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Best Practices to Incorporate the Informal Economy into the Formal Economy.

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BEST PRACTICES FOR INCORPORATING THE INFORMAL ECONOMY INTO THE FORMAL ECONOMY

By
Omar E. Garcia-Bolivar*

The informal economy is a global phenomenon. It is present in both developed economies and developing economies. The informal economy is a problem for some countries as long as it takes away a key source of revenue. But it is a real solution of livelihood for many people in countries where unemployment is rampant and few business opportunities are available.

Often those who retreat into the informal economy are often doomed to remain there indefinitely. With the goal of avoiding fees that must be paid to the state, informal entrepreneurs seek to be invisible, and this is typically achieved through limiting the size and nature of business activities. As a result (a) the state loses, because it cannot collect taxes and other contributions from individuals and entities that in effect do not exist, (b) the employer loses, particularly those in the informal sector, because they cannot easily grow and expand their operations and (c) the society loses, for various reasons that include regulation to assure safety or quality.

On the one hand, with the state having lost resources necessary to finance their public obligations, the public receives poor or less services. On the other, the informal business does not create significant numbers of jobs; or if they are created, it is not in the same way as would occur in the formal economy where the interplay of factors might allow the business to expand and create many more jobs. Alternately because this practice results in consumers being deprived the chance to enjoy and access many goods and services, the inventiveness of informal entrepreneurs tends to be more underrepresented than it might be in the larger formal economy.

Given this reality, many countries have taken actions to implement policies beneficial in reducing or modifying the conditions that motivate employers to take refuge in the informal economy.

The primary component of the external order needed to decrease informality is a sustainable economic growth that fosters job creation and market expansion, establishing a business climate favorable to the development of micro-enterprise.

With economic growth as a basic premise, we can divide the pro-formalization policies into different types. Thus, the informal can be "pulled" to a formality or "pushed" to the formality through various public policies. Practices that tend to "pull" the informality are aimed at creating an efficient business environment for formalization; these are practices that tend to reduce costs and the time needed to start or grow a business. Often these practices that "pull" the informal are not directed exclusively toward this sector of the economy, but are an indirect consequence of creating a business friendly environment overall; and, when put into place, they complete the effect of osmosis simply through the creation of favorable conditions, ones that "pull" and promote migration from the informal to the formal economy. That is the case of practices that are aimed at

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reducing the time and costs of starting and operating a business.

The practices that “pull” are based on the premise that the informal will be attracted to the formality by reason of the favorable conditions that are created. In many cases, experience shows that these various practices do not necessarily have the desired effect of expanding business or creating jobs as individuals or small operations pass from the informal to the formal economy. And even though it is often a necessary condition, a better business climate *per se* is not sufficient to promote the migration of the informal to the formal sector. Therefore, we will use the reference of practices that “pull” and practices that “push” informal enterprises as parallel or concurrent.

International practices described in this report have had a measurable impact in certain countries, and are highlighted to demonstrate these confirmed successes. In some cases, the positive impact has been through reducing the costs of starting or operating a business. In others it has been driven by the creation of and access to business opportunities. And in still others it has been an increase in access to capital.

Some countries have implemented, at one time or another, some of these practices. Others have performed, at one time or another, most of the practices. Developed countries have favored a policy of improving the climate of investment to grow the economy. For these, the quest to reduce operating costs of business has been fundamental to the process of fostering growth.

Within formal policies designed to improve business climate, these countries have developed schemes that specifically promote business opportunities for small-scale entrepreneurs. And they have also aimed to create positive incentives for migrating informal businesses to the formal sector, asserting that they are “pulled” by opportunities that provide value in exchange for participation in the larger scheme. Some countries have gone even further and have promoted capital access programs and even capitalization of citizens in countries with significant natural resources, causing some informal entities to be “pushed” toward the formal economy.

Developing countries have begun to implement similar strategies with the intent of improving their overall business climate and spurring economic growth. And a portion of these programs have been designed exclusively to reduce costs for small businesses and promote business opportunities.

However, for no country has reducing costs to businesses been a sufficient condition for this expansion of formalization. Rather, what has succeeded in establishing a business climate welcoming to all is the practice of combining strategies of cost reduction with the formation of business opportunities such as access to capital and training.

Thus far, what has not happened is the implementation of a consolidated plan that includes each and every one of the practices described herein. It would seem that, in order to successfully reduce informality, all efforts in this regard must run in the same historical moment and be pinned to a coordinated and integrated strategy that is executed, in essence, in parallel. For many reasons this approach has not always been viable, rather what appears to have been more feasible is the implementation of some or many of these practices in the process of improving overall investment climate, while continuing to promote economic growth in the private sector via macroeconomic

policies.

The best practices that will be reviewed are evident in relation to the variables used for inventory and diagnosis of the business climate of countries:

- Opening a Business
- Property assets
- Hiring
- Fiscal contributions.
- Development - Business expansion
- Environmental Aspects
- Dispute Resolution
- Closing a business

This table classifies a sample of the best practices with regard to the impact they have had in the three major policy areas and identifies each practice as "pull" or "push":

CATEGORIZATION OF BEST PRACTICE

<i>COST REDUCTION</i>	<i>PULL / PUSH</i>	<i>CREATING OPPORTUNITIES</i>	<i>PULL / PUSH</i>	<i>ACCESS TO CAPITAL</i>	<i>PULL / PUSH</i>
Creation of companies instantly	PUSH	Government procurement exclusive for MSEs	PUSH	Secured Transactions	PULL
Reduction and elimination of licenses and permits to operate	PULL	Training for MSEs	PUSH	Leasing and factoring	PULL
Special Labor Law for MSEs	PUSH	Enterprise restructuring and liquidation of companies in operation	PULL	Capitalization of citizens	PULL
Dispute resolution adapted to circumstances of MSEs	PUSH				

The following are business-friendly international best practices. The description of each practice is preceded by an explanation of the problem it seeks to combat:

1. Starting a Business.

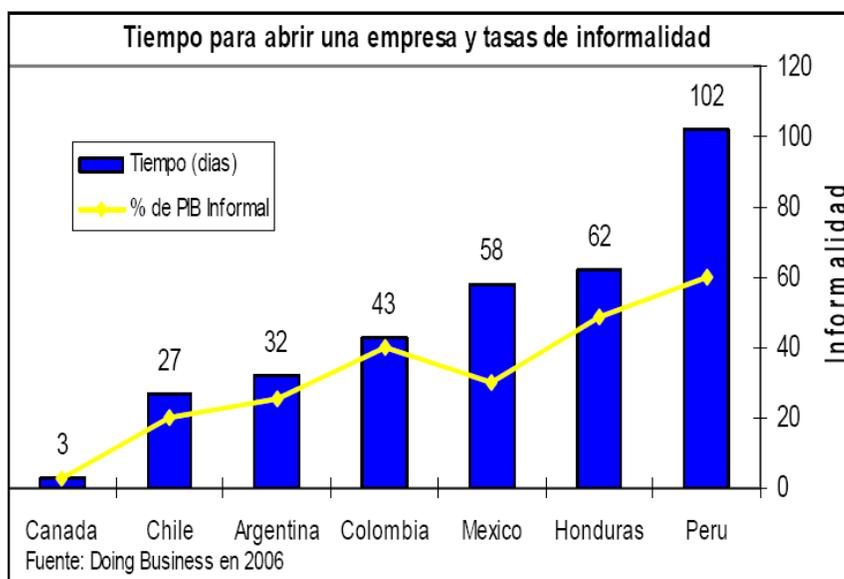
A. Creating low-cost companies instantly.

The cost required to formalize a business is one of the key determinants: the higher the costs, the lower the incentive to formalize. There are direct and indirect costs associated with formalization. Within the latter is the tremendous amount of time consumed by the process necessary to formally constitute a company; it can often result in additional costs to the fledgling

employer and, more importantly, it reduces the time that could be devoted to entrepreneurial and creative endeavors.

One effective means of reducing this pure time consumption aspect of indirect costs relates to transport costs. When requirements and overall process are simplified or services made more easily accessed, this can greatly reduce the number of visits or time an employer must spend interacting with officials to complete the formalities of starting a business.

In order for the real migration and formalization of informal enterprises, it is crucial that costs both direct and indirect costs are significantly lowered. Empirical evidence collected by the World Bank illustrates the direct relationship between the time it takes to formalize a business and the rate of informality.



The potential created for expanded growth and opportunity when less time is necessary to formally establish and maintain an enterprise offers an added rationale for an employer to enter into the formal economy. And, particularly with regard to those indirect, or overhead, costs, less time and effort expended correlates exactly with real cost reductions for businesses in the initial start-up phases.

For governments, the use of technology and simplified record-keeping to reduce costs and time has played an indispensable role in achieving this initial stage of formalization. One example is the process of allowing instant formation of a limited liability entity by immediately assigning the identification numbers necessary to begin actual business activities.

Other success stories have included the creation of user-friendly web pages that facilitate and accelerate requests by new businesses; these online methods require much less time from entrepreneur applicants and can minimize the steps necessary to effectively establish a new entities; this method is also helpful to the governments and municipalities in centralizing data for tracking and interacting with businesses. Of course, where Internet access is not universally available, it

would be necessary to maintain accessible offices with staff prepared to accept personal information and share relevant information with applicants, and ideally during some hours that do not compete with the traditional work day.

A useful example of this use of the internet is found in Peru where a web portal has been designed to facilitate the formalization of businesses. Another example is found in Puerto Rico, where simplified business registration procedures have been developed for companies that meet the following non-concurrent requirements: capital investment less than US \$ 6,000, annual turnover expectations less than US \$ 10,000, or a limited liability company owned by an individual. Under these conditions, applications are given incorporation status instantly, with the use of automated and standardized forms to register a new company; and these new entities are also exempt from corporate formalities, such as appointing officials, holding meetings, etc.

B. Reducing the Risk of Personal Wealth

The concept of limited liability of a person under the law has been identified, rightly, as one of the best inventions in the recent history of mankind. Through it the entrepreneur's ability to invest is not limited by untenable financial risks, instead leaving the business itself, along with its assets, to carry the risk. Thus, by way of legal status, the company is a separate entity and carries the liability generated; consequently business activities will not jeopardize the employer's own personal wealth and property. In fact, many business owners, without the limited liability option, would not have risked their own assets to develop some of the goods and products that we enjoy today. Unfortunately, in many countries initiating an enterprise under a limited liability status is costly and complicated, not to mention that it is rarely available to small-scale businesses or those without a partnership owner structure.

So, absent the opportunity to limit liability to the business assets or industrial property of the company, many entrepreneurs prefer to minimize risking their personal assets in the only way possible: operating small businesses under the aura of informality. These business owners, in order to minimize personal risk on behalf of liabilities tied to the business, often are doomed to exist on the edge of the formal economy; and the result is limited or no growth in their enterprises.

In some countries the law does not contemplate the creation of limited liability entities unless there is a partnership of at least two individuals. This actually creates a disincentive for individual informal entrepreneurs to take the risk of creating a business. Under that scenario, employers will ultimately benefit by seeking out a trusted partner and formalizing to reduce business risk; otherwise they are likely to remain in the informal economy, their businesses limited, and at continued risk to their personal wealth.

Some countries have eliminated the requirement of multiple partners to create a legal business entity. For example, under the LLC (Limited Liability Corporation) model in the United States of America, any individual business ("Sole Proprietorship") does not have a requirement that the company must be constituted by at least two (2) people. The LLC structure gives the employer not only the benefits of limiting personal liability to third parties, but also a number of tax benefits and the ability to sell the business through a transfer of limited liability entity. Regulations are in place as well to restrict abuse of this type of entity by establishing maximum corporate capital

requirements; so, from that maximum, companies must transform into regular limited liability companies and comply with the formalities thereof.

Example: Individual Enterprises in Peru.

In Peru, the ‘Law for the Promotion of Competitiveness, Formalization and Development of Micro and Small Enterprise’ and the state’s posture of access to decent employment has included a change that can serve as an example of this best practice. Article 29 of the Law states that, to qualify for the MSEs under the law, businesses need not be a legal person but may take the form of Individual Limited Liability Company or any of the corporate forms provided by law. Thus, entrepreneurs who want to formalize their business have the choice between incorporating as individuals or by using any of the following options: (1) Individual Limited Liability Company (EIRL), (2) Commercial Limited Liability Company (SRL), (3) Closed Stock Company (SAC) and (4) Sociedad Anónima (SA).

The portal Crecemype, <http://www.crecemype.pe/>, offers online help to create limited liability entities at a low cost and within a maximum period of 72 hours. While several required steps must be taken personally by the employer, the web site offers all the necessary information, contact details, physical addresses and related web sites to initiate a new business.

2. Property Assets.

Capitalization of citizens with direct ownership of natural resources or collective capitalization funds.

According to the report of the Commission for the Empowerment of the Poor, there are new forms of ownership of assets that can be granted to the poor; these are to increase the base of owners, to expand the market for assets and to facilitate access to credit.² With access to additional sources of capital, informal entrepreneurs may have enough resources to venture to grow in the formal sector.

This practice may consist of capitalization through financial instruments such as shares in legal entities that exploit the natural resources for the benefit of all adult citizens of a country; these are particularly a benefit to the poor. Through this method individuals not only receive an asset that is negotiable, but gain effective control of a substantial portion of public revenues.

An arrangement that has been successful in the state of Alaska, for example, is to universally grant rights to its residents to any revenues from the exploitation of its natural resources. The Alaska Permanent Fund Dividend was created in 1980 with the idea of distributing wealth among Alaskans. While the program was initially created to distribute the fixed amount of US \$50, it was later amended to distribute all dividends among persons residing in Alaska for more than 1 year. The amount varies annually and some of the income is reserved to certify residency requirements. Through 2008, distributions per resident ranged from US \$ 331 and US \$ 2,069 per year:

Historical Summary of Dividend Applications and Payments					
Year of Dividend	State Population	Dividend Applications		Dividend Amount	Disbursed Amount
		Received	Paid		
2008	679.720	641.291	610.096	\$ 2069.00	\$ 1,262,288,624.00
2007	676.987	628.895	595.237	\$ 1654.00	\$ 984,521,998.00
2006	670.053	623.792	594.029	\$ 1106.96	\$ 657,566,341.84
2005	663.253	627.595	596.936	\$ 845.76	\$ 504,864,591.36
2004	656.834	625.535	599.243	\$ 919.84	\$ 551,207,681.12
2003	647.747	619.552	595.571	\$ 1107.56	\$ 659,630,616.76
2002	640.544	612.377	589.420	\$ 1540.76	\$ 908,154,759.20
2001	632.241	608.600	586.230	\$ 1850.28	\$ 1,084,689,644.40
2000	627.533	607.910	583.098	\$ 1963.86	\$ 1,145,122,838.28
1999	622.000	589.738	572.877	\$ 1769.84	\$ 1,013,900,629.68
1998	617.082	581.803	565.256	\$ 1540.88	\$ 870,991,665.28
1997	609.655	573.057	554.769	\$ 1296.54	\$ 719,280,199.26
1996	605.212	564.362	546.045	\$ 1130.68	\$ 617,402,160.60
1995	601.581	563.020	541.842	\$ 990.30	\$ 536,586,132.60
1994	600.622	557.836	534.599	\$ 983.90	\$ 525,991,956.10
1993	596.906	549.066	527.946	\$ 949.46	\$ 501,263,609.16
1992	586.722	542.263	522.636	\$ 915.84	\$ 478,650,954.24
1991	569.054	533.692	512.098	\$ 931.34	\$ 476,937,351.32
1990	553.171	531.494	497.608	\$ 952.63	\$ 474,036,309.04
1989	538.900	524.272	507.547	\$ 873.16	\$ 443,169,738.52
1988	535.000	532.227	518.150	\$ 826.93	\$ 428,473,779.50
1987	541.300	535.578	529.478	\$ 708.19	\$ 374,971,024.82
1986	550.700	540.202	532.294	\$ 556.26	\$ 296,093,860.44
1985	543.900	525.145	518.479	\$ 404.00	\$ 209,465,516.00
1984	524.000	490.413	481.349	\$ 331.29	\$ 159,466,110.21
1983	499.100	465.567	457.209	\$ 386.15	\$ 176,551,255.35
1982	464.300	484.344	469.741	\$ 1000.00	\$ 469,741,000.00
Totals	15,280,838		14,740,109	\$ 29,605.41	\$ 16,531,302,074.89

Source: The Alaska Permanent Fund Dividend. <https://www.pfd.state.ak.us/>

Schemes exist and have been developed in other countries rich in natural resources where the individual has ownership rights, directly or jointly with the state, of these national resources. In some cases ownership of marketable securities is developed, such as shares in the entities (some private, some public) that are responsible for managing resources. Many of the poor, and those in

the informal economy that we are discussing, live in countries with a vast wealth of natural resources legally owned by the state. It is submitted, thus, that direct distribution of income from and shared ownership of that wealth to the poor could secure them the necessary capital to expand their opportunities and businesses, and eventually allow these citizens to cross the divide between the informal and the formal sectors.

In some countries, instead of direct distribution of royalties to its citizens, the wealth distribution can be developed through marketable titles of funds created by governments to invest public sector revenues; for example, those yielded by exploiting a natural resource, such as copper, oil, diamonds. [Another modality could be the distribution or ownership of marketable securities to all adult citizens of a country through an investment fund created with the revenues yielded by the provision of a special and essential logistics services for world trade, such as an inter-oceanic canal.](#)³

Another possibility worthy of consideration is the creation of investment funds from financial resources that developed countries provide to developing countries. These could be established, for example, in exchange for non-exploitation of forests or natural resources or as compensation for carbon dioxide emissions (CO₂), and would deliver marketable securities, representing ownership shares of these funds, among the citizens.

Countries like Norway, Chile, Palau and Iraq, among others, have developed mechanisms that somehow involve citizens in direct ownership of natural resources. The UK and the Czech Republic had already implemented similar schemes prior to the major privatizations of the early nineties.

Today, many countries have established sovereign wealth funds ("sovereign wealth funds") where public resources are allocated and whose surpluses are invested in businesses of various kinds around the world. Examples of these are funds from Russia, Norway, China, UAE, Singapore and others. Ownership of the funds typically are the states', and, in some cases, pension funds, citizens or a combination of these modalities. When ownership of the fund lies with the citizens, directly or indirectly, the result has been a substantial enrichment of the population; thus the citizens have a kind of financial seed, through which they are able access credit or venture to undertake some type of business, as evidenced by the experience of Norway ⁴.

In short, the benefits of these schemes are not only direct capitalization in terms of access to start-up capital, but there are also indirect benefits. In Kenya, for example, the state-owned company, Ken Gen, needed to raise 8 billion Schillings within Kenya but instead raised 26 billion Schillings; there were three times the number of anticipated prospective investors, many of which tripled their money. As a result, investments in the market increased from 50,000 investors in 2002 to more than 750,000, many of whom reside in rural areas. As well, the total value of transactions of Ken Gen stock increased from 1 to 12 billion Schillings ⁵.

3. **Hiring.**

Special Labor Law for MSEs.

In many countries the cost of labor is one of the biggest disincentives for a business to be

formalized. In fact, it is the cost of labor in general that affects the overall business climate and competitiveness of a country. In some cases the pay rates are low enough that very few companies are supported or there are companies with little ability to compete globally and as a result are condemned to remain informal.

Labor costs are diverse and it is obvious that worker protection is essential for social peace in a country. In this sense, the World Trade Organization (WTO) has set minimum conditions for such protections to be in effect. On the flip side, a very rigid labor system is likely to eliminate the potential emergence of new companies and this will lead to fewer employment opportunities. Therefore, within the framework of accepted international standards, a positive business climate dictates that labor systems are flexible. This flexibility is more likely to translate into reduced costs for building and operating a business.⁶

For those operating within the informal sector of the economy, labor cost is often listed as one of the main causes for not becoming formalized. Thus, informal entrepreneurs lend credence to the exaggerated report that labor costs remain a rationale for being informal. But informal entrepreneurs do not cease to hire staff that they need to operate their businesses; they simply avoid certain costs of labor and create an alternate picture of informality: informal employment. This may mean that employees receive a salary that does not necessarily conform to regulations of the formal economy, in regard to a minimum wage for example, are usually paid in cash and receive salaries that exclude social security or protection from termination of employment. Informal entrepreneurs often prefer to pay workers less to offset the cost of paying off corrupt public officials responsible for overseeing compliance with labor law. And, in most cases, the combined costs of lower labor rates and payoffs to corrupt officials are lower than the cost of complying with labor regulations.⁷

Labor costs can be classified into the following:

- The costs of hiring;
- Social security costs;
- The regular cost of employee activity;
- The costs of terminating the employment relationship.

The big dilemma facing public policy makers in many countries is balancing requirements for businesses to comply with labor protection regulations while also allowing companies to be competitive through the creation of conditions for a flexible labor market. *The point is* – how to eliminate employer expenses that do not benefit the worker, especially those that the typical worker rarely sees. For example, in many countries and for many companies, the cost of social insurance, what the employer must pay the employee beyond his wages, is expensive. In fact, social insurance can be substantially more expensive than worker wages. And, because social insurance entities are often insolvent or the funds collected have been expended for political patronage, even in cases where social insurance is paid workers rarely receive any benefits.

Adapting labor laws to the realities faced by informal entrepreneurs, especially those who have just concluded operations but which are classified as MSBs, is a successful practice in some countries. Simply reducing operating costs can make it easier for these businesses to stay in the formal sector.

An example of this practice is found in Peru:

The Labor System of the MSEs in Peru

Pay and working hours

Special Labor Regime includes: remuneration, working time of eight hours, working hours and overtime, weekly leave, vacation, holidays, protection against unfair dismissal.

Compensation for Time of Service (CTS)

The CTS is a payment received by the employee for use against the possible risk due to termination of an employment relationship and the consequent loss of income. Workers in small businesses are entitled to the CTS; the benefit compensation for this group will be fifteen (15) days pay for a full year of completed service, up to a maximum of ninety days of wages. Micro workers will not have this benefit.

Rewards

Employees of small businesses are entitled to two bonuses a year, one in Independence Day and the other at Christmas, with half the amount of the bonus paid per holiday. Micro employees do not receive this benefit.

Vacation

Workers in the micro and small enterprises have the right to a minimum vacation or leave of fifteen (15) calendar days for each year.

Unfair dismissal.

Compensation for unfair dismissal for microenterprise workers is equivalent to ten (10) days pay for each completed year of service, with a maximum of ninety (90) days pay. If workers are in a small business, severance pay will be equivalent to twenty (20) days pay for each completed year of service, with a maximum of one hundred twenty (120) days pay.

MSEs and Health System

Small business, employers must contribute 9% to ESSALUD, and there exists a micro special scheme for health services.

Special Health Scheme

Of the microenterprise workers covered by Law No., 28,015 are members of the Special Regime of Health Semi-Contributory, the Comprehensive Health Insurance (SIS) that covers their successors. This health insurance is partially subsidized by the state and is subject to the presentation of a certificate of registration or re-registration of the National Register of Micro and Small Enterprises (REMANyPE). The employer must contribute monthly, on behalf of each worker, half the monthly contribution to a semi-subsidized regime of the SIS; the other half of the contribution will be given by the state.

Pension regime for MSEs

Workers in small businesses make mandatory pension contributions to either the National Pension System (ONP) or the private pension system (AFP), whereas for workers in the microenterprises this contribution is optional.

Creating the Social Pension System

The contribution to the Social Pension System will be up to four percent (4%) of the minimum living wage, on the basis of twelve contributions per year. The State will contribute an amount equal to the minimum monthly contributions effectively made by a wage earner. To receive the retirement pension rights, members of the program must be sixty-five (65) years old and have completed at least three hundred (300) effective contributions to the Social Pension Fund.

Source: Gustavo Purilla Goicochea. Accounting Point, Peru.

The impact of different employment regimes is apparent in tangible cost savings to the employer in terms of disability as are the MSEs. But the impact is also reflected in the reduction of indirect costs, such as minimizing the amount of time that the employer must spend dealing with government bureaucracies to meet labor regulations.

Peru

Régimen Laboral	ANTES Ley General De Trabajo (D.L. N° 728)	AHORA D.L. N° 1086
	Régimen General	Régimen Especial Laboral
Vacaciones	30 días al año	15 días al año
CTS	1 sueldo por año	0.5 sueldo por año
Gratificaciones	2 sueldos al año	2 gratificaciones al año de ½ sueldo cada una
Despido Injustificado	1/2 sueldo por año trabajado (tope 12). Fracciones en dozavos	20 remuneraciones diarias por año. Tope 120 remuneraciones (4 sueldos)

Source: www.plades.org.pe

4. Fiscal contributions.

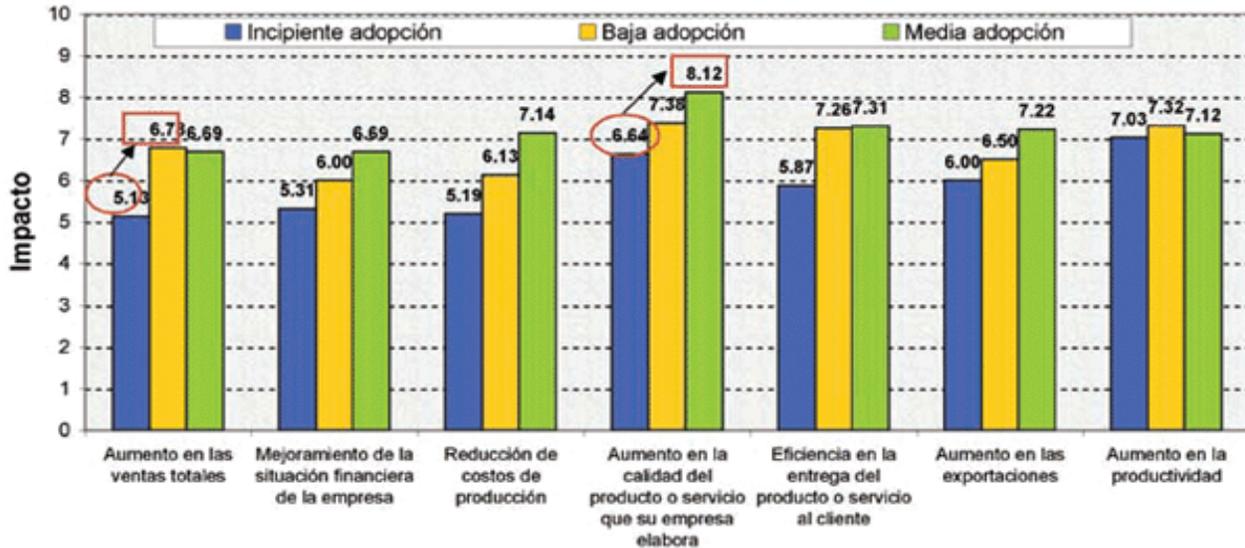
Training for MSEs: Involve the private sector through tax incentives.

Training informal entrepreneurs to successfully compete in the formal economy is crucial. Training is needed not only in the characteristics of entrepreneurship in general (business plan, cash flow, etc.) and in the professional skills required per industry (negotiating, marketing), but also in how to thrive in a much more complex and competitive environment (business strategies). The importance of training can not be underestimated; however, training is often misguided in that it may be limited to less critical industry-specific skills and offered by trainers with little or no practical experience in the business world.

A study conducted in Mexico in 2007 showed that each year an average of 200,000 companies are created; of these, approximately 10% are likely to develop in the formal economy, 25% have little chance of generating the resources needed for survival, and the remaining 65% disappear before reaching two years in existence. Within the group of SMEs that disappear before the end of two years, 66% close for lack of adequate and timely training.⁸ The study found that most managers of the MSEs believe that the cost of providing training as well as any right its employees have to update skills is an expense they are unwilling or unable to bear. Data clearly showed that even when free training is available, few workers attend because they are not given leave from their jobs for this purpose; this implies that even covering lost labor is a significant cost to small businesses to support training.

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As Mexico's experience shows, the survival of new MSEs often depends heavily on the training workers receive and how closely it fits the business needs. For example, the following chart shows the results of the impact of training in the use of computers, software and Internet on MSEs in El Salvador, with regard to group sales, profitability and productivity:



Source: *ICT in SMEs in Central America: Impact of the Adoption of Information Technologies and Communication in the Performance of Companies*. Ricardo Monge-González, Cindy Alfaro-Azofeita and Jose I. Alfaro Chamberlain. *Editoprial Tecnologica de Costa Rica*. ISBN 9977-66-174-X. Study funded by the Inter-American Development Bank, SIECA CEMPROPYME and the Organization for American States.

In many countries, employers are asking that newly formalized training be tailored to their needs and preferably provided by trainers with experience in business or via established companies in any specific industry.⁹

To achieve this, governments have contracted training through companies with experience in each specific category of interest, with training provided in exchange for tax benefits, such as tax credits for social responsibility. To qualify for this program, training would include issues of organization and business management, marketing techniques, financial opportunities, negotiation, etc. Ideally, trainers would be provided by companies within the same field of business and by local banks interested in providing services to MSEs. Under this arrangement, the MSEs not only would benefit by receiving suitable training, but it also would make possible the opportunity to network and make contacts with important business entities.¹⁰

From the standpoint of those in the private sector who provide the training, there are also multiple benefits. These entities would have direct access to the newly formalized businesses, allowing these established businesses to (a) expand their markets, (b) market their image to customers or potential customers by advertising their social benefit programs within the community and (c) obtain tax benefits. In the case of banks specifically, an additional benefit is the option to acquire new customers that will join and grow with the bank. As well, this benefit includes the opportunity to "educate" the MSEs regarding the possible opportunities through financing and the

critical importance of managing resources. Indeed, in this case banking institutions that pursue the option of providing training have not only a form of free marketing but the ability to meet directly with and understand the needs and characteristics of these groups, while avoiding the expense of market research services.

A clear example of the success of this idea is the Bank Muscat in Oman and the Bank of Galicia in Spain, both of which have been providing training in marketing and accounting, and in turn, have opened a division designed specifically to provide loans and financial solutions to MSEs .

Banco Galicia has provided free training through the program "From micro-enterprise to MSEs" that offers entrepreneurs the tools they need to better manage their businesses. This program has promoted growth and formalization, and the initiative is offered for no cost to new informal businesses. Among the central themes of this training program are: Strategic Planning, Accounting and Finance, Commercial, Tax and Legal Aspects, and Strategies to Strengthen and Increase Competitiveness. In turn, those who are formalized during the course of the program are able to access credit at a subsidized rate.

Source: Banco Galicia, www. E-Galicia.com

The role of government, through agencies specializing in the formalization and promotion of MSEs, should be to monitor and provide incentives that are commensurate with the cost of any training provided. Controls must consist of assuring (a) that training is given effectively and meets the expected requirements, and (b) that tax incentives are proportional. The proportionality of tax incentives granted to trainers should clearly imply that the tax credits constitute a fair return for the effort actually made by the qualified firms, so that any government funds distributed through loans are proportional to what it would cost to provide training directly. This public-private partnership represents the ideal configuration for effective participation between government and private enterprise.

Chile has developed an interesting idea to encourage training among MSEs called tax exemption, which allows MSEs to deduct from their income tax a percentage of expenses incurred in providing training to employees, including any training received by the owner of the company.

This idea serves as a starting point, with the tax incentive granted only to the entity trained (MSEs) but not the entity that is providing the training. Another approach might be to offer a tax deduction to these enterprises willing to provide training services to workers in MSEs.

The Franchise Tax in Chile.

The Franchise Tax is the tax incentive, established by Law No. 19,518, amended by Law No. 19,967, granted by the government of Chile to small businesses; it grants the ability to deduct from income tax to pay annually to the attendance of 1% of the annual return of remuneration of all workers hired by concept of expenses incurred by the actions of training reported to the National Training and Employment (SENSE). This entity has control of the expenses incurred in training through a process called "Communication". Communication is the information provided by the company to SENSE before the start of training through a form that exists for these effects, which must be endorsed to complete the training through the process called "Liquidation" (information

that must deliver the company conducting the training done through the form used in the "Communication", recording the information for the end of the course or the annual for the period the case is settled in the course go to the next tax year all within a period of 60 consecutive days from the completion of the training activity).

As a result of this system of promotion and training grant, over a million people were trained during 2009, up 9% over 2008.

Source: Chile Trains, www.chilecapacita.cl

5. Development - business expansion.

A. Government procurement exclusive for MSEs

The decision to formalize is a rational one where profits must be greater than the costs. But even when the cost of being formalized does not exist, the lack of benefit may also stop migration to the formal sector.

Thus, some countries have implemented practices that seek to create just the benefit to motivate the informal to be formalized. Immersed in the kind of policies we have described as "push", highlights the government procurement to MSEs. The premise behind this practice is that by creating business opportunities exclusively designed for MSEs, it creates positive incentives for migration to formality. In other words, although the practice is geared to benefit MSEs in fact it seeks to motivate informal to become formal, because it creates a business opportunity which is only available to companies that have been formalized.

In fact, this practice is about developing opportunities that coupled with the reduced costs of formalization, can create favorable conditions for growth of businesses that currently are confined to have a market only in the informal sector. Thus it is implicit, and sometimes explicitly stated, that in order to access the business opportunity created by the government procurement, it is necessary that the company has been previously formalized.

The practice in question can be developed in two ways. One is the compulsory set-aside of a percentage of all government procurement which must be purchased from companies with micro and small dimensions. In some cases it is stated that a certain percentage of such procurements is to be acquired from companies that were created within a certain period of time so that it benefits new entrepreneurs and those who have recently been formalized.

In the U.S., for example, all government agencies must make annual purchases in a percentage ranging between 10% and 20% for micro and small enterprises. The tenders opened to meet that quota are open only to such companies in a mode that is known as "separate contract" or "set-aside contracts".

Another method is to restrict government procurement to oscillate between certain amounts solely to certain types of companies already formalized but of micro and small dimensions. In Colombia, for example, the call for government procurement is limited to MSEs if the amount of the tender is below the 750 minimum monthly wages in force. There, the call is open to only one company that has previously been certified by a public accountant that stated such a condition, but also the

company will have registered at least one year before the call and must have its domicile in the place of contract performance. Likewise, it is allowed that in the limited invitation that temporary unions or associations could participate which shall be composed solely of MSEs.

The result of implementing this practice has been to create a single market opportunity for newly formalized small businesses. With the ability to maximize profits, the rational decision of many employers has been to formalize. In some cases they have not only been formalized, but through the dynamics produced by the creation of consortia, many productive chains and clusters have been successfully established to meet the needs of an expanded market. Obviously, reducing the costs of starting and operating a business in the formality must accompany this practice, along with the incorporation of positive aspects to the business climate.

Another successful example was the promulgation of Decree 3806 in Colombia to allow the government to request proposals exclusively from MSEs in the selection processes in public tendering, as well as selection on merits and abbreviated bidding processes. However, in order to participate in the process, MSEs are required to have been constituted for at least 1 year. Thus, although it appears the practice is intended to benefit the MSEs, it actually creates a positive incentive to formalize, because in order to access this opportunity the company must be incorporated.

Also there are cases of successful development of business opportunities for MSEs in the program financed by MIF-IDB in Chile, Peru and Argentina, through which special portals have been created for the MSEs to participate in state procurement. Working closely with various municipalities and public entities, the government posted on the website demands for goods and services required in order to award contracts to MSEs registered that participate in the tendering processes.

Comrapyme.com.ar

The portal Crecepyme Argentina is another successful example of how government procurement can contribute to creating growth opportunities for MSEs. This website was designed by APYME (Assembly of Small and Medium Business), with funding BID_FOMIN to spread product offerings and services of companies interested in participating in public procurement, as well as publishing the shopping needs of the various government entities.

Part of the services offered by the portal are to provide companies with ongoing technical assistance throughout the life cycle of procurement, as well as helping them overcome specific weaknesses, make partnership agreements and providing training to enhance their competitiveness. By 2008 there were more than 300 companies registered in the portal; more than 100 companies had submitted bids (a total of 438 bids), of which 224 bids were awarded tenders worth approximately \$ 1,000,000.

B. Secured transactions.

Limited access to credit is one of the barriers to growth that is commonly reported by informal entrepreneurs, and it can explain why they take refuge in the informal sector even though there are usually meager opportunities.

The access to credit is limited because banks and loan officers normally loan money when the risk of failure is guaranteed; a circumstance that also reduces interest rates in loans on the part of entrepreneurs. Because the regulatory framework is primarily developed for bank-preferred real estate collateral and because very often the informal entrepreneurs lack the required real estate holdings, the capital needed to start, operate or expand a business is limited to personal savings, family aid or non-competitive rate loans. This creates a disadvantage for the informal sector.

The regulatory framework of many countries does not facilitate the granting of security interests, except in the case of tangible and detached possessions. But the possibility of providing movable assets as collateral, such as accounts receivable, inventories, future crops, the good-will, livestock, etc., is non-existent in many countries. Since informal entrepreneurs only have the assets of their business operation to work with, the absence of a regulatory framework tailored to this reality deprives them of the possibility of access to credit.

Some countries have developed regulatory frameworks that facilitate the granting of security interests and unorthodox intangibles, such as accounts receivable, inventory or future harvests. The regulatory framework is built on an electronic registry that does not require the borrower to yield the possession of the property.

Thus, the secured transaction is constituted as a right of possession or preferred control of property over moveable assets. As such, it does not require that the secured debtor be the owner of the guarantor chattel, because it is the debtor's right to possession of it, even if it is concomitant with other possessory rights of the same property, the one upon which the security interest is created. The security can be created upon any security interest susceptible of pecuniary valuation, whether they are present or future, tangible or intangible, including rights upon them, as well as property rights derived or attributable to the sale or exchange of these securities, whether in a first or subsequent generation of such goods or attributable thereof. Therefore, the collateral as well as guarantees upon them are open number (numerus apertus) and are not limited to pledge of moveable with or without displacement of possession or mortgages or sales with title withholding, etc.. 11

In Latin America, Mexico, Peru and Guatemala have adopted broad and modern laws enshrining the figure of the secured transaction. In most cases, they have been inspired by the model law on secured transactions of the Organization of American States (OAS). Guatemala, particularly developed and put into operation its collateral registry in February 2009, allowing secured creditors to register rights to any property and against third parties.

In other developing countries such as Serbia, Albania, Kosovo, Macedonia, Bosnia, Morocco, Madagascar, Armenia and Kazakhstan have implemented reforms to allow a system of secured transactions. The system essentially is governed by these principles:

- A wide range of goods and interests. Secured transaction legislations should not have limits on what kind of property can be used as collateral. The parties may opt for a comprehensive list, for example in the case of inventories, or a specification of such goods when it comes to

a machine with serial numbers. Moreover, the goods must not be owned by the collateral giver, it is just enough to have an interest, an expectation or soft-law right. For example, a tenant could give as a guarantee the right to rent a property.

- Rapid and economic enforcement of the right. The creditor should enforce the rights upon the thing given as security in an expedited manner. Normally under the pertinent law the creditor can take possession of the goods and sell at public auction or otherwise at market prices.
- Priority. The law allows the creditor to establish priority over the property in the event that another creditor tries to take over, by recording the right or interest. The record makes public the priorities of rights on the collateral, without leaving room for confusion.

In Albania, the adoption and implementation of the law of secured transactions reduced the premium risk in half and interests fell to 5 percent. Interests in Romania fell by 20 percent since the law was implemented. In Guatemala the law on secured transactions was passed in 2007. Within two months of having entered into force, 91 secured transactions were recorded worth more than U.S. \$ 20 million. Most of the records pertained to harvest, industrial machinery, livestock and commercial stocks.

C. Leasing and factoring.

It is not only secured transactions that may facilitate access to credit for informal entrepreneurs, therefore motivating formalization. There are other figures in business financing such as leasing and factoring. Both can expand access to capital by entrepreneurs in general and informal entrepreneurs in particular. And although they are not exclusively aimed at the informal entrepreneurs, as long as the formal establishment of the business is usually a condition for leasing and factoring, in fact as practices that "pull" the informal, they can be an additional motivation to join the formal economy. Because, as noted above, reducing costs of incorporating a business in the formal economy is not enough to encourage informal entrepreneurs. And in those cases in which in addition to reducing costs, there is a business opportunity, it is possible that the entrepreneur lacks financial instruments suitable and adaptable to its size and needs in the formal economy. It is precisely that void that is filled by the leasing and factoring.

Leasing is a lease of immovable and movable property such as vehicles and machinery, with the option to purchase the property after a while. So, rather than pay the price of the property, monthly fees are paid for the use, which involves: (a) accelerated depreciation of the asset at the will of the company, (b) leasing taker must choose the asset that best suits their business and usually with discount for cash payment, (c) by paying a predetermined residual value of the contract the lessor can acquire the ownership of the asset, (d) unlike other sources of financing, leasing allows 100% financing of the property, which acts as collateral, (e) normally the operations close in less time than obtaining a bank loan.

The "factoring" is another product that can facilitate access to credit. Factoring discount or sale of accounts receivable is a financial contract that is entered into between a financial institution and a

business to which the entity acquires all loans at a discount for a certain period of time. In other words, the entrepreneur gets cash immediately to change receivables or invoices.

A new form of financing in some countries is the "Purchase Order Financing" or POF. In other countries, some banks dedicated to providing services to MSEs have introduced these forms of security interests similar to factoring. Unlike factoring, the POFs enable MSEs to raise funds before starting the production process, solving the problem of cash flow from the start, on one hand. On the other hand, allows them to accept purchase orders that exceed their abilities in principle, thus allowing them to grow in the medium term. For banks the POFs have the advantage of being very short-term and easy to monitor.

An example of this practice is found in Macedonia.

- **BEST PRACTICES: MACEDONIA**

Using only POFs, factoring and export orders, without any real estate collateral, the following results were achieved in the first 30 months of application:

- Loans were issued totaling \$ 6,000,000.
- It created 550 new jobs.
- It generated \$ 4,000,000 in new exports.
- They were awarded in the areas of agriculture, food processing, trade, textiles, leather, construction materials and so on.

Source: Crimson Capital Corporation Crimson Capital Corporation

SME Finance in the GMS SME Finance in the GMS - Building a Common Strategy

2006 2006

6. Environmental issues: licenses.

Usually associated with licensing and operating permits, environmental issues have been addressed from the perspective of simplifying steps and costs to operate.

From this perspective the following practice is presented:

Reduction and elimination of licenses and permits to operate and the incorporation of positive silence, subsequent inspections, economic unit and the simplified licensing.

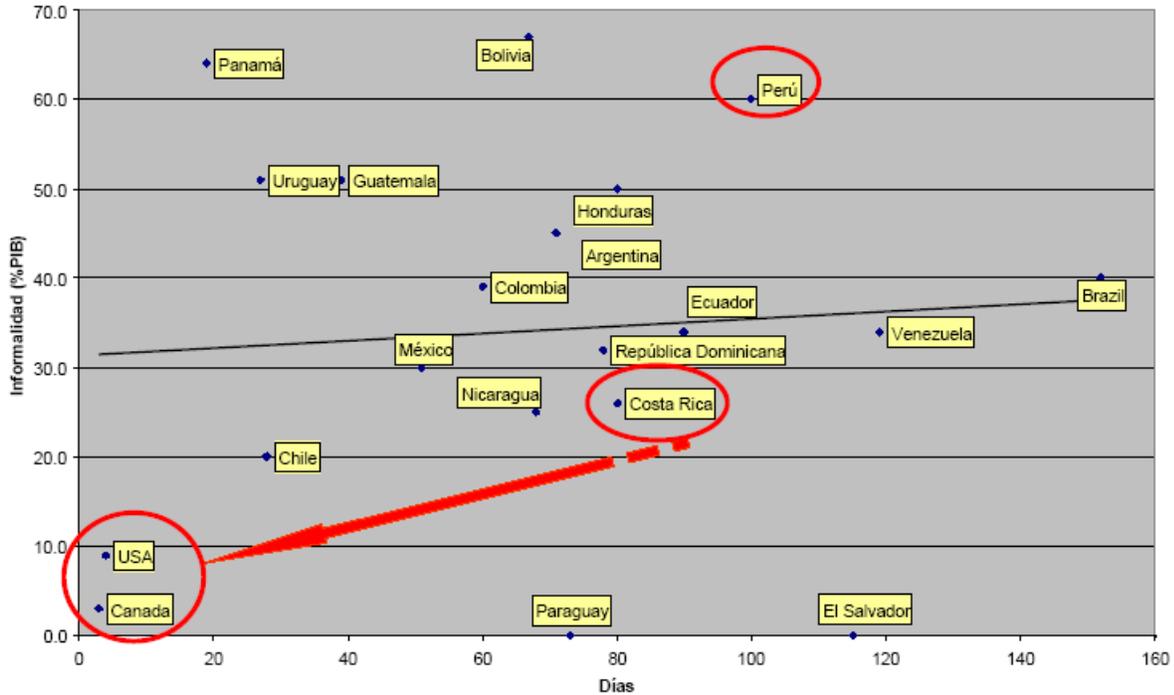
As the cost of starting a business can deter many entrepreneurs to formalize, equally the cost of operating a business can deter many from continuing in the formal economy.

The direct and indirect costs of obtaining licenses to operate a business, coupled with the time it takes to get and the discretion of officials to grant them experienced by some countries, are factors enough to kill the dreams of many entrepreneurs. To this we must add, as is the case in many

countries, the prevalence of a license to obtain another. For example, some countries require an environmental permit as a prerequisite for obtaining a commercial license.

In addition to licensing, many countries, especially at the municipal level, require specific permission to operate, to advertise or occupy a shop. Obtaining and maintaining permits is an additional cost and effort for entrepreneurs as well as being a source of corruption that costs money.

Duración de los Trámites vs. Informalidad



Source: USAID / mypecompetitiva / grow

The following practices have been introduced to facilitate and promote the licensing:

1. Economic unit concept: This concept allows a single entity encompassing several businesses within a category belonging to the same owner. The economic unit has the advantage that it can determine the true size and potential of the business of a person. On the other hand, it facilitates the licensing process, because instead of requesting a license for each business, one license is required for the economic unit. The closure or transfer of a business comprising the economic unit is simply notified to the relevant entity.

2. Positive Silence: The introduction of this principle in the process of licensing implies that (a) the agency that grants the license is required to respond within a certain time limit and (b) after that period of time, it is considered that the license has been approved. The applicant of the license can use the record of having introduced the petition as evidence of the positive silence response.

3. Inspections after the granting of licenses: The idea of this practice is to allow applicants not to have to wait for an inspection to be conducted to their business as a preliminary requisite for granting the license. Instead, inspections should be made after the granting of the license and based on clear and objective parameters.

4. Notifications instead of licenses: For those areas of the economy that do not involve risks to health, safety or the environment, it is recommended that notifications be used to inform the authorities via a simplified form.

An example of this practice is found in Peru.

Simplification in Peru.

The United States Agency for International Development (USAID), through its Competitive MSE Project Peru managed to formalize the past three years more than 12,500 new micro and small enterprises (MSEs) located almost entirely in the regions inside the country. This result was obtained thanks to the important achievements in administrative simplification, one of the main objectives of the project, which worked with 22 municipalities within the country and 15 ministries.

... ..

During these three years, 240 bureaucratic barriers applied by 15 ministries and crossed with municipal management were lifted.

... ..

But thanks to a coordinated effort such barriers were reduced by 47 percent as the requirements to obtain an operating license were targeted. In addition, the delay time was decreased in 75 percent since the time to obtain a license was reduced from 30 days to an average of 15 days. Similarly, the cost of formalization was reduced by 48 percent, and currently is 120 new Soles on average.

Source: Andina, Peru News Agency

(AND266178) Date: 25/11/2009

7. Settlement of disputes.

Dispute Resolution adapted to MSEs, E.G: small claims court and expeditious procedures or oral and summary.

One of the major drawbacks of the business climate in many developing countries are lengthy and costly legal proceedings. Obviously, slow and inefficient resolution of disputes not only affects the informal, but affects all sectors of the economy alike. However, those who most suffer the shortcomings of a justice system are those with fewer financial resources. For informal entrepreneurs, expensive and lengthy court proceedings are not a solution. The resources that should be invested in order to regain rights through judicial procedures are inconsistent with the amount in dispute. As a result, many debts are not paid or collected by illegal means. The corollary is that the informal transactions tend to be low-value, precisely because the risk of not being able to collect them in court proceedings, which is a factor that inhibits the growth of business.

Thus, the informal are affected by three problems as it pertains to the resolution of disputes.

- **Time of procedures.** Time-consuming procedures mean that time is not devoted to the business and time that passes without the availability of money in dispute.
- **Costs.** The procedures require payment of direct costs such as legal expenses and fees, but also indirect costs such as transportation, communication, forms, interests in loans, etc. Thus, money spent on litigation until its termination, is money not invested in the business.
- **Procedures are not adequate for the informal.** Most of the procedures in civil and commercial law of many developing countries are designed for different and more complex realities than those of small businesses. Thus, the procedures are usually written, for example, or ignore the possibility of submitting consolidated actions or "class actions" where many plaintiffs in similar conditions are joined. The fact of the matter is that it is very different to administer justice to litigation involving banking debt collection of mega companies with international component than settle disputes involving small amounts between informal entrepreneurs.

Some practices successfully implemented in many countries, include the creation of courts specialized in small claims as well as the implementation of expedited and oral procedures where preliminary issues and appeals are limited to very special circumstances. Some countries use standardized forms for submitting claims of a certain amount of debt, and restrict the use of certain type of evidence that can be presented as well as the possibility of delaying the proceedings with irrelevant testimony, along while the judge is compelled to issue its decision immediately after the conclusion of the hearing.

Similarly, introducing mechanisms such as prior conciliation of the dispute in an oral and professional manner has substantially reduced the percentage of cases that arrive at the stage of litigation. In other cases, arbitration centers have been created exclusively for disputes between small businesses.

In India there are such courts for disputes of \$ 200, but in Korea there for disputes up to \$ 21,000. In many countries the amount upon which a dispute is small amount has been determined based on income per capita and is usually set at 20% of that variable to be adjusted from time to time. Either way, these disputes are usually resolved quickly. In South Korea, they were resolved in 230 days on average.

Inspired by the Brazilian system is described below, Guatemala implemented a justice of the peace model installed in a mobile bus equipped and furnished, with a room to the public to be improvised on the side of the bus, and a room for mediation and hearings. In the courtroom is the judge, the clerk, an officer, a notifier social communicator who manages the matters dealt with by the mobile court, a sheriff- driver to drive the bus and a security officer. In this room the whole legal process takes place. The areas of competence are mixed in criminal matters and not criminal (family, civil, labor and commercial) such as offenses against persons and property, criminal cases likely to resolve through conciliation or mediation, know with prevention purposes intra-family criminal cases issues, consumer complaints against dealers, collections, small claims on acquisitions defects, issues of land boundaries, domestic issues of among neighbors, among others. Additionally, within the bus is a mediation center, which acts independently, made by an expert for mediation as an alternative mechanism that can be used before a judicial process. Both processes, mediation and judicial are free. Similarly, if once initiated a legal proceedings the judge decides to refer the case to mediation it may also be used at this time.

Small claims courts in Brazil.

The 1998 Constitution institutionalized the Civil and Criminal Special Courts with a view to prosecute cases of lesser complexity - civil - and minor criminal offenses. The system has the following virtues:

- The settlement hearing is mandatory and occurs before the respondent's reply. While the regular judicial system also provides for a mandatory settlement hearing, in most cases it does not yield any positive results. In the conciliation meeting under the system of special courts between 38% and 43% of cases are resolved, since that meeting happens before the respondent's reply, that is, before tempers incite and litigation is institutionalized, thus closing the space for compromise of the parties 12.
- The system is oral: Oral tradition is the rule of the system, written arguments are allowed only to summarize the essential acts.
- Access to the Small Claims system is free: the parties do not pay court costs and attorney's use is optional for cases that do not exceed 20 minimum wages.
- Appeals are limited to a single resource. In the regular process right of appeal is almost unlimited, which makes the trials endless. In the system of these special courts, the right to appeal is limited to just one resource, directed against the final decision and exercised at a college of judges of first instance.

Recent figures show that approximately 21% of the total civil cases are resolved in the system of Special Courts:

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
TOTAL	196.195	256.130	322.474	357.952	363.759	493.213	471.378	586.092	660.996	683.060	756.393
Justicia Común	188.799	236.717	278.128	291.860	284.527	351.859	341.294	455.150	518.518	535.837	596.013
JEPCs	7.396	19.413	44.346	66.092	85.232	141.354	130.084	130.942	142.448	147.223	160.380
% JEPCs	3,77%	7,58%	13,75%	18,46%	23,05%	28,66%	27,60%	22,34%	21,55%	21,55%	21,20%

By 1997 the project started the "Itinerant Justice," which operates in several states on buses that cover the areas of greatest need. These wandering courts, divided in turn into informal conciliation courts and special civil courts.

8. Closing a business.

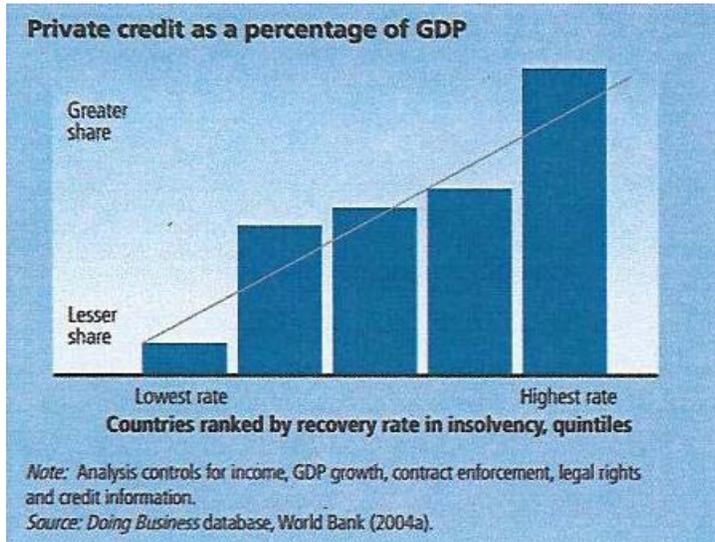
Restructuring and liquidation of companies in operation: possibilities to acquire operating companies operating out of debt or operating business units.

-

Bankruptcy laws, bankruptcy, insolvency, reorganization or business recovery laws, as they might be called, are good for countries for the following reasons:

- **They end up with unviable business.** Many businesses in the state of dissolution are moribund without actually closing. Productive assets are used frequently to other economic activities, but not without difficulty. As a result many businesses are active only in appearance and properties that otherwise could be devoted to productive activities, remain ineffective. In addition, companies that enter a state of dissolution can only pay and collect, causing problems for the economy that demands productive activities that generate income and create jobs. The assets of unviable businesses can be sold in parts or as on-going business. As a result, the goods reenter the production process. No wonder it has been shown that the closure of inefficient business increases the overall productivity of a country. For example, the exit of unviable businesses contributed 19% of productivity growth in Taiwan, 23% in South Korea and 39% in Indonesia in the 90's. [13](#)
- **Save viable businesses.** Businesses that are in distress can seek legal protection while restructuring takes place. As a result the business continues to operate and the economy is not affected at the same time that workers keep their jobs. In Brazil, for example, it is estimated that about 400,000 jobs could be saved with an appropriate legal framework for closing business. [14](#)
- **Increase credit.** Today, access to credit is de facto denied to those who can not give guarantees, either because they have no guarantee to grant or because the legal system does not accept what they could bestow. With an appropriate legal framework for insolvency, creditors, including unsecured creditors, can recover their claims of an insolvent debtor.

Thus, creditors are provided with a tool to efficiently collect their claims against a business with difficulties, even in the absence of guarantees, an element that can increase the amount of credits that may be offered, primarily from the microcredit entities to small and medium enterprises. In this way, with high recovery rates, banks are more willing to lend, the economy will grow, as more jobs will be created. 15



However, although the laws of corporate insolvency are not enough – as most businesses close voluntarily and the majority of creditors enforce their guarantees to satisfy the claims they have against insolvent companies 16 - the laws of insolvency are needed in modern economies.

Looking to the informal sector, a modern insolvency law can eliminate unnecessary competition by ending unviable business, create business opportunities by allowing companies to acquire on-going businesses or operating units free of liabilities and encourage the supply of credit because creditors are provided with better recovery conditions in case of default.

Perhaps one of the most tangible benefits of an efficient restructuring and liquidation of companies, is that whoever acquires the on-going business or one of its units after the split, acquires the business free of liabilities. This requires an independent judiciary, transparent and specialized that could deal with cleaning the credit of the company, determine fair value, determine the nature of the claims and priorities, satisfy creditors weighing the interests of all sectors involved and give certainty transferring ownership of the company free of responsibilities.

In Spain, Mexico, Colombia, Uruguay and Brazil insolvency legislation have recently been passed. In these three cases, the emphasis has been on developing a modern legislation that will save businesses and jobs, at the same time creating business opportunities for anyone wishing to acquire an operating business debt free.

In Brazil, the new states that the priority of the liquidators must be the sale of the company as a

whole. If this fails, try to sell operating units to preserve employment and intangibles such as brands. Only as a last resort should the liquidator try to sell the assets separately and eliminate the problem of responsibility for the new purchaser. In this way he who acquires an entire company acquires debt free.

In Spain, the Act seeks to conserve firms or productive units of goods or services integrated into the mass through its sale as a whole, unless it is more convenient to the interests of the creditors that the business be divided or the performance of any or all alone of its components, in preference to solutions that guarantee business continuity.

In Colombia, the law creates a non judicial entity in charge of dealing with insolvent companies, the Superintendency of Companies which may, ex officio initiate a process of reorganization of companies. This has helped to reorganize the assets of many insolvent companies so that those who purchase do it in optimal conditions. This circumstance has been proven to create business opportunities for all sectors, including the informal sector, who can make the transition to formality by acquiring an existing business, operational and solvent.

Colombia Insolvency Act

In December 2009 a special session of the Senate and the House approved the new insolvency regime in order to give the individual non merchant debtor access to a legal procedure that allows him to enter into a payment agreement with his creditors and meet their outstanding financial obligations. The means used to reach this goal is a process of debt negotiation in an out of court settlement hearing.

The member of the Colombian Congress stressed that this project is a fundamental right because "a person who is behind in his payment schedules could be able to declare insolvency and that is not going to affect his life."

The start-up procedure is quite simple: it would suffice just make the application for debt settlement proceedings before a mediation center, attaching a report that addresses the causes of its insolvency and the proposal for debt negotiation. This proposal should take into account the state of current assets, equity and credit and include an updated list of all creditors, and other documents.

Particularly this new law will allow the banking sector to recover about one billion pesos, which today are lost in difficult arrears collection processes.

Source: Ariel Cabrera, December 18, 2009 00:00 Colprensa, Bogotá

III. THE IMPACT OF IMPLEMENTATING BEST PRACTICE CONCEPTS IN CERTAIN COUNTRIES

COUNTRY	PRACTICAL TO IMPLEMENT	SITUATION BEFORE THE PRACTICE	SITUATION AFTER THE PRACTICE
PUERTO RICO	SIMPLIFIED AND INEXPENSIVE FORMS	Registration fee is 1% of income per capita (2004)	Registration fee is 0.7% of income per capita (2010)

COUNTRY	PRACTICAL TO IMPLEMENT	SITUATION BEFORE THE PRACTICE	SITUATION AFTER THE PRACTICE
	TO REGISTER BUSINESS		
ALASKA (US)	PETROLEUM FUND	Capital received by residents of Alaska: \$ 0 (1985)	Capital received by residents of Alaska: U.S. \$ 1,262,288,624 in dividends, equivalent to U.S. \$ 1.857 per person. (2009)
PERU	SPECIAL LABOR LAW FOR MSEs	Cost of termination of employment: 52 weeks (2004)	Cost of termination of employment: 17 weeks (2010)
SAINT VINCENT AND THE GRENADINES	REDUCTION AND ELIMINATION OF LICENSES AND PERMITS TO OPERATE	Cost of business licenses: 10.6% of income per capita (2007)	Cost of business licenses: 6.9% of income per capita (2010)
CHILE	TRAINING FOR MSEs (WITH THE FRANCHISE TAX)	MSEs number of trained: 0 (2005)	Number of MSEs trained: 4 million (2009)
ARGENTINA	PROCUREMENT FOR MSEs	Special BIDs for MSEs: \$ 0 (2006)	Special bids for MSEs: 438 bids submitted, 224 tenders awarded approximately US \$ 1 million (2008)
GUATEMALA	SECURED TRANSACTIONS	Amount of loans granted on the basis of secured transactions \$ 0 (2005)	Amount of loans granted on the basis of secured transactions \$ 283 Million (2009)
MACEDONIA	LEASING, FACTORING POFs ALTERNATIVES FORMS OF COLLATERAL	POF-based credit and other collateral instruments for MSEs: \$ 0 (2003)	POF-based credit and other collateral instruments for MSEs: \$ 15 million, 2,000 new jobs, \$ 58 million in new exports (2009)
KENYA	REDUCTION AND ELIMINATION OF OPERATING LICENSES AND PERMITS	Time required to obtain permits and licenses: 158 days (2005)	Time required to obtain permits and licenses: 120 days (2010)
BRAZIL	DISPUTE RESOLUTION ADAPTED FOR MSEs CIRCUMSTANCE	Cases resolved in expedited proceedings: 3.77% (1990)	Cases resolved in expedited proceedings: 21.2% (2000)
BRAZIL	BUSINESS RESTRUCTURING AND LIQUIDATION OF COMPANIES IN OPERATION	Number of jobs due to businesses sold during liquidation proceedings: 1000 (2000)	Number of jobs due to businesses sold during liquidation proceedings: 400,000 (2006)

