and avoid overlapping between public institutions ➢ Train border officials and develop interconnected transit information systems ➢ Harmonise customs documents and requirements with other countries of the region	➢ The trade regulatory framework improved, especially with digitalisation and for IP rights ➢ But implementation lags and regulatory barriers to services trade remain	➢ **Close the implementation gap and improve access to trade-related information for businesses** ➢ **Rationalise services trade regulation and improve regional co-operation to keep trade flowing**

Note: Orange – reform not initiated; Yellow – reform initiated/ being implemented; Green – reform close to completion/ completed.
Source: (OECD, 2020[1]), OECD analysis (2023).

Introduction

COVID-19 and Russia's full-scale invasion of Ukraine have challenged the government in maintaining reforms to sustain long-term growth

Continued reform efforts in Kazakhstan resulted in robust economic growth

Following the transition recession of the 1990s, Kazakhstan experienced growth from 2000 to 2022 driven largely by FDI inflows into the primary sector. While over this period, real gross domestic product (GDP) grew at an average annual rate of 6% in (IMF, 2023[2]), the trend rate of growth has been declining over time. In particular, trend growth never recovered to previous levels following the two main macroeconomic shocks of the past two decades (the Great Recession in 2008, the drop in global commodity prices in 2014-15) (Figure 2.1).

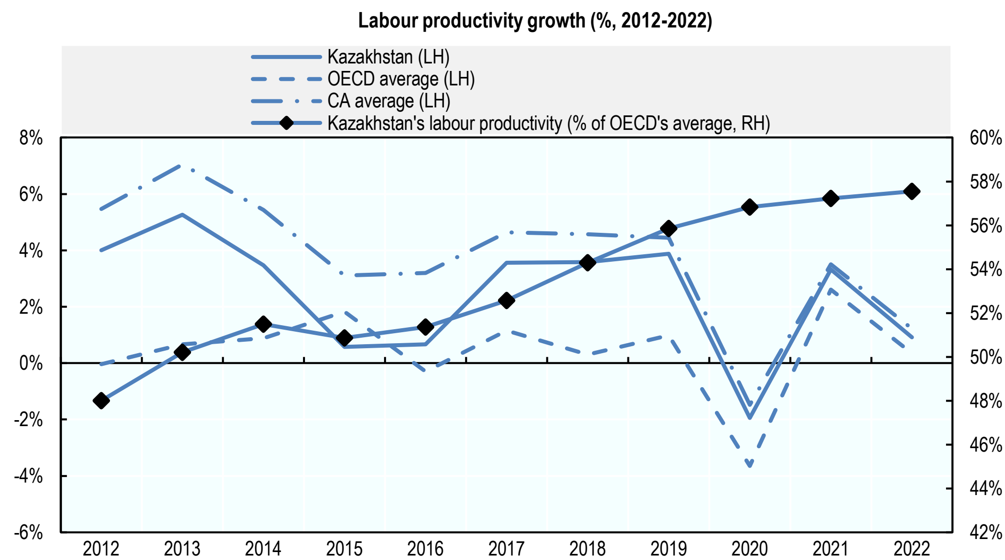
Figure 2.1. Real GDP growth

Source: (IMF, 2023[2])

More needs to be done to strengthen productivity and investment growth in the non-extractive sector, and private-sector development against the backdrop of the global push for decarbonisation (OECD, 2023[3]). The declining trend rate of growth seems to indicate that, despite the government's efforts to diversify the economy, the dominant extractive-driven growth model is no longer sufficient to sustain growth rates observed in previous decades, while convergence has stalled. In the absence of alternative and diversified sources of output, especially in the non-oil private sector, inclusive and sustainable growth will prove ever harder to achieve. In 2022 alone, 43% of new FDI inflows were directed to the mining sector (Ministry of Foreign Affairs of the Republic of Kazakhstan, 2023[4]).The government's commitment to sustained reforms will be critical, in particular in relation to improving the investment climate, raising the competitiveness of non-extractive sectors, limiting the role played by state-owned enterprises (SOEs), and levelling the competitive playing field (OECD, 2017[5]; OECD, 2020[1]).

The declining trend of growth has been largely driven by lower total factor productivity (TFP) and labour productivity (IMF, 2022[6])**.** The slowdown in labour productivity growth in particular has been noticeable in non-extractive sectors, which account for around 80% of employment (OECD, 2023[3]) (World Bank, 2021[7]). Labour productivity in these sectors stands around or below the national average, which only accounts for 28% of the average of the three most productive sectors (mining, real estate and services) (OECD, 2023[3]). A reallocation of the workforce to higher value-added activities outside the extractive sector would serve to enhance labour and TFP productivity but will require the creation of new sectors and opportunities. It is nonetheless worth mentioning that Kazakh labour productivity as a percentage of OECD average has been steadily increasing (Figure 1.2).

Figure 2.2. Labour productivity



Source: (ILO, 2023[8])

The government focused on short-term policies in the context of COVID-19 and Russia's war in Ukraine

At the onset of the COVID-19 pandemic in Central Asia, Kazakhstan enjoyed a sound macroeconomic environment with low unemployment (4.9%) and low debt (21% of GDP). As in other countries of the region, the crisis had a severe impact on Kazakhstan's economy, which recorded a contraction of 2.6% in 2020 before a return to 4% growth in 2021, thanks to continued fiscal expansion, strong consumer credit growth, and the relaxation of COVID-19 restrictions (World Bank, 2022[9]; OECD, 2021[10]).

The main impact of the COVID pandemic on the economy was the combination of a drop in commodity prices and a severe hit to the country's services sector. While the first reduced fiscal space, the latter had a strong effect on employment across the country as the services sector, mainly composed of SMEs, employed about 1.6m workers in retail trade, tourism, and catering alone. However, the government moved rapidly to support the economy. It introduced foreign exchange controls for SOEs to support the tenge, following a hike in the policy rate by the National Bank of Kazakhstan to limit domestic inflation, and an anti-crisis package to cushion the economic impact of the pandemic on the national economy by extending the social safety net to wage and unemployment subsidies provision, and dedicated support measures for businesses (Box 2.1) (National Bank of Kazakhstan, 2020[11]). The pandemic therefore highlighted the vulnerabilities in Kazakhstan's economy caused by its reliance on external demand for a narrow range of commodities. At the same time, the response to the crisis consumed significant resources that might otherwise have been directed towards addressing these vulnerabilities through reforms. There is therefore a need to ensure that policy is recentred on making those reforms to support private sector development over the long-term.

Box 2.1. Kazakhstan's support to businesses during and after the COVID-19 pandemic

In mid-March 2020, Kazakhstan adopted an anti-crisis package, complemented in May 2020 by the "Comprehensive Economic Growth Recovery Plan", for a total amount of 14 billion USD (5.9 trillion tenge), equivalent to 9% of GDP. Later during the year, additional tax breaks and local support as well as additional measures to support SMEs were provided. According to official statistics, by early 2021, more than 1.6 million people and 11.5 thousand SMEs had benefitted from a deferral of payments of loans, and the provision of new preferential loans totalling USD 870 m (360 bn tenge). Some of the main measures covered:

Support to workers and social assistance

- The National Fund of Social Security granted wage subsidies to employees of MSMEs on unpaid leave, while employees who lost their jobs because of the confinement were compensated at 40% of their former salary for up to six months.

Support to firms

- Firms with a drop in turnover above 40% received cash support up to 80% fixed costs, full compensation was provided to firms forced to temporarily close due to the lockdown.
- Payments of VAT and payroll taxes were deferred, and several loan guarantee schemes were set up to provide additional liquidity to firms. Public budget rules have been relaxed to encourage frontloading of public consumption and payments to private firms.
- Subsidised lending was provided under the state programme "Economy of Simple Things" (KZT 1 trillion) to grant additional liquidity to businesses.

Source: (OECD, 2021[10]).

Kazakhstan has felt the economic and social effects of Russia's invasion of Ukraine. Given its geographic and economic proximity with Russia, Kazakhstan experienced significant turbulences. These translated into currency depreciation, a significant influx of Russian citizens fleeing mobilisation, the disruption of supply chains and inflation. On the positive side, the country benefitted from company relocations following the introduction of sanctions against Russia and saw the value of its exports increase as a result of a spike in commodity prices (ODI, 2022[12]).

Addressing long-term reforms is crucial for the economy to withstand current shocks and adapt to the environmental challenge

Looking ahead, the need to pursue reform endeavours is more acute for the years ahead, as significant downside risks remain due to persisting structural weaknesses, including, in particular, sluggish productivity growth, as well as the twin effects of the war in Ukraine and the international sanctions imposed on Russia, and the impacts of climate change (EBRD, 2022[13]; IMF, 2022[14]; OECD, 2022[15]). While growth reached 3.2% in 2022 and is estimated to reach 4.3% in 2023, this trend is mainly supported by higher oil prices, fiscal stimulus, and sustained recovery of private consumption (IMF, 2023[16]). In the years ahead, new vulnerabilities could emerge from supply chain disruptions, risks of secondary sanctions given Kazakhstan's significant trade, investment, and migration linkages to Russia, and increased climate stress (World Bank, 2022[9]; EBRD, 2022[17]; OECD, 2022[15]).

The 2020 OECD report identified a need for improved implementation of reforms in three priority areas

Operational environment for SMEs

The 2019-2020 OECD assessment found that Kazakhstan had improved the simplicity and coherence of its business regulation. It highlighted the streamlining of legislations and administrative procedures with the introduction of the Entrepreneurial Code (EC) (Box 2.2), the creation of Public Service Centres (PSC) and sector-based self-regulatory organisations (SROs) supervising the implementation of licensing procedures, the design of supportive strategies (Roadmap 2020), and the establishment of the Entrepreneurship Support Fund DAMU.

However, businesses continued to report that the regulatory landscape was unpredictable and complex to navigate, and that procedures were unevenly implemented across the country. As a result, businesses were left subject to sometimes abusive practices, in particular in relation to licensing procedures. This perception reflected the experience of both local businesses and international investors, which in addition continued to face remaining restrictions in the legislation, such as exceptions to national treatment in certain sectors, and restrictions to the employment of foreign staff and transfer of property (OECD, 2020[1]).

Box 2.2. The Entrepreneurship Code of Kazakhstan

In October 2015, Kazakhstan introduced the Entrepreneurship Code (EC), consolidating the six pre-existing entrepreneurship- and investment-related legal acts into a single document, harmonised with the Civil Code to ensure consistency. Beyond its streamlining aspect, the EC also enacted a new approach to state-business relations with the introduction of the principles of presumption of good faith and mutual responsibility of state and business entities, as well as the principle that ambiguity in legislation should be interpreted in favour of businesses.

The EC has since become the main legislation regulating all domestic and foreign business activities in Kazakhstan (including investment) and includes among its main dispositions the codification of allowed circumstances for unscheduled inspections, of in-court and alternative dispute resolution mechanisms, as well as the role and supervision of the Business Ombudsman. However, relations between firms and the customs agency, subsoil use and the licensing thereof, and the activities of the prosecutor's office remain outside its scope.

Source: Entrepreneurial Code of Kazakhstan, (OECD, 2020[1]).

Contract enforcement

***De jure* investors' rights and property are explicitly guaranteed by the Civil Code and adjacent legislation on investment and international investment agreements.** Companies facing explicit or implicit corruption attempts or other forms of unfair treatment can seek dispute resolution either in domestic courts or international arbitration bodies. Efforts of the government have also focused on streamlining the procedural efficiency of the court system, with the Astana City Court and the Supreme Court being the only courts considering investment dispute cases, complemented by the creation of the Astana International Financial Centre (AIFC). In addition, alternative dispute resolution mechanisms have been developed with the establishment of protective and representative institutions such as the Investment Ombudsman, the Commissioner for the Protection of Entrepreneurs' Rights under the National Chamber of Entrepreneurs Atameken (business ombudsman).

However, concerns remained about the quality of judgments, and alternative dispute resolution mechanisms remained underused. While international investors remained concerned with the quality of judgments by the local courts, local businesses were mostly unaware of available dispute resolution tools, and if aware, expressed concerns about their impartiality when adjudicating disputes with the state or state-owned enterprises (SOEs) (OECD, 2020[1]).

Trade facilitation

Kazakhstan has been an active member of regional and international trade co-operation institutions. The country is a member of the Eurasian Economic Union (EEU) and the Central Asia Regional Economic Cooperation (CAREC), as well as the World Trade Organisation (WTO). The government has also been actively promoting regional connectivity with several reforms to automatise, digitise and harmonise its customs procedures with those of neighbouring countries. **However, the country remains at the margins of international trade flows** The pandemic and the effects on international trade of Russia's war in Ukraine highlighted that the country's integration in global value chains (GVCs) remains limited, as the country's landlocked position is compounded by persisting hard and soft infrastructure issues (OECD, 2023 forthcoming[18]; OECD, 2020[1]; OECD, 2023[3]).

Assessing implementation progress since 2020

The following sections provide an overview of implementation progress of the three priorities for improving the legal environment for businesses identified in the 2019-2020 OECD analysis, and suggest a way forward taking into account new priorities following the pandemic and the regional context.

Priority 1: Business regulation has become more transparent and equitable, but reforms require thorough implementation

The gradual phasing out of COVID-19 support packages to businesses coincided with a rethinking of business regulations

The COVID-19 crisis has had a strong negative effect on businesses: an estimated 300,000 SMEs stopped working nation-wide in 2020 and many more firms reduced their operations. The pandemic also exacerbated existing bottlenecks and issues in the regulatory framework governing daily business operations (OECD, 2021[10]). As recovery took hold, the government gradually phased out support policies that coincided with a renewal of business legislation, with a focus on relieving businesses of administrative burdens, and further simplifying and digitalising state-business interactions.

Reforms have focussed on stabilising regulatory and inspection procedures

These reforms, adopted in December 2021, seem to reflect a change in the rationale of business regulation towards a reduction of stringency, inspections and room for arbitrary action (Government of Kazakhstan, 2021[19]). On state involvement and stringency, Article 7 of the law introduces the automation of risk assessment and management systems, with the aim to restrict the number of inspections a given administration can carry out and limit business inspections only to cases of compliance with permit requirements. The main procedural change pertains to the alignment of Kazakhstan's risk classification system to OECD standards with the introduction of a third step (medium risk) to the previous binary system (high and low risk), and a ban on inspections motivated by reasons outside that scope. In addition, the law provides a legal basis to delegate some additional supervisory prerogatives away from the state to sectoral organisations, based on the outcomes of "market readiness analyses" for some sectors. These changes are also related to the first ever regulatory impact assessment (RIA) carried out by the Ministry of National Economy, with the support of the Business Ombudsman. The review, which is to be completed in 2024, covers all regulations, including technical ones, and has so far covered five sectors representing 60% of all businesses. According to official data, at the time of writing, the assessment had already resulted in a reduction of the number of permits (by 75%, from 1,115 to 287), of inspection duration (from 30 to 15 days), direct supervisory functions of the state (from 544 to 379), and the introduction of preventive control measures.

The new Environmental Code, introduced in January 2021, seems to bring Kazakhstan's regulatory framework for environmental management closer to OECD practices. While environmental permitting and licensing has long been considered a key issue by businesses, the Code aims at regulating activities of any individual or legal entity that could potentially have a negative impact on the environment, such as carbon emissions or other forms of pollution, and introducing the best available technologies (BAT) in the country as a basis for an integrated environmental permit framework, providing clarity for firms in the oil and gas, mining and metallurgical, chemical and electric power industries, which are responsible for a large share of pollution in the country (IEA, 2022[20]). Effects of these changes however need to be assessed in practice.

Further progress in the digitalisation of public services has supported easing the administrative burden for firms

The government's digitalisation agenda has borne fruit. This has been particularly visible in e-government and digital public service delivery, easing business-state interactions and lowering the costs and time involved in accessing public services, especially for small firms (OECD, 2020[21]; Government of Kazakhstan, 2020[22]). A recent OECD survey finds that businesses are satisfied with the quality of online service provision, such as licensing and permits for businesses (OECD, 2023[3]). Beyond these, the December 2021 law has renewed impetus to the digitalisation and simplification of key steps in the business lifecycle, especially bankruptcy requirements. In addition, since 2020, the e-government platform has increasingly been used to involve the business sector and individuals into discussions about regulatory changes.

The government has also deployed efforts to support an even implementation of reforms

Reform efforts have also focussed on ensuring coherent implementation across the country and the different levels of administration, and fair treatment among businesses. In early 2023, the government introduced the "Registry of Mandatory Requirements" which lays out mandatory rules for implementation of the law, with a focus on transparency and enforceability (mandatory publication of legislative changes and introduction of a timespan to allow businesses to adapt), and certainty with the publication of a closed list of claims for which inspection and sanction powers of public authorities apply. The government has also aimed to increase the awareness and capabilities of the public administration on regulatory requirements and changes. In 2022, civil servants and businesses also benefitted from training sessions by Atameken, the National Chamber of Entrepreneurs, to acquaint them with the changes introduced to the regulatory framework and ease implementation. Regarding fair treatment among businesses, the law of 31 December 2021 has laid the ground for levelling the regulatory playing field between private businesses and SOEs, while the government announced in early 2023 an SME-specific policy to be integrated into the *Concept of Small and Medium Businesses Development until 2030* by the end of August 2023. Available information about the policy suggests that it will provide targeted tax, and administrative incentives to support SME growth, while developing SME-FDI linkages, supplying contracts between national SMEs and large SOEs, and adapting state support to regional development to fit SMEs' needs.

Implementation lags and complexities remain

The regulatory landscape remains very changeable, and firms struggle to keep pace with reforms

Businesses report that uneven implementation remains a central impediment to the *de facto* improvement of the environment in which they operate. In particular, the pace of regulatory reform remains too high for businesses, especially small firms, to participate in public consultations and keep up with new requirements. For instance, according to official data, the Tax Code adopted in 2017 was amended 50 times between 2018 and 2022 (including 11 times in 2018, 18 in 2019, 9 in 2020, 7 in 2021, and 5 in 2022), with changes affecting about one third of its articles. While these changes include noticeable improvements, information about public consultations and changing regulatory requirements has not become more accessible in recent years. Businesses interviewed by the OECD during the assessment also report the persistence of perceived bias from some state authorities when conducting RIAs, doing so with predetermined outcome in mind rather than grounding their decisions for streamlining of regulations on the actual feedback of the private sector.

Business inspections remain a central issue in the operational environment for firms

Businesses also remain concerned about inspections. Despite recent improvements, their motives have not yet been fully reformed. Moratoria on business inspections continue to remain the main support measure for small businesses, and the moratorium adopted during the pandemic has been extended for an additional year, until 2024. The moratorium seems to have been effective in limiting the number of inspections, as official data suggest that there has been a marked decrease in the number of inspections since 2019[1]. However, this may in part reflect lower business activity during the pandemic as well.

The systematic use of moratoria on business inspections as a policy tool is at best a second-best option and creates additional complexity for firms. Moratoria on inspections can lead to a concentration of inspections on the periods right before and after their application, while not resolving the issue of unpredictability and partiality of inspections. In the current context, it might even add further uncertainty to the regulatory environment, as it remains unclear how the moratorium is articulated with the new risk management system introduced under the December 2021 law, giving the impression to businesses that the issue is still dealt with via exceptions in the regulatory framework rather than an actual overhaul of inspections as outlined in the law. Businesses also report a non negligeable number of unwarranted inspections, persisting excessive controls, and punitive inspections by some regulatory authorities. While this could partly be attributable to a transition between the law's adoption and its effective implementation, businesses report an increase in *de facto* administrative barriers.

License requirements have been streamlined and mainly automated following regular regulatory reviews, however new issues on the licensing system have appeared. While the complexity and unpredictability of licensing requirements were a major concern reported by businesses to the OECD in the 2020 report, early 2023, the permit system included a total of 345 permits and notifications, including 57 notifications of commencement or termination of activities which have been fully automated. This corresponds to the removal of 39 permits and notifications since 2019. However, businesses report concerns over sector-based self-regulatory organisations (SROs), which had been created in 2015 by the EC to supervise the implementation of licensing procedures. If initially their development was seen as an improvement to help businesses navigate licensing matters, businesses report that the *de facto* transfer of oversight responsibilities from the state to SROs is weak, with a large part entrusted to Atameken, equivalent to a state body. Businesses also reported that the development of SRO under its current form could potentially have a detrimental effect on SMEs, as membership might not be affordable to them due to high entry fees and absent regulation on methodologies to calculate associated costs, such as contributions to the compensation fund, insurance amounts and premia.

Box 2.3. Design of an Administrative Burden Index

Atameken is currently reviewing the Administrative Burden Index developed in 2020, which aims to improve the implementation of the law applicable to businesses with a view to reduce the administrative burden on firms. It will be based on statistical data from government agencies and the Committee on Legal Statistics and Special Records of the General Prosecutor's Office of Kazakhstan, as well as on the basis of survey indicators collected among businesses.

The Index will reflect the nature and attitude of the control and supervisory bodies. Preliminary index indicators will include data on:

- effective implementation of the risk assessment system when conducting business inspections,
- reduction of repressiveness of control and supervisory activities (e.g., fine rate)
- registered administrative offenses against business entities,
- number of illegal inspections; etc.

The Administrative Burden Index will be made publicly available.

Source: OECD analysis from Atameken contribution

The pace of regulatory changes still needs to adapt to implementation capacities

The government should stabilise regulation through a systematic use of regulatory impact assessments and improve the monitoring of reform implementation

Ensuring effective implementation of business regulation also requires stabilising it, introducing only necessary changes, while publicising them to both public authorities and businesses. The current pace of regulatory changes is a challenge to both businesses and public agencies' capacities and accountability. The government could introduce a more regular use of RIAs as a tool for ex ante and ex-post evaluation, in direct collaboration with the private sector and its representatives, including Atameken and its regional branches, as well as sectoral business associations, to identify remaining gaps or redundancies in business legislation. Such RIAs could be carried out on a regular and predetermined schedule, for instance once every two years, and their outcomes should feed into the policy process, involving all concerned agencies to ensure a better understanding across the government of the rationale for different policy and regulatory reforms for private sector development. Particular attention should be paid to the impact of reforms on SMEs, and to the examination of how simplification or revisions may address these issues. Lastly, there should be only limited exceptions to exemptions from RIAs (e.g., budget laws, national security matters). Too many exceptions to the obligation to perform RIA can become an alibi for administrations not to carry out the analysis (OECD, 2020[23]).

In parallel, the government could step up its efforts to ensure consistent implementation of reforms by supporting the capacities of the public sector. For instance, the trainings of civil servants that were initiated by Atameken in 2022 should be generalised at both national and regional levels and be carried out directly by state authorities on a regular basis. Doing so may help ensure that civil servants are up to date with regulatory changes and will be able to advise and support businesses in their adaptation journeys. In parallel, the government should also prioritise the development of channels through which firms can report instances of non-implementation, for instance in collaboration with the Business Ombudsman or a dedicated section on the e-government website accompanied by the creation of cross-agency steering body to provide oversight and guidance.

The government should develop tools to raise firms' awareness of and ability to cope with regulatory changes

Beyond increased consultation with the private sector, the government can also help businesses to better adapt to regulatory changes. For instance, more could be done to publicise new and revised regulation, and develop support programmes to help firms, especially SMEs, adapt. All regulatory changes should be widely publicised and regularly updated with latest legislative changes and made available to the private sector through the publication of information on a dedicated page of the competent authority's website as well as on the websites of Atameken and sectoral business associations. Atameken could also regularly update the website of the registry of issues. In a similar vein to trainings for civil servants, the competent authorities should design and provide targeted outreach programmes and trainings to help businesses, especially SMEs, adapt to new regulatory requirements. Such programmes should be financed by the government and could be administered via Atameken and its regional branches or other private sector organisations. Finally, public administrations should also develop a stronger culture of remediation to encourage firms to adjust operations to remain in line with their regulatory requirements. For instance, a predefined and widely publicised amount of time should be granted to businesses to adapt to new legislation after its introduction and publication. During that period, relevant public authorities should provide firms with explanatory documents and the opportunity to discuss these changes and their impact on individual businesses with an individual from the authority.

Priority 2: Judicial capacity and independence registered some progress, but dispute resolution tools can be further improved

Judicial and dispute resolution reforms have been a priority for the government

Recent judicial reform has focussed on strengthening judicial capacity and independence

In recent years, the government has focussed on increasing the trust of businesses in the judicial system. Recent reforms aimed at improving the probity and skills of judges, the quality and coherence of judgements, and businesses' use of in- and out-of-court dispute resolution mechanisms. In particular, they targeted a change of practice and improved implementation of the pre-existing well-developed legal framework for contract enforcement and dispute settlement. Judicial reform has been advanced through the Supreme Court's "Seven Pillar Strategy" to select and retain competent judges and enhance training on drafting judgements in accordance with international standards (OECD, 2020[1]). Businesses interviewed by the OECD report that the introduction of a new system of judicial recruitment and oversight under the High Judicial Council, and decision templates to guide the process of drafting judgements and increasing reliability have resulted in improved quality of court decisions. The Supreme Court and the government have also attempted to tackle corruption by raising the salaries of judges and prosecuting and dismissing senior judges involved in corruption cases. It however remains to be seen if those changes appear to be systemic, as so far Kazakhstan has not displayed a major score improvement in the World Justice Project index.

Advancing fair and accessible dispute resolution for businesses has become a priority for the government

The government has also advanced a more general dispute resolution reform, by making it as a priority means in business-state litigations and using it before pre-trial investigations. The adoption of the new Administrative Procedure Code (APC) in 2020 reflects this changed approach by introducing tools to provide individuals and businesses an equal opportunity with the state in the case of a dispute, as well as requiring more transparent operations and decisions of administrative bodies (Box 2.4). In particular, the code introduced a hearing procedure and pre-trial dispute resolution dispositions, shifted the burden of proof to the state body in case of disputes, and allowed courts to examine all circumstances relevant to the case without limiting themselves to the evidence submitted by the parties. It is to be noted that the law entered into force only one year after its adoption, to grant concerned institutions time to adapt to the new framework and allow judges and officials to attend specialised trainings (ZOiS, 2021[24]). Implementation of these reforms has also been entrusted to the chief justice of the Supreme Court and seems to have enjoyed support from the public and businesses. However, the first rulings by the administrative courts need to be assessed first to judge effectiveness.

Box 2.4. The Administrative Procedure Code of Kazakhstan

In his September 2019 Address to the People of Kazakhstan, President Tokayev pleaded for the introduction of dispute resolution mechanisms in administrative justice to level the playing field between individual and businesses, and the state in public law disputes. This led the government to shift towards the "listening state" principle and adopt the Administrative Procedure Code of the Republic of Kazakhstan (APC) in June 2020, which entered into force on 1 July 2021.

The new code is the first comprehensive legal document to regulate the country's general administrative law, referring to the state's exercise of power, its interaction with its citizens, and the mechanisms protecting and representing their interests. In particular, it allows for rule-of-law principles to be, for the first time, regulated in ordinary legislation. The code:

- replaces and streamlines two previous laws, the Law on Administrative Procedures and the Law on the Examination of Applications of Legal Entities and Individuals, as well as a part of the Civil Procedural Code, which contained the procedure for appealing against the actions of state bodies;
- codifies a set of rules for judicial proceedings in administrative courts such as the right of each individual to file a complaint against the state (*guarantee of legal protection*), the protection of this right - including the prohibition to deny an application or a complaint as well as applying pressure to a plaintiff to drop his complaint, the right to a "legally competent" judge, the right to be heard prior to any decision by an administrative court, and the introduction of the proportionality principle; and
- introduces a three-tier judicial system for administrative complaints, with the opportunity to appeal against first-instance decisions as well as an ultimate to the Supreme Court. As for first instance, the Code stipulates that they should be formed by specialised judges or by chambers of specialised judges and plans to establish independent specialised administrative courts.

Source: (Government of Kazakhstan, 2020[25]).

A Constitutional Court was re-established in 2022 and started work on 1 January 2023, with the explicit aim of better enforcing and communicating on individual and business rights. Both can indeed directly bring an appeal case to the court (Government of Kazakhstan, 2023[26]). Furthermore, the Ombudsman also received the right toa direct referral on matters concerning the rights enshrined in the constitution. Among them, "*the right to freedom of entrepreneurial activity*" guaranteed by article 26(4) stands out as particularly relevant for businesses.

Since its inception in 2016, the Business Ombudsman has played an active role in dispute resolution. The handling of out-of-court dispute settlement, in particular in relation to unfair treatment by government authorities, has met some success and received positive assessment by businesses according to official sources.

Similarly, tax administration and state audits have been reformed to be more supportive of business rights. A presumption of good faith of the taxpayer has been introduced in the Tax Code, and, following an initiative of Atameken, the appeal mechanism against the results of state audits has been improved by prohibiting the opening of a criminal case against an entrepreneur until all avenues of appeal against the results of a state audit have been exhausted in civil proceedings. It has been proposed to extend the results of inspections of all control and supervisory bodies as well. Finally, in July 2021, e-Otinish, an online platform and mobile app was created to receive and process appeals of individuals against any government body, to facilitate the appeals to and the filing of a lawsuit, to decrease the duplication of appeals and to increase their speed of processing. According to official data, for the first 15 months of operation (as of September 2022), the app received more than 2 million appeals, representing a six-fold increase of online appeals and appeals mainly directed towards the Presidential Administration, AlmatySu (Almaty city water supply), akimats, and the Prosecutor General's Office, with 700 thousand unique users across the country (Government of Kazakhstan, 2023[27]).

Despite improvements, contract enforcement and dispute resolution continue to be perceived as a major challenge for businesses

Businesses continue to raise concerns related to contract enforcement and dispute resolution, particularly in terms of the predictability and impartiality of decisions. This has been confirmed by a recent OECD survey where, when asked which reforms they considered most important for the government to pursue, over half of respondents (55%) suggested reforms to improve transparency in the justice system and effective contract enforcement (OECD, 2023[3]). Businesses' concern about a remaining gap between their *de facto* experience and the *de jure* provisions that ought to protect them cover mainly two issues: the existence of a two-tiered judicial system between international and domestic firms, and a persisting perception of court bias in favour of authorities in cases of business-state (or SOE) disputes.

Dispute resolution reforms need to be inclusive

The creation of the AIFC in 2018 was a major step towards the improvement of Kazakhstan's investment attractiveness. The Centre's work has helped improve the predictability of contract enforcement for large international investors and the AIFC's International Arbitration Centre (IAC) has been successful in establishing itself as an important arbitration hub, not only for Kazakhstan but for Central Asia as a whole (OECD, 2020[1]; OECD, 2023[3]).

However, this development is rather an exception in the legal landscape, bearing the risk of creating a two-tiered justice system for businesses. While the AIFC offers arbitration by highly competent common law judges, the high costs associated to its procedures, as well as English being the main working language, have caused the centre to be considered by many smaller domestic businesses an exceptional justice intended only for foreign investors without benefits for local entrepreneurs. For domestic businesses, besides the reforms led by the Supreme Court, efforts to improve the functioning of administrative courts have essentially focussed on increased cooperation among judicial bodies, but asymmetry of information issues have largely been left unaddressed, with a non-negligible share of businesses not being informed about their existence or the procedures they might benefit from. Advancing contract enforcement and predictability for domestic businesses is not only an important step for domestic private sector growth, but can also add to investment attractiveness, as it improves the daily operations of potential domestic suppliers and clients for large international businesses (OECD, 2023[3]).

Dispute resolution can sometimes lack impartiality

A perception of bias in favour of authorities in disputes between businesses and state bodies also continues to prevail among businesses. This perception stands out as official numbers suggest that the reform of the APC has resulted in more rulings in favour of businesses. This seems to be particularly the case for disputes on tax matters for which in the first half of 2022 about 55% of rulings were in favour of businesses, compared to an average of 15% before the entry into force of the code. This difference between numbers and businesses' perception might therefore reflect other litigation topics such as land relations, public procurement and subsidies, which, according to a recent review of business complaints against authorities carried out by Atameken and regional business chambers, are the most common issues for business complaints against authorities in the country.

The automation of procedures has created new barriers for businesses, in particular in relation to tax and public procurement matters, while court procedures are not perceived to be supportive of businesses in these cases. For instance, tax notifications and inclusion in the register of unfair participants in public procurement are generated automatically. If businesses are to challenge these in court, practice shows that the latter tend to rule based on the automated notification of decisions' findings rather than the businesses' explanations or newly provided documents. Businesses have also raised the concern that administrative sanctions remain outside of the scope of the APC so far, being governed by the Code on Administrative Infractions, which might leave room for interpretation.

The absence of specialised judges weakens the protection of intellectual property rights

Finally, at the intersection of both issues lies a gap in specialised courts for intellectual property (IP) rights protection and the absence of clearly defined responsibilities and functions for the public organisations that have a role in IPR-related disputes. Despite an extensive regulatory framework for IP protection (enshrined in the Civil Code, the Law on Patents, and the Law on Copyrights and Neighbouring Rights and recently amended in June 2022), businesses indeed report a significant number of contentious decisions (Government of Kazakhstan, 2022[28]). Discontent is particularly expressed in relation to procedural aspects such as the lack of specific qualification of judges, a great variability in the interpretation of laws, the lack of qualified experts for expertise and the high cost of their services.

More support to domestic businesses' use of dispute resolution tools, and an improved protection of intellectual property rights are required for better contract enforcement

The government should pursue its efforts to improve the quality of the court system

The government should closely monitor and assess the implementation of the new rules on judicial independence and continue to improve them. The reforms conducted in recent years have contributed to the development of a more independent court system of better quality. However, avoiding a hasty implementation is key to ensure that the changes are properly understood by judicial institutions and that the framework designed by renewed rules is properly applied. Therefore, the government should consider conducting trainings for the judges to build the required institutional capacity. It must be noted that, since some provisions have a delayed implementation (e.g., acquiring applicability only from the 1 January 2024) and that changes always require some time to produce tangible results, it remains for now difficult to assess the effectiveness of the implementation of the reforms.

The government must also ensure that the provisions stated in the law are effectively enforced during the conduct of administrative proceedings by the courts. As per today's situation, businesses' perception of a persisting bias of court rulings in favour of the State, especially in relation to land rights, public procurement, and subsidies, might be attributable to a lack of awareness of the rights the new APC grants to them. Addressing this would require the government to improve businesses' knowledge of the functioning of administrative courts.

The government should improve domestic businesses' awareness of available alternative dispute resolution tools

In parallel to increasing the independence of the court system, the government should develop awareness-raising and outreach campaigns about the availability and functioning of other processes for dispute resolution. As for now, it seems that businesses remain unaware of available alternative dispute resolution tools, as well as time, cost, process and benefits to be expected from these procedures (OECD, 2023[3]). Therefore, the government should share resources, alongside information about the court system, about available processes for dispute resolution including out-of-court and alternative dispute resolution tools.

Targeted outreach campaigns could be developed in co-operation with the Business Ombudsman, Atameken, regional business chambers and sectoral business associations. The goal for them would be to identify their members' most recurrent procedural complaints, as well as their main gaps in terms of procedural knowledge. Based on this, the government could develop targeted outreach media campaigns (dedicated website or page on the institution's website, explanatory leaflets, and videos, etc.), implemented or relayed by the business associations[2]. The latter could also regularly organise online or in-person training sessions on the most common procedural issues faced by their members, inviting representatives of the competent dispute resolution bodies. On a related matter, the government should also ensure that IAC best arbitration practices are shared with domestic courts to contribute to the creation of a wider arbitration culture in Kazakhstan.

The government should set up an effective institutional framework for intellectual property rights enforcement

Effectively protecting IPR in Kazakhstan requires building the technical expertise of judges. A focus on building the technical expertise of judges, in particular for patent enforcement, in civil and criminal courts can support the effective protection of IPR and advance Kazakhstan's ambitions to support innovation. As a first step, developing IP expertise in these courts would require creating specialist IP benches within them and allow courts to call on a third-party institution with IP expertise, such as the National Institute of Intellectual Property, or inviting "friends of the court" (*amicus curiae*) briefs to express their views on a given issue in a dispute. In parallel, judges with a representative level of expertise in the relevant areas for IPR disputes should be appointed where possible, while ensuring that all judges having to deal with IP matters are provided with mandatory continuing education and training opportunities and encouraged to engage in exchanges with international IP courts to allow them to keep abreast of the rapid evolution of IP law and related legal concepts and developments. Finally, courts should be encouraged to publish IP case decisions on online databases both to improve transparency of judicial processes and to build precedents other judges might draw upon (Gurgula, Padamczyk and Shemtov, 2022[29]; de Werra, 2019[30]).

Priority 3: Trade procedures have become more accessible and protective of IP rights, but restrictions to trade remain in the services sector

Kazakhstan has improved the regulatory framework, with a focus on digitalisation of procedures and intellectual property rights

Developing international trade has been a longstanding priority of Kazakhstan's government to support the diversification agenda for its economy, against the backdrop of the country's landlocked position. The government has been actively developing an open and fair regulatory framework, which culminated in the country's accession to the WTO in 2015, and it has been deepening its regional integration through its membership in the Eurasian Customs Union (Belarus-Kazakhstan-

Russia) and then the Eurasian Economic Union (EEU), as well as in the Central Asia Regional Economic Cooperation (CAREC). Since 2017, the country has been constantly improving its trade facilitation framework, with a strong focus on improving the transparency and predictability of trade-related information, through the streamlining of documentation requirements and processes, an increased role of digital tools, and improved internal border agency co-operation (Box 2.5) (OECD, 2023[3]).

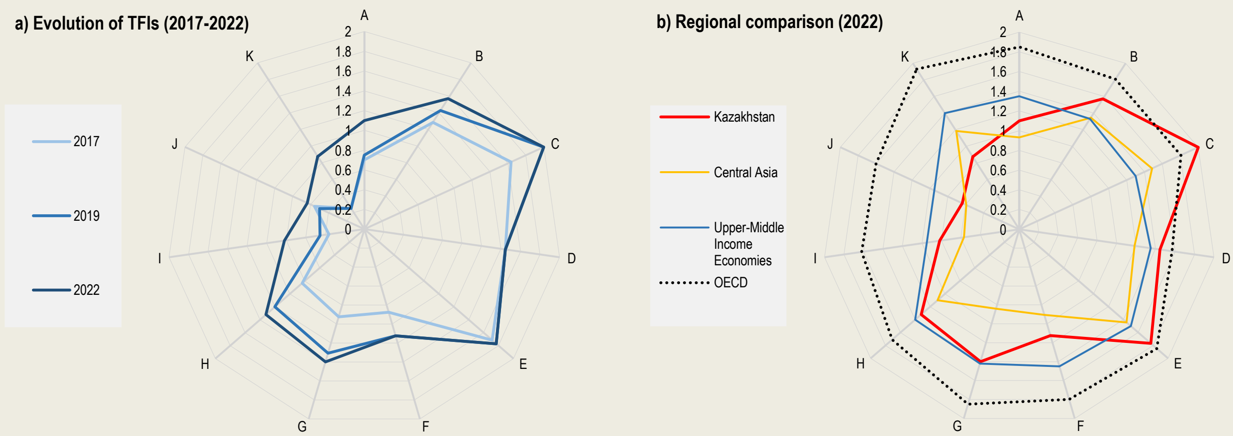
Kazakhstan launched several online trade portals and single windows and reformed the Customs Code to favour digitalisation of border procedures. For instance, the Single Window for Export-Import Operations, the Kazakhstan Trade Portal, the Trade Facilitation Information Portal, as well as the *Automated System of Customs and Tax Authorities* (ASTANA-1) customs border portal, provide firms e-permits, information, references, and documents related to exports (Atameken, 2019[31]; OECD, 2023 forthcoming[18]). In particular, the introduction of ASTANA-1, compliant with the WTO, European Union and UNCTAD Customs standards, in January 2020, has been an important step to bring down the time and cost of trade by allowing fully automated customs procedures and the harmonisation and digitisation of all customs- and trade-related documentation. In 2021, reforms to the Customs Code further advanced the digitalisation of procedures, by allowing applications for a preliminary electronic classification of goods from the State Revenue Committee which reduced by half (from 20 to 10 working days) the review period for classification of goods (Government of Kazakhstan, 2021[32]). Additional reforms include the introduction of a new risk management system for on-site audits, increasing the number of cases when customs declarants are not accountable under the Administrative Violations Code, as well as the authorisation for foreign individuals and businesses to import and declare goods at a port of entry without the support of domestic customs brokers. However, business report that in practice, foreign individuals and businesses may still need domestic customs brokers in order to file electronic customs declarations, due to customs software compatibility issues (U.S. Department of Commerce, 2022[33]).

Finally, Kazakhstan has also been successful in developing a legal framework more protective of intellectual property rights in relation to international trade. In particular, a new law adopted in June 2022, and accompanied by a Roadmap, has introduced a series of protections such as geographical indications and appellations of origin, a system of short-term protection of unregistered industrial designs, and an opposition system for trademarks, as well as clarification of qualification requirements for patent attorneys (Government of Kazakhstan, 2022[28]). If these amendments may open up new opportunities for domestic producers to enter global markets, their implementation and effect on businesses have yet to be assessed.

Box 2.5. Kazakhstan's performance in the OECD Trade Facilitation Indicators

The 2022 TFIs database highlights that Kazakhstan has consistently improved its performance since 2017 across all areas covered by the TFIs. Areas where improvements are most notable concern making trade-related information available, advance rulings, simplification and harmonisation of trade-related documents, automation and streamlining of border procedures, as well as domestic border agency co-operation.

Figure 2.3. Kazakhstan's trade facilitation performance since 2017



Legend: A - Information availability, B - Involvement of the trade community, C - Advance rulings, D - Appeal procedures, E - Fees and charges, F - Documents, G - Automation, H - Procedures, I - Internal border agency co-operation, J - External border agency co-operation, K - Governance and impartiality.
Note: 2 is the maximum score. Central Asia includes information for Kazakhstan, Kyrgyzstan, Tajikistan, and Uzbekistan.
Source: (OECD, 2023[34])

Kazakhstan also performs above the TFIs average for the group of upper-middle income economies in many areas relating to transparency and predictability (involvement of the trade community, advance rulings, appeal procedures, fees and charges) as well as the automation of border procedures). Fees and charges and advance rulings are also areas where Kazakhstan is on par or above the average performance in the OECD area.

The 2022 TFIs database also reveals Kazakhstan as the overall top performer in Central Asia. It performs better than the other economies in the region covered by the database (Kyrgyz Republic, Tajikistan, Uzbekistan) in the majority of the TFIs areas, except for information availability and governance and impartiality.

Implementation lags behind for trade facilitation and regulatory barriers to services trade remain

Implementation and access to trade-related information remain an issue for businesses

Despite these *de jure* improvements, firms continue to report persisting cumbersome trade procedures and unpredictable implementation. In a recent OECD survey, over a third of respondents indicated that improvements to trade and customs regulation should be a government priority, while only 3% said that major progress had been made in this area over the past five years (OECD, 2023[3]). It seems that the implementation gap arises mainly from an entanglement of policies and lack of information about regulatory and legislative changes on the side of businesses and implementing agencies, which leave room for varying interpretations.

Information is fragmented across several platforms. The coexistence of several online trade portals, ranging from information provision to registration of online procedures, also serves to complicate firms' access to information, especially for the smallest among them, which limits the reach of these tools and reforms.

Arbitrary interpretation of the Customs Code by customs officials is most frequently cited in relation to transit declarations and the non-use of electronic queuing. For instance, the US Department of Commerce reports that so-called transaction passports for goods clearance can vary in nature, ranging from document procurements to bank transfers, and represent a significant barrier to trade (U.S. Department of Commerce, 2022[33]). Similarly, online pre-declarations are not always functional, and are sometimes duplicated by paper procedures at border ports. Customs processing can also remain costly and cumbersome due to an absence of priority procedures, for instance for perishable goods despite the relevant example of the "green corridors" implemented during the pandemic, or because of targeted requirements, such as the one applicable to equipment and spare parts imported to implement an investment project, which need to be placed in a temporary storage warehouse operated by a customs-licensee pending clearance (OECD, 2021[10]; U.S. Department of Commerce, 2022[33]).

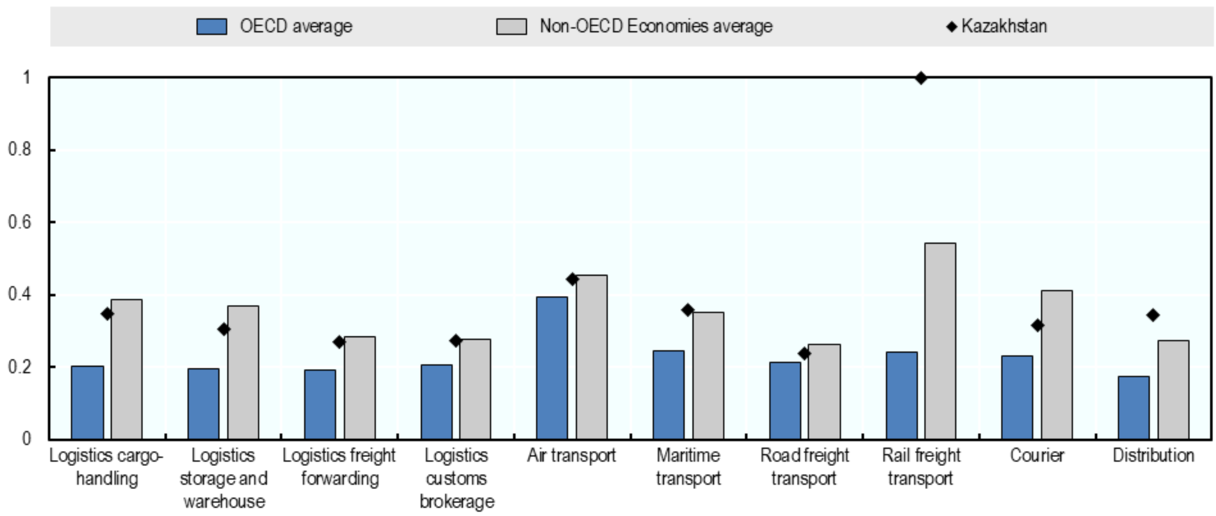
Regulatory barriers to services trade remain an impediment for both domestic and international firms

Despite a relatively open overall regulatory framework for investment, restrictions remain in crucial sectors necessary for the broader competitiveness of the economy, especially services trade. The OECD Services Trade Restrictiveness Index (STRI) reveals that Kazakhstan is the seventh most restrictive of the 50 economies covered by the index, even if services trade restrictions have been somewhat relaxed in recent years following the country's WTO accession (OECD, 2023[3]). Investors face more restrictions in relation to trade and investment than in most OECD and non-OECD countries, particularly in relation to work permitting issues for foreign nationals looking to provide short-term services, the maintenance of foreign investment screening mechanisms, limited access to public procurement for foreign service suppliers, and restrictions on the acquisition of land and real estate by foreigners (OECD, 2022[35]).

Among the most heavily regulated service sectors are the ones in logistics and related services. This weighs negatively on the operational environment for both domestic and international firms, in particular on their ability to deepen regional integration and engage in international trade by integrating regional and global value chains. This issue is even more important in the current context, where the country will have to open new trade routes and diversify its exporting partners to successfully navigate the tensions arising from sanctions on Russia and associated trade blocs of which Kazakhstan is a member (OECD, 2022[15]).

Figure 2.4. OECD Services Trade Restrictiveness Index: Kazakhstan (2022)

Focus on performance in logistics and related services



Note: The maximum score 1 represents the highest level of regulation, often in relation to a total State monopoly, which is for instance the case for rail freight transport in Kazakhstan.
Source: (OECD, 2022[35]).

Further improving trade facilitation requires additional progress on implementation of reforms and the easing of regulatory barriers to services trade

> *The government should focus on closing the implementation gap and improving access to trade-related information for businesses*

On the trade facilitation front, the government should more actively and systematically involve the trade and business community. Closing the remaining implementation gap will help Kazakhstan's firms engage more in international trade, and the government to continue deepening regional integration (OECD, 2023 forthcoming[18]). In particular, the government should develop institutional feedback mechanisms in the form of regular meetings to discuss implementation issues in relation to customs procedures and regulatory and legislative changes. Online reporting tools or regular surveys could also be developed and channelled through Atameken, regional and sectoral business associations. Finally, the government could also establish an inter-governmental steering committee, for instance under the authority of the Ministry of Trade and Integration (MTI), monitoring implementation of trade-related decisions, or a joint working group between businesses, customs, and state administration to decrease barriers at customs.

However, these tools will only be effective if businesses are better aware of trade-related information, decisions, and legislation. To do so, the government should develop outreach tools such as improved publication of applicable legislation on the website of relevant authorities (key among which QazTrade, the MTI and the Customs authorities), as well as harmonise the several existing trade portals. This information can be complemented by thematic interactive pages for businesses, and the development of online and physical enquiry points. Finally, as regards legislative and regulatory changes, the government could introduce systematic notice-and-comment procedures that are communicated about using the most relevant channels to reach concerned businesses (for instance through Atameken).

The government should also rationalise services trade regulation and improve regional cooperation to keep trade flowing

On the business and investment climate front, the government should continue liberalising services trade regulation. Keeping trade flowing, developing new trade routes and joining new regional and global value chains are an important challenge for landlocked Kazakhstan in a context of mounting regional and international tensions. The government therefore should focus on rationalising regulation in logistics and related services sectors and aligning it with regional neighbours and its international commitments under the WTO. Similarly, the government should continue advancing effective regional integration by developing interconnected transit information systems with other countries in the region and harmonising customs documents and requirements.

References

Atameken (2019), *Single window portal for export-import operations launched in Kazakhstan: Atameken The National Chamber of Entrepreneurs*, https://atameken.kz/en/news/31765-portal-edinoe-okno-po-eksportno-importnym-operaciyam-nachinaet-rabotu-v-kazahstane (accessed on 9 December 2022). [31]

Bureau of National Statistics of Kazakhstan (2023), *Labour Productivity GVA (database)*, https://stat.gov.kz/en/industries/economy/national-accounts/dynamic-tables/. [40]

Council of Europe (2022), *Centre for Alternative Dispute Resolution launches an awareness raising initiative about benefits of mediation "Through mediation to an agreement - choose an alternative"*, https://www.coe.int/en/web/podgorica/-/centre-for-alternative-dispute-resolution-launches-an-awareness-raising-initiative-about-benefits-of-mediation-through-mediation-to-an-agreement-choos. [39]

de Werra, J. (2019), *A closer look at specialized intellectual property courts*, https://www.wipo.int/wipo_magazine/en/2019/03/article_0005.html. [30]

EBRD (2022), *Regional Economic Update - In the shadow of the war*, https://www.ebrd.com/rep-ukraine-war-310322.pdf. [17]

EBRD (2022), *Transition Report 2021-22. System upgrade: Delivering the digital dividend*, https://www.ebrd.com/publications/transition-report-202122-digital-divides. [13]

Government of Kazakhstan (2023), *Constitutional Court of Kazkahstan*, https://www.gov.kz/memleket/entities/ksrk?lang=en. [26]

Government of Kazakhstan (2023), *e-Otinish Submission of appeals to government agencies*, https://eotinish.kz/. [27]

Government of Kazakhstan (2022), *Law of the Republic of Kazakhstan "On Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan on Improvement of Legislation in the Field of Intellectual Property and State-Guaranteed Legal Aid"*. [28]

Government of Kazakhstan (2021), *Customs Code of the Republic of Kazakhstan*, https://adilet.zan.kz/eng/docs/K1700000123. [32]

Government of Kazakhstan (2021), “Law on the Republic of Kazakhstan”, *"On Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan on the Introduction of a New Regulatory Policy in the Sphere of Business Activities and Redistribution of Certain Functions of Internal Affairs Bodies"*, https://adilet.zan.kz/rus/docs/Z2100000095 (accessed on 6 July 2023). [19]

Government of Kazakhstan (2020), *Administrative Proecedural and Process-Related Code of the Republic of Kazakhstan*, https://adilet.zan.kz/eng/docs/K2000000350. [25]

Government of Kazakhstan (2020), *State of the Nation Address by President of the Republic of Kazakhstan Kassym-Jomart Tokayev*, https://www.akorda.kz/en/state-of-the-nation-addressby-president-of-the-republic-of-kazakhstan-kassym-jomart-tokayev-38126. [22]

Gurgula, O., M. Padamczyk and N. Shemtov (2022), *Specialised IP Judiciary: What Are the Key Elements to Consider when Establishing or Reforming an Effective IP Court?*, pp. Pages 206–212, https://doi.org/10.1093/grurint/ikab172. [29]

IEA (2022), *Environmental Code of the Republic of Kazakhstan, No. 400-VI*, IEA Publishing, Paris, https://www.iea.org/policies/12917-environmental-code-of-the-republic-of-kazakhstan-400-vi-as-amended. [20]

ILO (2023), *Labour productivity*, https://ilostat.ilo.org/topics/labour-productivity/. [8]

IMF (2023), *World Economic Outlook April 2023: A Rocky Recovery*, https://www.imf.org/en/Publications/WEO/Issues/2023/04/11/world-economic-outlook-april-2023. [16]

IMF (2023), *World Economic Outlook Database, April*, https://www.imf.org/en/Publications/WEO/weo-database/2023/April/download-entire-database. [2]

IMF (2022), *Regional Economic Outlook Middle East and Central Asia: Divergent Recoveries in Turbulent Times*, https://www.imf.org/en/Publications/REO/MECA/Issues/2022/04/25/regional-economic-outlook-april-2022-middle-east-central-asia. [14]

IMF (2022), *Republic of Kazakhstan: Selected Issues*, https://www.elibrary.imf.org/view/journals/002/2022/368/article-A001-en.xml (accessed on 7 September 2023). [6]

IMF (2020), *World Economic Outlook: A Long and Difficult Ascent*, World Economic Outlook, IMF, Washington DC, https://www.imf.org/en/Publications/WEO/Issues/2020/09/30/world-economic-outlook-october-2020. [36]

Ministry of Foreign Affairs of the Republic of Kazakhstan (2023), *Foreign Direct Investments to Kazakhstan Reach Record High in 10 Years*, https://www.gov.kz/memleket/entities/mfa/press/news/details/530609?lang=en (accessed on 11 October 2023). [4]

National Bank of Kazakhstan (2020), *Base Rate Raised to 12%*, Press Release, No. 7, 10 March, National Bank of Kazakhstan, Almaty, https://nationalbank.kz/cont/PR%20march%202020.pdf. [11]

ODI (2022), *What is the economic impact of the war in Ukraine on Kazakhstan*, https://odi.org/en/insights/what-is-the-economic-impact-of-the-war-in-ukraine-on-kazakhstan/ (accessed on 6 October 2023). [12]

OECD (2023), *Improving Framework Conditions for the Digital Transformation of Businesses : Peer-Review of Kazakhstan*. [37]

OECD (2023), *Insights on the Business Climate in Kazakhstan*. [3]

OECD (2023), *OECD Trade Facilitation Indicators*, https://sim.oecd.org/default.ashx?lang=En&ds=TFI&d1c=eca&d2c=aze&cs=eca. [34]

OECD (2023), *Review of Kazakhstan against the OECD Guidelines on Corporate Governance of SOEs*. [38]

OECD (2022), *Assessing the impact of the war in Ukraine and the international sanctions against Russia on Central Asia*, https://www.oecd.org/migration/weathering-economic-storms-in-central-asia-83348924-en.htm. [15]

OECD (2022), *Kazakhstan (2022)*, OECD Services Trade Restrictiveness Index (STRI), OECD Publishing, Paris, https://www.oecd.org/trade/topics/services-trade/documents/oecd-stri-country-note-kaz.pdf. [35]

OECD (2021), *Beyond Covid-19: Prospects for Economic Recovery in Central Asia*, OECD Publishing, https://www.oecd.org/eurasia/Beyond_COVID%2019_Central%20Asia.pdf. [10]

OECD (2020), *Improving the Legal Environment for Business and Investment in Central Asia*, OECD Publishing, https://www.oecd.org/eurasia/Improving-LEB-CA-ENG%2020%20April.pdf. [1]

OECD (2020), *OECD Best Practice Principles for Regulatory Policy*, OECD Publishing, https://doi.org/10.1787/7a9638cb-en. [23]

OECD (2020), *The COVID-19 Crisis in Kazakhstan*, OECD Publishing, https://www.oecd.org/eurasia/competitiveness-programme/central-asia/COVID-19-CRISIS-IN-KAZAKHSTAN.pdf. [21]

OECD (2017), *Reforming Kazakhstan*, OECD Publishing, https://www.oecd.org/eurasia/countries/OECD-Eurasia-Reforming-Kazakhstan-EN.pdf. [5]

OECD (2023 forthcoming), *Improving trade connectivity in Kazakhstan*. [18]

U.S. Department of Commerce (2022), *Kazakhstan - Country Commercial Guide*, https://www.trade.gov/country-commercial-guides/kazakhstan-customs-regulations. [33]

World Bank (2022), *Europe and Central Asia Economic Update, Spring 2022: War in the Region*, https://openknowledge.worldbank.org/handle/10986/37268. [9]

World Bank (2021), *Kazakhstan's Productivity Quest: Unleashing Financing for Dynamic Firms*, https://blogs.worldbank.org/europeandcentralasia/kazakhstans-productivity-quest-unleashing-financing-dynamic-firms (accessed on 7 September 2023). [7]

ZOiS (2021), "The Republic of Kazakhstan's New Administrative Procedures Code", *ZOiS Spotlight* 25, https://www.zois-berlin.de/en/publications/the-republic-of-kazakhstans-new-administrative-procedures-code. [24]

Notes

[1] Data varies between sources: according to Atameken, between 2019 and 2021 the total number of business inspections has decreased almost 4 times or by 74.6% (from 128 364 to 32 566 inspections), and by 9 times for SMEs (from 93,175 inspections to 10,127); according to the Prosecutor General's Office, the number of inspections for SMEs decreased, by 7 times (from 64,009 to 9,335) between 2019 and 2020, and 6 times between 2019 and 2021 (10,127).

[2] For instance, in Montenegro, the Council of Europe in collaboration with the Centre for Alternative Dispute Resolution has developed such outreach programmes, combining targeted media campaigns with training sessions to increase awareness about alternative dispute resolution procedures in the country (Council of Europe, 2022[39]).

3 Kyrgyzstan

This chapter assesses progress in implementing the three priority reforms identified in 2020, namely streamlining legislation, simplifying the tax code and tax administration and ensuring predictable contract enforcement. It takes into account action to support business activity and economic growth during and after the COVID pandemic and in response to Russia's war in Ukraine. Since 2020, the government has been taking measures to encourage business formalisation, facilitate interactions between the administration and firms through digitalisation, and provide tax incentives in priority sectors, such as tourism, high technologies, and creative industries. The chapter concludes with a series of policy recommendations.

Table 3.1. Summary of priority reform implementation and updated recommendations

2020		2023	
Challenges identified	**Recommendations**	**Implementation assessments**	**Way forward**
Streamline business-related legislation and ensure predictable enforcement	➢ Create physical and online one-stop-shops for SME access to regulatory information ➢ Streamline and digitalise license and permit processes ➢ Legislative consolidation and streamlining	➢ The government's digitalisation efforts have begun to bear fruit, but further streamlining of business-related legislation and predictable enforcement are needed	Ensure consistent implementation of reforms, in relation to digitalisation and business inspections Develop tools to raise firms' awareness of and ability to cope with regulatory changes
Simplify the tax code and tax administration	➢ Further tax stabilisation is needed for business development as well as more support for the business community to comply with the legislation ➢ Revising tax regimes for small firms to address possible disincentives to their growth ➢ Improving the digitalization of the tax administration and increasing the uptake of e-filing	➢ New amendments to the Tax Code, aimed at creating conditions to level the playing field for businesses, but tax administration and policy remain complex and unpredictable	Simplify the tax system by developing a long-term strategy and paying attention to implementation challenges Close the implementation gap by developing a client-oriented approach
Ensure predictable, fair, and efficient contract enforcement	➢ Further improve the justice and ADR systems ➢ Consider becoming a party of the ICSID Convention to provide an additional arbitration option to investors ➢ Strengthen the development of activities of the Business Ombudsman using good practices on transparency and efficient claim process	➢ The judicial system is evolving, but further steps to ensure predictable, fair, and effective enforcement of treaties would be preferable	Strengthen the general dispute resolution system to increase quality of justice, clarity of proceedings and business confidence Resume the functioning and independence of the Business Ombudsman Institute

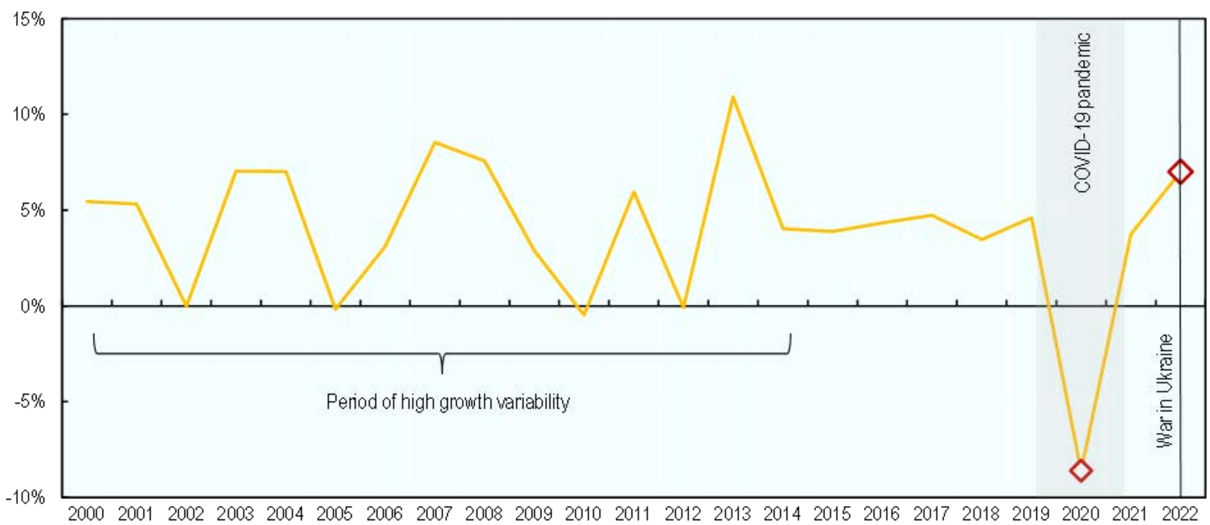
Source: (OECD, 2021[1]), OECD analysis (2023).

Introduction

The economy has so far withstood the shocks of COVID-19 and Russia's invasion of Ukraine

Kyrgyzstan has recorded average annual growth of 3.9% since the beginning of the 21st century, driven mainly by the export of gold and remittance inflows from migrant workers. However, this growth has not been uniform over time and the average rate hides two distinct trends in the development of the economy: from 2000 to 2013, growth was unsteady and fluctuated between 0% and 11%; from 2014 to 2019, less variability was observed (except during the pandemic) and the growth rate stabilised at around 4.2% (Figure 3.1). The COVID-19 pandemic disrupted this relative stability based on remittances and trade and GDP contracted by 8.6% in 2020, the biggest drop in Central Asia (IMF, 2023[2]). Nonetheless, the economy quickly recovered from the crisis and showed a certain resilience, despite the war in Ukraine and the sanctions against Russia, as growth reached 3.7% in 2021 and 7% in 2022 (EBRD, 2023[3]).

Figure 3.1. Kyrgyzstan's real GDP growth (2000-2022)

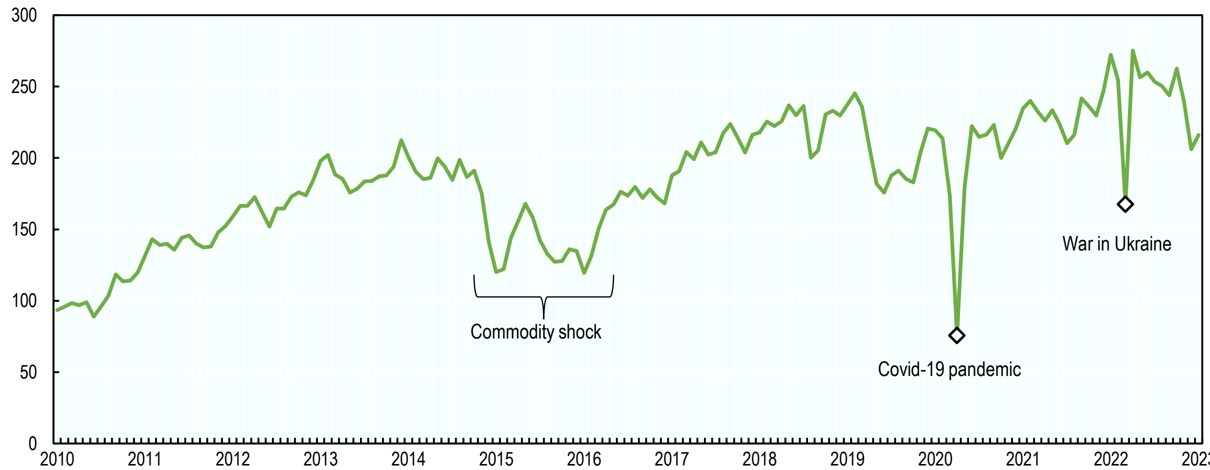


Source: (IMF, 2023[2])

Remittances from labour migrants remain an important growth driver, particularly supporting household consumption. Between 2010 and 2019, they amounted to 29.2% of GDP on average (World Bank, 2023[4]), with approximately 80% originating from Russia (Central Bank of Russia, 2023[5]). Such a dependency on Russia's needs for migrant labour increases Kyrgyzstan's vulnerability, as shown during the 2014-15 crisis and the commodity shock's impact on Russia's economy (Figure 3.2). More recently with the beginning of the war in Ukraine, remittances dropped, but not as abruptly as during the COVID-19 pandemic. Going forward, the impact of sanctions on Russia's economy could have a long-lasting effect on remittances inflows, and therefore negatively affect demand in Kyrgyzstan in the medium term, as there has been a decreasing trend in inflows since late 2022.

Figure 3.2. Inflows of remittances made through the money transfer system (2010-2023)

Million USD

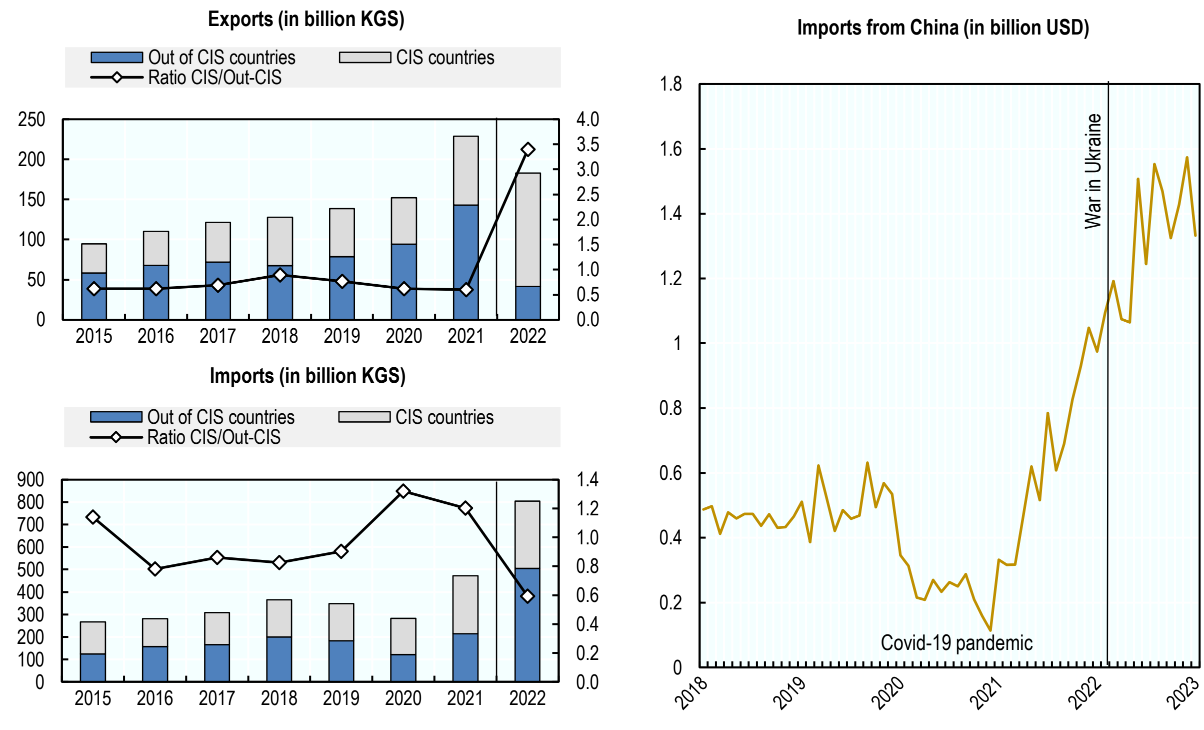


Note: Remittances made through the money transfer system are not exactly equal to total remittances, but account for a large enough share to infer on consequences of economic shocks on inflows.
Source: (National Bank of Kyrgyzstan, 2023[6])

In 2020, the COVID-19 pandemic shook the economy, and the government implemented anti-crisis measures. Public debt rose to 68% of GDP that year, the som depreciated by 19% against the US dollar, and inflation began rising, reaching 14.5% in April 2022 and 16.2% in February 2023 (National Statistical Committee of the Kyrgyz Republic, 2023[7]), driven by high global food and fuel prices (also as a consequence of the war in Ukraine due to supply chains disruptions). The government immediately restricted travel and trade in the country, hampering regional flows of people and goods, and drastically reducing economic activity. The closure of the border with China in 2020 led to a decrease in imports (Figure 3.3) as China is the main foreign supplier of the Kyrgyz economy. Remittances fell sharply but quickly recovered. Yet, the economy recovered relatively quickly and reached its 2019 GDP level in 2022, thanks to economic growth in 2021 and 2022, driven by trade (rebound in exports in 2021), agriculture and gold production.

The war in Ukraine disrupted the economy and considerably changed Kyrgyzstan's trade patterns. Historically, Kyrgyzstan mainly exports gold, which accounted for 49.2% of total exports on average between 2015 and 2021 (Observatory for Economic Complexity, 2023[8]), in particular to Europe. During the same period, 53.8% of total imports came from China (mostly textiles) while 18.3% came from Russia (mostly oil). However, in 2022, because of the war in Ukraine, the structure of trade reversed (Figure 3.3). Both for imports and exports, the ratio of CIS/non-CIS countries inverted, meaning that Kyrgyzstan now exports more to CIS countries than to other countries, and imports more from non-CIS countries than from other countries. At the same time, imports from China, already high in the past, skyrocketed after the pandemic and reached record-high levels in 2023.

Figure 3.3. Recent developments of Kyrgyz trade



Source: (National Statistical Committee of the Kyrgyz Republic, 2023[9]) (General Administration of Customs People's Republic of China, 2023[10])

In 2022, a record number of companies with foreign participation were registered in Kyrgyzstan. The number of new companies with non-residents of the Kyrgyz Republic that were registered or re-registered in 2022 was 2,609, almost twice as many as in 2021. At the same time, 771 more companies with foreign participation were registered in January-March 2023 (Data Insider, 2023[11]). This increase is likely due to the significant inflow of Russian entrepreneurs resettling in Kyrgyzstan.

To help the government strengthen the business environment and create conditions to level the playing field between firms, the OECD conducted research in 2019-20 into the legal environment for business and pointed to the need for further structural reforms in three policy domains: the operational environment for businesses, the tax system and contract enforcement.

The 2020 OECD report identified a need for improved implementation of reforms in three priority areas

Streamline business-related legislation and ensure predictable enforcement

(OECD, 2021[1]) **found that the number of licenses remained significant, and the licensing process itself had been complicated by the limited digitalisation of most procedures and the lack of a consolidated one-stop shop (OSS) for entrepreneurs**. The government has worked to shift licenses and permits into an online format, supported by the Tunduk platform. Overall, it was recommended to consider codifying key regulations, permits and licenses, as was done in other Central Asian countries. For the SMEs in the country, business inspections also remained an important problem, with businesses calling for a moratorium on inspections during the pandemic their only relief.

Simplify the tax code and tax administration

In 2020, the tax system had already undergone significant reform since 2018 in order to modernise tax administration and harmonise the burden between businesses of all sizes. Whilst the government reduced the burden on businesses by postponing by six months the submission of tax declarations for businesses and removing tax penalties and sanctions, the tax system remained complicated and unpredictable. A simplified regime and patent system for small businesses supported entrepreneurs, but they have also discouraged businesses from growing and shifting to the normal regime. It was recommended to consider revising both regimes to incentivise businesses to grow. Additionally, digitalisation of the tax administration can be used as one of the ways to improve transparency and lower compliance costs for firms.

Ensure predictable, fair, and efficient contract enforcement

Procedures for dispute settlement for all investors, including SMEs and foreign investors, were clearly set out in the Civil Procedure Code, the Law on Investment and model law on international commercial arbitration of UNICTRAL. The Law on Arbitration Courts recognises alternative dispute resolution (ADR) mechanisms. Moreover, with the help of several donors, an International Arbitration Court was created.

However, the 2020 assessment found that the government had not established specialised economic courts, which made contract enforcement difficult and expensive for businesses. In addition, 95% tax disputes in courts were settled in favour of the authorities due to the lack of independence of the courts (OECD, 2021[1]). This problem was exacerbated by the low rate of digitalisation and constant changes in priorities regarding the development of court system.

To support the protection of business rights it was recommended to further strengthen the Business Ombudsman (BO) by the use of good practices on transparency and efficient claim process, and through the establishment of a mechanism to present the results of the work of BO to the Prime Minister and the Cabinet.

Assessing implementation progress since 2020

Since 2020, Kyrgyzstan's reform efforts have mainly focused on advancing the digitalisation of public services and tax collection. Data digitisation is underway, the "Tunduk" portal has been launched, the principle of "single window" in interaction with business is being applied. Yet according to business associations and SME representatives who participated in the assessment process, the business environment has not been improving. There have even been some setbacks. After the pandemic, the government has had less fiscal room for manoeuvre, including for adequate support of business, while a deterioration of communication between the government and businesses did not contribute to a more targeted use of already limited funds. As a result, measures taken by the state in the field of taxation and business regulation have brought mixed results, and there remains much to do to ensure predictable, fair, and efficient contact enforcement.

The following sections of this chapter provide an overview of Kyrgyzstan's progress with respect to the three priorities identified in 2020, and suggest ways forward, taking into account new priorities following the pandemic and the changed regional context (Table 3.1).

Priority 1: Digitalisation efforts have begun to bear fruit, but further streamlining of legislation and predictable enforcement are needed

Increased digitalisation of procedures has eased the administrative burden for firms

The government has established a one-stop shop to simplify business procedures

Positive changes can be observed in the operational environment for SMEs. By Order of the Cabinet of Ministers, in November 2021 the first one-stop shop (OSS) for entrepreneurs started to function in Bishkek. OSS have opened in Osh and Osh region since April 2023. This allows entrepreneurs to register their businesses, obtain licenses and permits and submit tax declarations in one place. In addition to the Tax Service, the OSS offer services from the Ministry of Justice, the Ministry of Transport, the Department of Precious Metals, the Financial Market Regulation and Supervision Service, services related to foreign trade and others (State Tax Service under the Ministry of Finance of the Kyrgyz Republic, 2021[12]). Moreover, the OSS provide entrepreneurs with consulting support through call centres.

“Tunduk” platform also continues to support the digitalisation of licensing and government services

Since 2020, in order to improve the quality of public services provided electronically, the state enterprise "Tunduk" has begun modernising the state portal of electronic services. New databases and information systems of governmental bodies are being integrated into it. Digital tools, such as a cloud-based electronic signatures or biometric passports, are now being used to access electronic services, the former being issued free of charge at public service centres. In addition, the mobile version of the application is now available, where services can be accessed online through a mobile device. The portal is accessible throughout the country, including in the regions remote from the capital. Within the framework of the development and implementation of the State Portal of Electronic Services, as well as to improve the quality of state and municipal services, "Tunduk" trained 120 employees and 83 managers of 50 government agencies to work on the new portal.

New enforcement mechanisms have started to function

Since 2021, the Business Protection Advisory Council has been created in partnership with the Business Ombudsman. It is chaired by the Attorney General, and the work of the Advisory Council is aimed at protecting the rights of entrepreneurs and investors, as well as at creating conditions for the development of businesses in the Kyrgyz Republic. Since its inception, the Prosecutor General's Office has worked with the business community and the OSCE Programme Office in Bishkek to develop new tools to protect businesses. In particular, the automated information system "Registration of inspections of business entities" was created to enable the registration of business inspections in an electronic format. Also, with the support of the Council, a mobile application "Protection of Business" was developed, which is aimed at eliminating unwarranted interference of law enforcement and tax authorities in business activities. Going forward, the Council plans to include all types of tax control in the list of inspections registered by prosecutors, as well as to work on ways to prevent the initiation of criminal cases on issues to be resolved with civil and administrative orders, and to fight smuggling.

Deteriorating business consultations and hasty implementation create complexity and unpredictability for firms

Businesses lack awareness of regulatory changes and opportunities to participate in policy consultations

The government is making efforts in the area of licensing, but they are not always carried out on the basis of public consultations with businesses nor are Regulatory Impact Analysis (RIAs) conducted. In 2022, a new draft law regulating public participation in the law-making process was published, reducing the review period for bills from 30 days to no less than 15 days (Jogorku Kenesh of the Kyrgyz Republic, 2022[13]). Such a reduction gives little time for businesses to get acquainted with, and provide comments on, draft laws. In addition, businesses have expressed concern about licensing decisions that were made without conducting a RIAs. Results of some regulatory impact assessments have not been considered in making a final decision, such as in the case of the creation of a state monopoly on ethyl alcohol production, which businesses opposed, arguing that it contradicts several existing laws, as well as international agreements in the field of competition, consumer protection, and investment.

Recently, there have been normative acts adopted without conducting an analysis of their regulatory impact. The legislative drafters refer to numerous exceptions to the rules, including that under conditions of *force majeure*, RIA is not carried out.

Business inspections are a key issue for implementation

Despite numerous moratoria on inspections, implementation issues remain a major concern for businesses. A three-year moratorium on inspections of business entities ended in 2021 and a temporary one was introduced in 2022, to run until December 2023. It is, however, difficult to say to what extent such measures are stimulating for businesses, as the latter are still subject to unscheduled inspections. Businesses have indeed repeatedly expressed concerns about the growth of inspections and the growing involvement of the prosecutor's office in tax policy. During the 2021 moratorium, the Law on Inspections only applied to scheduled inspections, which allowed state inspectors to conduct unplanned inspections, as well as tax audits. Since 2021, in addition to the State Tax Service, the Prosecutor's Office has the mandate to initiate scheduled and unscheduled tax inspections and other verification activities.

The frequent revision of legislation on inspections does not reduce the number of supervisory bodies, but in some cases increases it. In 2021, the State Inspectorate of Environmental and Technical Safety was restructured and its functions were transferred to sixteen different controlling bodies, which has sometimes resulted in a duplication of mandates: four government agencies are now responsible for environmental inspections (International Finance Corporation, 2021[14]). Thus, the increase in the number of inspections is mainly a problem of an overlap of functions across government agencies, with more than 800 different administrative procedures overseen by 25 government bodies (International Finance Corporation, 2021[14]).

Incomplete digitalisation requires a doubling of procedures in person

The number of licenses and permits that can be obtained online remains limited. The government has identified the optimisation and digitalisation of licensing and permits as one of the goals of the National Development Programme through 2026. By order of the government in 2021, a single electronic registry of permits was created. The latest available information states that only about 10 out of 190 licenses and permits can be obtained online (Ministry of Economy and Commerce of Kyrgyz Republic, 2022[15]). Weakness in promoting digitalisation may be due to lack of ownership among the government and the absence of a unified strategy for the digitalisation of public service provision. According to business associations, most of the services still require personal contact, which counteracts the state's efforts to reduce time spent dealing with administrative issues.

Further improving the operational environment for firms requires consistent implementation and better involvement of the private sector in the regulatory process

The government should focus on ensuring consistent implementation of reforms, in particular in relation to digitalisation and inspections

The priority should be set on significantly accelerating the digitalisation of all licensing and permits and widening the network of OSS for entrepreneurs in the country, especially in remote areas. The digitalisation of licenses and permits for SMEs could help reduce their exposure to excessive red tape, given their limited capacity to deal with public authorities' differing opinions or interpretations of regulations when compared to large domestic or international businesses. The OECD indeed finds that administrative compliance costs per employee in some countries can be at least over five times higher for the smallest SMEs than for the largest companies (OECD, 2021[16]). OSS for entrepreneurs, which now operate in Bishkek, Osh and Osh region, should be rolled out across the country and strive to become the single point for all services for businesses, including licensing.

It would be useful for the government as a whole to monitor the implementation of regulations and policies and evaluate their effectiveness on an ongoing basis. Capacity building needs to be pursued through training of civil servants on changes in regulation, with on-the-job learning when possible. Some training in evaluation methods is useful for most staff members involved in policy or regulatory areas, since it can enhance their ability to identify and take into account various impacts and help avoid unintended consequences (OECD, 2020[17]). For instance, in Kazakhstan, in 2022 the National Chamber of Entrepreneurs Atameken together with the Ministry of National Economy conducted a series of trainings of civil servants on the changes introduced to the regulatory framework. In parallel, the government should also develop effective channels for firms on cases of non-compliance, for example ona dedicated section of Tunduk's website, as well as a process for the authorised body to review these appeals on an ongoing basis.

Attention should be paid to conducting a functional analysis of government agencies before restructuring, with the aim of reducing and optimising the number of inspecting bodies. Ultimately, the government could consider reducing the number of inspection bodies and review the scope of their competences. As a result of the latest restructuring, the number of inspecting bodies has increased, which is a worrying factor for entrepreneurs. Strengthening the capacity of risk-based approaches in all areas of inspections, including tax controls, could help reduce the number of inspections and optimise the resources required for it. Moreover, there is need for the development of an online system for inspections which will be transparent so that business can access information regarding planned inspections.

The government should develop tools to raise firms' awareness of and ability to cope with regulatory changes

Communication and consultation channels with the private sector could be improved by better publicising consultations and regulatory changes to businesses and business associations, for instance through a dedicated page of the websites of the competent authority and sectoral business associations. As deterioration of trust was one of the main concerns reported during OECD interviews with entrepreneurs and business associations in Kyrgyzstan, the government should pay special attention to involving SMEs in major regulatory changes. Engaging business associations and firms in a systematic and planned way can rebuild trust in the review process and give a sense of "ownership" of the outcomes. When allocating resources for public consultations, it is suggested to take into account the experience of OECD countries, which shows that the extent of consultation is generally greater in the later than the earlier stages of regulatory development, although the number of countries engaging with stakeholders at an early stage has increased (OECD, 2018[18]).

Competent authorities should also train and inform firms about new regulatory requirements and digital skills through outreach programmes and targeted and thematic trainings. OSS could provide a platform for the trainings for the SMEs. Moreover, government officials should actively participate in the events organised by international donors and international organisations who provide specific trainings for business, for example trainings for women entrepreneurs organised by the EBRD.

Priority 2. New amendments to the Tax Code level the playing field for businesses, but tax policy and administration remain complex and unpredictable

The government has taken steps to simplify the Tax Code and tax administration

Since the original OECD report in 2021, major changes have been made to the country's Tax Code. Positive aspects of the changes in the Tax Code (in force from January 2022) include better VAT offset and returns, digitalisation, and tax breaks for the green economy and several other sectors. At the time of writing, new amendments to the Tax Code have been introduced, which aim to further improve the conditions to level the playing field for businesses and reduce the shadow component of the economy. It seems that negotiations and consultations with the business community have borne fruit and some of the wishes of the business community have been reflected in the amendments (International Business Council, 2023[19]). For instance, among other important proposals of the International Business Council, the proposal for the exemption of the maintenance of cash registers from VAT services was adopted. Additionally, tax rates were reduced for tourist services to 2-4% (from 4-6%) and public catering (restaurants and cafes) to 2-6% (from 8%) to support the tourism sector. Several VAT exemptions were introduced on the purchase of equipment for tax administration purposes (cash registers, POS-terminals, devices with a software cash register with a built-in receipt printer, which is required by law).

> *Together with changes in the tax rates the government has also improved some aspects of tax administration*

Electronic filing has been introduced to facilitate tax administration. A "single window" for taxpayers began operations in 2021 and is available in 52 tax authorities and four service centres, including the Taxpayers Service Centre in Bishkek (Ministry of Economy and Commerce of the Kyrgyz Republic, 2023[20]). This service has significantly reduced the time citizens require to fulfil their tax obligations and has also reduced physical contact between taxpayers and tax officials, which helps reduce corruption risks. According to those procedures, individual entrepreneurs, including those working by patent (- a document attesting that the company benefits from the simplified taxation system, provided its revenue does not exceed 8 million soms), must file declarations only electronically through a personal account on the website of the State Tax Service.

In accordance with the changes in tax regulations several projects are under implementation to improve the efficiency and digitalisation of the tax administration. With the assistance of the World Bank until 2025, the State Tax Service will be actively working on operational development, including the automation of business processes to improve the efficiency of tax administration and reduce the compliance burden on taxpayers (The World Bank, 2020[21]). Today there are six information systems in Kyrgyzstan for tax procedures: electronic invoices; a system of control over the movement of goods imported from the Eurasian Economic Union countries; labelling of goods; electronic completion of bills of lading; electronic cash registers, and e-patent, which allows users to generate a combined patent and insurance form. A special tax regime for e-commerce activities has also been introduced.

Attempts have also been made to support businesses and move from a punitive to a preventive approach to tax administration. This approach is welcomed by entrepreneurs, but at the same time more comprehensive explanatory work is required.

Box 3.1. Recent changes in the tax policy of the Kyrgyz Republic

The most recent amendments to the Tax Code were made on 3 April, 2023. Overall, the law provides for several measures to support businesses and investors by introducing special tax regimes and exemptions. For example:

- To support small enterprises, it provides for an extension of the single tax-based regime without a limitation on revenue (previously up to 30 million soms, around 300k EUR), which will contribute to the expansion of activities without the need to "split the business" in order to remain in a special tax regime; an indefinite tax exemption for small entrepreneurs with annual revenues up to 8 million soms who fulfil requirements to use cash registers as a stimulus to formalise their activities; and the establishment of 0.1% tax for entrepreneurs in the markets, whose annual turnover does not exceed 100 million soms.
- It also introduced a reduction of the single tax rate for trade from 4% for cash payment and 2% for cashless payment to: 0,5% - with annual turnover up to 30.0 million soms; 1% - with the turnover from 30 million soms to 50 million soms.
- Residents of newly created Creative Industries Park are granted a special tax regime (in 2023 and 2024 - 0,5%, in 2025 and 2026 - 1%, from 2027 - 2%), while residents of the High Technologies Park are exempt from the payment of "Reverse VAT".
- The new amendments also introduced remedies such as the postponement of the introduction of penalties for failure to use electronic waybills until 1 January 2024; to address issues with cash registers and insufficient preparation of businesses to use them, the law also provides for a reduction in fines:
    - for the first offense - a warning,
    - for the second - 500 soms for individuals and 5 thousand soms for legal entities, and
    - for the subsequent - 3 thousand soms for individuals and 13 thousand soms for legal entities.

Finally, if fines are paid within 30 days, the amount due is reduced by 70%.

In addition, the Code provides for the granting of exceptional tax provisions through *ad-hoc* investment agreements concluded between the Cabinet of Ministers and investors. However, such a measure might in practice add complexity and unpredictability to the tax system as it prevents the establishment of a level-playing field among firms and reduces incentives for the government to review the general tax framework for investors.

The business community is pressing for the introduction of measures to stimulate the non-cash circulation of money, to encourage the use of preventive measures over punitive ones; to exclude double liability for the non-use of invoices; and to adopt a classifier of products by type of economic activity for further differentiated regulation.

Source: (Ministry of Economy and Commerce of the Kyrgyz Republic, 2023[20])

Fiscal policy has focused on digitalising services and providing incentives to the digital sector

To stimulate the inflow of highly skilled workers in the digital economy, the Digital Nomad project is being implemented in the country until the end of 2023. This status allows IT specialist “nomads” to be exempted from residence registration and from obtaining work permits. Such specialists also receive a personal individual number that allows them to carry out business activities for up to 12 months. The special status can be granted to those working in software development, information technology, export of media arts, including digital arts, animation, etc. from Armenia, Azerbaijan, Belarus, Kazakhstan, Moldova, and the Russian Federation. This status has already been granted to more than 1 000 citizens. If the digital nomads register in the High Technology Park, they are subject to a special favourable tax regime.

Tax policy and administration policy remain complex and unpredictable for firms

The amendments to the Tax Code have increased implementation challenges for SMEs in particular

As the government has repeatedly stressed, one of the main purpose of changes to the tax legislation is to widen the tax base and encourage private sector formalisation. In 2019, about 24% of firms surveyed reported informality as the top constraint to the development of their business, and 39% ranked it as a major constraint. While informality has decreased over time (from approximately 42% of GDP in 1993 to 24% in 2017) (World Bank Group, 2021[22]), the informal labour market still employs 71.8% of workers in such sectors as trade and services and construction (Friedrich-Ebert-Stiftung, 2021[23]). According to OECD interviewees, businesses are not optimistic about recent changes in tax legislation, which provide for lower rates, but do not provide incentives and measures to encourage entrepreneurs to formalise, as the different tax regimes do not decrease the complexity of navigating the tax administration.

Thus, despite several changes aimed at helping SMEs, small businesses face uncertainties and difficulties in adapting to the changes, which sometimes entails additional financial costs. The main obstacle relates to the lack of awareness of entrepreneurs and the lack of explanatory work on changes introduced. Changes to the Tax Code have been adopted without the broad participation of business and have lacked awareness-raising initiatives to facilitate implementation. For example, the mandatory introduction of cash registers for small businesses starting 2022 came as a surprise as it was immediately implemented and caused additional, unforeseen expenses for many businesses.

Businesses remain unaware of digital tax administration tools, while the implementation of reforms remains incomplete and sometimes inconsistent

Digitalisation, which should simplify the interaction of businesses with the tax authorities, is sometimes seen as a burdensome procedure, according to firms interviewed by the OECD[1]. Existing systems present difficulties for some taxpayers due to the duplication of information in different systems, as well as a lack of awareness of entrepreneurs about their existence and ways of use. As of 1 January 2023, the paper patent system was eliminated, and patents can only be received electronically via personal accounts on the State Tax Service portal. However, due to limited promotion efforts and lack of understanding of their tax obligations in the season of tax returns, many still come to the tax office in person. Tax officers must issue electronic patents to them via their computers. In addition, businesses still come to submit declarations in paper form due to insufficient information during the declaration period, except in some regions where there is no means of submission other than paper. The mobile application of the State Tax Service, which has the function of submitting tax declarations in the app experiences frequent disruptions and is underused, probably also due to a low awareness of the population about its benefits.

The administration still lacks a client-oriented approach when dealing with businesses

OECD interviewees report a persisting lack of client-oriented approach and transparency from the tax authorities. The Ministry of Finance and National Statistical Committee do not publish publicly available reporting on state budget expenditures and provide incomplete information on their websites (US Department of State, 2022[24]). Another important concern relates to the interpretation of tax law and its application. With the introduction of the new Tax Code in 2022, the Ministry of Economy and Commerce has been instructed to provide written explanations of the application of the Tax Code and tax legislation in general. Such a function is binding on tax officials, but in practice, the absence of an elaborated methodology to ensure uniform interpretation of the text has resulted in the issuing of various, and sometimes conflicting, directives by the tax authorities.

Further improving the tax system requires a long-term vision and greater attention to taxpayers' concerns

Simplify the tax system by developing a long-term strategy

Further development of the tax system requires the drafting of a single policy document, which will set out the basic principles and objectives of the country's tax policy. Numerous changes in the Tax Code made in recent years have created confusion. The basic concepts and principles of the tax system are not formulated within the framework of state policy and are often adjusted for political and economic reasons. Despite the fact that the Strategy for the Development of the Tax Service under the Ministry of Finance for 2023-2025 indicates plans for the development of tax administration, it is insufficient, because the development of the tax system involves many other government agencies and it is necessary to have a common strategy for all (Ministry of Finance of the Kyrgyz Republic, 2022[25]). Therefore, it is important to have a document with a five to ten-year horizon setting out the main directions for tax reform. Moreover, in designing a long-term strategy, it is important to be clear on communication and engagement objectives. Such objectives are also helpful to evaluate the outcomes of the strategy. They could include objectives such as improving taxpayers' understanding, building trust in the tax system, and making it easier to comply with (OECD, 2023[26]).

The government should better communicate changes to the Tax Code to reduce implementation challenges for entrepreneurs. Tax administrations may review the various available channels and their effectiveness, alone or in combination, at reaching the SME population and/or relevant sub-sectors. This could also include consideration of those in the SME segment that do not have online access or do not want to use it (OECD, 2023[26]). Among tools for the awareness-raising, text messages could be used in Kyrgyzstan, as mobile penetration in the country, even in the remote regions, is high and smartphones are the only technology some small firms have. Thus, short texts or recorded messages can be effective in garnering attention. It should not be overused, as it can cause frustration with some customers being susceptible to risks from fraudsters. For example, tax authorities in Uzbekistan have already been using social media such as a Telegram to relay information to SMEs. But at the same time, classic explanatory channels of communication, like the State Tax Service's website and call centres, should remain the main source for more in-depth information on specific topics and, if necessary, provide links to other sources.

Close the implementation gap by developing a client-oriented approach

Improving the client-oriented approach when dealing with businesses can contribute to a better implementation of reforms. Given the size of the informal sector, the authorities should design targeted programmes to change behaviours and widen the tax base. Raising awareness of the societal benefits of public spending enabled by tax is an aspect to consider. In several countries, the targets of campaigns for formalisation are not informal businesses, but rather their customers. The aim is to change their behaviour by demanding tax receipts, thereby compelling sellers to adapt. When people avoid buying goods from the informal sector, sellers start to comply with tax laws (OECD, 2021[27]). A case in point is the introduction of a cashback system in Uzbekistan through the Soliq application, which has proved very useful in increasing the number of formal businesses (see chapter on Uzbekistan). Other campaigns could aim at incentivising customers to adopt desirable behaviours such as collecting receipts to receive tax deductions or participate in lotteries.

The tax authorities should conduct extensive consultations with the business community prior to developing changes to tax legislation. Preliminary consultations should become systematic, with the government providing full information on the additional net costs and burdens on taxpayers as a result of the changes. In order to receive the greatest number of comments, documents should be published with explanations if the language is too complex. Moreover, it is important to test new fiscal tools in a pilot phase for SMEs before implementation (*e.g.,* cash registers). It is also important in this regard to provide ICT trainings for small entrepreneurs, especially in the markets (*bazaars*) taking into account the importance of their practicality and efficiency.

Finally, the government should introduce mandatory regulatory impact assessment (RIA) of new tax regulations, with a focus on the expected impact on SMEs. Thus, mandatory RIAs could be part of a comprehensive long-term tax strategy. It is worth keeping in mind that RIA alone will never be successful in improving the quality of regulation, unless coupled with additional regulatory reform tools such as the use of consultation, the adoption of a "policy cycle" approach with the use of monitoring and *ex-post* evaluation alongside regular reviews of existing legislation (OECD, 2020[28]).

Priority 3. The judicial system is evolving, but further steps are needed to ensure predictable, fair and effective enforcement of treaties

The government has introduced some reforms to the judicial system

To improve the quality of justice and create easy access to it for citizens, a system of remote proceedings in the Supreme Court of the Kyrgyz Republic will be introduced. Such a measure aims to remotely consider criminal, civil, economic, and administrative cases using technical means of communication, electronic proceedings, as well as simplified (written) consideration of cases in the court of cassation**.**

In 2022, one of the decisive steps in reforming the judiciary was the rotation of judges for the first time in the history of the country. Judges from the southern regions were rotated to and from the northern regions of Kyrgyzstan at the level of district, city and oblast judges. The rotation of judges is expected to promote independence from political pressure from certain institutions of power, especially the prosecutor's office and national security bodies (Supreme Court of the Kyrgyz Republic, 2022[29]).

In a move to improve the investment climate, in 2022, the new Tax Code created arbitration courts where tax disputes with the government can be resolved, rather than in a trial court. Previously, almost 90 percent of tax cases were decided in favour of the state under the trial court system. The hope of the arbitration court system is that it will be more independent and allow for disputes to be resolved faster (US Department of State, 2022[24]).

Economic and non-economic cases are now treated separately in courts

The resolution of economic disputes from inter-district courts was transferred to the jurisdiction of district and city courts in 2020. Inter-district courts, which have become administrative courts as a result of these changes, will only deal with administrative cases. Such changes aim to contribute to a more efficient resolution of economic disputes, as the courts have become "closer" to the population and to businesses with increased specialisation of courts. In general, the reform is aimed at optimising the functioning of the judicial system. It provides for the elimination of the practice of unjustified return of cases for a new trial and simplifies the procedure for the consideration of applications for actions of bailiffs. Recent changes in the Tax Code introduced the consideration of individual tax disputes by the arbitration court, while previously tax legal relations were regulated only by the tax authorities and the judiciary.

However, the judicial system remains a key obstacle for business development and investment

A justice system reform remains pending, while businesses suffer from undue pressures from some judicial bodies

Despite some attempts to reform the judicial system, it is difficult to trace the systematic nature of these changes. The long-awaited reform of the judiciary, one of the 2026 priorities of the National Development Programme of the Kyrgyz Republic is still pending. Despite the announced plans of the government, including the creation of a single investigative body combining the functions of investigation carried out by the relevant departments of the Ministry of Internal Affairs, the Prosecutor General's Office, and the State Committee for National Security, several problems in the process of interaction between business and law enforcement agencies remain unresolved. Businesses still report the unjustified initiation of pre-trial proceedings, subsequently terminated for lack of evidence, and unjustified seizures of property and the refusal to return it. The unlawful dissemination of information that discredits the reputation of businessmen, numerous arrests of entrepreneurs and the refusal of alternative measures of accountability and non-transparency of procedures carried out by law enforcement bodies do not increase trust between the government and business (Business Ombudsman Institute of the Kyrgyz Republic, 2023[30]).

Businesses, especially SMEs, remain poorly aware of available dispute resolution tools

SMEs have limited awareness of mediation or arbitration mechanisms. Despite the EBRD project to develop mediation, the latter remains popular for civil cases but not for commercial disputes (Anadolu Agency, 2022[31]). Instead of mediation, SMEs prefer to use arbitration mechanisms, which are more costly. Changes concerning the consideration of individual tax disputes by the arbitration court became one of the positive innovations of the Tax Code, but businesses are not satisfied with the remaining provision on the consideration of complaints against territorial bodies of the State Tax Service. Thus, they are being transferred to the central office of the State Tax Service. This is an inefficient mechanism, which contributes to a conflict of interest. Instead, it could be useful to centralise all tax-related appeals in the the Ministry of Economy and Commerce and consider them by a collegial mechanism with the participation of government agencies, business representatives and the expert community in a transparent way. For example, in Kazakhstan, in July 2021, e-Otinish, an online platform and mobile app was created to receive and process appeals of individuals against any government body (see chapter on Kazakhstan).

Further improving contract enforcement requires increasing trust in the judicial system through more dialogue and openness to innovation

Strengthen the general dispute resolution system to increase quality of justice, clarity of proceedings and business confidence

Introducing a clear distinction of cases in the courts to level out the categorisation of economic cases as general cases, could be a first step preceding the establishment of economic courts. Despite the government's attempt to segregate cases by court level, businesses still mostly resort to arbitration courts. It is therefore difficult to assess the effect of this reform on entrepreneurs.

The decriminalisation of economic cases in Kyrgyzstan requires introducing a transparent hearing procedure and pre-trial dispute resolution dispositions. The gradual decriminalisation of economic affairs could be implemented following the example of neighbouring Kazakhstan. For instance, the new Administrative Procedure Code of Kazakhstan shifted the burden of proof to the state body in disputes and allowed courts to examine all circumstances relevant to the case without limiting themselves to the evidence submitted by the parties.

In parallel with judicial reforms, the State needs to work on strengthening the dispute resolution system as a whole. Business confidence in arbitration courts is growing, which is a good sign, and this momentum should be used to stimulate this trend by developing clear methodologies describing which cases can be heard where. At the same time, it is proposed to develop mechanisms to encourage the use of existing and proven effective mediation and arbitration institutions.

> *In the light of recent developments regarding the BO, the government should maintain the functioning and independence of the BO*

The government should re-establish the Business Ombudsman Institute. Given the role of the BO in building a dialogue between businesses and the State, as well as in helping business to understand the law and build cases in the courts, the BO office could be rebuilt as a part of existing business chambers (e.g., Kazakhstan, Uzbekistan). At the same time, it is vital that the independence and impartiality of the office is balanced through the law and source of funding.

Secondly, to maintain a relationship of trust with business it is important to preserve the existing roles of the BO in governmental advisory bodies. As it was indicated by the BO itself, the Business Protection Advisory Council aims to build an effective mechanism for interaction between the state and the business community in protecting the rights of entrepreneurs and investors, whereas the Monitoring group under the Supreme Court is a good initiative in bringing the voices of the business community in reforming the judicial system and law enforcement practice. These platforms have played an important role for businesses in many aspects.

References

Anadolu Agency (2022), *Mediation: Kyrgyzstan's Experience in Resolving Disputes Without Court*. [31]

Business Ombudsman Institute of the Kyrgyz Republic (2023), *СИСТЕМНЫЙ ОТЧЕТ*, https://boi.kg/media/pdfs/810f156f-f1aa-4629-a4c4-f09cc10272d4.pdf. [30]

Business Ombudsman Institute of the Kyrgyz Republic (2022), *ОТЧЕТ БИЗНЕС-ОМБУДСМЕНА ЗА IV КВАРТАЛ*, https://boi.kg/media/images/3f07adc6-420d-47da-a87f-e7ae5dfbf597.pdf. [33]

Central Bank of Russia (2023), *External Sector Statistics*, http://www.cbr.ru/eng/statistics/macro_itm/svs/. [5]

Data Insider (2023), *Record number of companies with foreign participation appeared in Kyrgyzstan in 2022*, https://www.osoo.kg/report/non-resindent-legal-entities-2022/. [11]

EBRD (2023), *Regional Economic Prospects*, EBRD, London, https://www.ebrd.com/what-we-do/economic-research-and-data/rep.html. [3]

Friedrich-Ebert-Stiftung (2021), *ANALYSIS OF THE INFORMAL ECONOMY IN KYRGYZSTAN: Through social justice for workers, to sustainable development in the country*, https://library.fes.de/pdf-files/bueros/bischkek/18022.pdf. [23]

General Administration of Customs People's Republic of China (2023), *Statistics*, http://english.customs.gov.cn/statics/report/monthly.html. [10]

IMF (2023), *World Economic Outlook Database*, IMF, DC, https://www.imf.org/en/Publications/WEO/weo-database/2023/April. [2]

International Business Council (2023), *Business recommendations to the draft amendments to the Tax Code discussed at the Economy Ministry*, https://www.ibc.kg/en/news/ibc/6123_business_recommendations_to_the_draft_amendments_to_the_tax_code_discussed_at_the_economy_ministry_. [19]

International Finance Corporation (2021), *Kyrgyz Republic – Inspection Reform: The Reform Process (2006-2019): What Can We Learn?*, IFC, Washington DC, https://www.ifc.org/wps/wcm/connect/145985d8-d571-4661-b51b-75ac94f17e53/Inspection+Reform+Case+Study_KR.pdf?MOD=AJPERES&CVID=ntEi3ad. [14]

Jogorku Kenesh of the Kyrgyz Republic (2022), *On the draft law "On Amendments to the Law of the Kyrgyz Republic "On normative legal acts of the Kyrgyz Republic*, http://kenesh.kg/ru/draftlaw/608581/show. [13]

Ministry of Economy and Commerce of Kyrgyz Republic (2022), *A single electronic registry of permits will minimize contacts between government agencies and the private sector*, https://mineconom.gov.kg/ru/post/8118. [15]

Ministry of Economy and Commerce of the Kyrgyz Republic (2023), *JOGORKU KENESH*. [34]

Ministry of Economy and Commerce of the Kyrgyz Republic (2023), *On the new tax policy of the Kyrgyz Republic: the position of business and government*, https://mineconom.gov.kg/ru/post/9086. [20]

Ministry of Finance of the Kyrgyz Republic (2022), *Strategy for the Development of the Tax Service under the Ministry of Finance of the Kyrgyz Republic for 2023-2025*, https://www.sti.gov.kg/docs/default-source/other/%D1%81%D1%82%D1%80%D0%B0%D1%82%D0%B5%D0%B3%D0%B8%D1%8F-%D0%B3%D0%BD%D1%81-%D0%BD%D0%B0-%D1%80%D1%83%D1%81%D1%81%D0%BA%D0%BE%D0%BC.pdf?sfvrsn=2. [25]

National Bank of Kyrgyzstan (2023), *Statistics*, https://www.nbkr.kg/index1.jsp?item=1785&lang=ENG. [6]

National Statistical Committee of the Kyrgyz Republic (2023), *International economic activity*, http://www.stat.kg/en/statistics/vneshneekonomicheskaya-deyatelnost/. [9]

National Statistical Committee of the Kyrgyz Republic (2023), *Prices and tariffs*, http://www.stat.kg/en/statistics/ceny-i-tarify/. [7]

Observatory for Economic Complexity (2023), *Kyrgyzstan Country Profile*, Observatory for Economic Complexity, Cambridge, MA, https://oec.world/en/profile/country/kgz. [8]

OECD (2023), *Communication and Engagement with SMEs: Supporting SMEs to Get Tax Right*, OECD Forum on Tax Administration, OECD Publishing, Paris, https://doi.org/10.1787/f183d70a-en. [36]

OECD (2023), *Communication and Engagement with SMEs: Supporting SMEs to Get Tax Right*, OECD Forum on Tax Administration, OECD Publishing, Paris, https://doi.org/10.1787/f183d70a-en. [26]

OECD (2021), *Building Tax Culture, Compliance and Citizenship: A Global Source Book on Taxpayer Education, Second Edition*, OECD Publishing, Paris, https://doi.org/10.1787/18585eb1-en. [27]

OECD (2021), *Comprehensive redesign of the licensing system in Romania: Enhancing the business environment in Romania through industrial and manufacturing licensing simplification*, https://www.oecd.org/economy/surveys/enhancing-the-business-environment-in-romania-through-industrial-and-manufacturing-licensing-simplification.pdf. [16]

OECD (2021), *Improving the Legal Environment for Business and Investment in Central Asia*, OECD Publishing, https://www.oecd.org/eurasia/Improving-LEB-CA-ENG%2020%20April.pdf. [1]

OECD (2020), *Regulatory Impact Assessment*, OECD Best Practice Principles for Regulatory Policy, OECD Publishing, Paris, https://doi.org/10.1787/7a9638cb-en. [28]

OECD (2020), *Reviewing the Stock of Regulation*, OECD Best Practice Principles for Regulatory Policy, OECD Publishing, Paris, https://doi.org/10.1787/1a8f33bc-en. [17]

OECD (2018), *OECD Regulatory Policy Outlook 2018*, OECD Publishing, Paris, https://doi.org/10.1787/9789264303072-en. [18]

State Tax Service under the Ministry of Finance of the Kyrgyz Republic (2021), *One-Stop Shop in Bishkek since opening provided tax services to 1.3 thousand taxpayers*, https://www.sti.gov.kg/news/2021/12/15/sop-v-bishkeke-so-dnya-otkrytiya-okazal-nalogovye-uslugi-1-3-tys-np. [12]

Supreme Court of the Kyrgyz Republic (2022), *Rotation of judges is already bearing fruit - expert*, http://sot.kg/post/rotatsiya-sudej-uzhe-daet-svoi-plody-ekspert. [29]

The World Bank (2020), *Kyrgyz Republic to Improve Effectiveness of Tax Administration and Modernize Statistical System with Support from World Bank*, https://www.worldbank.org/en/news/press-release/2020/02/28/kyrgyz-republic-to-improve-effectiveness-of-tax-administration-and-modernize-statistical-system-with-support-from-world-bank. [21]

UNCTAD (2022), *Investment Dispute Settlement Navigator*, https://investmentpolicy.unctad.org/investment-dispute-settlement/country/113/kyrgyzstan. [32]

US Department of State (2022), *2022 Investment Climate Statements: Kyrgyz Republic*, https://www.state.gov/reports/2022-investment-climate-statements/kyrgyz-republic/. [24]

World Bank (2023), *World Development Indicators*, World Bank Group, Washington D.C., https://databank.worldbank.org/source/world-development-indicators. [4]

World Bank Group (2021), *Creating markets in the Kyrgyz Republic: Unleashing the private sector to rebuild development success*, https://documents1.worldbank.org/curated/en/099708108082242045/pdf/IDU01fc40efb0be3d04df90bc43088db3b9a9193.pdf. [22]

ZOiS (2021), “The Republic of Kazakhstan’s New Administrative Procedures Code”, *ZOiS Spotlight* 25, https://www.zois-berlin.de/en/publications/the-republic-of-kazakhstans-new-administrative-procedures-code. [35]

Notes

[1] See Annex A

4 Tajikistan

This chapter focuses on Tajikistan's achievements and remaining challenges in the three areas of reforms identified in 2020, namely the investment framework, the enforcement of contracts and arbitral decisions in domestic courts, and tax administration. Taking into account the impact of the international context on the country's economy, the chapter offers a series of policy recommendations.

Table 4.1. Summary of priority reform implementation and updated recommendations

2020		2023	
Challenges identified	**Recommendations**	**Implementation assessment**	**Way forward**
Legal and regulatory framework for investment: **Ensure the implementation of laws on investment and improve access to information**	➢ Improve the implementation of the investment law ➢ Lift remaining sectoral restrictions ➢ Improve access to business- and investment-related legislation ➢ Clarify legislation to increase protection against indirect expropriation	➢ The investment framework has seen some progress thanks to trade facilitation efforts and more communication ➢ Yet, restrictions and uncertainties still need addressing	➢ **Strengthen the investment framework** ➢ **Relax restrictions on land access** ➢ **Improve access to financing and capital**
Contract enforcement: **Improve the enforcement of contracts and arbitral decisions in domestic courts**	➢ Ensure the systematic enforcement of international arbitration awards ➢ Create a Business Ombudsman ➢ Improve the quality and independence of domestic courts	➢ The legal framework for businesses has registered some improvements ➢ Dispute resolution mechanisms need strengthening	➢ **Strengthen judiciary independence** ➢ **Simplify the arbitral process**
Taxation **Make tax administration simpler, more consistent and more transparent**	➢ Stabilise tax policy with the passing of the new Tax Code ➢ Improve tax administration for SMEs ➢ Complete the full digitalisation of tax procedures ➢ Enhance the VAT regime and VAT rebate system	➢ Fiscal policy developments have reduced the tax burden on firms ➢ However, tax administration remains the most contentious issue mentioned by firms	➢ **Address interpretation and implementation issues** ➢ **Work on improving relations between the Tax Committee and the taxpayers** ➢ **Review tax incentives**

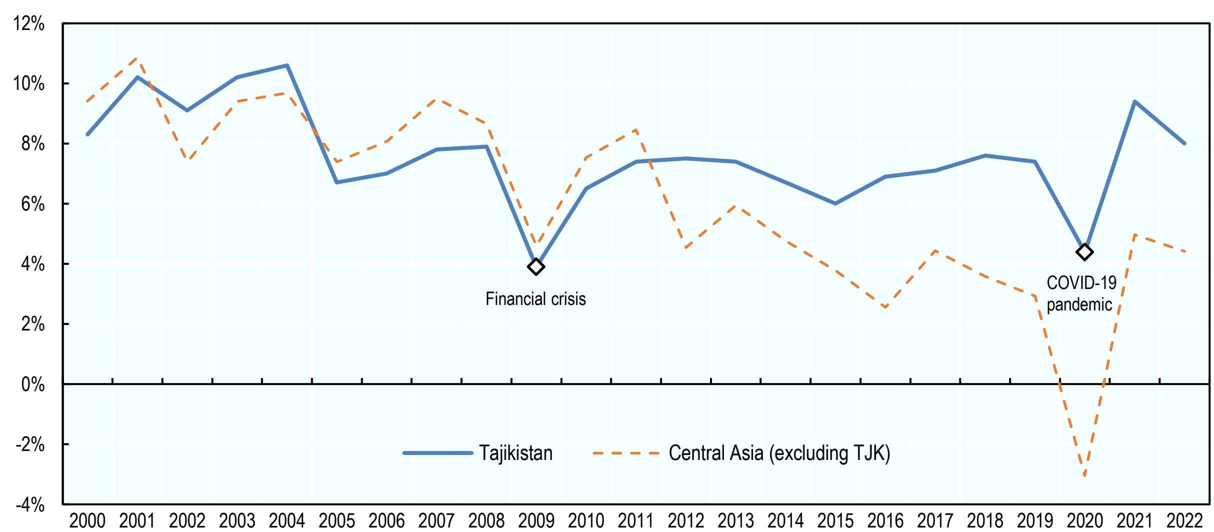
Source: (OECD, 2021[1]), OECD analysis (2023).

Introduction

Tajikistan has weathered the economic storms of COVID-19 pandemic and Russia's war in Ukraine fairly well

Since the beginning of the 21st century, real GDP has grown at an average annual rate of 7.6%, mainly driven by the extraction of minerals and metals, and supported by remittances inflows from labour migrants. Tajikistan has recorded the highest growth in Central Asia since 2016 and is the only country apart from Uzbekistan where growth remained positive during the pandemic in 2020. Growth slowed from 7.4% in 2019 to 4.4% the following year, due to worldwide and regional mobility restrictions drastically reducing economic activity. It appears that the war in Ukraine has had minimal impact on the economy so far: real GDP grew by 8% in 2022 (Figure 4.1). On the contrary, Tajikistan received large financial inflows through remittances and maintained low inflation. As of May 2023, annual inflation stood at 2.4%, which represents the lowest rate among all Central Asia countries (EBRD, 2023[2]).

Figure 4.1. Real GDP growth (2000-2022)



Source: (IMF, 2023[3])

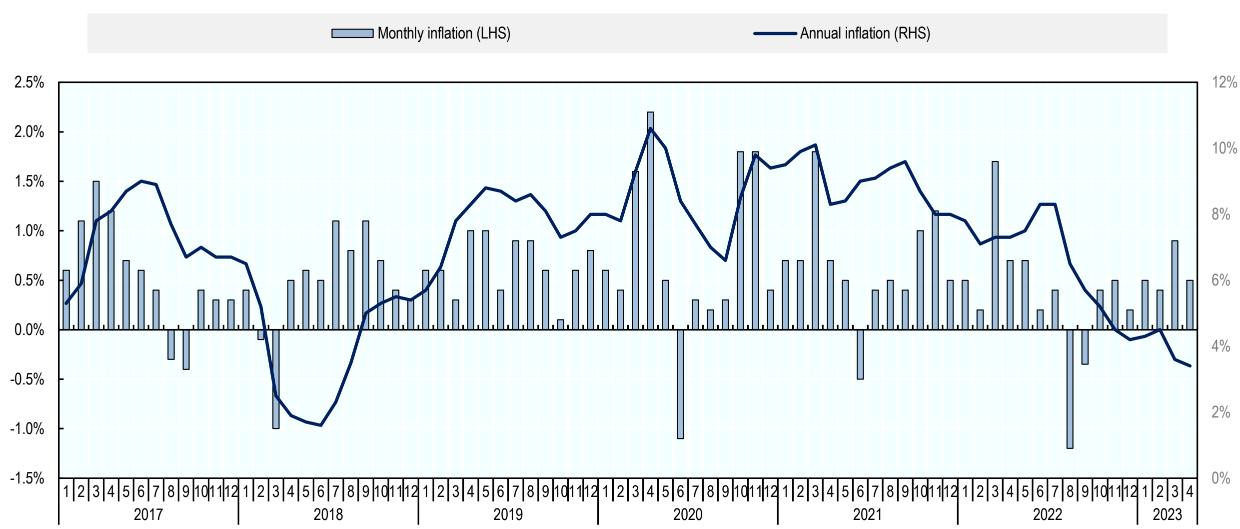
Surprisingly, trade is one of the factors responsible for the country's post-COVID recovery. In 2020, total exports jumped 20%: exports to Europe almost tripled due to increased metals demand, offsetting the fall in exports to every other part of the world, including CIS countries (-36%) and the rest of Asia (-18%). Then, in 2021, exports increased by 53% with the reopening of Asian borders. At the same time, it appears that imports were not heavily disturbed by the pandemic, as total imports only decreased by 6% between 2019 and 2020, almost entirely due to lower imports from China according to OECD computation based on data from (National Bank of Tajikistan, 2023[4]). In 2022, export volumes normalised following COVID-19 with substantial inventory sales of precious metals from the preceding two years (World Bank, 2023[5]).

Like the pandemic, the war in Ukraine has disturbed geographical trade patterns. In aggregate, it seems that the conflict did not have any effect on trade: in 2021, total exports amounted to USD 2.15 billion, while, in 2022, they amounted to USD 2.14 billion. However, geographical patterns changed. Exports were reoriented towards Asia, as exports to Europe dropped by 48% in 2022, offset by a 32% increase in exports to CIS countries and a 131% rise in exports to China. Moreover, imports increased by 23%, driven by Russia and China. This positive evolution of imports actually increased the trade deficit, as imports are now 2.5 higher than exports (OECD computation based on data from (National Bank of Tajikistan, 2023[4])).

Annual inflation has been decreasing since the pandemic and recently reached record low levels, unlike elsewhere in Central Asia. In early 2020, inflation peaked at 10.6% due to the restrictions related to the COVID-19 (Figure 4.2), hampering the supply of goods and foodstuffs. Indeed, the increase in food prices was responsible for more than 80% of total inflation. The National Bank of Tajikistan implemented restrictive monetary policies and eventually managed to contain this sudden increase in prices.

If the war in Ukraine provoked a regional inflation shock, the situation in Tajikistan remained almost unchanged. Following a brief uptick in inflation, in the longer run, the decreasing inflationary trend was maintained: a restrictive monetary policy has enabled the country to contain inflationary pressures, while the rise in the costs of food and fuel imports appears to have been offset in the first half of 2022 by a stronger somoni and the release of strategic food reserves (IMF, 2023[6]). In addition, the banking sector benefited from a significant increase in liquidity and fee-based earnings (IMF, 2023[6]). In May 2023, annual inflation reached 2.4%, far below other countries in the region.

Figure 4.2. Monthly and annual inflation in Tajikistan (2017-2023)



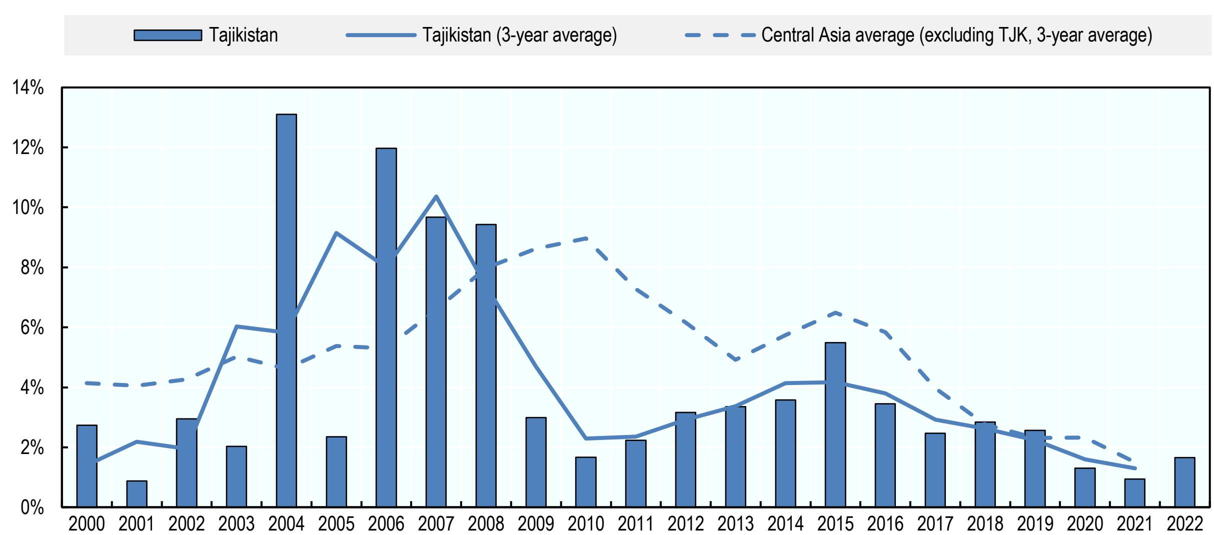
Source: (National Bank of Tajikistan, 2023[7])

Remittances from labour migrants amounted to 28.7% of GDP between 2016 and 2021. Remittance inflows support private consumption, being a major driver of growth in the country, and are responsible for the reduction of poverty, as a large majority is used for food and basic needs. Around 85% of remittances originate from Russia; indeed, Russia reported 850,000 Tajik migrants with valid work permits at the end of June 2022. The increase in external labour demand in Russia as a consequence of the war in Ukraine has resulted in remittances rising to a record high value of 51% of GDP for 2022 (USD 5.2 billion). Tajikistan is the only Central Asia country for which net migration to Russia was positive that year. The appreciation of the ruble against the somoni also contributed to this rise. Finally, new employment opportunities for migrants arose on the Russian labour market due to war mobilisation and the departure of some Western companies and their staff. However, this increase in remittances is likely to be temporary; normalisation is expected in 2023, also because the value of the ruble against the somoni is regaining its pre-war level (The World Bank, 2023[8]) (ROSSTAT, 2023[9]).

The structure of trade shows Tajikistan's limited economic diversification and complexity. On the one hand, the country exports a limited number of raw resources: mineral products represented 28% of total exports between 2016 and 2021, while gold accounted for 25% and non-precious metals for 22%. Over the same period, the range of imports was slightly broader and mostly composed of machines (23%), metals and minerals (22%), food (17%), textiles (10%) and chemicals (8%). Nonetheless, Tajikistan's trade turnover almost doubled during the last decade: total exports and imports respectively increased by 80% and 94% between 2010 and 2022. Export growth was mostly driven by gold, metals and mineral product sales, as well as textiles to a lesser extent. CIS countries (especially Kazakhstan and Russia) remain the main partners (58% of exports and 35% of imports in 2022), but Europe (24% of exports) and China (17% of exports and imports) still play major roles in Tajikistan's trade (OECD computation based on data from (National Bank of Tajikistan, 2023[4]).

This reliance on migrant remittances, an undiversified production and export base, and the country's high risk of debt distress make Tajikistan highly vulnerable to external shocks. Considering the important share of remittances from Russia, inflows are dependent on the state of the Russian labour market, and also influenced by the value of the local currency against the ruble. If 1 RUB was equal to 0.146 TJS in February 2022, the ruble's value increased by 38% by May 2022, when it peaked at 0.202 TJS. However, since then, the value of the ruble has dropped, to reach 0.121 TJS in July 2023. Therefore, everything else being equal, the amount of remittances going to Tajikistan would have fluctuated by +/- 40% only because of the foreign exchange market. Massive arrivals of Tajik citizens in Russia counterbalanced the depreciation of the ruble, as the number of migrant workers entering Russia from Tajikistan rose by 40% in the first quarter of 2023 compared to same period of the previous year. Going forward, it is uncertain to what degree Tajikistan will remain unscathed by Russia's reduced economic activity, the falling ruble and the migration trends. Furthermore, even if the volume of external debt decreased from 63.5% of GDP in 2021 to 49.0% in 2022, the country is still considered to be at high risk of debt distress due to the repayment of Eurobond in 2025-2027 (The World Bank, 2023[8]).

Figure 4.3. FDI inflows in Tajikistan and Central Asia (2000-2021, % of GDP)



Note: Due to the irregularity of FDI inflows in the region, values were smoothed using a 3-year moving average
Source: (World Bank, 2023[10])

After a significant FDI decline in 2020, FDI started recovering in 2021 and the country managed to strengthen its position in 2022 with the mining sector leading investment inflows (Figure 4.3). Between 2010 and 2020, 48.3% of total FDI inflows were directed to the mining and quarrying sector, while

18.7% were directed to manufacturing and 12.2% to transport and warehousing. The remaining 20% of FDI inflows on this period mostly concerned construction, finance and agriculture (National Bank of Tajikistan, 2023[11]). When looking at the evolution of the distribution of inflows, we observe a large increase in the mining and quarrying sector (from 29% of total inflows in 2015 to 68% in 2020), compensated by a major decline in manufacturing (from 45% to 4% between 2015-2020). Tajikistan benefits from a major investor, China, contributing to 55% of total inflows this last decade, up to 75% for some years. CIS countries represented only 13.2% of FDI inflows on the same period, with Russia accounting for 11.4%.

Box 4.1. Measures implemented by the government to support businesses during COVID-19

To keep firms afloat, policymakers extended business liquidity and credit lines via designated funds and commercial banks. Countries also advocated bank loan repayment deferral. Taxation has been another significant policy lever, within the frameworks of which deferring tax declarations, deferring payments, halting audits, and/or exempting corporations from social obligations have been implemented. Lastly, business inspection moratoria have been also implemented in the country.

Additionally, under the COVID-19 Active Response Plan and Expenditure Support Program (CARES), the government of Tajikistan received a USD 50 million grant from the Asian Development Bank (ADB) for the implementation of the countercyclical package of actions.

- Health sector measures for COVID-19 country preparedness and response implemented
- Increased social assistance and food security measures implemented
- Enhanced support for business entities and measures to safeguard employment implemented

To assist business entities and employees, the following steps were planned: (i) tax breaks for 40,000 micro, small and medium enterprises (MSMEs), (ii) moratorium on business inspections, including tax audits, until the program was completed, and (iii) concessional loans to MSMEs, 24% of which were owned by women. As a result, tax breaks were awarded in part; a suspension on business inspections was enforced for a shorter period than expected; and the issuance of concessional loans to MSMEs reached only around 17% of the amount planned by the end of the program.

Source: (Asian Development Bank, 2023[12]) (OECD, 2021[13])

The OECD has been working with Tajikistan to improve the business and investment climate

To help the government improve the business and investment environment and create enabling conditions for private sector development, the OECD conducted research in 2019-2020 in the legal environment for business and pointed to the need for more structural reforms in three policy domains, namely the investment framework, contract enforcement and tax administration (OECD, 2021[1]).

Implementation of existing laws for investment and entrepreneurial activity

The initial OECD assessment noted that Tajikistan had built a relatively solid legislative framework for business and investment activity, with the introduction in 2016 of a new investment law (IL) that outlines key provisions for, and protection afforded to, foreign and domestic investors. In particular, the IL provides numerous guarantees, such as equality of foreign and domestic investors before the law, guarantees from direct expropriation, provisions for compensation for indirect expropriation, and access to freely convertible currency, among others (OECD, 2021[1]). Tajikistan's FDI regime is open and non-discriminatory in principle, with the country's score in the OECD FDI Regulatory Restrictiveness Index close to the average for non-OECD countries, and in line with regional peers.

However, several areas for concern remained for foreign investors. While Tajikistan's FDI regime is relatively open, some restrictions persisted in relation to land use rights, which are limited to long-term leases, and sectors such as agriculture and forestry, media, and financial and legal services, which are among the industries where legal limitations remain significantly more restrictive than in OECD countries. Lastly, indirect expropriation was identified as a roadblock to investment, especially as the method of calculation of compensation was not clearly defined (OECD, 2021[1]).

Enforcement of contracts and arbitral decisions in domestic courts

Investors report that Tajikistan's courts have at times failed to implement foreign arbitral awards and rulings, sending a negative signal to prospective foreign investors, despite the country having ratified other international and bilateral treaties and conventions such as the Recognition and Enforcement of Foreign Arbitral Awards Convention (the New York Convention). In addition, Tajikistan is not yet a member of the International Centre for the Settlement of Investment disputes (ICSID) Convention. Investors have also complained about the lack of transparency of dispute settlement decisions. It was recommended in the OECD 2021 report to create a business ombudsman to independently represent the views and rights of businesses and support out-of-court dispute settlement and develop alternative dispute resolution mechanisms which have not been common practice for business case resolution.

Tax administration

Tax rates in Tajikistan were the highest in Central Asia, resulting in a large fiscal burden on firms. In addition, the complexity of the tax administration has made compliance costs high (OECD, 2021[1]). Both domestic and international firms have reported difficulties in accessing information on taxation, further challenging reporting. Finally, out-of-cycle inspections from the side of the tax administration were identified by businesses as another major challenge. A new Tax Code was in the drafting process at the time of writing the OECD 2020 report to address those issues and is discussed in further detail below.

Assessing progress since 2020

The following sections provide an overview of implementation progress of the three priorities for improving the legal environment for businesses identified in the 2020 OECD report and suggest a way forward taking into account new priorities following the pandemic and the regional context (Table 4.1).

Priority 1: The investment framework has improved, but there is a need to further soften existing restrictions

The government has taken steps to improve the business and investment environment

An online platform developed in testing mode provides access to information on investment and entrepreneurial activity

The government undertook measures to improve access to information on investment-related legislation. A website now provides access to legislation, decrees, and regulations in the Tajik and Russian languages (Ministry of Justice of the Republic of Tajikistan, 2023[14]). The website also includes information on the regulatory impact assessment and legislative process developments of draft laws and other legal acts, as well as a register of such drafts (UNCTAD, 2023[15]). An online platform was also developed by the State Committee on Investment and State Poverty Management (SCIPSM) in test mode to give access to information to both international and local investors and entrepreneurs. The platform was developed (i) to automate the process of coordination of inspections between inspection bodies, (ii) to co-ordinate the planning of inspections among those bodies, (iii) to prevent the repetition of inspections, (iv) to ensure the non-admission of violation of terms of inspection of business entities and the use of data for risk assessment in each sector, (v) to control compliance with the law in inspections and analysis results and (vi) to use the data to feed into sectoral risk analysis. The roll-out of the platform across the government is however still pending.

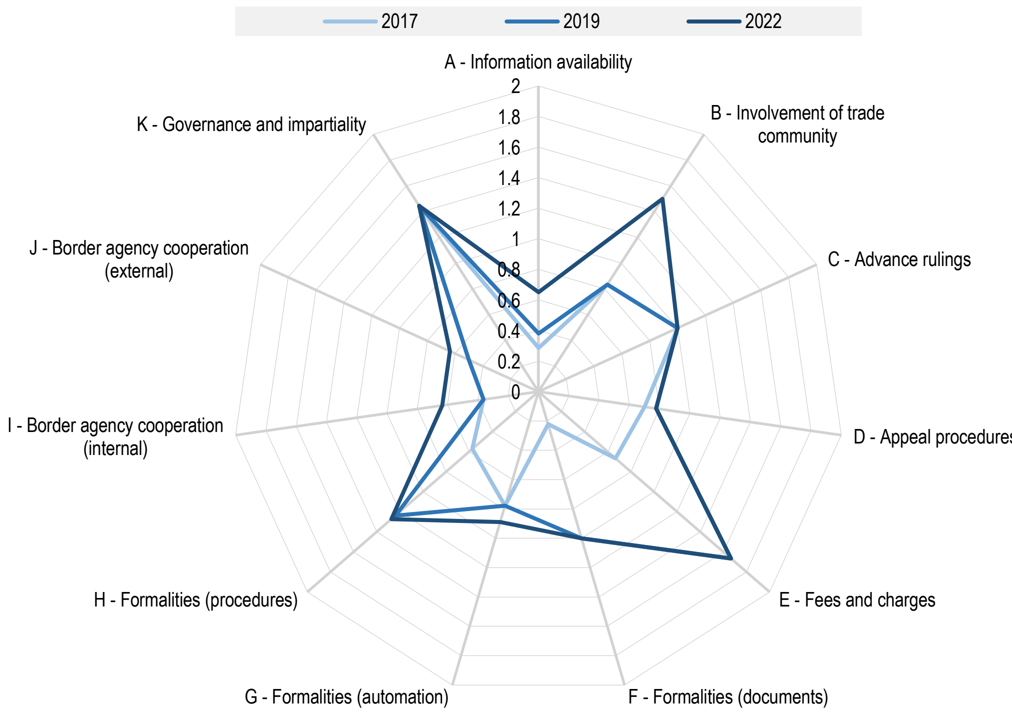
Greater trade and investment links have improved the investment climate in recent years

Several developments demonstrate efforts to streamline investment policies and processes. There are in theory no restrictions on foreign ownership or control of firms and no sector-specific restrictions that prevent market access (Lloyd's Bank, 2023[16]), and opportunities in the energy, agribusiness, food processing, tourism, textiles, and mining sectors have been identified as promising. In 2021, authorities continued moving towards compliance on intellectual property rights protections (US Department of State, 2022[17]).

A physical one-stop-shop was established to serve those trying to create a business, obtain construction permits and access to electricity, register property, and other procedures for free. The number of registering structures was lowered from four to one, and the registration time was reduced from forty-nine days to five days (UNCTAD, 2023[15]). The announcement in December 2022 of fresh negotiations on an enhanced partnership and co-operation agreement with the European Union bodes well for investment prospects (Economist Intelligence Unit, 2023[18]), as it should improve access to the EU market for goods originating from Tajikistan.

Tajikistan has consistently improved its overall trade facilitation performance since 2017 (Figure 4.4**), which has contributed to enhancing the country's investment attractiveness.** Notable improvements took place in the areas of information availability, involvement of the trade community, fees and charges, simplification of trade documents, automation, streamlining of border processes, and border agency co-operation. Compared to the average performance of the Central Asia region, Tajikistan has a strong performance in the involvement of the trade community, streamlining of fees and charges, simplification of trade documents, automation, streamlining of border processes, border agency co-operation, and governance and impartiality. A trade portal was launched in 2019 and continues to be developed with step-by-step procedures for export, import and transit, including information on trade partners, local producers with their contacts, regulations related to trade, processing procedures in the customs territory re-import, re-import, temporary importation, temporary export and special customs procedures. The Trade Portal also provides access to five tools to analyse the international market.

Figure 4.4. Tajikistan in the OECD Trade Facilitations Indicators (2017-2022)



Source: OECD TFIs database, 2022

The legislative framework for investment still creates hurdles for foreign investors

Foreign investors still face registration, property, land, and capital restrictions

While Tajikistan has an investment law, it does not specify the list of sectors and activities in which FDI is prohibited or permitted subject to conditions. The IL does not clearly define entry restrictions for foreign investment, nor does it clarify what constitutes national interest considerations, which can limit or prohibit foreign investments (UNCTAD, 2023[15]). A negative list can therefore sometimes help clarify restricted areas for FDI.

When registering their business, foreign investors must go through a lengthy process. Despite provisions of the IL which guarantee non-discrimination and equal rights between domestic and foreign investors, the latter must manoeuvre through a more arduous process to obtain licences. A single-window business registration system was created in 2019, which the Tax Committee is responsible for, but companies must also register with the Social Protection Agency, the Statistics Agency, the Ministry of Labour, Migration, and Employment, the Sanitary-Epidemiological Service at the Ministry of Health, and with local authorities and municipal services. In theory, registering a business should not take more than five business days, but in practice it can take several weeks or even months (US Department of State, 2022[17]). The procedure for closing a business remains complex and can take more than six months.

Foreign real estate ownership is allowed but restricted, as notaries require foreign investors to obtain approval from the Ministry of Justice to certify a real estate transaction (U.S. Department of State, 2023[19]). Security services may have a veto right for business activities in certain regions, and access to agricultural land is not allowed to foreign investors, despite the fact that agriculture is a prioritised sector for investments. Land ownership is not possible, as all land belongs to the State according to domestic law. Foreign investors and companies may be granted land-use rights for fifty years, while Tajik individuals and entities may have indefinite land-use rights. If leaseholders do not use land in accordance with the purpose of their lease, the authorities can revoke the lease rights (US Department of State, 2022[17]). Compensation is foreseen but usually only covers the market price of the factory but not that of the land.

Investors also face convertibility issues and restrictions on capital movement. All trade must be conducted in local currency, and hard currency cannot be withdrawn. According to the IL, foreign investors are guaranteed the right to transfer their income in foreign currency outside of Tajikistan, but OECD interviewees reported that, once profit is generated, a company needs to wait for several months to have it converted or transferred, and any transfer above 20k USD requires an approval from the National Bank of Tajikistan, if that transfer is considered as capital movement. The online form to request such a transfer has been reported not to work.

Finally, the absence of distinction between shareholder remuneration and re-investment means that the tax authorities tax the whole amount of dividends. Such a practice removes incentives for investors to reinvest proceeds. Providing incentives for reinvestment can induce reinvestments of amounts higher than in the absence of the tax incentive.

Access to information remains challenging

Presidential decrees, legislation, government orders, instructions, ministerial memos, and regulations are not always easily accessible to the public. To receive up-to-date legal and regulatory information, businesspeople and investors may need to purchase access to Adliya, a commercial legal database. Some unpublished regulations have been found to contradict other state structures' regulations, while draft laws and regulations are rarely published for public consultation (US Department of State, 2022[17]). OECD interviewees were not aware of the existence of the online platform for investors, and updates to the website have been reported as irregular (OECD, 2022[20]).

Indirect expropriation risks persist

While the IL guarantees protection for direct expropriation, the government can indirectly expropriate property as per the terms of the IL (article 14), the law on privatisation, the civil code, and the criminal code. As a result, expropriation risk is still present in Tajikistan. OECD interviewees have reported that the *de facto* primacy of the security, customs and tax laws over the IL adds uncertainty with regards the protection of investment projects. This has prompted some investors to ask to conclude investment contracts under common law rather than in domestic legislation to secure their investments.

Further improving investment attractiveness requires to strengthen the investment framework, relax restrictions on land access and diversify sources of financing

Clarifications in the investment legislation and framework would give investors greater certainty

The hierarchy and content of the IL could be improved. Clarifying the hierarchy of the IL with other laws would reduce the level of uncertainty associated with indirect expropriation risks. In addition, the IL could contain a publicly available negative list with sufficient details on the sectors involved to clarify authorised and prohibited areas for FDI. The list could enumerate all the sectors, activities or areas where i) foreign investors cannot invest, ii) can only invest up to a certain percentage of equity, or iii) can only invest after going through a special screening or approval process. All other activities not explicitly mentioned in the list should be considered as automatically open to FDI.

A streamlining of establishment procedures could also be considered. Most procedures involving foreign businesses still need to be conducted in person and could be made available online. The one-stop-shop for investors should be effectively implemented, including its e-version, and information should be regularly updated. This streamlining could also involve devolving more powers to institutions dealing with investments: the SCISPM’s and Tajinvest’s respective roles in designing and implementing investment policy and promoting and facilitating investment should be strengthened (UNCTAD, 2023[15]).

Restrictions on land and property access could be relaxed

Current restrictions on land rights represent a significant barrier to investment. If the introduction of private property in land is not under consideration, the government could ensure that the alienability of land use rights is extended to foreign entities, as it is already the case for Tajik individuals and legal persons. In the same vein, the government could undertake measures to guarantee equal access to property ownership between local and foreign firms by ensuring that procedures to access property are the same for both. The provision on compensation in case of indirect expropriation should also be reviewed to include not only the market price of the factory or other assets but also that of the land.

Funding and capital constraints should be addressed

The government could consider easing restrictions on access to finance and withdrawal of capital. In particular, it could support the development of a wider array of financial instruments to foster private investment. A limited range of financial products is currently offered to SMEs, which mostly rely on debt instruments such as commercial bank loans or microfinance (ADB, 2019[21]). Developing new financial instruments allowing access to equity investment, such as convertible loans, venture funding, factoring, and leasing could be considered, which would allow to address high collateral requirements, prohibitive interest rates, and the short tenors currently offered by traditional commercial loans. The government is currently working on a new venture capital funding law which should unlock new funding opportunities for start-ups. In addition, facilitating money transfers outside of the country would reassure foreign investors that they can reallocate profits as they see fit, as hard currency deposited in a Tajik bank account is difficult to withdraw, despite the fact that there are no legal limits on money transfers (US Department of State, 2022[17]).

Priority 2: The judicial system has become more transparent, but the dispute resolution mechanisms need strengthening and simplification

The legal framework for businesses has registered some improvements

The government has taken steps to improve judicial transparency

In June 2021, the government adopted the law “On Access to Information on the Activities in the Courts” to increase the transparency and openness of judicial proceedings. The law aims to improve public access to information about the activities of the courts through the appointment of dedicated staff in charge of public relations and the creation of court websites. The latter provide the opportunity for citizens to access a schedule of appointments, hearing dates, and email addresses of the judges and representatives of the Supreme Economic Court and to read about court decisions. An e-case management system was created for parties to a case to access court notices online. Press conferences with the media are planned on a bi-annual basis to take stock of the activity of economic courts.

Pre-trial dispute resolution is being developed especially in tax-related disputes

OECD interviewees have mentioned the Tax Committee’s and Ministry of Finance’s endeavours to foster dialogue and resolve disputes with the business community. In particular, the Tax Committee created an independent Council of Pre-trial Dispute Settlement, which serves as an advisory body to consider tax disputes between the taxpayer and the tax authority and review complaints from taxpayers.

This advisory council is formed of representatives from the justice, financial, business support and tax government agencies and ministries, as well as of independent consultants. Following a pre-trial review of the taxpayer's complaint, the Council issues a recommendation submitted for the relevant state body to make a decision. Such a Council can serve as an alternative dispute resolution mechanism to solve taxpayers' and tax authorities' litigation cases.

Dispute resolution mechanisms need further strengthening

The creation of a Business Ombudsman has been delayed

The government had undertaken to create a business ombudsman, but this ambition has not yet been realised. First discussions about its establishment were included in the Midterm Development Programme of the country for 2021-2025, with implementation planned for 2022.The process is, however, still at the level of discussion, and it is considered to transfer the business ombudsman's functions to the Commissioner for Human Rights. A Business Ombudsman with oversight for inspection agencies and regulations would provide a strong public-private dialogue mechanism and could play an important role in dispute settlement (OECD, 2021[1]). Ensuring the independence of such an institution could be met following the example of Kyrgyzstan, through the appointment of a foreign citizen.

Judges are perceived to lack independence

Parties seeking dispute resolution submit their claims to economic courts. However, firms have reported a lack of independence in decision-making, lengthy delays of court decisions and a cumbersome process, which act as deterrents to reliance on the judiciary. OECD interviewees and (U.S. Department of State, 2023[19]) state that outcomes tend to favour the government, and decisions are not always made publicly available. It remains to be seen if the new law on access to information will change this.

Commitments to international conventions are not always followed

Tajikistan is signatory to several bilateral and international conventions on dispute settlements, but domestic courts do not always enforce or recognise their rulings (US Department of State, 2022[17]). For instance, the country ratified the New York Convention on the recognition and enforcement of foreign arbitral awards and acceded to the Convention in 2012 but several arbitral awards have been overturned. OECD interviewees have also mentioned disputes related to double taxation issues. Whilst Tajikistan has signed several agreements to avoid the issue of double taxation, tax authorities still require firms to pay taxes in Tajikistan notwithstanding provisions agreed upon in those agreements.

Improving contract enforcement requires strengthening judicial independence and simplifying the arbitral process

More judicial independence will lead to greater confidence in the courts

Strengthening the independence of the courts would help improve the impartiality of court decisions and businesses' trust in the judiciary. Judges should be free of influence and pressures that could affect the way they perform their duties. Efficient and impartial institutions for the administration justice, the predictability of legal outcomes, the protection of property rights and the maintenance of stability are indeed preconditions for a supportive investment environment, as a functioning justice system contributes to firms making longer-term investment decisions (OECD, 2021[22]). In practical terms, measures to ensure the independence and accountability of the judiciary could include publishing objective criteria for the appointment of judges based on merit and qualifications, the security and irremovable character of their tenure and the random allocation of cases to minimise corruption risks (ENCJ, 2014[23]), (OECD, 2018[24]).

Formal reporting mechanisms can support judicial independence and accountability

Reporting is a key aspect of the transparency and accountability of the judicial system. Formal reporting mechanisms on issues such as case disposals, timeliness, case duration, appeal waiting times and other aspects of the quality of the judicial process should be created through regular reporting structures and a database on the performance of the judicial system along these aspects. Data would allow observers to analyse the performance of justice procedures and understand where efforts should be focused. The reporting should be periodically published and could include a benchmark of the different courts to foster emulation (ENCJ, 2014[23]). An independent body such as a Business Ombudsman, involving business associations and representatives, could also report cases of non-implementation or mis-implementation of the law.

Simplifications in the arbitral process can reduce costs associated with dispute resolution

The government could consider introducing simplified procedures to offer legal and judicial services proportionate to SMEs' cases. There are currently no specialist courts to hear disputes relating to land or intellectual property rights, nor are there small-claims courts. Small claim courts can provide tailored and fast-track procedures proportionate to the amount of money at issue. Such courts improve access to justice for SMEs as they free up court time and financial resources and contribute to judicial efficiency (OECD, 2017[25]). Robust small claims procedures usually limit the role of lawyers to reduce the cost of legal representation, require smaller court fees associated with filing the claim, and restrict the use of expert assessments and oral witness testimony as expenses for collecting evidence can be time-consuming and expensive for the litigants (World Bank, 2021[26]). Specialist courts focusing on land or property rights could also be created to reduce the number of cases pending before the main first-instance court and lead to shorter resolution times.

Alternative dispute resolution mechanisms such as mediation, negotiation and arbitration for international investors can also be further developed to settle disputes outside of the courtroom and reduce the strain on the judiciary. The creation of a Mediation Centre and of the Council of Pre-trial Dispute Settlement to resolve tax disputes are already positive steps in that direction. The project of a law on mediation could also be resumed.

Priority 3: Tax administration has benefitted from digitalisation and more public-private dialogue, but interpretation issues need addressing

Tajikistan adopted a new Tax Code in 2022

Tajikistan adopted a new Tax Code in January 2022 with the aim of promoting socio-economic development and strengthening public finances through the reduction of tax evasion and the easing of the tax burden on firms. The new version of the Tax Code states that it is based on the principles of legality, obligation, cooperation of tax authorities with the taxpayer, fairness, unity of the tax system, and transparency. Key changes to the code include the introduction of chapters on transfer pricing and tax monitoring, the creation of a tax avoidance commission and of a Council for Pre-Trial Dispute Resolution, the use of electronic fiscal receipts, virtual cash registers, and an e-marking system to track goods imported into Tajikistan, the provision of independent assistance to taxpayers by tax consultants, and tax monitoring based on voluntary requests from taxpayers whose turnover is higher than 15 million TJS (about 1.25 million EUR). The new code also foresees the development of risk assessment criteria to determine the different levels of non-compliance risks, with KPIs associated with the system. The tax system was simplified through a reduction of the number of taxes from ten to seven, and several amendments and additions were made to account for the issue of bad tax debts and their writing-off. Tax exemptions for the mining sector were gradually phased out, and a rise in the income tax rate for mining businesses supported an increase in tax revenue (Economist Intelligence Unit, 2023[18]) (IMF, 2023[6]). The Tax Committee reported that the amount of tax collected for 2022 exceeded the target by almost 600 million TJS (around 55 million USD).

Box 4.2. Key rate changes of Tajikistan's 2022 Tax Code

The rates of several taxes were reduced or reviewed:

- the VAT rate was reduced from 18% to 15% and is expected to be reduced to 13% as of January of 2027;
- a flat rate for the income tax of 12% was introduced and replaced the degressive income tax system (8% to 12%);
- income tax was kept at 13% for companies producing goods;
- income tax was reduced from 23% to 20% for financial institutions and telecom companies;
- income tax for other companies was reduced from 23% to 18%; and
- social taxes were reduced from 25% to 20%;

The road user's tax and excise tax were withdrawn.

Source: Tax Committee of the Republic of Tajikistan (2023)

The Tax Committee has been actively engaging with the private sector on the Code's changes

OECD interviewees praised the proactiveness of the Tax Committee in collecting feedback, sharing drafts of the new Tax Code, and integrating the private sector's comments in the last version of the Code. Following its adoption, the Tax Committee was mindful of communicating the changes of the Code to the private sector, with a focus on SMEs. Tax authority specialists organised offline and online seminars with taxpayers, domestic and foreign investors, and diplomatic missions to explain the new provisions of the Tax Code (how to submit requests for tax returns, issues of land, real estate and vehicles valuation, etc.) and provide the opportunity to engage in Q&A sessions. A dedicated page on the Tax Code providing the latest updates was created on Telegram and Viber, TV programmes were brought to a wide audience through the Tojikiston and Safina channels, 150 thousand text messages were sent to citizens, and taxpayers can now submit questions and complaints on the Tax Committee's website. A call centre can also be contacted on a daily basis. Tax administrators provide support to citizens and businesses looking to pay their taxes on the publicly accessible terminals in cities. Written appeals have become much less frequent, as taxpayers can now submit their cases by phone, email or on their personal account.

Compliance monitoring is increasingly grounded on risk-based approaches

The Tax Committee, together with the SCISPM, developed criteria to assess the level of risk of taxpayers' activities and non-compliance, differentiated by company size. The level of risk may be defined as low, medium or high. A taxpayer falling under a high risk is contacted by an authorised state body online on the personal account to remedy the situation. The new Tax Code stipulates new provisions on tax monitoring, where a taxpayer earning more than 15 million TJS can, on a voluntary basis, agree with the tax authorities on exemptions on in-house controls and tax audits for a period of one year. Improvements in monitoring have resulted in a decrease in the share of tax audits in proportion to the number of tax entities: if in 2018 2.8% of businesses were audited, this figure decreased to 1% in 2021.

Positive changes in compliance and appeals trend can be noticed

According to the Tax Committee, the reduction of the type and the rate of taxes has resulted in a lower burden on the taxpayers, which has had a positive impact on compliance and the reduction of the shadow economy. Tax administration was also enhanced thanks to the reduction of the costs and time spent by taxpayers filing tax returns. The introduction of the concept of ultimate recipient of income (or beneficiary) and strides in the implementation of international treaties have improved tax relations with non-residents receiving income from Tajikistan. Combined, these developments resulted in a decrease in the number of taxpayers' appeals in 2022.

A wide range of tax services is available digitally

The Tax Committee has intensified its efforts to digitalise tax administration, which has been positively received by firms. Satisfaction with the ongoing digitalisation of the tax services has been reported by firms interviewed by the OECD. Since 2020, the Tax Committee has developed and implemented more than 80 e-services. Companies can register online on the Tax Committee's website. Among concrete examples of available e-services, one can mention the ''Andozi Man'' (''My Tax") application, which can be used both by citizens and entrepreneurs to fulfil tax obligations and interact with the tax authorities. More than ten e-services are currently available on the app, such as information about the activity of the Tax Committee, the submission of e-documents for verification, inspection authorities' addresses, a tax calculator, the Tax Code, the taxpayer's identification number, tax payments made, etc. The Tax Committee and the State Savings Bank Amonatbank developed a tax payment functionality on the Amonatmobile application. Taxpayers can also pay real estate, land and vehicle taxes on the Tax Committee's website. The procedure to register as a VAT payer can be done through an online application form in a few minutes. All this has increased the number of taxpayers who file their tax returns electronically. During 2022, the number of taxpayers who filed their tax returns electronically increased by more than 6.5 thousand. According to the Tax Committee, the total volume of transactions carried out using cash registers increased by 28% in 2022 compared with 2021. In general, smoother and easier interactions between tax authorities and taxpayers have resulted in improvements in tax administration.

However, challenges related to interpretation, implementation and administration remain

Frequent legislation changes and varying interpretations create implementation challenges

Businesses have expressed concerns about the lack of harmonised interpretation of the Code across the government, which adds confusion to the implementation of the law. They reported an added layer of complexity related to unclear formulations and conflicting interpretations of specific clauses among different offices of the tax administration itself. Whilst large foreign firms may have the in-house capacity and leverage to resolve these issues with the tax authorities, SMEs may not be able to do so. Overall, the lack of clarity of certain clauses of the Code has significantly challenged the government's objective to simplify tax policy with the introduction of the new text.

Unplanned inspections and early tax payment requests have been mentioned as roadblocks to tax compliance

Firms have also complained about the frequency of tax inspections. A moratorium on inspections was implemented in 2022 considering the instability of the international context and to let taxpayers adapt to the new code. However, the retroactivity of the inspection period was increased from five to six years to account for the absence of checks in 2022, meaning that checks for 2022 will still take place retroactively. In addition, while tax inspections can apply on business activity of the five previous years, in case of irregularities, tax authorities can further investigate tax compliance in the ten previous years and calculate the sum due on that past ten-year period, applying interest and penalties amounting to double the tax payment due. Such a measure does not encourage firms outside the tax base to start paying taxes and hampers the government's efforts to reduce the size of the shadow economy. Cashless firms paying taxes online do not understand why they are still subject to cameral inspections.

Payments are sometimes requested or refunded outside of the scope of application of the text. Firms have reported that the tax administration attempts to make them fit under different articles of the code to request several tax payments which should not apply (e.g., mining companies) or to proceed with advance tax payments. On the other hand, VAT refunds have been subject to delays, which can take one year. Delays have resulted in firms declaring additional other income to benefit from an indirect tax deduction corresponding to the VAT return amount due, while some OECD interviewees increased their prices following the withdrawal of the VAT incentive which allowed offsetting. Some importers reported to illegally bring goods in Tajikistan do not pay VAT and transfer VAT payment obligations to their retailers.

Further improving the tax administration requires addressing implementation issues and working on adopting a more client-oriented approach towards the taxpayers

Harmonising the interpretation of the Tax Code should be a priority area of work

Streamlining interpretation across the different areas of the government is a low-hanging fruit to ease the tax burden on firms and improve the implementation of the Tax Code. Online reporting tools or regular surveys could be developed and channelled through the Chamber of Commerce or regional and sectoral business associations for firms to report cases of misinterpretation or lack of clarity on an anonymous basis. More generally speaking, avoiding frequent changes to the law is an objective that should be pursued by the authorities to increase tax compliance.

The Tax Committee should pursue its efforts to improve relations with the taxpayers

The Tax Committee has already worked to raise awareness on changes made and should pursue endeavours for businesses to understand new provisions. Measures to do so include conducting awareness-raising activities on an ongoing basis with businesses and other segments of society, to foster the acquisition of tax knowledge and financial literacy. Firms should also have the possibility to appeal conflicting interpretations of the law before an administrative judge. In parallel, tax authorities need to train all staff to be informed of regulatory changes and communicate accurate information to businesses.

The Tax Committee should define a clear scope for inspections to decrease the administrative burden on firms. Looking at the example of Kazakhstan (Government of Kazakhstan, 2021[27]), the Tax Committee and other relevant government agencies could define a short and clear list of cases where an inspection should be performed. It could also introduce a clause on the responsibility of the administration when conducting an inspection whereby any inspection conducted beyond the framework becomes illegal and can be a motive for litigation by the firm concerned.

Digitalisation is another part of the Tax Committee's agenda to support smoother interactions with the taxpayers which can be further rolled out across the government. The Tax Committee mentioned the importance of providing IT equipment, necessary software and technologies to other ministries and agencies, as well as the processing of large volumes of data to achieve tax reform goals. This also requires the development of a stable, high-speed, and accessible Internet across the regions as well to ensure businesses in remote areas can access online tax services. Dushanbe-based agencies are expected to switch to the cashless payment system SmartPay to ensure that the payment of all taxes, duties, fines, license and insurance fees, fees for utilities and other types of public services is performed in a non-cash form (Asia Plus, 2023[28]).

References

ADB (2019), *Leveraging SME Finance through Value Chains in Tajikistan*, https://www.adb.org/sites/default/files/publication/534291/adbi-wp1020.pdf (accessed on 4 July 2023). [21]

Asia Plus (2023), *All Dushanbe-based government agencies will be shifted to non-cash payment system from August 1*, https://asiaplustj.info/en/news/tajikistan/economic/20230711/all-dushanbe-based-government-agencies-will-be-shifted-to-non-cash-payment-system-from-august-1. [28]

Asian Development Bank (2023), *Tajikistan: COVID-19 Active Response and Expenditure Support Program*, https://www.adb.org/sites/default/files/Evaluation%20Document/873251/files/pvr-0706.pdf (accessed on 29 May 2023). [12]

EBRD (2023), *Regional Economic Prospects: Getting by High Inflation Weighs on Purchasing Power of Household*. [2]

Economist Intelligence Unit (2023), *One-click report: Tajikistan*, https://viewpoint.eiu.com/analysis/geography/XG/TJ/reports/one-click-report (accessed on 11 July 2023). [18]

ENCJ (2014), *Independence and Accountability of the Judiciary*, https://www.encj.eu/images/stories/pdf/workinggroups/independence/encj_report_independence_accountability_adopted_version_sept_2014.pdf. [23]

Government of Kazakhstan (2021), *"On Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan on the Introduction of a New Regulatory Policy in the Sphere of Business Activities and Redistribution of Certain Functions of Internal Affairs Bodies"*, https://adilet.zan.kz/rus/docs/Z2100000095 (accessed on 6 July 2023). [27]

IMF (2023), *Mission Concluding Statement: Tajikistan: Staff Concluding Statement of the 2022 Article IV Mission*, https://www.imf.org/en/News/Articles/2022/12/22/tajikistan-staff-concluding-statement-of-the-2022-article-iv-mission#:~:text=After%20growing%20by%209.2%20percent,)%2C%20agriculture%2C%20and%20construction. (accessed on 24 May 2023). [6]

IMF (2023), *World Economic Outlook Database, April*, https://www.imf.org/en/Publications/WEO/weo-database/2023/April. [3]

Lloyd's Bank (2023), *Tajikistan: Investing*, https://www.lloydsbanktrade.com/en/market-potential/tajikistan/investing (accessed on 2023). [16]

Ministry of Justice of the Republic of Tajikistan (2023), , http://portali-huquqi.tj/publicria/ibtido.php?language=ru (accessed on 16 October 2023). [14]

National Bank of Tajikistan (2023), *Balance of payments*, https://www.nbt.tj/en/payments_balance/. [4]

National Bank of Tajikistan (2023), *Foreign direct investments*, https://nbt.tj/en/statistics/tavozuni-pardokhti-jt/sarmoyaguzori-oi-mustakimi-khorii/index.php. [11]

National Bank of Tajikistan (2023), *Monthly Inflation Reviews*, https://www.nbt.tj/en/monetary_policy/shahri-tav/sharhi_mohonai_tavarruv.php. [7]

OECD (2022), *Enhancing Investment Promotion in Tajikistan*, OECD Publishing, https://doi.org/10.1787/1e3a7c4f-en. [20]

OECD (2021), *Beyond COVID-19: Prospects for Economic Recovery in Central Asia*, https://www.oecd.org/eurasia/Beyond_COVID%2019_Central%20Asia.pdf (accessed on 29 May 2023). [13]

OECD (2021), *Improving the Legal Environment for Business and Investment in Central Asia*, OECD, https://www.oecd.org/eurasia/Improving-LEB-CA-ENG%2020%20April.pdf (accessed on 1 May 2023). [30]

OECD (2021), *Improving the Legal Environment for Business and Investment in Central Asia*, OECD Publishing, https://www.oecd.org/eurasia/Improving-LEB-CA-ENG%2020%20April.pdf. [1]

OECD (2021), *OECD Framework and Good Practice Principles for People-Centred Justice*, OECD Publishing, https://doi.org/10.1787/cdc3bde7-en. [22]

OECD (2018), *Fourth Round of Monitoring: Tajikistan Progress Update*, https://www.oecd.org/corruption/acn/OECD-ACN-Tajikistan-Progress-Update-2018-ENG.pdf. [24]

OECD (2017), *OECD Policy Roundtable on Equal Access to Justice*, OECD Publishing Paris, https://www.oecd.org/gov/A2J-RT-Session-notes-May-2017.pdf. [25]

Orbitax (2022), *Tajikistan Tax Changes from 2022 Under New Tax Code - Orbitax Tax News and Alerts*, https://www.orbitax.com/news/archive.php/Tajikistan-Tax-Changes-from-20-48812 (accessed on 31 May 2023). [34]

ROSSTAT (2023), *Socio-economic situation of Russia in 2022*, https://rosstat.gov.ru/storage/mediabank/osn-12-2022.pdf. [9]

The World Bank (2023), *Tajikistan Economic Update: Focusing on Boosting Private Sector Dynamism in Tajikistan*, World Bank Group, https://thedocs.worldbank.org/en/doc/46328951bdfc3b29c26b4aa8255ea773-0080012023/original/Tajikistan-Economic-Update-2023-ENG.pdf. [8]

The World Bank (2023), *The World Bank in Tajikistan: Overview*, https://www.worldbank.org/en/country/tajikistan/overview (accessed on 25 May 2023). [32]

The World Bank (2020), *The World Bank: Tajikistan's Post COVID-19 Recovery Could be Faster and More Susutainabe with Private Sector Participation*, https://www.worldbank.org/en/news/press-release/2020/12/23/tajikistan-economic-update-fall-2020 (accessed on 26 May 2023). [33]

Trading Economics (2022), *Ease of Doing Business in Tajikistan*, https://tradingeconomics.com/tajikistan/ease-of-doing-business (accessed on 11 May 2023). [31]

U.S. Department of State (2023), *2023 Investment Climate Statements: Tajikistan*, https://www.state.gov/reports/2023-investment-climate-statements/tajikistan/#:~:text=Tajikistan's%20legislation%20provides%20a%20right,that%20discriminate%20against%20market%20access. (accessed on 13 October 2023). [19]

UNCTAD (2023), *Report on the Implementation of the Investment Policy Review*, https://unctad.org/system/files/official-document/diaepcb2022d1_en.pdf (accessed on 8 May 2023). [15]

United Nations (2012), *United Nations, Press Releases*, https://unis.unvienna.org/unis/pressrels/2012/unisl174.html (accessed on 1 May 2023). [29]

US Department of State (2022), *2022 Investment Climate Statements: Tajikistan*, https://www.state.gov/reports/2022-investment-climate-statements/tajikistan/ (accessed on 9 May 2023). [17]

World Bank (2023), *Foreign direct investment (database)*, https://data.worldbank.org/indicator/BX.KLT.DINV.WD.GD.ZS?locations=TJ. [10]

World Bank (2023), *Tajikistan Economic Update*, https://thedocs.worldbank.org/en/doc/46328951bdfc3b29c26b4aa8255ea773-0080012023/original/Tajikistan-Economic-Update-2023-ENG.pdf. [5]

World Bank (2021), *Two For One: How Leveraging Small Claims Procedures Can Improve Judicial Efficiency and Access to Justice*, https://documents1.worldbank.org/curated/en/487041607706210590/pdf/Two-For-One-How-Leveraging-Small-Claims-Procedures-Can-Improve-Judicial-Efficiency-and-Access-to-Justice.pdf. [26]

WTO (2023), *Law on Foreign Investment in The Republic of Tajikistan*, https://www.wto.org/english/thewto_e/acc_e/tjk_e/wtacctjk13a1_leg_7.pdf (accessed on 31 May 2023). [35]

5 Turkmenistan

This chapter focuses on Turkmenistan's progress and challenges in implementing the three priority reforms identified in 2020, namely the implementation of the investment law and access to information for investors; the streamlining of business registration and licensing, and the creation of a one-stop shop; and the simplification of the operational environment for firms. Taking into account the impact of the COVID-19 pandemic and that of Russia's war in Ukraine, the chapter offers policy recommendations to improve the legal environment for investors and businesses.

Table 5.1. Summary of priority reform implementation and updated recommendations

2020		2023	
Challenges identified	**Recommendations**	**Implementation assessment**	**Way forward**
Investment regulation: Ensure the enforcement of the Law on Investment and improve information availability	➢ Improve availability of legislation ➢ Consolidate body of by-laws ➢ Streamline, consolidate and publish all investment-related legislation on the legal database of the Ministry of Justice	➢ The government has increased communication about changes in the law ➢ Reform efforts seem to have slowed down due to the COVID-19 pandemic	➢ **Create an Investment Promotion Agency (IPA)** ➢ **Improve contract enforcement** ➢ **Review the legal framework to encourage domestic investment transactions**
Business registration: Streamline business registration and licensing, and introduce a one-stop-shop	➢ Create a one-stop shop for business registration ➢ Consolidate and harmonise legislation for licensing and permits ➢ Take into account connectivity and capacity constraints	➢ The government has revised and simplified some procedures for business registration and licensing ➢ Procedures are still paper-based and cumbersome	➢ **Streamline the registration process, clarifying the key steps and timelines** ➢ **Limit State interventions to specified instances and create an independent reporting mechanism through a Business Ombudsman** ➢ **Improve access to information by regularly updating the government's websites**
Operational environment for SMEs: simplify the operational environment	➢ Dedicate attention to the needs of SMEs when simplifying the investment regulatory framework ➢ Develop SME-targeted public instruments ➢ Create a Business Ombudsman	➢ The post-pandemic period has provided some relief to businesses ➢ The business environment remains difficult to navigate	➢ **Expand the range of available financial instruments** ➢ **Expand digital infrastructure** ➢ **Capitalise on the Middle Corridor's renewed interest to facilitate trade**

Source: (OECD, 2021[1]), OECD analysis (2023).

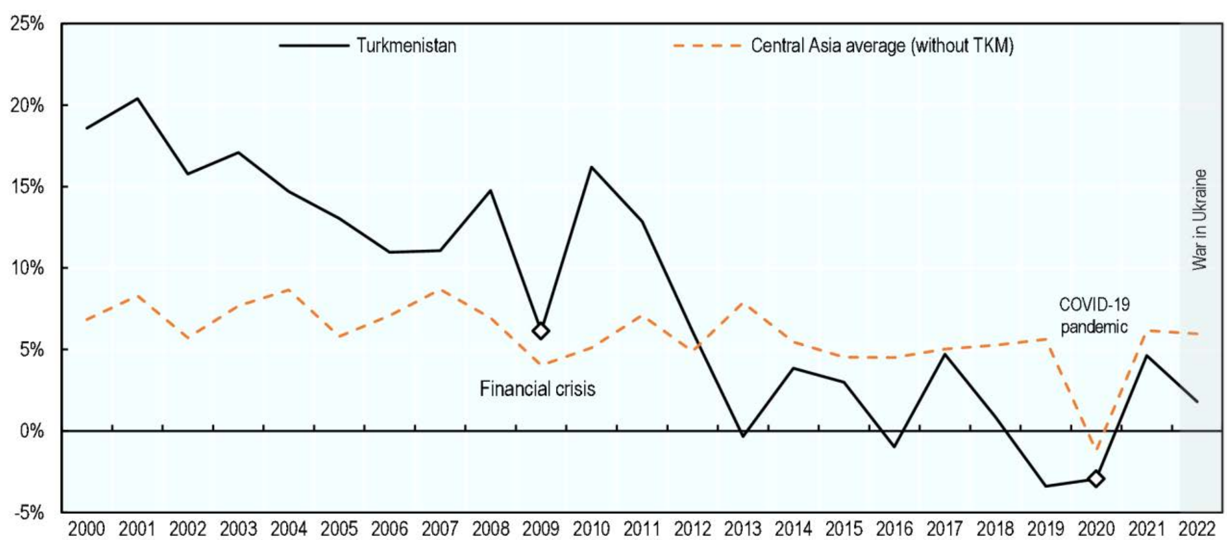
Introduction

Turkmenistan's growth has been positive but on a declining trend

The oil and gas sector has been driving economic growth

Turkmenistan's economic growth has been driven chiefly by the extractive sector. The government has pursued an investment-led growth strategy underpinned by export promotion and import substitution policies and directed concessional lending (IMF, 2019[2]). Foreign direct investment remains largely limited to oil and gas extraction in the form of production-sharing agreements. Despite the government's ambition to diversify the FDI base, foreign exchange controls, the absence of property rights in land, and the interference of the state in business matters have constrained such a diversification. The economy remains dominated by state-owned monopolies, including in the oil and gas, electricity, cotton, telecommunication, and manufacturing sectors (BTI Transformation Index, 2022[3]). Growth has been on a declining trend and below double digits since 2012 on IMF estimates. Whilst these estimates significantly diverge with government data, the latter informed the OECD of an upcoming Article IV consultation in 2024 during which this issue should be discussed.

Figure 5.1. Real GDP growth (2000-2022)



Source: (IMF, 2023[4])

The economy was hit by COVID-19 but recovered in 2021

Whilst the government reported stable economic growth and no officially confirmed cases of COVID-19, restrictions on international and domestic travel as well as the closing of some businesses are reckoned to have resulted in negative growth in 2020. The economy quickly rebounded in 2021 and surpassed its 2019 levels, with a robust recovery in exports, although abnormally dry weather had a detrimental effect on agriculture and the production of staple goods (EIU, 2022[5]).

Reliance on exports to China has mitigated the trade disruptions caused by Russia's war in Ukraine

Turkmenistan has felt little impact from Russia's full-scale invasion of Ukraine due to its limited trade links with the two countries. It recorded growth of 1.6% in 2022 according to the IMF, driven by elevated global energy prices and higher-than-planned natural gas production and exports boosted by the opening of one of the world's largest gas fields, Galkanysh (EBRD, 2023[6]). Turkmenistan has remained highly reliant on gas exports to China, with the latter accounting for 74% of exports in value terms in 2022 (EIU, 2023[7]). Gas exports to China rose to USD 10 billion, a 51% year-on-year increase. Construction, manufacturing, and services have been booming, while exports of tomatoes and footwear have also been on the rise (ibid). Expansion was spurred by greater domestic mobility, the re-opening of borders, the gradual resumption of international flights, increased trade and revitalised services in 2022 (ADB, 2023[8]).

The war increased trade with and transit through the Middle and Southern Corridors

The war in Ukraine and traffic reductions along the Northern Corridor going through Russia have led to a shift to alternative trade routes, increasing Turkmenistan's trade with its neighbours. Its strategic positioning along the Trans-Caspian International Transport Route (TITR) (also called the Middle Corridor) and the Southern Corridor, connecting the region to the Indian Ocean via Iran, has made the country an important trade node. The seaport of Turkmenbashi recorded a 2.5-fold increase in transit cargo volumes in 2022 due to the increase in the transit of petroleum products, metals, machinery, food, spare parts, chemical cargo, and construction materials. Turkmenistan also intensified trade relations with Iran and operators have been more frequently using the road-based Southern Corridor to avoid bottlenecks along the Middle Corridor (EBRD, 2023[9]).

However, seizing these opportunities will require Turkmenistan to diversify trade and boost investment attraction and the competitiveness of its private sector

Looking ahead, significant downside risks, including a structural slowdown of China's economy, require Turkmenistan to conduct structural reforms to diversify its export base. The government has yet to conduct structural reforms to improve its investment attractiveness, reduce the presence of the state in the economy, increase data and government transparency and unleash private sector development.

The OECD 2020 assessment had identified a need for improved implementation of business- and investment-related legislation, a streamlining of processes for business registration, and simplification of the operational environment for SMEs

Ensure enforcement of the Law on Investment and improve information availability

Turkmenistan's Law on Investment (LoI) governs investment activity in the country and establishes equal rights for investors, their main rights and duties, the procedures for state investment, and protections against abrupt regulatory changes and expropriation. It also guarantees the investor's right to claim compensation and the principle of non-discrimination between domestic and foreign investors and prevents officials and state bodies from interfering in investment activities except as provided by law (OECD, 2021[1]).

The LoI suffers from several weaknesses addressed in the initial assessment, chief among them are unclear protection against direct and indirect expropriation (Art.22), the lack of definition for the amount or method of compensation in case of expropriation, the unconsolidated body of laws governing investments, and the fact that there are two separate investment laws for domestic and international firms, despite the LoI stating that conditions for both should be the same. The OECD had recommended to enhance investment legislation and consolidate it into one act to improve access to information and ensure consistency and coherence (OECD, 2021[1]).

Streamline business registration and licensing, and introduce a one-stop-shop

The main obstacles to conducting business in Turkmenistan relate to long and complex registration, licensing and taxation, with personal connections perceived to play an important role in business success. Business registration is governed by outdated legislation and differs between domestic and international businesses. *De jure* timelines to complete registration are not respected, with domestic businesses reporting an average of six weeks for registration, and international businesses going through an opaque, and altogether different, process involving the Interdepartmental Commission for Protection from Economic Risks at the Agency for Protection from Economic Risks under the Ministry of Finance and Economy (MFE) and the Ministry of Foreign Affairs (MFA). At the time of writing, there was no one-stop shop (OSS) for business registration, although the MFE had initiated the development of a single-window registration platform (OECD, 2021[1]).

The OECD recommended to remove redundant and cumbersome business registration and licensing legislation, as part of a wider effort to simplify the investment-related regulatory framework and to articulate a dedicated SME strategy. In particular, the development of a digital OSS to inform businesses of all procedures, address requests and fulfil all procedures online was recommended, taking into account connectivity constraints and low internet access in Turkmenistan. To improve public-private dialogue, the OECD recommended the creation of a Business Ombudsman with oversight powers over inspection agencies and regulations (OECD, 2021[1]).

Simplify the operational environment for SMEs

Various forms of support to SMEs, including access to finance through state-owned banks, technology, training, and internationalisation are guaranteed by the Law on State Support for Small and Medium Enterprises (2009). The law also provides for simplified procedures for SMEs regarding accounting, taxation, insurance and guarantees regarding regulatory stability, allowing them to apply legislation for five years from the time of registration, regardless of any legislative changes that would lead to prohibitions or restrictions on their activities. A National Development Plan for 2018-2024 was approved to provide support to the development of SMEs, but its implementation remains to be assessed (OECD, 2021[1]).

In 2020, the OECD advised the creation of SME-targeted public instruments, for instance an entrepreneurship fund such as DAMU in Kazakhstan or a dedicated service centre such as the Georgian Innovation and Technology Agency to help SMEs and entrepreneurs access financing, infrastructure, and legal assistance (OECD, 2021[1]).

Priority 1: Legislation can be accessed online, but endeavours to strengthen the Law on Investment and improve contract enforcement would improve the investment climate

The government has increased communication about changes in the law

OECD interviewees reported that access to information has improved through the publication of laws, codes, and decrees on the Ministry of Justice's official website, as well as communication on TV and the radio (Ministry of Justice, 2023[10]). The Ministry has also been conducting seminars with businesses on the topic of foreign investment. Latest amendments to the law date back to 2015, but some terminology was recently clarified according to interviewees. The government is also considering the drafting of a single act compiling provisions of foreign and domestic investment laws. As part of its accession process to the WTO, Turkmenistan has committed to translating into English and Russian laws related to trade and investment.

Efforts to improve the investment framework are taking time to materialise

Information related to legislation and investment conditions is difficult to access

OECD interviewees nonetheless reported the difficulty of accessing information related to legislation. Proposed laws and regulations are not generally published in draft form for public comment. Laws have frequent references to bylaws that are not publicly available and are rarely translated into English. Decrees are not categorised by subject, which makes it difficult to find relevant cross references. There is no information available on whether the government conducts any quantitative analysis of the impact of regulations, and regulations often appear to follow the government's "try-and-see approach" to addressing issues (U.S. Department of State, 2022[11]).

More generally, informational support to investors is not provided. Turkmenistan does not have an investment promotion agency. It seems that the government could do more to incentivise foreign direct investment outside the oil and gas industry. As a result, foreign companies spend significant time conducting due diligence in Turkmenistan and can rely on a limited number of consultants to support them with their prospecting on the ground, with limited information and studies on specific sectors or markets.

Underdeveloped legislation limits opportunities for investment

According to OECD interviewees, existing legislation requires that upon the registration of a new business, the owner should declare a nominal capital figure, which cannot be amended. In case of a later-stage acquisition, the real cost of the company cannot be reflected, which implies that the seller cannot register a profit for his sale and must sell his company at the initial nominal figure. The law in place therefore does not encourage a company to formally invest in another one, which has resulted in investments taking place unofficially.

Contract enforcement remains an issue

Investment and commercial disputes involving Turkmenistan usually involve the non-payment of debts, the non-delivery of goods or services, and contract renegotiations, with the government justifying non-payment because of contract breach. Several cases of disputes between businesses and the government have been caused by the latter's unwillingness to pay in freely convertible currency as contractually required. Contracts can be entirely reviewed and reconsidered following a change in leadership in the government agency that signed the contract, affecting profit distribution, management responsibilities, and payment schedules (U.S. Department of State, 2022[11]).

Enhancing the investment framework requires improving access to information, strengthening contract enforcement, and facilitating domestic investment

Create an Investment Promotion Agency

Turkmenistan should still consider the creation of an Investment Promotion Agency (IPA). Such an agency can be a powerful means to attract FDI and maximise its benefits, in the context of a broadly sound investment climate (OECD, 2020[12]). It can be used as a focal point in the institutional landscape to facilitate the establishment of new investors in the country and can serve to promote the country as an attractive investment destination, bring new investors, and help existing ones expand their activity. For instance, the Government of Kazakhstan reported that Kazakh Invest supported the implementation of 57 projects worth over $3.8 billion in 2021 with the creation of about 5 thousand jobs. The IPA also organised 190 visits of foreign investors to the regions of Kazakhstan with visits to production sites, during which negotiations were held with representatives of government agencies and local businesses (Kazakh Invest, 2022[13]).

IPAs can also play an advocacy role within the government and provide inputs in investment policy design, taking into account their field experience with foreign investors' projects. In designing the agency's role, the government of Turkmenistan could consider selecting priority sectors, countries, and investment projects. It should also ensure that the mandate of the institution is not too large and focuses on investment promotion and facilitation. A clear strategy with well-identified priority sectors and key performance indicators that would be outcome-oriented would optimise the agency's role.

Improve contract enforcement

A first measure to consider includes the government's meeting contract obligations notwithstanding institutional changes. Effective systems of domestic commercial arbitration, mediation, or conciliation matter to foreign investors, as high litigation costs and delays may discourage them from investing in a jurisdiction (World Bank, 2019[14]). In addition, the authorities could adopt a series of good practices to improve the quality, efficiency, and independence of the court system to reduce the time and cost needed to resolve a commercial dispute. For instance, introducing case management systems can improve record-keeping, reduce delays, and case backlogs. Case management intends to ensure the timely and organised processing of cases from initial filing through final outcome. The Ministry of Justice could introduce an electronic case management system by automating key components, such as access to laws, regulations and case laws, access to forms, the generation of a hearing schedule, and access to court orders and decisions (World Bank, 2019[14]). This would serve to improve the transparency of dispute resolution mechanisms.

Review the legal framework to encourage domestic investment transactions

The investment legislation should be reviewed and updated to support domestic investment. Such a review should allow to perform an asset valuation based on the real value of the firm to be invested in.

Priority 2: Administrative procedures for business registration have been revised, but business services could be further digitalised and harmonised among domestic and foreign firms

The government has revised and simplified some procedures for business registration and licensing

Several provisions were introduced by the government in 2022 and 2023 to ease administrative procedures for firms. With regards to licensing, the number of required documents was reduced. Information on how to register a business, registration fees, and an online payment option are now available on the website of the Ministry of Finance and Economy. Whilst a one-stop-shop has not yet been created, registration, licensing and tax procedures are all carried out by the Tax Department under the MFE. A mobile application is currently being tested in demo mode by the Ministry to allow entrepreneurs submit documents online. Customs procedures have also reportedly improved slightly (U.S. Department of State, 2022[11]).

However, procedures are still paper-based and cumbersome

Business registration is based on a lengthy process

Obtaining licenses and authorisations is cumbersome, as these need to be renewed every two years, an exception in the region. In specific sectors, licenses need to be renewed on a yearly basis, while fees charged also differ depending on the industry. OECD interviewees reported that obtaining these licenses is particularly difficult for firms in the pharmaceutical and oil and gas sectors. Under Turkmen law, all local and foreign entities operating in Turkmenistan are required to register with the Registration Department under the MFE. Before the registration is granted, an inter-ministerial commission that includes the Ministry of Foreign Affairs, the Agency for Protection from Economic Risks, law enforcement agencies, and industry-specific ministries must approve it.

Business registration is even more difficult for non-domestic companies. Foreign companies face an even stricter screening process, and encounter difficulties registering a local representative office. The commission evaluates foreign companies based on their financial standing, work experience, reputation, and perceived political and legal risks. Explanations are not provided when registration is denied (U.S. Department of State, 2022[11]).

While the Tax Committee has centralised registration, licensing, and tax payment procedures, as well as contributions to social security, these remain paper based. OECD interviewees reported that while the centralisation of procedures is a welcome step in principle, the Tax Committee has to handle many tasks beyond tax administration, which results in long waiting times and offline queues. Interviewees reported that the issuance of documents requires much more time than stated on paper and renewing a licence for a domestic business can take up to ten days, as tax officers must deal with several other tasks. The lack of online access to information also results in entrepreneurs relying on word-of-mouth to obtain information on financial incentives, programmes and amounts of social contributions.

Bid submission procedures are complex

According to OECD interviewees, companies face several obstacles related to bid submission in tenders. In the absence of digital procedures, interested organisations must submit originally stamped documents, sometimes in sealed envelopes. As such, international companies which do not have a representative office or a branch based in Turkmenistan are less likely to apply due to cumbersome administrative procedures. Local companies wishing to bid must be registered members of the Union of Industrialists and Entrepreneurs to participate in such tenders.

Firms remain subject to arbitrary interventions from the state

Investors complain that they have been discriminated against with excessive and arbitrary tax examinations, license extension denials, and customs clearance and visa issuance obstacles (U.S. Department of State, 2022[11])**.** In several cases, the government has insisted on maintaining a majority interest in joint ventures (JV), which firms have been reluctant to accept because of differing business cultures and conflicting management styles. Although there is no specific legislation requiring foreign investors to receive government approval to divest, in practice they are expected to co-ordinate such actions with the government. In addition, despite *de jure* equal treatment between domestic and foreign firms, the latter reportedly face higher tax rates than local companies (U.S. Department of State, 2022[11]).

The government should further simplify business registration procedures, and level the playing field between domestic and international firms

Streamline the registration process, clarifying the key steps and timelines

The authorities should clarify the key steps required for registration and licensing and provide those services online, including information about fees, procedures, and expected delivery. Announced waiting times for the obtention of documentation should, to the extent possible, be respected. The government should also consider reviewing the requirement to renew licenses every two years, as this is not a common practice and would significantly ease the administrative burden on firms and reduce stress on the public administration. Information could be published on the Ministry of Justice's website as well as on the website of the Union of Industrialists and Entrepreneurs in Turkmen, Russian and English.

Improve access to regulatory information by regularly updating the government's websites

Legislation previously available in Russian has been fully translated into Turkmen, which is a positive development since it has simplified navigation of the legal framework for local entrepreneurs. The Ministry of Justice also provided a clarification on some terms of the legislation. However, legislation should be more regularly updated online, and draft laws should be published for public consultation and comment.

Define the scope of business inspections

To improve the predictability of the operational environment for businesses, the authorities should define and restrict the number of inspections. Turkmenistan could take inspiration from Kazakhstan's Entrepreneurial Code, which codifies allowed instances of unscheduled inspections and bans inspections motivated outside of the scope defined. The Law on the Ombudsman of Turkmenistan was adopted in 2016 and entered into force on 1 January 2017, but the office of the Business Ombudsman is still pending creation according to the government. The creation of the Business Ombudsman can help receive complaints from businesses about unfair treatment by public authorities, including repetitive audits or inspections, unreasonable fines and penalties, or threats and acts of retaliation by government officials (OECD, 2021[1]). Such complains could be integrated into an independent reporting mechanism to the authorities.

Priority 3: The operational environment for SMEs could be further boosted by trade facilitation reforms and the provision of a wider array of financial products

The post-pandemic period has provided some relief to businesses

Foreign trade has resumed thanks to the re-opening of borders

OECD interviewees mentioned the reopening of borders following the COVID-19 pandemic as a very positive development as it allowed firms to resume trade with their international partners. Borders were closed from March 2020 to spring 2022. Recent developments also show that Turkmenistan is increasingly integrating into regional trade. In August 2022, Turkmenistan agreed to jointly develop the international north-south corridor running through its territory, improve bilateral trade and transport connectivity, and simplify its visa regime (EBRD, 2023[6]). In addition, a new Trade Facilitation Portal was launched by the Ministry of Trade and Foreign Economic Relations and the International Trade Centre (ITC) in April 2023, to reduce the time and costs for trade across borders. The Portal guides businesses through import, export, and transit requirements; gives access to agreements, laws, regulations, forms, acts of inspections and other documents; as well as shares international trade statistics covering more than 25 product groups, with a focus on the agrifood sector. It should help exporting SMEs have a better access to information and support the government in its accession process to the World Trade Organisation (WTO). In addition, Turkmenistan was added to the Info Trade Central Asia Gateway which provides direct access to step-by-step guides on licenses, pre-clearance permits and clearance formalities for most goods traded within, to and from Central Asia (Info Trade Central Asia Gateway, 2023[15]).

Access to SME financing has registered some progress

Access to finance has also improved. Firms can borrow and save foreign currency in local bank accounts, as credit lines are available in both Turkmen manat and in USD. Vneshekonombank provides foreign currency loans guaranteed by the Islamic Development Bank (ISD). According to OECD interviewees, an investment loan type of product is priced at an interest rate of about 5-6%, trade-related loans at a 13%-interest rate. The number of required documents was also reviewed and streamlined, which allows for a faster application process. According to the Union of Entrepreneurs and Industrialists, the state programme on SME support for 2018-2024 has provided certain benefits to SMEs, such as land granted free of charge for up to 100 years, preferential loans, tax breaks for agricultural producers, etc. Discussions are ongoing to lift manat convertibility restrictions for products produced in free economic zones (FEZ) (U.S. Department of State, 2022[11]).

However, the business environment remains difficult to navigate

Foreign currency controls and a limited array of public financing instruments restrict firms' access to finance

The lack of suitable legislation for financial instruments, such as the absence of capital venture funds, currency conversion, and dividend repatriation restrictions impede both domestic and foreign investment. The spread between the official and black-market exchange rates remains distortive and is being used as an import substitution subsidy, distorting competition and raising costs (EBRD, 2023[6]). Foreign investors can access Turkmen manats exclusively through equity loans from the EBRD and the Turkmen-Turkish Bank, while domestic firms have restricted access to foreign currency beyond foreign currency denominated loans. Despite their existence on paper, capital markets are not resorted to in Turkmenistan, although the 1993 Law on Securities and Stock Exchanges outlines the main principles for issuing, selling, and circulating securities. The 1999 Law on Joint Stock Societies further provides for the issuance of common and preferred stock and bonds and convertible securities in Turkmenistan, but in the absence of a stock exchange or investment company, there is no market for securities (U.S. Department of State, 2022[11]). The EBRD is currently working with local entrepreneurs to foster an early community of private investors in the country, with a product called star venture for SMEs. However, the infrastructure around it, such as an accelerator and business incubator, needs to be created.

Access to land remains restricted

Land is owned by the state. Whilst citizens have land rights, they cannot sell or mortgage land, and land rights can be transferred only through inheritance. This restricts options for firms to use land as collateral, and for the government to collect taxes on property. Foreign companies or individuals are permitted to lease land for non-agricultural purposes, upon approval of the Cabinet of Ministers, which issues the leases. There were no data available on the number of leases granted in 2021 or 2022 (U.S. Department of State, 2022[11]).

Access to finance, digitalisation and trade facilitation are areas where the government can pursue its efforts to improve the operational environment for businesses

Expand the range of available financial instruments

The banking system could be developed to offer a wider range of financial products available for firms. The government has recently started talks with international organisations to develop a national start-up ecosystem involving the development of venture capital funding with USAID. Other products such as SME lines of credit for longer tenors, the provision of partial credit guarantees, or leasing could be provided to SMEs by financial institutions in Turkmenistan. Such products would allow firms to rely less on their own funds and retained earnings to finance operations. At the macro-level, improving financial inclusion can drive employment, productivity gains and tax collection (IMF, 2019[16]).

Expand digital infrastructure

Whilst interviewees mentioned that internet speed has slightly increased, it remains the world's slowest (0.77 Mbps) and the most expensive in Central Asia, at an average fixed broadband monthly cost of USD 45.80 (Cable.co.uk, 2023[17]). An area for further improvement includes the development of the digital infrastructure, as unreliable Internet access, slow download and upload speeds hinder business development, especially in rural areas, which may not have access to the internet altogether. Such a development should go together with the implementation of the government's strategy for digital transformation, which includes the development of e-government services. When upgrading its digital infrastructure, policymakers should be mindful of inclusive access in rural areas, as digital access gaps are strongly associated with gaps in productivity, scaling up, innovation and growth, which contribute to inequalities among firms, and, in turn, people and places (OECD, 2022[18]).

Capitalise on the Middle Corridor's renewed interest to facilitate trade

Turkmenistan can seize the opportunity of the renewed interest in the Middle and Southern Corridors to address transport and logistics bottlenecks, **and attract investment in pipelines, railways, roads, sea transport, and logistics infrastructure** (EBRD, 2023[6]). The opportunity to play a more central role in serving trade between China, Iran, Central Asia, Türkiye and southern Europe could lead to a gradual modernisation of the country's transport networks and logistics capabilities, including border management. The government should conduct trade facilitation reforms to reduce border crossing times in tandem with an infrastructure development plan, to ensure that better infrastructure use can capitalise on smoother trade procedures (OECD, forthcoming[19]). Turkmenistan has started work with the OECD to join the OECD Trade Facilitation Indicators database (OECD, forthcoming[20]).

References

ADB (2023), *Turkmenistan - Asian Development Outlook April 2023*, https://www.adb.org/sites/default/files/publication/863591/tkm-ado-april-2023.pdf (accessed on 27 July 2023). [8]

BTI Transformation Index (2022), *BTI 2022 Country Report - Turkmenistan*, https://bti-project.org/en/reports/country-report/TKM#pos8. [3]

Cable.co.uk (2023), *Global Broadband Pricing League Table 2023*, https://www.cable.co.uk/broadband/pricing/worldwide-comparison/#speed (accessed on 21 July 2023). [17]

EBRD (2023), *Country Assessments Turkmenistan*, https://2022.tr-ebrd.com/. [6]

EBRD (2023), *Regional Economic Prospects - Getting By: high inflation weighs on purchasing power of households*. [9]

EIU (2023), *Country Report Turkmenistan 3rd Quarter 2023*, https://country.eiu.com/turkmenistan (accessed on 21 July 2023). [7]

EIU (2022), *Country Report Turkmenistan 1st Quarter 2022*, http://www.eiu.com/FileHandler.ashx?issue_id=1251756108&mode=pdf (accessed on 24 July 2023). [5]

IMF (2023), *World Economic Outlook Database, April*, https://www.imf.org/en/Publications/WEO/weo-database/2023/April. [4]

IMF (2019), *Financial Inclusion of Small and Medium-Sized Enterprises in the Middle East and Central Asia*, https://www.imf.org/en/Publications/Departmental-Papers-Policy-Papers/Issues/2019/02/11/Financial-Inclusion-of-Small-and-Medium-Sized-Enterprises-in-the-Middle-East-and-Central-Asia-46335 (accessed on 21 July 2023). [16]

IMF (2019), *IMF Staff Concludes Staff Visit to Turkmenistan*, https://www.imf.org/en/News/Articles/2019/11/14/pr19414-turkmenistan-imf-staff-concludes-staff-visit (accessed on 21 July 2023). [2]

Info Trade Central Asia Gateway (2023), *Central Asia Gateway: Connect Central Asia and international markets*, https://infotradecentralasia.org/?utm_source=Sarbacane&utm_medium=email&utm_campaign=1st%20%20Edition%20%20-%20ENG%20%202023%20Ready4Trade (accessed on 24 July 2023). [15]

Kazakh Invest (2022), *Government Considers Results of Activities of KAZAKH INVEST in 2021*, https://wkr.invest.gov.kz/media-center/press-releases/v-pravitelstve-rassmotreli-itogi-deyatelnosti-kazakh-invest-v-2021-godu/ (accessed on 27 July 2023). [13]

Ministry of Justice (2023), *Turkmenistanyn Adalat Ministrligi*, https://minjust.gov.tm/ (accessed on 21 July 2023). [10]

OECD (2022), *Key Messages - EMnet Working Group on Digital Transformation in Emerging Markets 2022*, https://www.oecd.org/dev/Key_Messages_EMnet_WorkingGroup_DigitalTransformation_EmergingMarkets.pdf (accessed on 21 July 2023). [18]

OECD (2021), *Improving the Legal Environment for Business and Investment in Central Asia*, OECD Publishing, https://www.oecd.org/eurasia/Improving-LEB-CA-ENG%2020%20April.pdf. [1]

OECD (2020), *Investment Promotion in Eurasia: A Mapping of Investment Promotion Agencies*, OECD Publishing Paris, https://www.oecd.org/eurasia/competitiveness-programme/Investment-Promotion-in-Eurasia-A-Mapping-of-Investment-Promotion-Agencies-ENG.pdf. [12]

OECD (forthcoming), *Realising the Trade Potential of the Middle Corridor*. [19]

OECD (forthcoming), *Trade Facilitation in Central Asia*. [20]

U.S. Department of State (2022), *2022 Investment Climate Statements: Turkmenistan*, https://www.state.gov/reports/2022-investment-climate-statements/turkmenistan/. [11]

World Bank (2019), *Enforcing Contracts*, https://subnational.doingbusiness.org/en/data/exploretopics/enforcing-contracts/good-practices (accessed on 21 July 2023). [14]

6 Uzbekistan

This chapter assesses progress made and challenges ahead in the three priority areas for reform identified in 2020, namely the investment climate, the operational environment for businesses, and taxation, considering the impact of the pandemic and Russia's war on Ukraine. Progress has been made in particular in clarifying the regulatory framework for investment, making the business environment easier to navigate for firms, and digitalising tax services.

Table 6.1. Summary of priority reform implementation and updated recommendations

2020		2023	
Challenges identified	**Recommendations**	**Implementation assessment**	**Way forward**
Legal framework for investment: Improve implementation of investment legislation	➢ Ensure proper implementation of the new investment law and remove sectoral restrictions ➢ Ensure consistent enforcement of ICSID judgments ➢ Continue to reduce the role of the state in sectors where its present has an indirect discriminatory effect	➢ Significant reforms to increase investor protection rights were undertaken ➢ But a lack of transparency remains	➢ **Provide additional guarantees on the impartial treatment of investment projects** ➢ **Remove restrictions where relevant and level the playing field**
Operational environment for SMEs: Streamline business regulation	➢ Streamline and consolidate legislation and licenses for firms and entrepreneurs ➢ Accelerate digitalisation of procedure for all firms ➢ Improve dispute resolution including in local courts and through ADR	➢ The streamlining of procedures and legislation has made significant progress ➢ Yet the pace of reforms creates implementation challenges ➢ Market competition is limited	➢ **Improve the dialogue with the business community** ➢ **Pursue reforms to increase competition** ➢ **Increase the transparency of rulemaking**
Taxation: Improve tax administration	➢ Ensure predictability of changes to tax requirements and improve tax administration for SMEs ➢ Complete the full digitalisation of tax procedures ➢ Streamline the tax code and ensure its implementation	➢ Fiscal policy developments have reduced the tax and administrative burden on firms ➢ However, tax administration remains the most contentious issue mentioned by firms	➢ **Address implementation issues** ➢ **Work on improving relations between the Tax Committee and the taxpayers** ➢ **Review the incentive regime**

Source: (OECD, 2021[1]), OECD analysis (2023).

Introduction

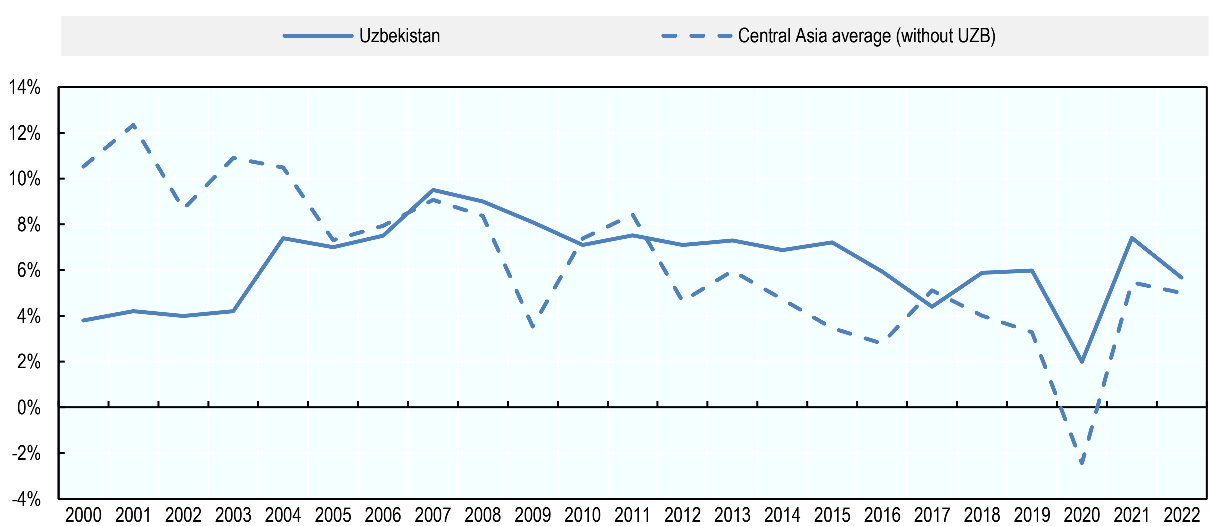
Uzbekistan has shown resilience to the pandemic and war, but further structural reforms will prove necessary to navigate a volatile environment

Reform have recently supported robust economic growth

Uzbekistan has registered sustained growth since the mid-1990s: following the transition recession of 1990-1995, Uzbekistan's real GDP has grown at an average annual rate of 5.7%, from 1995 to 2022, above the regional average of 5.3% (World Bank, 2023[2]). Growth during the early years of independence was driven by the state-led distribution of resources and outputs among state-owned enterprises and the export of commodities, especially gold (Brookings, 2022[3]). Development relied on the use of natural resources and physical capital, with little focus on productivity, efficiency and the employment and development of human capital.

Uzbekistan's economic transformation started in early 2017, when the country embarked on a wide-ranging reform programme launching the transition to a more open and competitive economy (World Bank, 2022[4]). The government's initial efforts focused on liberalising the foreign exchange rate and prices, increasing expenditures in the social sector, revamping the tax system and increasing fiscal and debt transparency, with the aim of enabling the private sector to play a larger role in the economy and to reduce that of the state. Whilst the COVID-19 pandemic has arguably been one of the deepest economic shocks to hit Central Asia since independence (OECD, 2021[5]), Uzbekistan was one of the few countries worldwide to avoid recession in 2020 (Figure 6.1).

Figure 6.1. Real GDP growth (2002-2022)



Source: (IMF, 2023[6])

The COVID-19 pandemic and Russia's war in Ukraine have shifted the government's focus to relief measures

Uzbekistan's recent economic performance has been impressive, but the fundamentals of a market economy are still being created. A low public debt-to-GDP ratio (although it has risen significantly in recent years), significant inflows of remittances and high gold prices have allowed the country to mitigate the impacts of the COVID-19 pandemic and the war (OECD, 2023[7]). However, these two shocks seem to have also shifted the government's focus to short-term relief and delayed more structural reforms to transform and reduce the size of the state in the economy. Privatisation and enterprise restructuring in particular have slowed, limiting the effectiveness of other reforms to improve the business climate and to create a level playing field for firms. Uzbekistan's rate of new firm creation remains among the lowest compared with regional and income-level peers (World Bank, 2022[4]), due to the misallocation of resources towards less efficient firms and the lack of reward for firms with growth potential.

Table 6.2. Summary table of government support measures during the COVID-19 pandemic and at the beginning of Russia's war in Ukraine

Relief measures	COVID-19	Beginning of Russia's war in Ukraine
Monetary policy	• base rate decrease from 16% to 15% in April 2020 and from 15% to 14% in September 2020 to stimulate liquidity support	• base rate increase from 14% to 17% by the National Bank of Uzbekistan; • hire of international consultants by Uzbek banks to limit their operations with sanctioned Russian banks and avoid the risk of secondary sanctions;
Fiscal policy	• deferred tax payments for up to 6 months granted to businesses; • tax benefits granted to the tourism sector;	• halt in non-priority public spending for the purchase of fixed assets and building repair; • extension of several temporary exemptions to fiscal rules and transportation tariff waivers for food importers;
Household support	• creation of an Anti-Crisis Fund endowed with UZS 10 trn (USD 1 bn) • excise tax and customs duties were set at zero for the import of 20 types of basic consumer goods; • expanded funding for healthcare • increased the number of families with children and low-income families receiving social benefits;	• introduction of more comprehensive measures to support labour migrant workers and their families; • increase in basic food stocks to prevent further price increases; • increase in land allocation and agricultural output targets to ensure food security;
Firm support	• extension of loan repayment period for the tourism and catering, transport and logistics sectors; • provision of interest-free loans through banks to industries most exposed to the virus; • allocation of UZS 200 bn to the Public Works Fund; and • allocation of UZS 500 bn to the State Fund for Entrepreneurship Support to assist business entities creating jobs. • loan repayment deferral by businesses to commercial banks.	• allocation of additional funds to the State Entrepreneurship Support Fund to increase concessional lending; • allocation of an additional UZS 10Tn of revolving loans for purchase of raw materials and turnover increase; • introduction of work and visa programmes to attract foreign IT specialists.

Source: (OECD, 2021[8]), (OECD, 2022[9])

Further structural reform is crucial for the economy to become more inclusive and resilient to climate change

Maintaining reform momentum is essential to ensuring that the benefits of Uzbekistan's economic growth are more widely shared (World Bank, 2022[4]). In the current volatile environment, policymakers should focus on market-oriented structural reforms, such as the privatisation of state-owned enterprises (SOEs) and state-owned banks (SOBs), increasing competition and levelling the playing field for firms. Reforms are needed to foster firm and job creation and absorb a rapidly expanding labour force, which would ultimately serve to reduce vulnerabilities to external downswings in key external labour markets (OECD, 2023[7]). On the environmental front, continuing efforts to reduce the high levels of CO2 emissions and energy should contribute to reducing the social cost of inefficiency and emissions: the OECD Environment Directorate estimates that Uzbekistan has by far the highest level of premature deaths due to particulate matter 2.5 (PM2.5) exposure in Central Asia (around 800 per 1,000,000 inhabitants) (OECD, 2022[10]).

To help the government of Uzbekistan strengthen the business environment and create conditions to level the playing field between firms, the OECD conducted research in 2019-2020 in the legal environment for business that pointed to the importance of further structural reforms in three policy domains, namely the investment framework, the operational environment for businesses and tax administration (OECD, 2021[1]).

The OECD 2019-2020 research identified a need for improved implementation of investment legislation, the legislative framework for businesses and tax administration

Implementation of investment legislation

The Law on Investment and Investments Activity (LoI) passed in 2019 has served to clarify the investment framework by replacing obsolete legislation and systematising existing laws and by-laws (OECD, 2021[1]). It has also helped level the playing field for domestic and foreign investors, with a *de jure* impartial granting of investment protections to both types of investors. However, the (OECD, 2021[8]) report identifies the need to ensure enforcement of this new law and had also spotted several loopholes in this new framework, including, among others, (i) the exclusion of numerous forms of investments from the scope of the law, such as those under production-sharing agreements, concession contracts, public-private partnerships (PPPs), and special economic zones (SEZs). It was also pointed out that the legal hierarchy between laws governing these areas of activity and the LoI needed clarification to improve certainty, especially regarding the SEZ laws' interactions with national legislation. In addition, (ii) stabilisation guarantees granted to investors, stating that detrimental regulatory changes would not apply for a period of ten years, appeared unfavourable to the government. Lastly, whilst Uzbekistan outperforms the rest of the region when it comes to regulatory openness to foreign investment, (iii) some sectoral restrictions, such as in the banking and business service sectors, could be re-evaluated.

Legislative consolidation for businesses

Reforms such as price liberalisation, the reduction of import tariffs, and foreign exchange liberalisation have contributed to improving the business environment and fostering private-sector development in Uzbekistan. However, the pace of legislative changes and their speedy enforcement has created difficulties for the administration and for firms to implement and adapt on time. In addition, a critical challenge identified in 2020 related to contradictions between primary and secondary legislation. It was suggested to the government to adopt a single coherent piece of legislation that would supersede and annul previous contradictory laws. Such legislation should also include a single, clear definition of SMEs to adapt legislation to the reality of the economic landscape of the country. Finally, it was recommended to speed up the digitalisation of procedures and to publish the Business Ombudsman's reports of companies' feedback to identify and address the most important bottlenecks.

Tax administration

Tax administration was identified as the most contentious issue for the private sector. Whilst several tax rates were reduced in the new version of the Tax Code, frequent tax changes were highlighted as a source of uncertainty for investors and businesses. A simplified regime was introduced for SMEs with a turnover below 1 billion UZS (roughly 79,000 EUR), but it created significant challenges to the tax administration when around 22,000 firms qualifying for the simplified regime registered under the standard one. Overall, it was recommended to ensure changes were more predictable, to improve tax administration, especially with regards to VAT refund, and to further digitalise tax procedures to reduce face-to-face interactions and red tape.

Assessing progress since 2020

The following sections provide an overview of implementation progress of since 2020, and suggest ways forward, taking into account new priorities following the pandemic and the changed regional context (

Table 4.1).

Priority 1: The investment climate has improved but efforts should be pursued to create a level-playing field among investors

The government has prioritised investment dispute resolution reforms to improve the investment climate

A review of the LoI is underway

Recent legal developments have contributed to improving the investment environment. The 2019 LoI helped increase transparency and predictability for investors, with a streamlining of the law. The government has recently tasked itself to further review it with IFC support to provide additional clarity on investor protections and treatment standards, to align its provisions more closely with international legal frameworks and to address remaining ambiguous clauses (see above). Updating *de jure* provisions will however need to go hand in hand with proper implementation and enforcement.

The Tashkent International Commercial Court is to be established

The government recently announced the creation of the Tashkent International Commercial Court, with the aim of establishing a domestic court to settle international investment disputes (The Tashkent Times, 2023[11])**.** It will be part of the country's court system, but will be independent in its regulation and proceedings, and should serve as a trusted and neutral platform for investors to solve their litigation cases with the government. The language spoken in the court and documentation will be English, and judges will be selected internationally based on their track records in dealing with investment disputes. International lawyers will be able to represent their clients and will be supported by locally registered lawyers, giving opportunities for the local legal community to benefit from international peer-learning. Whilst such an initiative is a positive development, the government should ensure regular exchanges of good practice with national courts to avoid the creation of a two-tiered justice system. As seen in the case of the AIFC Court in Kazakhstan, arbitration provided in English and the high costs associated with its procedures have not always proven accessible to domestic entrepreneurs.

Uzbekistan is becoming more integrated in the global investment and trade community

Uzbekistan's increased engagement with the international trade and investment community has proved useful in boosting the country's investment attractiveness. The creation of an annual foreign investor platform for the government and foreign companies has served to discuss and address challenges in the investment environment. In August 2021, the President chaired the first session of this platform with investors and businesses. Uzbekistan's adhesion to the EU's GSP+ Arrangement in 2021 has also enhanced the country's investment attractiveness, as it now benefits from more favourable trade conditions. Domestic firms are eligible to a full removal of customs duties on two-thirds of tariffs lines when exporting to the EU in a wide range of sectors. The joining of the GSP+ also reflects the country's progress in improving the business climate, the judicial system and labour conditions (UNCTAD, 2021[12]). Finally, aligning the country's trade regime with WTO requirements should also serve to reduce trade barriers and further integrate Uzbekistan in regional and international trade.

The competitive field remains distorted, and dispute resolution still needs strengthening

Further progress could be made to increase the transparency of public procurement and privatisation

The creation of a transparent environment for investors is nonetheless taking time to materialise. The selection process for large investment or privatisation projects is not always made on the basis of a public tender due to the government's desire to attract investment and the cumbersomeness of the public procurement system. Capital flows are directed towards major export-oriented or import-substituting industries, while investments in import-consuming projects generally see limited support from the government (U.S. Department of State, 2022[13]). This also results in little investment in knowledge-intensive sectors (World Bank, 2022[14]).The government scrutinises investments, but there is no standard screening mechanism in place to assess, authorise and condition FDI based on a range of clearly stated criteria. This can challenge the creation of a level playing field and increase the risk of corruption, as firms may need to negotiate individually the terms of the screening mechanism as well as special decrees to obtain authorisations for investment projects. Such practices also disadvantage SMEs, which do not have in-house capacity to address gaps in the law with *ad-hoc* agreements with the government.

The need for greater transparency also applies to investments in the privatisation process. The government has announced an ambitious privatisation programme which plans to reduce the number of SOEs by 75% by 2025. However, this effort seems to precede the spelling out of a rationale for privatisation and the establishment of a strong legal foundation to pursue those objectives and create an attractive investment framework (World Bank, 2022[4]). In particular, the government has not thoroughly updated its asset valuation law since 1992. Setting an appropriate firm valuation method requires the establishment of specific criteria for the evaluation process in the context of competitive bidding, especially as valuing a firm aways involves a certain degree of subjectivity. The valuation method would allow the government of Uzbekistan to justify the share price it offers, ensure value for money and maintain a high quality of privatisations. In some OECD countries such as France, Italy, Poland, Spain and Türkiye, valuation prior to privatisation is mandated by law (OECD, 2019[15]). Another gap identified in the investment legislation relates to the persistence of restrictions on (i) private investment in SOE-dominated sectors, such as equity restrictions - there is currently a 49% share limit in the charter capital of SOEs being opened to privatisation. (ii) capital movement transactions, as transfers of funds above 10,000 USD outside of Uzbekistan require according to a Central Bank of Uzbekistan regulation, approval from the Cabinet of Ministers or the President (Lex.uz, 2013[16]).

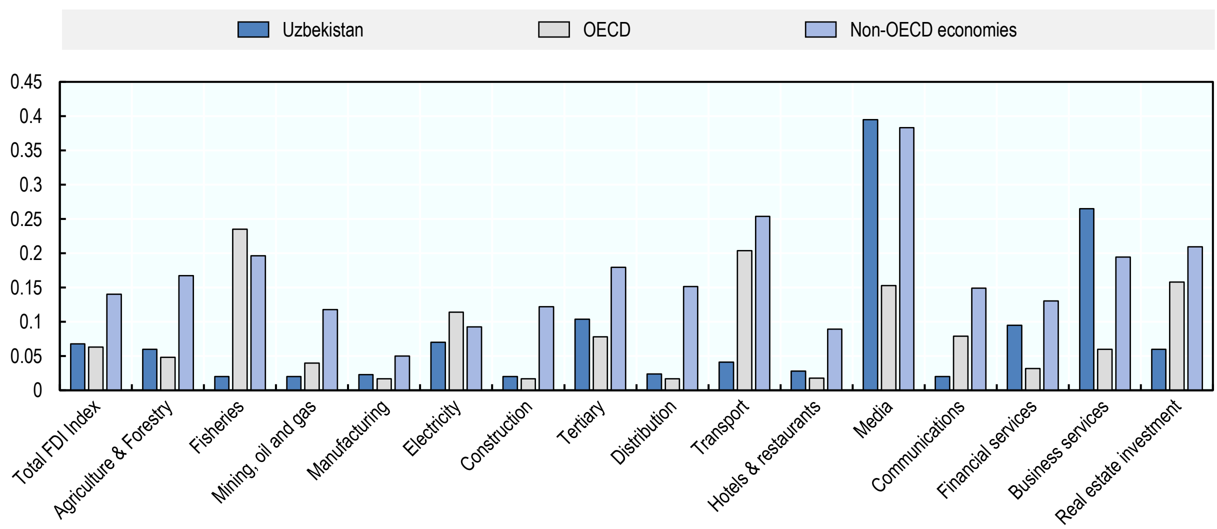
The channelling of preferences and incentives distorts the level-playing field

There seems to be a gap between *de jure* equal treatment and *de facto* selected incentive allocation. Current legislation states that equal opportunities should be granted to domestic and foreign investors alike. Several incentives and benefits are nonetheless still given to legal entities involving private foreign direct investment and specialising in manufacturing products and services, depending on the share of FDI, and on a case-by-case basis. Tax breaks are granted in the form of exemption from land tax, property tax and tax for the use of water resources under certain conditions, such as a minimum 15% foreign stake in a legal entity. Such customs exemptions, subsidies and tax breaks offered according to the LOI, the Tax Code and investment contracts, contradict other legislation, which states that the granting of opportunities should be made equal between foreign and domestic investors. Conversely, protectionist measures to support domestic production and limit foreign competition remain, such as a ban from the public procurement process of a list of specified imported items, preferential access granted to SOEs to land, infrastructure, credit, state support, contracts, and cheaper business establishment procedures for domestic firms; which also contribute to distorting market entry.

Statutory sectoral restrictions on foreign investment are few but not so clearly stated

Sectoral restrictions for foreign investment *de facto* remain, such as in agriculture, transport, media and banking (Figure 6.2**).** For instance, land ownership in the agriculture sector is not allowed, but leases can be granted to both domestic and foreign entities. While these are stated in legislation, they are scattered across different laws, and can be issued by ministries or government agencies which could define an up-to-date negative list of sector-specific restrictions on FDI while restrictions mentioned in the LOI under a negative list are not publicly available (World Bank, 2022[14]). Similarly, market entry and operational restrictions remain in some commercial sectors, such as aviation, chemicals, and telecoms. SOEs' persisting influence over regulation and policies in energy, transport and telecoms have contributed to higher prices, less innovation, fewer services and lower quality (World Bank, 2022[4]).

Figure 6.2. OECD FDI Regulatory Restrictiveness Index for Uzbekistan (2020)



Note: Open = 0, closed = 1.
Source: OECD (2020).

Dispute resolution mechanisms are not fully aligned with international best practices and commitments, despite the creation of the Tashkent International Arbitration Centre (TIAC)

Uzbekistan has not fully aligned its dispute settlement legislation with international treaties and agreements. The country is a signatory to both the Convention on the Settlement of Investment Disputes between States and Nationals of Other States and the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention). However, it has not fully aligned its procedural legislation with the latter. Old bilateral investment treaties are still in place, which include ambiguous formulations that expose the country to a high risk in investor-state disputes (World Bank, 2022[14]), and may create complexities with the enforcement of arbitral awards in domestic courts (Dentons, 2023[17]).

Alternative dispute resolution mechanisms exist, including mediation and conciliation, and are increasingly used in commercial disputes. The LOI introduced a dispute-resolution mechanism based on four steps, where an investor may only seek to commence international arbitration proceedings against the state if he has first attempted to resolve a dispute through negotiations, mediation and litigation in Uzbek courts (OECD, 2021[8]). However, the stage at which it is deemed impossible to resolve the dispute following negotiations and mediation is not clearly defined. In the absence of clear investor grievance and dispute resolution mechanisms, the government exposes itself to an immediate resort to international arbitration procedures, with significant cost and reputation implications. The Spanish company Maxam's recent filing to an international arbitration court following an unresolved dispute with Uzkimyosanoat poses a major test for the government's efforts to attract Western FDI.

Levelling the playing field, more communication on existing restrictions and the strengthening of dispute resolution mechanisms will enhance the investment climate

Additional measures should be taken to level the playing field among firms

Further transparency around the existing incentive regime should be provided. Detailed communication around the criteria for, and the beneficiaries of, exemptions and breaks is lacking, increasing the risk of corruption and capture by vested interests (World Bank, 2022[4]). Current practices grant SOEs favourable access to inputs and regulatory preferences, impeding private sector market entry, while individually negotiated resolutions provide large foreign investors more favourable terms than to smaller ones. The government should publish in a more consistent manner a list of the beneficiaries of such exemptions and consider performing a cost-benefit and impact analysis of the regime, given its implications in terms of forgone public revenue. On that basis, it could decide whether to perpetuate the system, and ground the granting of selected, clearly communicated preferences on sound economic arguments. This would serve to increase the transparency of the investment environment, which would have a positive effect on attracting and retaining FDI: only 15% of the OECD's latest business climate assessment survey respondents in Uzbekistan highlighted incentives and special services to foreign investors as a main reason for doing business in the country (OECD, 2023[7]), suggesting that incentives only play a marginal role in an investor's decision to set up activity in a country.

Explicit statutory restrictions on foreign investment could add clarity to the investment framework

Whilst statutory restrictions are comparatively low in Uzbekistan, explicitly stating which sectors are subject to FDI restrictions, and what the screening mechanisms are, would prove useful. At the time of writing, such information did not seem to be available on the Investment Promotion Agency's website or in the LOI. Although not needed to be enshrined in a legal act, providing guidance in an implementing regulation and on freely accessible online resources as to what considerations, including restrictions, are taken into account when assessing an investment project would mitigate perceived risks and increase investor confidence (OECD, 2017[18]). Beyond the immediate impact on inflows, the government should also evaluate how these restrictions affect downstream industries and consumers. Attention should also be paid to ensuring that the lifting of restrictions and privatisation do not result in merely replacing public with private monopolies.

Involving foreign investors in SOB privatisation is a welcome initiative that should be pursued. Notwithstanding the potential risks associated with foreign bank entry (increased vulnerability of an inter-connected cross-border banking system to international financial crises) (IMF, 2000[19]), clarifying the bank licensing environment and lifting restrictions on foreign investments in the financial sector and on the establishment of foreign-owned banks would make it possible to expand the role banks can play as financial intermediaries and increase competition in the financial sector. Studies show that a greater presence of foreign banks in a banking system has a positive spillover effect on loan growth (EBRD, 2002[20]). Foreign banks can also spur innovation by increasing competitive pressure on the market and introducing better technologies, skills and products, in a context where the government has expressed its intent to privatise eight out of the twelve state-owned commercial banks by 2025, which would increase the share of private banking assets from 15% to 60% of the total (World Bank, 2022[21]). The recent privatisation and acquisition of Ipoteka Bank by Hungarian OTP Bank is a significant step in that regard (OTP Group, 2022[22]).

The government should consider lifting restrictions on the opening of branches of foreign legal entities. Legislation does not explicitly prohibit the establishment of branches of foreign entities, but in practice Uzbek authorities do not register such branches (EY, 2021[23]). Relaxing this provision would allow foreign companies and banks to conduct operations in Uzbekistan.

Further align dispute resolution mechanisms with international best practices

The authorities should build awareness across the public administration of the international commitments taken to ensure that domestic courts recognise and enforce decisions accordingly. This would also serve to resolve the issue of conflicting interpretations of legislation which may arise between government officials, attorneys, and judges. The Ministry of Justice could publish internal guidelines and conduct trainings and capacity building in courts to inform attorneys and judges of Uzbekistan's commitments with regards to international conventions.

In parallel, spelling out a clear investor grievance mechanism would serve to process and conciliate issues between investors and the state, and prevent escalation to legal proceedings. It would also contribute to increasing the retention of existing investment projects in the country (World Bank, 2022[14]). The government could initiate the creation of an investor grievance committee, detail its design and functioning processes, and publish informal guidelines on its expectations and examples of its operations in practice. It could also create an interactive electronic platform for investors to submit and follow their grievances easily. The Foreign Investors' Council could play such a role and formulate proposals to update and revise policies for investment protection, but this would require an independent status.

Despite the importance of non-judicial mechanisms, an independent judiciary is a critical foundation for law enforcement that affects investment, as firms need an impartial mechanism to resolve disputes. Whilst the government's recent governance reforms have focused on improving judicial and law enforcement services, judges' ability to decide cases autonomously could still be improved. Uzbekistan could look at Kazakhstan's ''Seven Pillar Strategy'', which aims to raise the quality and coherence of judgments, and businesses and citizens' trust in judicial bodies. The Supreme Court developed a decision template to guide the process of drafting judgments and increase its reliability and developed a new system of judicial recruitment to select competent judges trained in accordance with international standards (OECD, 2021[1]). The draft law to appoint Constitutional Court judges for a ten-year term without the right to re-election is a positive development to increase the independence of the judiciary (Kun.uz, 2023[24]).

Priority 2: The operational environment for businesses has improved through digitalisation and simplification but could benefit from impact assessment and more competition

The government is working to make the operational environment simpler for businesses

The streamlining of procedures and legislation has made significant progress

A wide array of government services has been digitalised and is now available online. According to the government, around 50% of public services have been digitised (President of the Republic of Uzbekistan, 2023[25]), with plans to raise that figure to 80%. The licensing regime update in July 2021 has made it possible to streamline the obtention of licenses, permits and notification procedures (World Bank, 2022[4]). Respondents to the latest OECD business climate survey in Uzbekistan reported the digitalisation of procedures and the removal of redundant licenses and permits as the two most useful measures implemented to assist foreign companies (OECD, 2023[7]).

Another important development is the drafting of a new Entrepreneurship Code which streamlines and consolidates existing business legislation, clearly defines the rights and obligations of firms, and clarifies the process of opening and closing a business (Box 6.1). It proposes to divide business entities into several categories depending on their average annual turnover and number of employees. The concept of social entrepreneurship is also introduced. The Ministry of Justice reported that 73 types of documents previously required in licensing procedures had been withdrawn, and that the fees charged have been reduced for several types of services. The drafting of the code involved consultations with the private sector and international community, although most OECD interviewees were not aware of its existence.

Significant efforts have also been pursued to reduce the regulatory burden on firms. Several government and Presidential Decrees have aimed at streamlining existing legislation. For instance, the parliament and the government reported the adoption of 35 laws and over 100 regulations or amendments to legislation, which abolished nearly 1,000 laws and regulations in 2020 (Lex.uz, 2020[26]) (Lex.uz, 2020[27]). In late 2022, a presidential decree aiming to simplify the state regulation of business activities was signed and defined the limits of state regulation of entrepreneurial activity, limiting them to the registration of business entities, tariff and non-tariff regulation, compulsory liability insurance, and the protection of competition, among others (Lex.uz, 2022[28]). The number of business inspections is to be cut in half, required licences and permits reduced by 30% and exclusively performed online. Starting from January 1, 2024, the Chamber of Commerce and Industry and the Business Ombudsman, in collaboration with industry representatives, will introduce an open entrepreneur rating. Those with high ratings will be exempt from all forms of tax audits, and any excess value-added tax will be returned to them within a day. The modalities for running the rating system are yet to be defined. Among other important initiatives, a Unified Electronic Registry of Mandatory Requirements in the Field of Entrepreneurship to reduce the regulatory burden on firms will be launched in July 2025 and operated by the Ministry of Justice. The aim of this registry is to make an inventory of all established requirements for business regulation and make proposals to review them. The first stage of creating this registry includes forming a list of mandatory requirements for firms in the areas of construction, trade, public catering, education and transport. The second stage should encompass more sectors. However, it remains to be seen whether this register will simplify the operational environment or add complexity and layers of administrative requirements for firms. The latest update of the Centre for Economic Research and Reforms (CERR)'s business climate indicator showed an improvement in the business environment, driven by less difficulties in accessing financing and a better assessment of the tax administration (Trading Economics, 2023[29]).

Box 6.1. Drafting a new Entrepreneurship Code

The OECD provided comments to the draft Entrepreneurship Code (EC), which aims to consolidate all business-related laws and regulations, at the request of the Ministry of Justice. The draft EC included key sections that are organised in line with international standards. These include a definition of:

- businesses, in particular of SMEs with associated thresholds and a time-bound reference period, as well as a clear distinction between the definition and purpose of business entities and social enterprises;
- their rights and obligations;
- the provisions needed for a sound regulatory framework for businesses, in particular the definition of the procedure for business registration and closure, an important step for enterprise formalisation; and
- the rules concerning the nature and modalities of state support to businesses.

In addition, the document spells out a hierarchy of normative acts between international treaties and national laws, as it gives primacy to international treaties ratified by Uzbekistan over the Entrepreneurship Code, and primacy of the Entrepreneurship Code over all other legal acts related to entrepreneurship. Some instances of a duplication of laws and regulations, however, remain to be addressed.

Source: OECD analysis (2022)

Communication on legislative changes has improved

The government has significantly enhanced communication of legislative changes through more systematic publication of draft laws and decrees. Draft legislative changes are published and submitted for public consultation on regulation.gov.uz. Laws and decrees adopted are accessible online and for free on Lex.uz. The Ministry of Justice communicates these on its official Telegram channel, in the press and on TV. The Ministry also launched an online platform called ‘’Advice for Business’’ (b-advice.uz), where entrepreneurs can receive free legal advice and consultations online. Services include a listing of free land plots, information on the issuance of licenses and authorisations, credit access, and connecting to the telecom network.

Market competition is limited

Competition remains a long-standing issue

Lack of institutional capacity to foster competition, preferential treatment granted to SOEs, and the latter’s regulator role in their own sectors impede the creation of competitive market conditions and private firm entry (World Bank, 2022[4]) (OECD, 2022[30])**.** Whilst Uzbekistan has a strong *de jure* competition law regime (OECD, 2022[30]), 56% of a recent OECD survey respondents considered that competition policies are weak, and none reported that they were strong (OECD, 2023[7]). For each of the sub-indicators for competition policy, monopoly practices were reported as weak by the largest number of respondents, followed by control of market dominance and measures in place against cartels and concerted practices (ibid). Many SOEs enjoy monopolies in activities that are otherwise carried out by the private sector and, in sectors where they co-exist with private firms, the former benefit from preferential access to financing and land and are responsible for regulatory policy.

Reform of the operational environment should prioritise impact assessment and market competition

Pursue legislative simplification involving RIAs and public-private consultations

The review of business-related legislation can take the form of legislative simplification initiatives, *ex ante* reviews through regulatory impact assessments (RIAs) and a mapping of fiscal and parafiscal charges paid by SMEs with the view to rationalising them. With regards to legislative simplification, a regulatory guillotine approach can be applied to abolish previous laws and remove contradictions between old and new legislation. This method can help contribute to regulatory offsetting (OECD, 2019[31]) and should be paired with regulatory impact assessment before implementation to evaluate the impact of new legislation. To ensure RIAs are not a "box-ticking exercise", they should be initiated early in the conceptualisation of new legislation rather than when the draft legislation has already been prepared (OECD, 2022[32]). Oversight bodies, independent from line ministries, should perform binding quality controls for RIAs, to ensure that the government criteria for conducting RIAs are respected.

Major regulatory changes should systematically involve a formal public-private consultation. The government should ensure that SMEs are well represented and engaged in those consultations, and that they can raise comments and concerns regarding changes that apply to them. To the extent possible, urgent procedures bypassing consultations should be avoided. Prior to enacting, the relevant authorities should ensure clear communication on implementation and resolve issues related to the interpretation of new provisions. Monitoring and evaluating those consultations would allow to evaluate the degree to which key stakeholders are involved in the process and identify areas where further outreach or capacity building is needed (OECD, 2022[32]).

Box 6.2. Serbia's e-Papir programme

The government of Serbia adopted a Programme for the Simplification of Administrative Procedures and Regulations (2019-2021), called e-Papir, which aims to identify and simplify administrative procedures for businesses. Within the framework of the programme, a register of administrative procedures for businesses was created and linked to the government's portal of digital public services.

In setting up the Unified Electronic Registry of Mandatory Requirements in the Field of Entrepreneurship, the government of Uzbekistan could take inspiration from Serbia's programme which combines the process of simplifying administrative procedures with their digitalisation, processes which are often considered independently. The overall benefit of the programme once fully implemented is estimated at around EUR 4.5 million. This parallel digitalisation and simplification can be seen as a first step toward designing digital services with the end user's experience and needs in mind.

Source: (OECD, 2022[32]), https://epapir.rsjp.gov.rs

Pursue reforms to increase competition

Several measures can serve to increase market competition. The OECD had already recommended that the Consumer Protection and Competition Promotion Committee benefit from more operational independence to allow for more effective enforcement and is ensured a sufficient and stable budget to execute its mandate effectively (OECD, 2022[30]). In addition, it appears essential that the government pursues the splitting of operation, policy, and regulatory responsibilities within SOEs to reduce the risk of conflicts of interests. Lastly, as discussed above, preferential access to land and inputs to SOEs should be reviewed.

Priority 3: Taxation has become more digital and less burdensome, but tax administration could be improved to increase compliance

The fiscal regime has been recently overhauled

The tax burden on firms has been reduced

The overhaul of the tax policy has led to a decrease in the tax burden, reduced complexity and lowered mandatory social contributions (World Bank, 2022[4]). The latest version of the Tax Code has optimised the types and number of taxes and levies, as well as special tax regimes (Box 6.3). In particular, the number of taxes for firms was reduced to ten and a special tax regime was introduced for small companies with a turnover of up to UZS 1 billion (about 75,000 EUR), which must pay a single turnover tax. The reduction of the value-added tax (VAT) was intended to provide fiscal relief to businesses and consumers. Several measures, such as the simplification of the VAT refund procedure with the removal of additional checks, the automatic inclusion of businesses with a turnover of UZS 1 billion without verification, and the provision under which taxpayers in high-risk areas will be notified before the VAT certificate is suspended, have reduced the administrative burden. In addition, a new resolution introduced the prohibition of applying the tax gap coefficient in cases of negative VAT reimbursement (podrobno, 2023[33]). The period for in-house audits related to the validity of VAT amounts was shortened from 60 to 30 days (Foreign Investors Council under the President of the Republic of Uzbekistan, 2023[34]), and certain actions such as accessing the taxpayer's territory, requesting or seizing documents and inspecting premises have been forbidden during criminal tax audits. Businesses report that this has made Uzbekistan's tax regime the most attractive in the region. The accountability of the tax authorities was also strengthened with the introduction of a new mechanism that provides for payment of interest to the taxpayer by the tax authority for each day of overdue tax refund, with excessively recovered amounts of taxes and financial penalties refunded in the form of interest calculated based on the refinancing rate of the Central Bank. Overall, tax reforms have supported record increases in new business and personal taxpayer registrations, and a 7.4% increase in tax revenues collected for H1 2023 compared with the same period in 2022 (World Bank, 2022[4]) (UzDaily, 2023[35]).

Box 6.3. Recent fiscal policy developments in Uzbekistan

The new Tax Code, effective on 1 January 2020, lowered corporate and individual income taxes by almost 50% and simplified taxation procedures for private entrepreneurs. It also abolished outdated methods of determining the tax base based on the cost of goods and services sold.

Key changes since 2020 include:

- firms with a turnover below 1 Bn UZS do not pay VAT;
- the 8% social security contributions and all mandatory payments to various state funds were abolished;
- corporate and individual income taxes were reduced from a progressive rate of up to 24% to a single flat rate of 12%;
- the income tax rate on dividends was reduced from 10% to 5% for residents, 10% for non-residents;
- the VAT tax rate also decreased from 20 to 12% effective in 2023;
- a 0% corporate (profit) tax rate on profit from the sales of goods (services) for export was introduced;
- a 50% corporate (profit) tax rate reduction was introduced for taxpayers that change from the single turnover tax regime to the corporate (profit) tax regime after 1 September 2022;
- tax losses can be carried forward indefinitely, thus reducing the taxable income of the respective year; and
- 13 forms of tax inspections were consolidated into two.

Source: OECD analysis

The digitalisation of tax procedures has made substantial progress

Taxation has also widely benefitted from investments in digitalisation according to the Uzbek authorities, including investments in data centre infrastructure and the procurement of servers, telecommunications, software upgrades, the switching online of more than 40 types of tax services and plans to rely on big data and AI to better analyse tax revenue trends in the future. All those measures also serve to improve tax administration and create easier conditions for firms to pay tax. The Tax Committee introduced an online cashback system for individuals at retail, catering and consumer services purchases upon the scanning of the QR code of the receipt on the Soliq application, which has led to an increase of income reporting from businesses and tax compliance.

Nonetheless, tax administration remains the most contentious issue mentioned by firms

Tax administration has not simplified

OECD interviewees have complained about issues in tax administration, such as the added complexity of new tax registration procedures, VAT refund delays and the hasty introduction of digital instruments not always ready on time. The government itself has reported that several resolutions of the Cabinet of Ministers have made the VAT refund system more complex (Lex.uz, 2020[36]) (Lex.uz, 2021[37]). Exporting firms are now subject to in-house and desk tax audits to be eligible for expedited VAT refund, which reduces working capital available. The government also requires firms to ensure that suppliers have active VAT payer certificates, no tax arrears, a good colour grade in the risk assessment, and mandatory digital labelling, among other requirements. These new requirements have led to the creation of an atmosphere of mistrust among firms, which refuse to conduct business with enterprises classified as red in the risk assessment system.

Tax compliance is further challenged by mutual mistrust between the Tax authorities and the taxpayers

A complex system based on a dual tax regime (based on the 1 bn UZS threshold, around 77k EUR), frequent changes, conflicting referential acts and resulting interpretation issues have all been mentioned as roadblocks to voluntary tax compliance. While the Tax Code stipulates that all ambiguities and contradictions in the law should be interpreted in favour of the taxpayer, OECD interviewees mentioned lack of customer-oriented approach and a sense of suspicion from the tax authorities with respect to the taxpayers' good will. The number of business inspections doubled between 2021 and 2022, with more than 70% of inspections coming from the tax authorities in 2022 (Gazeta.uz, 2023[38]). To address issues and inconsistencies with tax and regulatory measures, foreign investors often resort to government benefits through special cabinet of minister resolutions or presidential decrees, including tax holidays for land taxes, property taxes and water use taxes granted to some companies with foreign direct investments on a case-by-case basis. These can however be revoked (U.S. Department of State, 2022[13]).

Further improving tax administration requires building more trust and engagement between the tax authorities and the taxpayers

Legislation changes need to be predictable

The tax authorities should ensure the stability and clarity of tax legislation. To do so, new legislation should systematically be based on prior consultations to identify the additional net costs and burdens on taxpayers from the changes. Consultative documents should be published and be accompanied by a call for responses to ensure the largest number of stakeholders has the opportunity to provide comments. Consultations can also take the form of "town hall" consultations led in specific locations. It could be particularly useful to conduct such consultations in areas where firms have not necessarily gone digital. Changes should limit the references to norms and by-laws to avoid contradictions, and be consistently interpreted across government institutions, to avoid conflicting communication to businesses.

The way the tax administration engages and communicates with businesses could be improved

The approach to increasing tax compliance should focus more on encouraging formal activity than on discouraging informal activity. An enforcement-based approach is likely to lead to a cycle of inspections, sanctions and closing of activities, and encourages hide-and-seek strategies. On the other hand, policies supporting firm productivity can encourage the latter to formalise and support the transition to the formal sector. Such policies can also create positive examples for other firms (OECD, 2021[39]).

The Tax authorities could also conduct targeted educational campaigns aimed at improving communication and ultimately increasing the number of people meeting filing and payment deadlines and taxpayer registration in the informal economy (OECD, 2023[40]). The tax authorities have already been relying on social media such as a Telegram channel to relay information to SMEs. The style of messages should be targeted, action-oriented, goal driven, easy to understand and engaging. The State Committee could also consider publishing detailed guides with step-by-step instructions on life cycle events (registering for tax, employing staff, reaching VAT thresholds, audits or closing a business) and conducting virtual or in-person workshops. Given the size of Uzbekistan's informal sector, the authorities should design targeted programmes to widen the tax base. Taxpayer workshops have been identified as having a positive impact on the relationship with the tax authority: following the attendance at a workshop, there was near unanimous acceptance of the legitimacy of the tax authority and a widespread commitment to increase compliance (OECD, 2021[41]). Such a measure would prove more cost-effective than targeting many small taxpayers owing only negligible amounts of tax. Campaigns for formalisation could also target customers rather than the informal businesses directly (Box 6.4), as when people avoid buying goods from the informal sector, sellers will start to comply with tax laws (OECD, 2021[41]). The cash-back system introduced on the Soliq application is a case in point.

Box 6.4. Türkiye's tax week

The government of Türkiye has been organising a yearly tax week aiming at enhancing tax awareness among children, taxpayers and the society at large. During the week, campaigns are run across the country to invite citizens to pay taxes and help tackle the informal economy. 500 tax officials participate across the country.

Campaigns include:

- visits to taxpayers at their workplaces to collect their opinions and suggestions;
- visits to civil society organisations to collect their opinions and suggestions;
- stands at universities providing students with information on tax awareness, the dangers of the informal economy employment, career opportunities, etc.;
- seminars at universities; and
- posters on tax awareness for the general public and children.

Source: (OECD, 2021[41])

Such initiatives should go together with efforts to increase trust and dialogue with and among the private sector. Tax authorities should pursue transparency efforts and publish more exhaustive data on large taxpayer contributions and civil servants' income declarations to develop understanding of the purpose of tax. Another measure to consider could be the reformulating of tax authorities' KPIs, currently based on tax amounts collected, to help define a more collaborative relationship between the latter and the private sector. The recent announcement to abolish all tax inspections from 1 January 2024 for firms with a high openness rating should already serve to reduce physical interactions between entrepreneurs and tax authorities. Lastly, given the negative impact of the new risk-assessment system on business-to-business operations, the system should probably be re-evaluated.

References

Brookings (2022), *High expectations in Uzbekistan*, https://www.brookings.edu/blog/future-development/2022/02/08/high-expectations-in-uzbekistan/. [3]

Dentons (2023), *Doing Business Guide - Uzbekistan 2023*, https://www.dentons.com/en/insights/articles/2023/march/31/doing-business-in-uzbekistan-2023?utm_source=substack&utm_medium=email. [17]

Dentons (2020), *Reforms in the investment legislation of Uzbekistan*, https://www.dentons.com/en/insights/alerts/2020/january/9/reforms-in-the-investment-legislation-of-uzbekistan. [43]

EBRD (2002), “Banking reform and development in transition economies” Working Paper 71. [20]

Eurasianet (2023), *Uzbekistan woos investors as dispute with Western firm goes to arbitration*, https://eurasianet.org/uzbekistan-woos-investors-as-dispute-with-western-firm-goes-to-arbitration. [42]

EY (2021), *Doing Business in Uzbekistan - An introductory guide to tax and legal issues*, https://assets.ey.com/content/dam/ey-sites/ey-com/en_uz/home/doing-business-in-uzbekistan-ey-2021.pdf. [23]

Foreign Investors Council under the President of the Republic of Uzbekistan (2023), *Brief Investor Handbook - Taxation in Uzbekistan*, https://drive.google.com/file/d/1QfqZ1VV0gSbkQ9RZgdAQJPFy-hlj6_wU/view?usp=sharing. [34]

Gazeta.uz (2023), *Количество проверок бизнеса в Узбекистане удвоилось в 2022 году*, https://www.gazeta.uz/ru/2023/06/29/business-checks/ (accessed on 18 July 2023). [38]

IMF (2023), *World Economic Outlook Database, April*, https://www.imf.org/en/Publications/WEO/weo-database/2023/April. [6]

IMF (2000), “International Capital Markets. Developments, Prospects and Key Policy Issues”, *World Economic and Financial Surveys*, p. 225, https://doi.org/10.5089/9781557759498.083 (accessed on 9 October 2023). [19]

Kun.uz (2023), *Konstitutsiyaviy sudning vakolatlari kengayadi*, https://kun.uz/uz/news/2023/07/25/konstitutsiyaviy-sudning-vakolatlari-kengayadi (accessed on 25 July 2023). [24]

Lechner, M. and M. Schnitzer (2008), “Entry of foreign banks and their impact on host countries”, *Journal of Comparative Economics*, Vol. 36/3, pp. 430-452, https://doi.org/10.1016/j.jce.2008.02.002 (accessed on 9 October 2023). [48]

Lex.uz (2022), *О мерах по упрощению государственного регулирования предпринимательской деятельности*, https://lex.uz/ru/docs/6279884 (accessed on 8 June 2023). [28]

Lex.uz (2021), *О мерах по дальнейшему совершенствованию учета налогоплательщиков и упрощению порядка возмещения налога на добавленную стоимость*, https://lex.uz/docs/5660085. [37]

Lex.uz (2020), *О внесении изменений и дополнений в некоторые законодательные акты республики узбекистан в связи с дальнейшим сокращением бюрократических барьеров и внедрением современных управленческих принципов в деятельность государственных органов и организаций*, https://lex.uz/ru/docs/5020304 (accessed on 8 June 2023). [26]

Lex.uz (2020), *О мерах по соверщенствованию налогового администрирования, связанного с зарубежными юридическими лицами и налогом на добавленную стоимость*, https://lex.uz/docs/4948600. [36]

Lex.uz (2020), *О мерах по улучшению деловой среды в стране путем внедрения системы пересмотра утративших свою актуальность актов законодательства*, https://lex.uz/ru/docs/5019108 (accessed on 8 June 2023). [27]

Lex.uz (2020), *Об организационных мерах по сокращению теневой экономики и повышению эффективности деятельности налоговых органов*, https://lex.uz/ru/docs/5073461. [47]

Lex.uz (2013), *On the approval of the regulation on the procedure for the implementation of certain foreign exchange operations related to the movement of capital*, https://lex.uz/docs/2296324. [16]

OECD (2023), *Communication and Engagement with SMEs: Supporting SMEs to Get Tax Right*, https://doi.org/10.1787/f183d70a-en. [40]

OECD (2023), *Insights on the Business Climate in Uzbekistan*, https://doi.org/10.1787/317ce52e-en. [7]

OECD (2022), *An introduction to competition law and policy in Uzbekistan*, https://www.oecd.org/competition/an-introduction-to-competition-law-and-policy-in-uzbekistan.htm. [30]

OECD (2022), *Green Economy Transition in Eastern Europe, the Caucasus and Central Asia*, OECD Publishing, https://doi.org/10.1787/22229523. [10]

OECD (2022), *SME Policy Index: Western Balkans and Turkey 2022: Assessing the Implementation of the Small Business Act for Europe,*, https://doi.org/10.1787/b47d15f0-en. [32]

OECD (2022), *Weathering Economic Storms in Central Asia: Initial Impacts of the War in Ukraine*, https://doi.org/10.1787/83348924-en. [9]

OECD (2021), *Beyond COVID-19: Prospects for Economic Recovery in Central Asia*, https://www.oecd.org/eurasia/Beyond_COVID%2019_Central%20Asia.pdf. [5]

OECD (2021), *Building Tax Culture, Compliance and Citizenship*, https://doi.org/10.1787/18585eb1-en. [41]

OECD (2021), *Improving the Legal Environment for Business and Investment in Central Asia*, OECD Publishing, https://www.oecd.org/eurasia/Improving-LEB-CA-ENG%2020%20April.pdf. [1]

OECD (2021), *Improving the Legal Environment for Business and Investment in Central Asia*, https://www.oecd.org/eurasia/improving-legal-environment-business-central-asia.htm#:~:text=The%20Improving%20the%20Legal%20Environment,%2C%20Kyrgyzstan%2C%20Tajikistan%2C%20Turkmenistan%20and. [8]

OECD (2021), *Informality and COVID-19 in Eurasia: The Sudden Loss of a Social Buffer*, https://www.oecd.org/eurasia/COVID-19-informality-Eurasia.pdf. [39]

OECD (2020), *Investment Policy Reviews: Georgia*, https://doi.org/10.1787/0d33d7b7-en. [46]

OECD (2019), *Chapter 4. Organising the process of privatisation*, OECD Publishing, Paris, https://doi.org/10.1787/ea4eff68. [15]

OECD (2019), *ONE-IN, X-OUT,Regulatory offsetting in selected OECD countries*. [31]

OECD (2017), *OECD Investment Policy Reviews: Kazakhstan 2017*, https://doi.org/10.1787/9789264269606-en. [18]

OTP Group (2022), *Contract signed: OTP Bank acquires Uzbekistan's Ipoteka Bank*, https://www.otpgroup.info/news/uzbekistan-ipoteka-bank. [22]

podrobno (2023), *Мирзиёев утвердил меры по совершенствованию налогового законодательства. Рассказываем, что изменится*, https://podrobno.uz/cat/obchestvo/mirziyeev-utverdil-mery-po-sovershenstvovaniyu-nalogovogo-zakonodatelstva-rasskazyvaem-chto-izmenits/ (accessed on 6 September 2023). [33]

President of the Republic of Uzbekistan (2023), *Обсуждены задачи в сфере информационных технологий*, https://president.uz/ru/lists/view/5943 (accessed on 11 October 2023). [25]

The Tashkent Times (2023), *An international commercial court to be set up in Uzbekistan, says president Mirziyoyev*, http://tashkenttimes.uz/national/10960-an-international-commercial-court-to-be-set-up-in-uzbekistan-says-president-mirziyoyev (accessed on 11 October 2023). [11]

Trading Economics (2023), *Uzbekistan Business Confidence*, https://tradingeconomics.com/uzbekistan/business-confidence (accessed on 4 September 2023). [29]

U.S. Department of State (2022), *2022 Investment Climate Statements: Uzbekistan*, https://www.state.gov/reports/2022-investment-climate-statements/uzbekistan/. [13]

U.S. Department of State (2021), *Investment Climate Statements: Uzbekistan*, https://www.state.gov/reports/2021-investment-climate-statements/uzbekistan. [44]

UNCTAD (2021), *Report on the Implementation of the Investment Policy Review - Uzbekistan*, https://unctad.org/system/files/official-document/diaepcb2021d3_en.pdf. [12]

UzDaily (2023), *Июнь ойида Ўзбекистоннинг қайси вилоятлари энг юқори ишбилармонлик фаоллигини кузатилди*, https://eur02.safelinks.protection.outlook.com/?url=http%3A%2F%2Fuzdaily.uz%2Fuz%2Fpost%2F8325%2520&data=05%7C01%7CCeleste.LAPORTETALAMON%40oecd.org%7Cdaacc338842c4383a94808db8cfc5acf%7Cac41c7d41f61460db0f4fc925a2b471c%7C0%7C0%7C638258787715461779%7CUnkno (accessed on 25 July 2023). [35]

World Bank (2023), *World Bank Development Indicators*, https://databank.worldbank.org/source/world-development-indicators. [2]

World Bank (2022), *Project Appraisal Document on a Proposed Credit in the Amount of USD 15 Million to the Republic of Uzbekistan for a Uzbekistan Financial Sector Reform Project*. [21]

World Bank (2022), *Recommendations for a National Foreign Direct Investment Strategy and Roadmap for Uzbekistan: New Sources of Growth*, https://documents1.worldbank.org/curated/en/099430406302241587/pdf/P17672901802190a108e00089316ad3dc7e.pdf. [14]

World Bank (2022), *The Second Country Diagnostic for Uzbekistan*, https://documents1.worldbank.org/curated/en/933471650320792872/pdf/Toward-a-Prosperous-and-Inclusive-Future-The-Second-Systematic-Country-Diagnostic-for-Uzbekistan.pdf. [4]

World Justice Project (2022), *Rule of Law Index 2022*, https://worldjusticeproject.org/rule-of-law-index/global/2022. [45]

7 Going forward

Since the pandemic and despite global headwinds, governments of Central Asia have worked to simplify tax systems and business procedures, dynamise public-private dialogue and digitalise public services. This section offers ways forward for the region's governments to consider to further boost private sector development.

The governments of the region have carried out reforms to support the private sector as a means to achieve more sustainable and inclusive development

Since achieving independence, governments of the region have recognised the contributions of firms of all sizes to employment and growth and have been supporting private sector development. Central Asian countries have made significant reforms in the investment and business climate, developed medium- and long-term business support programmes and allocated significant funds to increase the share of the private sector, and more specifically SMEs, in the economy and to support job creation in the context of dynamic demographic growth. Governments are also increasingly turning to new ways of supporting inclusive and climate-friendly growth through tax incentives for green industries, as well as creating favourable conditions for sustainable start-ups, creative sectors and technology-intensive industries.

The OECD's assessment of progress achieved over the past three years has shown that the region has made strides in a number of areas to create a more favourable regulatory framework for businesses, to address the infringement of entrepreneurial rights, and to build framework conditions to foster entrepreneurship development. To varying degrees, all five countries have worked to make tax systems more effective, fairer, and more digital; trade smoother; and public-private dialogue more dynamic. FDI inflows and SME performance in the region confirm to some extent the effectiveness of policy measures taken by governments. Improvements in the operational environment for business at the regional level can indeed encourage local businesses to expand within the region but can also increase Central Asia's attractiveness to international investors as a regional market.

Concerted efforts can help address shared challenges

Nevertheless, additional efforts are required for the legal environment for business to become an enabler of diversification and inclusiveness. Whilst each of the Central Asian countries has its own economic model and development path, the OECD has identified a set of challenges common across the region:

- **Predictability**: Governments should particularly ensure the predictability of application and enforcement of business-related legislation and policies for SMEs and investors. Although governments have shown adaptability and flexibility in emergency responses to the COVID-19 crisis and Russia's war in Ukraine, ensuring the stability and predictability of legislation would benefit SMEs greatly. Further government support to help firms adapt to regulatory changes would also be welcome to increase clarity. This requires establishing effective channels of communication with businesses, as well as mechanisms to run consultations and collect feedback at all stages of the development of policies. Such endeavours will contribute to building business resilience to future economic shocks.
- **Implementation and consistency of interpretation:** In addition to the unpredictability and complexity of the regulatory framework, entrepreneurs also often note the uneven implementation of procedures. As a result, enterprises have to face misconduct, in particular with regard to licensing and taxation. More systematic consultation and communication with businesses and business associations is needed. Training of civil servants could be disseminated at both national and regional levels and conducted directly by public authorities on a regular basis. This can help ensure that civil servants are aware of changes in legislation and can advise and support businesses on their adaptation journey. In parallel, the government should prioritise the development of channels for companies to report mis-implementation cases.
- **Public-private dialogue (PPD).** PPD can promote an inclusive approach to problem solving and policymaking. By joining the private and public sector analysis of bottlenecks, opportunities and possible interventions, it can contribute to strengthening the business and investment environment.

To make PPD effective, stakeholders should ensure they identify concrete, measurable and achievable outputs, and include the underrepresented (MSMEs, firms from rural areas, emerging sectors, women- and youth-led companies, etc.).

- **Regional integration.** Trade integration can help address the region's distance penalty to major markets. Despite significant trade facilitation improvements in recent years, Central Asia falls behind most of the regions covered by the OECD's Trade Facilitation Indicators (TFIs) in terms of trade integration. Further can be done by the Central Asian countries to improve soft (such as streamlining procedures) and hard infrastructure and ultimately boost regional trade and connectivity.
- **Competition.** Fostering competition promotes consumer welfare and economic growth while making markets more innovative. The large footprint of SOEs in Central Asia's economies creates a significant fiscal burden for governments and distorts market conditions, hampering the development of the private sector. Improving governance, streamlining subsidies and examining which activities could be better served by the private sector can help level the playing field between public and private firms.
- **Digitalisation.** Interacting digitally with businesses and citizens can contribute to more effective stakeholder engagement. The region has displayed a constant growth of digitalisation in the interactions between government agencies and with citizens and businesses through the provision of digital public services. Governments could adapt digitalisation efforts to local specificities, such as the development of convenient and easy-to-use smartphone applications for tax returns, due to the high percentage of their use among entrepreneurs and try to bridge the digital divide among the population. Mobile-friendly platforms should be prioritised in places where fixed broadband access is limited or faces important barriers.
- **Data availability for monitoring and evaluation.** More and better-quality data can make policy making, monitoring and evaluation more effective**.** A systematic evaluation of the effectiveness of programmes and strategies for investors and for SMEs will facilitate timely adjustments and achievement of objectives. The countries of the region have started to develop regulatory impact analysis, but implementation remains to be seen. The use of RIA in the development of legal acts, as well as the development of clear methodologies for such application will help countries to cut out in its infancy legislation that does not work and causes harm to business.

Going forward, additional steps to level the playing field and reduce the share of the state in the economy will ensure a more inclusive development path. Establishing clearer, more predictable and stable rules will not only help establish dynamic markets offering better job opportunities to a growing labour force but will also contribute to making the region more vibrant and attractive to foreign investment. Increased cross-border co-operation will also benefit the competitiveness and attractiveness of Central Asia as a region. Ultimately, a bolstered private sector will only serve to increase the resilience of the region to trade and climate change headwinds.

Annex A. Methodology

Overview of the OECD monitoring framework

In the framework of the Central Asia Competitiveness IV Project co-financed by the European Union under its Central Asia Invest Initiative, the OECD has been reviewing progress in addressing problems in the business and investment climate, foregrounding the need for long-term reforms to encourage investment and private sector development in Central Asia. The OECD Eurasia Competitiveness Programme, in collaboration with representatives from the governments of Central Asia, private sector representatives, and other development partners, and with contributions from international experts, carried out analysis, data collection and consultations with stakeholders in each Central Asian country to assess progress in business environment reform implementation and developed updated recommendations for institutions and policies to support long-term growth prospects.

This report assesses progress and remaining challenges for the five Central Asia countries in implementing the three priority reforms areas identified in 2020 to improve the legal environment for business (Table A A.1).

Table A A.1. Priority reforms in the legal environment for business in Central Asia

Kazakhstan	Kyrgyzstan	Tajikistan	Turkmenistan	Uzbekistan
Operational environment for firms Implement consistently and thoroughly the new code for entrepreneurs	**Operational environment for firms** Streamline the legal environment for entrepreneurs and small businesses, especially legislation and service delivery	**Legal and regulatory framework for investment** Ensure the implementation of existing laws for investment and entrepreneurial activity, and improve the accessibility of necessary information	**Legal and regulatory framework for investment** Enforce, streamline, and publish all legislation on investment on the Ministry of Justice's legal database to ensure transparency	**Legal and regulatory framework for investment** Ensure proper implementation of the new investment law and remove sectoral restrictions
Legal and regulatory framework for investment Improve dispute settlement for all businesses operating in the country	**Contract enforcement** Ensure transparent fair and efficient contract enforcement for businesses	**Contract enforcement** Improve the enforcement of contracts and arbitral decisions in domestic courts	**Operational environment for firms** Develop a simplified targeted legal framework and support for SMEs and small entrepreneurs	**Operational environment for firms** Streamline and consolidate business-related legislation and licenses for domestic firms and entrepreneurs
Trade facilitation Enhance trade facilitation and improve cooperation between agencies involved in export procedures	**Taxation** Simplify the tax code and tax administration for companies of all sizes	**Taxation** Make tax administration simpler, more consistent and more transparent	**Business registration** Streamline business registration and licensing, and introduce a one-stop-shop	**Taxation** Ensure changes to tax requirements are predictable, and improve tax administration for small firms

Source: (OECD, 2020[1]).

The analysis also considered the effect of the COVID-19 pandemic and the disruption caused by Russia's war in Ukraine on the ability of the governments to implement the corresponding recommendations

(Figure A A.1). In particular, the OECD assessment integrated three main dimensions: (i) a measure of implementation progress based on the reforms identified with the government in 2020; (ii) an assessment of the causes of any implementation delays; and (iii) an assessment of new challenges and priority areas for action.

Figure A A.1. Example of detailed policy recommendations (2020)

Source: (OECD, 2020[1]), OECD analysis (2023).

The monitoring exercise relied on a continuous dialogue between the OECD, the governments of the region, the private sector, and international partners, including through working group meetings and several bilateral consultations in late 2022 and 2023 (Table A A.2). In particular, the OECD used a series of monitoring tools, including a matrix table of recommendations, questionnaires, data requests and collection, as well as an analysis of existing surveys and interviews to collect data and information. For each country-specific priority, the OECD assessed the current state of implementation, identified challenges and priority areas for further action, and discussed possible drivers for implementation.

Table A A.2. List of OECD public-private working group meetings

Agenda of meetings	Key participants	Date
Regional launch event	Ministry of Trade and Integration of the Republic of Kazakhstan, Ministry of Finance of the Republic of Kazakhstan, Agency for Financial Monitoring of the Republic of Kazakhstan, Ministry of Finance of the Kyrgyz Republic, Ministry of Economy and Commerce of the Kyrgyz Republic, Tax Committee of the Republic of Tajikistan, State Committee for Investment and State Property Management of the Republic of Tajikistan, Ministry of Economy and Finance of Turkmenistan, Agency for Strategic Reforms under the President of the Republic of Uzbekistan, Ministry of Investments, Industry and Trade of the Republic of Uzbekistan, Ministry of Justice of the Republic of Uzbekistan, Ministry of Innovative Development of the Republic of Uzbekistan	13 December 2022
Kyrgyzstan: discussion of methodology, initial findings and priorities	Ministry of Economy and Commerce, State Tax Service, Ministry of Justice	20 June 2023

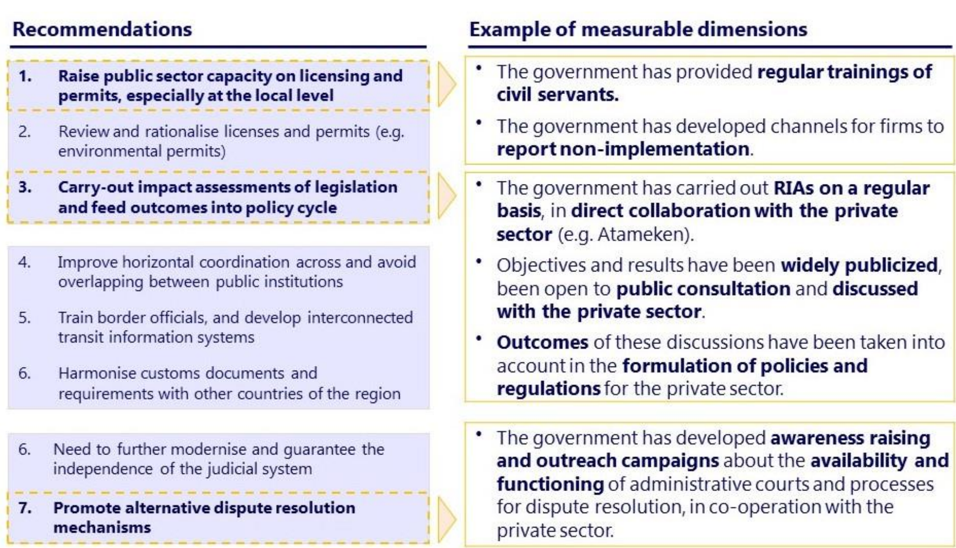
Agenda of meetings	Key participants	Date
Uzbekistan: discussion of methodology, initial findings and priorities	Agency for Strategic Reforms under the President of the Republic of Uzbekistan, Ministry of Economy and Finance, Ministry of Investments, Industry and Trade, State Tax Committee, Ministry of Justice, IT Park, Digital Economy Research Centre	23 June 2023
Kazakhstan: discussion of methodology, initial findings and priorities	Ministry of National Economy, Atameken, Ministry of Justice, State Revenue Committee, Kazakh Invest, Ministry of Digital Development, Innovations, and Aerospace Industry, QazIndustry, Economic Research Institute	27 June 2023
Tajikistan: discussion of methodology, initial findings and priorities	Ministry of Economic Development and Trade, Tax Committee, State Committee for Investment and State Property Management	17 July 2023
Turkmenistan: discussion of methodology, initial findings and priorities	Ministry of Economy of Finance, Ministry of Trade and Foreign Economic Relations, Union of Entrepreneurs and Industrialists, Tax Committee	8 November 2023

The approach taken by the project was split into two components:

- The OECD developed two sets of detailed questionnaires for each country-specific priority, based on the 2020 recommendations broken down into several measurable policy areas (Figure A A.2). The first set of questionnaires was issued to the governments in each country and gave the OECD a robust overview of the *de jure* regulatory conditions and reforms for business since 2020.

  A second questionnaire was sent to business associations and international organisations active in each country of the region and discussed during online, anonymous interviews, as a means of obtaining a better understanding of improvements and remaining challenges in the implementation of reforms and the operational environment for firms.

Figure A A.2. Example of policy dimensions used in the OECD assessment



Source: (OECD, 2020[1]), OECD analysis (2023).

- Online interviews were conducted with representatives of the public and private sector, as well as international organisations in each project country, during which the OECD discussed the findings of the questionnaire, received additional input and clarification, and heard from public and private sector stakeholders on legal and implementation challenges.

Table A A.3. Questionnaires collected by the OECD among in January 2023 for the review

Country	Institution
Kazakhstan	Ministry of National Economy of the Republic of Kazakhstan
	Ministry of Trade and Integration of the Republic of Kazakhstan
	National Chamber of Entrepreneurs of the Republic of Kazakhstan “Atameken”
	Astana International Financial Centre (AIFC)
Kyrgyzstan	Ministry of Economy and Commerce of the Kyrgyz Republic
	Ministry of Justice of the Kyrgyz Republic
	State Tax Service of the Kyrgyz Republic
	International Business Council
	Business Ombudsman Institute of the Kyrgyz Republic
Tajikistan	Tax Committee of the Republic of Tajikistan
	State Committee for Investment and State Property Management of the Republic of Tajikistan
Turkmenistan	Ministry of Economy and Finance of Turkmenistan
	Union of Entrepreneurs and Industrialists
Uzbekistan	Agency for Strategic Reforms under the President of the Republic of Uzbekistan
	Ministry of Justice of the Republic of Uzbekistan
	Ministry of Investments, Industry and Trade of the Republic of Uzbekistan
	Customs Committee of the Republic of Uzbekistan

Improving the Legal Environment for Business and Investment in Central Asia

PROGRESS REPORT

While Central Asia has proven relatively resilient to the shocks of COVID-19, China's slowdown and Russia's war in Ukraine, declining trend rates of growth across the region, lacklustre productivity performance and lingering global uncertainty underscore the need to address weaknesses in the business and investment climate. The implementation of predictable rules, the creation of a level-playing field between firms and greater competition in markets, in particular, could encourage both local entrepreneurs and foreign investors to invest and grow in the region. This report presents an assessment of progress since the 2019-2020 analysis of the legal environment for business and investment in Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan against the backdrop of the changing international context brought about by COVID and the war.

Funded by
the European Union

PRINT ISBN 978-92-64-51239-9
PDF ISBN 978-92-64-78853-4

9 789264 512399