

**Seminar on the Promotion of
Foreign Direct Investment to
Southeastern Europe**

Albania

8 November 2002, Tokyo, JIIA

**Ministry of Foreign Affairs of Japan
The Japan Institute of International Affairs**

QUESTIONNAIRE

PRESENTED IN THE SEMINAR ON FOREIGN DIRECT INVESTMENT INTO SOUTHEASTERN EUROPE

Tokyo 8 november 2002

Transition to market economy

Public Sector Investment in the 1990s

Albania entered the post-communist period with an infrastructure that was totally inadequate to support the transition to a modern market-based economy. Consequently, increased levels of public investment have been a key component of the programme of economic reforms adopted by the Government since 1991. Between 1994 and 1996 investment levels increased rapidly from US\$ 119 million to US\$ 237 million. Over this period external aid became the major source of financing for public investment and in 1996 accounted for around 65% of total disbursements for public investment projects.

Increased investment levels have been accompanied by changes in the scope and definition of public investment. These have reflected the withdrawal of the state from direct involvement in the industrial and trade sectors and the changing role of government as an investor. Thus the major focus of public investment in recent years has been on: (i) the rehabilitation and development of public infrastructure; (ii) improvements in public sector service provision involving re-equipping, retraining and the introduction of improved management practices; and (iii) supporting institutional reform and development in areas such as legislative reform, public administration, the judiciary and law and order.

In general, Albania has made considerable progress in its transformation process towards a market economy. After the successive shocks of the demise of the communist regime and the consecutive period of chaos (1990-1992), fundamental social and systemic reforms have been initiated. Quick progress was achieved in liberalisation and private sector development, especially in agricultural production and small and medium enterprises. An entirely new legal and institutional framework was being elaborated. However, implementation and enforcement lagged behind legislative work and the overall administrative capacity remained weak. The financial sector remained as well largely unreformed. The result was the collapse of the schemes in late 1996 and early 1997 and the subsequent breakdown of law and order. Parliamentary elections were held under international supervision in June 1997 and a new government was elected. The main elements of the new Government's strategy for political, social and economic reform and recovery are:

- (i) political normalisation and democratisation;
- (ii) restoration of law and order;
- (iii) institutional reform;
- (iv) addressing poverty caused by the 1997 crisis;

- (v) macro-economic stabilisation;
- (vi) financial sector reform and resolution of the pyramid schemes; and
- (vii) privatisation of strategic sectors.

Developments in the Banking System

The Bank of Albania is implementing the law no.8873, dated 29.03.2002 "On the creation of the Deposits Insurance Agency" and other legal obligations. With support of USAID and FSVC it continues the work for creating a Deposits Insurance Agency.

Based on the cooperation between the Bank of Albania and the FDIC (Federal Deposit Insurance Corp.), some experts for training the future staff of the Agency, are going to be present in Albania very soon.

- On the functioning of the Supervision Department

The review of the regulations "*On the functioning of the Supervision Department*" were made necessary in order to reflect the changes of the structure of the supervising Department and to improve the way of reporting. They add important elements of reporting to the Supervisory Council of the Bank of Albania. Particular attention was paid to the approximation of the licensing regulatory framework and banking regulations with the most recent international practices, methods and principles of supervision and improvement of legal documentation as well as in the licensing process.

- Free movement of capital

Albanian legislation does not apply any restrictions on foreign exchange related to any type of investment, the quantity of the investment, the amount of foreign currency that can be exchanged or the possibility for foreign investors to repatriate their profits in foreign currencies or in Lek which are earned through their investment (every type of investment including deposits) and/or the initial capital invested in Albania. The law No. 7764 dated 02.11.1993 "On Foreign Investments" sets forth and ensures the free movement of capital related to direct investments carried out in Albania by foreign companies.

In the report of the Working Party on Accession of Albania to the World Trade Organization and in the schedule of Specific Commitments on Services, Albania is committed to allow legal and natural persons (not including Banks), residents and non-residents to carry out freely the following outflows of capital transactions:

- Outflow of capital transfers equaling the amount of the previous inflow of capital plus the profits derived from returns (return means an amount derived from or associated with an investment including profit, dividend, interest, capital gain, royalty payment, management fee, technical assistance fee or 'other fee');
Compensation; payments arising out of an investment dispute; loan repayments according to a loan amortization schedule; proceeds from the sale or liquidation of any or all parts of an investment, and the return of shareholders equity resulting from the diminution of capital.

- Outflow of capital transfers representing the amount of profits derived from non-residents' deposits placed with Albanian resident banks.
- Outflow of capital transfers representing the wealth of Albanian emigrants leaving the country forever.

Any other outflow of capital transactions cannot be carried out freely either by residents or non-residents. Residents and non-residents who may want to transfer capital abroad, other than the above-mentioned cases, have to obtain prior written approval from the Bank of *Albania*. This regime will be removed not later than 2010. No restrictions apply to the inflow of capital.

The first phase of the study "On free movement of capital" is over. The Bank of Albania prepared this study in collaboration with the European Commission. This collaboration will continue in preparing the next steps to be undertaken in order to finalize this process according to Albania's commitments to WTO and the European Union.

During the first half of 2002, the Albanian economy has performed its activity almost within the same framework as the previous year, being determined by the following targets: the economic increase at a rate of 6%, annual inflation rate of 2-4%, budget deficit at a rate 8 per cent of GDP, current account deficit at about 8.2 per cent of GDP and financing through the domestic lending at a rate of 3.2 per cent of GDP.

Industrial structure

The economic growth and the structure of GDP of the main sectors of the economy for 2002 are estimated as follows:

	<i>Growth</i>	<i>Structure</i>
<i>GDP</i>	6.0	100.0
<i>Agriculture</i>	3.0	33.2
<i>Industry</i>	5.0	13.0
<i>Construction</i>	11.5	10.8
<i>Transport</i>	11.0	10.6
<i>Services</i>	6.5	32.4

-Agriculture- is still the largest sector. There were positive developments during the first quarter of year. There are favourable conditions for the increase of the agricultural production and the increase of the agricultural-industrial sector on this basis, which is expected to grow by 10 per cent. Although the percentage of agricultural production of GDP is estimated to be 33.2 per cent, against 34.2 per cent resulted at the end of 2001, agriculture still remains the main sector of economy. The domestic agricultural production, although in low quantities, is exported to Germany, Italy, Greece and Turkey. Imports come mostly from Italy and Greece.

-Industry- Due to the energy crisis the industrial growth is estimated to have fallen, from 6.5 per cent at the end of 2001 to 5.0 percent now or 13.0 per cent on GDP.

-Telecommunication and transport manifested increases, but not to the extent as foreseen. It is projected that the growth, by the end of 2002, will be at the level of 11.0 percent which accounts for 10.6 per cent of Albania's GDP.

-Construction and services- mainly contribute on GDP, with expected growth rates of respectively 11.5 percent and 6.5 percent, reflecting the increased demand for buildings, trade centres, hotels etc.

-Unemployment rate- Registered unemployment declined from about 15.23 percent in 2001 to 14.2 percent in 2002. This was as a result of the increased controls on enterprises and the grey economy.

-Inflation-The main reason for the growth of the economy is the anticipated increase of the agricultural production and as well a result of its contribution to the GDP. Under these circumstances, the targeted rate of inflation and the increase of GDP seem to be realistic. This year's economic development seems to prove these assumptions. In August 2002, the annual inflation was 5.5%, about one and half percent higher than the targeted 4 per cent that the Bank of Albania had foreseen by the end of 2002. The annual inflation rate resulted to be higher than the target: for the entire year, their average was 6.6 per cent. The "food-staff" group has had the highest impact on the monthly inflation as well as the group "rents, electricity and fuel".

The path towards lowering the inflation rate has already started by recording a figure of 4.6 per cent for the month of May 2002.

The electricity crises had a direct impact on the development of prices. The Bank of Albania will continue to strive at maintaining the price stability during the next three years, aiming at a level ranging from 2 to 4 percent, under the conditions of a flexible exchange rate regime.

Socio economic infrastructure

Albania's strategic transport infrastructure consists of a road network of 18,000 km, including 2,900 km of paved and 4,900 km of unpaved national roads, a railway network comprising 477 km of main lines and 230 km of secondary lines, the international airport at Rinas and the ports of Durrës, Vlorë, Sarandë and Shengjin. Traffic patterns have changed dramatically since 1990 with substantial increases in the levels of domestic goods and passenger traffic and also the rapid growth in international transit traffic via the port of Durrës to Greece and Macedonia. While road, air and sea traffic levels have all increased, rail traffic has fallen to insignificant levels reflecting both the comparative advantage of road transport for short-haul loads and operational difficulties faced by Albanian Railways. Most infrastructure in the sector is under-designed for current traffic levels and has suffered from inadequate capital and maintenance provision over many years. The road network has faced rapid deterioration as a result of recent increases in road traffic and axle loads. Road safety has become an urgent issue since Albania now has the highest road fatality rate in Europe. Traffic congestion and vehicle-related air pollution have become significant problems in Tirane.

Since 1991, the transport sector has undergone major reform. Road transport, apart from some urban bus operations, has been deregulated and over 90% of the publicly owned vehicle fleet has been privatised. The port of Durres has been turned into an autonomous body. The Government has formulated a programme to upgrade transport infrastructure for which it has obtained substantial international support. This focuses on infrastructure along two main arterial routes: (i) the 430 km North-South corridor between the borders with Montenegro and Greece; and (ii) the 240 km East-West corridor which links the port of Durres with the Macedonian and Greek borders.

Project financing has been secured for: (i) reconstruction of 171 km of the North-South and 207 km of the East-West highways; (ii) a rural roads rehabilitation programme covering the main agricultural areas in the coastal plain; (iii) the redevelopment of Durres Port; (iv) the relaying of railway track between Tirane and Durres; and (v) the modernisation of Rinas Airport. PIP expenditures on the sector during 1996 and 1997 totalled US\$ 84.8 million compared with US\$ 175 million projected for this period in the 1996-98 PIP document. Apart from the effects of the 1997 crisis, this shortfall can be explained by the much longer than anticipated lead-in time between the approval of project financing and the commencement of implementation.

Roads

Experiences in implementing road projects have been mixed. Progress on the IDA First Transport Project which is financing the improvement of 84 km of main road and the provision of road maintenance equipment has been satisfactory. By contrast, projects for the East-West and North-South corridor projects and for the construction of border crossings have faced considerable delays. Key factors behind these delays have been: (i) inadequate initial design; (ii) lengthy donor procedures; and (iii) delays in securing the expropriation of land. Of these the most pressing issue is now the expropriation of land for which domestic financing of around US\$ 10 million will be required during 1998 if programme implementation is not to be further delayed.

Ports

A first phase programme for development of Durres Port, financed by the Kuwait Fund, IDA, PHARE and Italy has now been completed. This has involved repair and upgrading of quay facilities, provision of cargo handling equipment, institutional strengthening of the Port of Durres Authority, and the preparation of a Ports Master Plan. Construction of a new ferry terminal at Durres being financed EIB/PHARE has been delayed and is not now expected to commence until mid 1998. Financing from IDA/OPEC for the second phase of the development of Durres Port has recently been negotiated with implementation expected to commence by mid 1998. In addition to further infrastructure investment, this project will support the commercialisation and privatisation of port operations.

Railways

The project to relay rail track between Tirane and Durres has been under implementation since 1995 with financing from Italy. Implementation was halted during the disturbances, when the project was 92% complete.

Resumption of work under the contract was delayed pending resolution of a claim from the contractor, and resumed in November 1997 with completion expected in 1998. However, a more critical issue is the sharp fall in rail passenger numbers and freight volumes during 1997 which has precipitated a financial crisis within Albanian Railways and has again brought into question the long-term economic viability of the rail system.

Civil Aviation

A project to upgrade facilities at Rinas Airport involving runway resurfacing, extension of apron areas and taxiways, and installation of runway lighting and navigational aids has been under implementation since 1996. When completed, in 1998, this will allow night-time operations at the airport.

Sector Policy Framework

The main objectives of government policy in the transport sector are to provide an adequate transport infrastructure necessary for the development of the economy and to ensure appropriate regulation of transport operations in the interests of safety and the environment. The primary role of government within the sector is in the provision and maintenance of transport infrastructure, particularly in the roads sub-sector and in the management of the regulatory framework.

The main strategies through which the Government is pursuing these objectives include:

- rehabilitating and upgrading existing transport infrastructure including roads, civil aviation and ports in order to permit the development of an efficient transport system required to facilitate economic growth;
- commercialising and where possible privatising port, airport, road maintenance and railway operations in order to promote greater efficiency in operations and reduce financing demands on the State Budget;
- promoting private sector involvement in the development of transport infrastructure;
- strengthening maintenance of the road network requiring the reorganisation of maintenance arrangements and substantially increased maintenance budgets;
- increasing cost recovery in the sector through appropriate pricing and taxation policies thereby reducing net demands on the State Budget;
- establishing a legislative, regulatory and institutional framework for the sector that ensures the safe operation of transport services while promoting a high level of competition;
- creation and extension of transport data information systems; and
- monitoring and disseminating information on trends and requirements in the transport sector so that private sector operators can plan the development of their operations.

Priority Areas for Technical Assistance

Priority areas for technical assistance support under the PIP include: (i) transport sector planning; (ii) the establishment of data information systems; (iii) the preparation of a roads master plan; (iv) road safety and environmental legislation; (v) advice on the commercialisation and privatisation of Durres Port and Rinas Airport; (vi) establishment of regulatory functions; (vii) review of the viability of Albanian Railways; (viii) project feasibility and design studies; and (ix) contract supervision and management. Special measures may also be required in order to retain qualified Albanian engineers and transport economists within the MoPWT and the General Directorate of Roads.

Legislation in Infrastructure

The Ministry of Public Works and Transportation acts according to the legislation of Albanian Republic. The completion with legal clauses about foreign investments in general and especially investments in public works and transport field are considered as very important. Law No.7764, Dt. 2/11/1993 "For foreign investments" foresees that each physical and juridical entity, native or foreign has the right to make investments in the territory of Albanian Republic.

The law No.7980 Dt.27/07/1995 "For the land sell" gives the possibility to foreign investors for the purchasing of land, after the physical compensation of owners is carried out. Its sell is done according to the prices set by MCD No. 312 Dt.30/06/1997, "For the prices of land and for the rent of land that is given to physical and juridical entity for use".

The law No.7973 Dt.26/07/1995 " For concessions and the participation of the private sector in public services and infrastructure " presents new forms of investment where each physical and juridical entity, native or foreign, is entitled to take in the form of concession a wealth, to carry out the specialised services for a long period of time.

Law No.7720 Dt.14/06/1996 " For the control and the discipline of building " is applied for all the physical and juridical entities, native or foreign that make design and implementation of construction works.

Law No 8093 Dt21/03/1996 " For water reserves" aims at the preservation, development, utilization as well as environmental protection and consumption of water reserves. Based on that, it has been approved Law No.8103 Dt.28/03/1996 " For the privatisation of the enterprises of water supply sector and removal of waste water ".

Law No.8102 Dt28/3/1996 " For the regulatory framework of water supply sector and the removal of waste water " aims to guarantee and protect the public interest on one hand and to establish a legal fair framework on the other one.

Through the Law No.7848 Dt.25/04/1996 " For the expropriation of public interest, and also for the temporary use of real estate ", the state is entitled to expropriate or to take in temporary use only for public interest, the real estate and accept the rights of the subjects affected by expropriation.

Through the Law 8094 Dt 21 /03/ 1996 " For the waste disposal " it is aimed at the protection of urban environment , according to yellow lines under each municipality, and at regulation of public services for waste management.

Industrial Policy

Privatization

Private sector activity has expanded rapidly since 1990. Following the privatisation of wholesale and retail enterprises, the initial growth was in enterprises supplying the domestic market for goods and services. Over 58,000 small and medium-scale enterprises (SMEs) were established between 1994 and 1997. Foreign investment began to play an increasingly significant role, involving mainly Italian investors in the Durres, Tirane, Vlore corridor and Greek investors in the areas around Korce and Gjirokaster. Most of this investment was in relatively small-scale joint venture enterprises.

The fall in industrial output was halted in 1995, even though many old plants continued to close, and output increased in real terms by 14% in 1996. Most of this increase was attributable to investment in new SMEs, although implementation of the mass privatisation programme for medium and large scale enterprises, which was initiated in 1995, also played a role. A substantial number of export-oriented SMEs were established, particularly in the garment and shoe industries. These employed an estimated 130,000 workers by the end of 1996. The impact of economic recovery was also apparent in the construction industry where output increased by 18% in real terms between 1995 and 1996. Significant investment had begun to take place in the tourism industry, initially in the construction and rehabilitation of hotels in Tirane, but also extending the development of coastal resort complexes. Output in former strategic industries such as copper, chromium and metallurgy which had remained under state control continued to decline and enterprises in these sectors remained unprofitable.

Status of Programme Implementation

Privatisation

With the privatisation of small and medium-scale enterprises largely completed by 1995, the emphasis of the privatisation process switched to a voucher-based mass privatisation programme covering the remaining medium-scale and strategically important enterprises. However, the process became increasingly politicised, lacked transparency and was not linked to any wider strategy with clear economic and social objectives. The retention of state majority shareholdings meant that many enterprises effectively remained under state control. Excessively fragmented shareholdings, the absence of a securities exchange on which shares could be traded and the lack of adequate information campaigns served to undermine the potential economic benefits from privatisation. By mid 1997 only 16% of privatisation vouchers had been utilised and some 53% of state owned enterprises included in the mass privatisation programme had been privatised, representing around 20% of the total assets of the economy. The unsatisfactory initial outcome of the mass privatisation programme led the Government, during the second half of 1997, to reformulate its strategy for privatisation.

Legal and Regulatory Framework

Basic legislation necessary for the development of a private enterprise economy was in place by the end of 1995¹. However, weak enforcement of the legal and regulatory framework has continued to hamper the development of the private sector. Particular problems have been: (i) difficulties in securing legal redress in cases of contractual default; (ii) the lack of effective procedures for claiming collateral in the event of loan default; (iii) lack of respect of land titles and land ownership disputes caused by the restitution process; (iv) the absence of a central registry of companies and the ease with which falsified company documents can be obtained; and (v) the tolerance of illegal business practices, especially evasion of customs duties and taxes, which have placed compliant businesses at a competitive disadvantage.

Credit for Enterprise Investment

In the absence of financial intermediation, a number of PIP projects have provided credit lines for private sector investment which have been handled by the three state-owned banks. The most important of these credit lines have been for SME development, agri-processing enterprises and tourism enterprises. However, their impact has generally been limited and undermined by the unwillingness of beneficiaries to repay their loans and the absence of an operational framework for enforcing repayment. There has also been minimal impact on the participating financial institutions, two of which are now to be liquidated. It also appears that implementation of the credit lines was adversely affected by the bureaucratic culture associated with public sector managed projects.

Against this experience, some international financial institutions have recently sought a more direct involvement by providing credit directly to the private sector. The most important of these initiatives are the USAID supported Albanian American Enterprise Fund and the KfW financed FEFAD. The EBRD is also in the process of establishing an SME credit line to be channelled through the privately-owned Italo-Albanian and Tirane Banks, and, with co-financing from Italy, is also setting up an Equity Fund to provide risk capital to enterprises recovering from 1997 crisis. Initial indications are that supervision of these directly funded interventions is more effective and less bureaucratic than where credit lines are financed through the PIP.

Community-Based Micro-Credit Programmes

A highly successful community-based micro-credit programme has been established by the ADF since 1992. The ADF is an autonomous institution with the aim of addressing poverty and unemployment through the provision of micro-credits and financing of small-scale public works projects. It has received support from a number of donors. The programme has been characterised by careful and sensitive design, effective arrangements and high quality management. As a result implementation performance has been impressive. At the end of 1997 the ADF had financed: (i) rural micro-credits in around 200 villages with lending of US\$ 2.5 million in loans of up to US\$ 1,000; and (ii) urban micro-enterprise credits with over 900 loans

¹ Including: (i) a liberal foreign exchange law; (ii) the civil code; (iii) legislation covering contracts, securities, mortgages etc.; and (iv) legislation on rights of land ownership and land use.

issued in amounts up to US\$ 2,500. Loan delinquency rates on the credit sub-programmes have been very low and are currently around 3% of the loan portfolio.

Investor and Business Advisory Services

PIP financing has been used to support the establishment of investor and business advisory services. The most important initiatives have been the establishment of the SME Foundation (SMEF) and Regional Business Agencies (RBAs) which have received assistance from PHARE and from USAID. The SMEF was intended as a national coordinating unit for SME support activities and credit lines. It also oversaw the establishment of seven RBAs² covering the 37 districts of the country. The RBAs provide advice to local entrepreneurs and assistance with the preparation of business plans. Financing to support foreign investment promotion activities, through the Albanian Centre for Foreign Investment Promotion (ACFIP) has been provided by UNDP. Proposed PHARE assistance for a Trade Information Centre was not taken up as a decision could not be reached on the establishment of the Centre.

6.3.9 The impact of these initiatives has been less than expected. The RBA network has worked with around 500 clients each year, preparing some 200 business plans with the approval of 59 business loans in 1996. A number of problems have been encountered with the implementation of the programme. These have included the absence of a clear mandate for the SMEF, insufficient attention to policy and marketing issues and the limited professional capacities within the RBAs. To some extent these problems reflect the inherent difficulties of publicly funded organisations in providing advice and assistance to private sector businesses.

Sector Policy Framework

Government policy aims at providing the conditions for the development of a competitive and internationally integrated enterprise sector. The main elements of the strategies to achieve this objective are:

- privatisation of the remaining state-owned enterprises including the progressive privatisation of enterprises in the strategic sectors of telecommunications, energy, transport, mining and public utilities;
- the establishment of an enabling policy, legal and regulatory framework and a secure and stable environment in which the private sector can flourish;
- the promotion of foreign direct investment and of efficient financial intermediation in order to make available investment resources to the private sector;
- the promotion of business information and advisory services, particularly to serve the SME sub-sector; and
- investment in infrastructure necessary for the development of a modern private enterprise-based economy.

In implementing these strategies the main focus will be on policy measures rather than on direct interventions involving substantial

² Located in Tirane, Shkoder, Kruje, Elbasan, Vlore, Korce and Gjirokaster.

commitments of public investment resources. Measures will be taken to ensure effective coordination between government ministries and departments which have direct dealings with the private enterprise sector.

Privatisation of Strategic Sectors

In early 1998, the Government introduced its new privatisation strategy for strategically important sectors. Recognising that the vast majority of these enterprises continue to operate unprofitably and represent a net drain on the State budget, the Government will pursue a more active and transparent programme for privatisation with the objectives of: (i) increasing economic efficiency; (ii) promoting competition; (iii) attracting foreign direct investment; and (iv) establishing the basis for a capital market.

Three main methods of privatisation will be pursued involving: (i) the transfer of shares to a strategic investor able to bring management skills and capital to the company, with limits set for the proportion of shares to be exchanged for privatisation vouchers; (ii) the issuing of management contracts and operating concessions, such as for power and water utilities, with the state retaining ownership of the enterprise; and (iii) the award of concessions to private investors to exploit natural resources such as oil, gas, minerals, and hydropower resources. Where privatisation involves the transfer of some element of monopoly powers, it will be linked to the establishment of regulatory bodies³.

The Business Environment

The most critical requirement for the 1998-2001 period is to provide a more certain environment for private enterprise and to restore the confidence of businessmen and investors following the 1997 disturbances. The measures, outlined in Chapter 9, to strengthen security, ensure fairness in the operation of the tax and customs collection systems, improve the legislative and regulatory framework, strengthen the judicial system and improve standards of public administration will play a key role in establishing such a framework. Further initiatives will be taken to bring Albanian trade, investment and business legislation in line with accepted international norms and thereby enable Albania to move towards accession to the WTO and other international and regional bodies.

Promotion of Business Investment

A priority for the 1998-2001 period will be the implementation of measures to restore foreign investor confidence in Albania. These will include:

- The establishment of a credit instrument to cover the costs of repairs to business property damaged during the crisis and the restarting of business activities. This will involve the provision concessional financing to be extended in conjunction with commercial bank loans.
- The establishment of a political risk guarantee scheme for foreign investors for which IDA financing has been sought.

³ The privatisation programme in the telecommunications, power and water sectors is considered further in the relevant sectoral strategies in Chapter 7.

Experience from previous initiatives supported under the PIP suggests that the financing of credit for enterprise investment is most appropriately provided directly through private sector banks. The Government will therefore give greater emphasis to encouraging the international financial institutions (IFIs) to become directly involved in supporting investment lending to enterprises, rather than to seek funding under the PIP for credit lines. However, some further financing for SME credit lines is expected to be required linked to the implementation of the new strategy for SME development (see para 0).

The activities of ACFIP will be reviewed and a programme for further support developed. Emphasis will be given to encouraging foreign investment in natural resources based industries, particularly in the energy sector, which will be facilitated by the Government's privatisation programme. With the support of the IFIs, the Government will also encourage private sector investment in business parks and the development of serviced industrial sites as a means of reducing the cost and risks of setting up businesses in Albania. Future initiatives to promote investment in the tourism sector will be linked to the restoration of stability and the scope for Albania to market itself as a potential tourist destination. The privatisation of existing state tourism enterprises will be pursued.

SME Development

A review of the SME support programme and the role of the SMEF and RBAs will be undertaken during 1998 and will lead to a new strategy for SME development. The aim will be to provide a more comprehensive and inclusive framework for SME policy development involving the strengthening of inter-ministerial cooperation and greater involvement of SME representative groups. The legal status of the SMEF and RBAs will be reviewed with the aim of transforming them into independent bodies and increasing the impact of their activities. A strategy for supporting the training of entrepreneurs and the provision of business-related services (legal services, accountancy etc.) will be developed, and the possibilities for providing financial support for training initiatives investigated.

Community Micro-Credit Schemes

The experiences under the ADF have shown that community-based credit schemes can play an important role in supporting the development of farm enterprises and micro-businesses. During the 1998-2001 period, it is planned to initiate the development of savings and loan cooperatives as a means of channelling increased resources for investment in such enterprises. Initial support will be provided through the ADF in establishing savings and credit societies in those districts where economic conditions are considered sufficiently favourable. Building on this experience, the creation of a cooperative credit system will become an integral part of the Government's strategy for financial sector reform

Priorities for Privatisation

- The end of 2003 will complete in the energy sector, the restructuring of the Albanian Electro-energetic Corporate (KESH) with the aim of privatisation.
- Start of the privatisation of the Local Hydropower Plants (under 2 Meg Watts), by beginning with the bidding.
- **In the oil and gas sector** will continue the preparatory procedures for the privatisation of Albpetrol”Sh.a. and “Armo”Sh.a supported by the assistance of the international adviser IMI. The preparatory procedures for the privatisation of the “Servcom”Sh.a and the other companies created after its restructuring will continue.
- In the international Airport of Rinas the services of Albtransport Join Stock Company should be transformed through a concession agreement on BOOT basis after the restructuring phase. This process is going to be concluded by the end of 2002.
- The phase of the liberalizing the services market for the “General Directorate of Railway” state company will continue during 2003.
- The Water Supply Join Stock Companies of the cities Kavaja, Berat, Kuçove, Durrës, Lezhe, Fier Sarandë will sign the management contracts with private companies by end of 2002.
- **In the Telecommunications** sector the Government aims to complete the privatisation of Albtelecom during 2003.

Trade and investment system

FOREIGN INVESTMENT PROTECTION AND AGREEMENTS TO AVOID DOUBLE TAXATION

The foreigners, either juridical or physical persons, enjoy the right of exercising different economic activities in Republic of Albania and invest their capital in different sectors of the Albanian economy.

They are allowed to exercise economic activity and carry out investments in Albania generally enjoying no less favorable conditions than those recognized to local subjects. except the right of ownership on land.

The most important law, which in really provide a number of basic guarantees and protections for foreign investors is Law No. 7764, dated November 2, 1994 “On Foreign investments”.

According to this Law, all the foreigners either physical or juridical persons, who intend to invest in Albania have no need to demand for permission or authorization, they shall not be expropriated or nationalized or be subject to

any other measure equivalent with these. The foreign investor enjoys the right to transfer out of the Republic of Albania all funds in currency and any article related to his investment.

The investor enjoys juridical protection of his rights related to an investment made in Albania. Such a protection is guaranteed both for a dispute that arises between a foreign investor and the Albanian party.

It is up to the parties to define the procedures for the resolution of the dispute that implies the Arbitration Clause and in the event of failure of such provision, the foreign investors enjoy the right to submit the matter to an Albanian court or to an Arbitration Court in Tirana.

In the event of a dispute involving discrimination, transfers of assets, or indirect expropriation of a foreign investment by the Albanian Government, the investor may submit the dispute to the International Center for the Settlement of Investment Disputes ("ICSID"). Special protection is guaranteed to foreign investments in Albania and to foreign investors from the states with which the Republic of Albania has signed agreements concerning avoidance of double taxation and mutual guarantee of investments.

To provide security and protection against losses arising from political risks, thereby providing confidence to potential exporters and investors in Albania, the International Development Association (the World Bank) has approved a credit of USD 10 million to the Albanian Government under its Private Sector Recovery Project to support a Political Risks Guarantee Facility, to be administered by the Albanian Guarantee Agency (AGA), a statutory corporation owned by the Government of Albania.

It is a Program to give guarantees to private sector entities that have financial exposure in Albania for a productive purpose. The guarantee covers a range of political risks, including the risk of civil disturbance of the kind experienced in March of 1997.

BANKING SYSTEM

To facilitate the transition to a market economy the Albanian banking system underwent major changes from the year 1992. The bank system was transformed according to Law 7559, dated 22.04.1992 "On the Bank of Albania" and Law 7560 dated 28.04.1992 from a centrally planned system to a two tiered system. The reviewed legislation of 1996 and 1997 further developed banking sector. Actually, the structure and functioning of the banking system is regulated by the Law 8269 dated 23.12.1997 "On the Bank of Albania" and the Law 8365 dated 2.07.1998.

The main principle is that banks should operate on a fully commercial base whether they deal with private or public sector. According to this new system the commercial banks and other financial institutions can provide a whole range of services under the supervision of the Bank of Albania which operates as an independent legal entity bound directly to the Albanian Parliament, and is responsible for the formulation and implementation of the monetary and foreign exchange policy in Albania.

The primary objective of the Bank of Albania is to achieve and maintain price stability in the country. In order to reach this objective the Bank of

Albania is empowered to foster monetary and credit conditions beneficial to the economic development of the country. It license, supervise, and regulate the activities of banks and financial institutions, hold and manage the official foreign exchange reserves of Republic of Albania, emit the domestic currency in the Republic of Albania, distribute securities for the account of the state and issue securities for its own account.

The Supervisory Council of the Bank of Albania is responsible for approving the monetary and foreign exchange policy of the Bank of Albania, determining the interest rates for deposits and extensions of credits, and setting the types and levels of reserves the commercial banks are required to maintain with the Bank of Albania.

To promote private commercial banking sector development. the Bank of Albania has adopted a liberal policy regarding the licensing of private commercial banks-and this sector will see significant growth in the future.

Commercial banks may be established as joint stock companies according to Law 7638 on Commercial Companies, and they may be founded exclusively with Albanian capital, foreign capital, or with common capital. These banks have the right to hold all kinds of deposits, borrow funds and extend credit lines, provide banking and consulting services etc. Any person wishing to act in the business of banking must obtain a license from the Bank of Albania. Banks licensed under foreign law can open subsidiary, branch, agency, or other banking offices in Albania. The license to operate as a bank in Albania is unlimited in duration and is not transferable. Subsequent requests to expand or change the bank's network in Albania must be approved by the Bank of Albania.

The principal credit lines in Albania are as follows:

The National Commercial Bank, FEFAD (Foundation for Enterprise Finance and Development), Savings Bank, International Finance Corporation (IFC-Member of World bank Group), Albanian Development Fund, Italian Albanian Bank,

Albanian American Enterprise Fund, International Commercial Bank-Malaysian Bank, Tirana Bank, Alpha Credit Bank,

National Bank of Greece and Arab Albanian Islamic Bank will have their credit lines in Albania.

Investment Funds

Law no. 7979, dated 26.7.1995, regulates the establishment and operation of Investment Funds.

Investment Funds are joint stock companies involved in investment, reinvestment, hold or exchange of privatisation vouchers. The minimum capital requirement is the equivalent in lek of USD 20 000. Foreign entities and companies whose capital is partly owned by foreigners may subscribe no more than 50% of the basic capital of the Fund. The Fund is managed by a licensed administrator in accordance with the management contract. The administrator must be a subject not employed in the investment fund. The investment fund must appoint a licensed depositor to accomplish depositor's duties as well as a certified public account. Normally the organisation of an Investment fund follows the rules found in the company Law for joint stock

companies. except for some specific rules and regulation as specified in the Investment Law.

TAXATION SYSTEM

During the transition from a central to a market economy, Albania has developed new tax laws. These laws have been developed with the assistance of the International Monetary Fund, the European Union, the United States Treasury Department, and others; and Albania is continuing to revise its tax legislation to accommodate it to the needs of market economy. Therefore, the foreign investor should seek counsel in order to ascertain the relevant tax regime in force.

Albania has already signed international agreements on avoiding double taxation with numerous countries, like Croatia, Greece, Hungary, Italy, Malaysia, Poland, Turkey, Rumania, Czech Republic, Russian Federation.

The Albania taxation system includes:

- profit tax
- income tax
- property tax
- value added tax
- excise tax

• Profit Tax

The profit tax applies to all legal entities performing commercial activity in Albania, whether domestic or foreign ones. This tax applies equally to companies with their seat in Albania and to branches of foreign companies.

All taxpayers pay profit tax at the rate of 30% of the profit resulting by the end of fiscal year the balance is set of. If after the balance is set of, there is a loss, than the loss is carried forward to the following tax period. Tax losses can be carried over into next year for a period up to three years. However, for entities generating profits through tourism activities, the rate is 40% and for profits generated from oil and gas exploration, the rate is 50%.

Profit tax is paid in advance during the course of the year, based on the business results stated in business books and financial reports.

Tax credits of up to 60% may be available when a company reinvests its profit in the production sector. In addition, if a company does business in the production sector in Albania for at least ten years, profit earned during the first four years of activity is exempt from profits tax. If the company ceases its activity prior to the expiration of the ten year period, it becomes liable for the full amount of the taxes ex-empted.

Companies that act in the tourism sector enjoy a five-year tax exclusion on profits as well as certain customs and excise tax benefits.

• Income tax

Taxpayes liable to pay income tax are Albanian and foreigner, physical persons realising profit in the Republic of Albania. Foreigners are liable for personal income tax if they have an income in Albania and spend a period of more than 183 days in Albanian territory.

The minimum wage and remuneration taxable is 10000 Lek/month. The maximum level of personal tax is 20%. Other kind of incomes are taxed at 10%. Exception is for creative work which is taxed at the level of 5%.

- **Property Tax**

There is a tax on agricultural land and buildings imposed by Law 7805 on Property Tax Revenues Tax on agriculture land which varies depending on the quality and dimensions of the agricultural activity.

The tax on buildings is paid by the owners of the buildings. It varies from 3 to 6 lek/m² per year for living houses depending on whether the house is single building, buildings in co-ownership or in the countryside. For buildings for manufacturing activities or service activities including trade activity, the tax rate varies from 50 to 100 lek/m² per year.

- **Value added tax**

On July 1, 1996, Albania implemented a value-added tax (VAT), Law 7928 on value-added Tax provides for a VAT at a rate of 20% (October 1, 1997). Currently, there are very few exemptions (e.g, financial services), although exports are zero rated. Businesses are required to register for this tax if their annual turnover exceeds 5 million lek (1 January 1998).

VAT taxpayers are required to issue receipts (according to the model approved by the General Directorate of Taxation at the Ministry of Finance). Also, they are required to keep detailed books documenting the VAT paid on purchases and charged on sales. At the end of each month, VAT taxpayers must total the amount of VAT paid and charged and submit this information on a VAT declaration. To the extent VAT is due, the proper payment must accompany this declaration.

A VAT taxpayer may request refund of VAT paid if two conditions are met. First, the taxpayer must have carried forward a VAT tax credit for six consecutive months; and second, the total refund claimed must exceed 400,00 lek.

- **Excise tax**

Actually, law 7678 on Excise Duties imposes an excise tax on certain items, including tobacco, alcohol, petroleum products, leather, soft drinks, and water. This excise tax is levied on all individuals and legal entities. The excise duty is only paid once by importers or producers of goods and not on subsequent transfers.

In the actual Albanian legislation, there is a discrimination between the imported products such as tobacco, cigars, cigarettes, alcoholic drinks, soft and fresh drinks, electrical energy, derivatives of petroleum and coffee. For these products there is a difference in excise between domestic and imported products.

The Government has prepared a new law on excise. In this law there will be some excise system for both products that are produced in the country and those imported.

INSURANCE SYSTEM

Law 7506, dated 31.7.1991 "On the Insurance Institute" and law nr 8081, dated 7.3.1996 "On insurance and reinsurance activity" established the modern insurance system in Albania.

Private insurance companies can be established. Foreign insurance companies can exercise their activity in Albania only through their branch in Albania, upon the condition that the mother company must have at least a ten years activity in the field.

Participation of foreign capitals in Albanian insurance companies can not exceed 40% of the capital and voting rights.

The required capital for insurance and reinsurance jointstock companies, excluding the contributions in kind, must be no less than 30 million lek.

The license for insurance and reinsurance companies is granted by the Supervisory Commission of Insurance.

The Insurance Institute (INSIG) is for the moment the only insurance entity exercising insurance activity in the territory of Albania. It is a state owned entity and has branches in 28 districts of Albania.

INSIG offers the following services:

- insurance of property against fire and other risks, such as explosion, lightning, earthquake,
- insurance against any kind of tempest, snow, avalanche etc.
- insurance of economic units from burglary
- CAR, EAR and machinery insurance
- cash in transit insurance
- contractor's all risk insurance
- business interruption insurance,
- agriculture insurance
- insurance of livestock
- insurance of liabilities toward third parties
- KASKO insurance
- Green Card
- marine hull
- insurance from personal accidents
- credit life insurance
- traveller's health insurance
- insurance of passengers
- credit insuran
- reinsurance and coinsurance activity and co-operation with well known interantional reinsurance companies.

FINANCIAL SECTOR

Albania is trying to develop a diversified modern financial system. The operators in the Albanian financial system can be classified as follows:

The central issuing bank, commercial banks including saving bank, stock market, investment funds, insurance and reinsurance companies and credit associations (cooperatives)

Banks

Law nr. 7559, dated 22.4.1992 " On the Bank of Albania" and Law nr. 7560, dated 28.4.1992 transformed bank system from a centrally planned, single tier system, to a Western two tier system with the Bank of Albania as the central bank and second level or commercial banks. Law nr 8076, dated 22.2.1996 and law nr. 8075 dated 22.2.1996 further developed the banking sector. The activities of the Bank of Albania have paralleled those of central banks in other market economies. The main principle behind the legislation is that banks should operate on a fully commercial base whether they deal with public or private sector.

Bank establishment

Joint banks or totally private banks with Albanian or foreign capital can be established. The licence to establish and operate a bank is obtained upon written application at the Bank of Albania. In accordance with a form issued by the Bank of Albania, a list of documents must be presented together with the request for getting a license. Actually in Albania there are three state-owned commercial banks, two joint banks with participation of foreign capitals, three foreign private banks and the branch of the National Bank of Greece. Other foreign banks or branches of foreign banks have got the license and are in the process of establishment. There are programs for the privatisation of second level state-owned banks.

Credit policy

Substantially all Albanian banks provide a full range of services and operations for their clients and operate in accordance with the private-sector banking practices. The majority of commercial banks generally lend their funds preferably to private persons although they can also finance major public works. The most common credits are of short and medium terms. Indications on credit and deposit interest rates of some commercial banks (as per second quarter 1996

Stock market

Tirana stock exchange was established on May 1996 and is a relatively new institution. For the moment governmental bonds, treasury bills with 12 month maturity and privatisation vouchers are traded. A National Stock Exchange Commission controls the activity of the stock exchange and co-operates in the development of its regulations. Indication on security rates, as per July 1996.

Insurance

Law 7506, dated 31.7.1991 " On the Insurance Institute" and law nr 8081, dated 7.3.96 "On insurance and reinsurance activity" established the modern insurance system in Albania. Private insurance companies can be established. Foreign insurance companies can exercise their activity in Albania only through their branch in Albania, upon the condition that the mother company must have at least a ten years activity in the field. Participation of foreign capitals in Albanian insurance companies can not exceed 40% of the capital and voting rights. The required capital for insurance and reinsurance joint stock companies, excluding the contributions in kind, must be no less than 30 million lek. The license for insurance and reinsurance companies is granted by the Supervisory

Commission of Insurance.

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INSIG offers the following services :

- insurance of property against fire and other risks, such as explosion, lightning, earthquake,
- insurance against any kind of tempest, snow, avalanche etc.
- insurance of economic units from burglary
- CAR, EAR and machinery insurance
- cash in transit insurance
- contractor's all risk insurance
- business interruption insurance
- agriculture insurance
- insurance of livestock
- insurance of liabilities toward third parties
- KASKO insurance
- Green Card
- marine hull
- insurance from personal accidents
- credit life insurance
- traveler's health insurance
- insurance of passengers
- credit insurance
- reinsurance and coinsurance activity and cooperation with well known international - reinsurance companies

Investment Funds

Law nr. 7979, dated 26.7.1995 regulates the establishment and operation of Investment Funds. Investment Funds are jointstock companies involved in investment, reinvestment, hold or exchange of privatization vouchers. The minimum capital requirement is the equivalent in lek of USD 20 000. Foreign entities and companies whose capital is partly owned by foreigners may subscribe no more than 50% of the basic capital of the Fund. The Fund is managed by a licensed administrator in accordance with the management contract. The administrator must be a subject not employed in the investment fund. The investment fund must appoint a licensed depositor to accomplish depositor's duties as well as a certified public account. Normally the organization of an Investment Fund follows the rules found in the company Law for jointstock companies, except for some specific rules and regulation as specified in the Investment Law.

TAX SYSTEM

There are two level of taxation in Albania:

- at national level
- at regional level (municipality level)

Taxes at national level are by far the most important one, while those at municipality level are mostly related with hotels, restaurants, advertising, cleaning and ambulatory trade.

National tax system in Albania can be classified as follows:

Direct taxes:

- a) On income:
 - corporate income tax (tax on profit)
 - personal income tax

- b) On assets:
 - tax on buildings
 - tax on agriculture land

Both these taxes are marginal and normally doesn't play any important role

Indirect taxes:

- value added tax
- excise tax
- custom duties on imports

Legal acts

The main legal acts that determine the Albanian tax system are the followings:

- Law nr. 7681, dated 4.3.1993 "On the administration of taxes and fees in the Republic of Albania"
- Law nr. 7677, dated 3.3.1993 " On the tax on profit"
- Law nr. 7678, dated 3.3.1993 " On excise tax"
- Law nr. 7679, dated 3.3.1993 " On small business tax"
- Law nr. 7928, dated 27.4.1995 " On value added tax" and their amendments. There are a number of circulators issued by the Ministry of Finance on the implementation of the legal acts concerning the tax system.

Corporate income tax (Tax on profit)

This tax applies to all legal persons, Albanian or foreigner, that exercise economic activity in territory of Albania and for that reason are considered as resident in Albania for tax purposes. This applies equally to companies with their seat in Albania and to branches of foreign companies. A tax on profit of 30% is level on profits made by resident companies in Albania, irrespective of their legal form. Normally the tax on profit is prepaid each quarter and by the end of the year the balance is set off. For companies that exercise economic activity in tourism, this tax is 40%. Companies that exercise economic activity in oil and gas exploitation pay an average of about 50a/o tax on profits depending on the quantity produced.

Taxable income is determined according to the Law No.7671, dated 19.1.1993 "On the Accounting" and is in line with standard western business practices.

Personal income tax

This tax is a progressive one. Foreigners are considered as residents in Albania and liable for personal income tax if they have an income in Albania and spend a period of more than 183 days in the country. The minimum wage and remuneration taxable is 10000 lek/month. The maximum level of personal tax is 20%. Other kind of income are taxed at 10%. Exemptionally the creative work is taxed at the level of 5%.

Tax on assets.

The tax on buildings is paid by the owners of the buildings. It varies from 3 to 6 lek/m² year for living houses depending on whether the house is single building, buildings in co-ownership or in the country side. For buildings for manufacturing activities or service activities including trade activity, the tax rate varies from 50 to 100 lek/m² year.

Tax on agriculture land varies depending on the quality of agriculture land from 1500 to 6000 lek/ha year.

Value added tax

The value added tax entered in force in July 1, 1996 and substituted the turnover tax that was applied up to that moment. The basic purpose of VAT law was to adapt the Albanian legislation to EU VAT directives and regulations. The value added tax is levied on all legal and natural persons that performs goods or services supply. supply and is calculated based on the total sum paid for the goods or services. The tax rate is 20%. (Law 8240 dates 16.9.1997) For exports and international services the tax rates in 0%. Following the EU model certain transaction are VAT exempt e.g. services and supplies of goods related to financial activities, transaction related to shares, stocks, bonds and other securities, transactions related to bank accounts, transfers, cheques, transaction related to life insurance policy, management of pension funds, rental of residential property etc. Also goods supplied under the temporary importation regime for job processing activities, are VAT exempt. VAT must be paid within the first 14 days of the next month.

Excise tax

Excise tax is applied on limited number of goods such as tobacco, cigars, cigarettes, alcoholic drinks, soft and fresh drinks, electrical energy, derivatives of petroleum and coffee. This tax is applied only for goods produced in Albania or imported. For goods produced in Albania the excise tax is calculated on the bases of the value of each lot of goods sold and for imported goods it is calculated on the bases of the custom value. Excise tax is not applied on above mentioned goods when they are exported. Excise tax for tobacco and tobacco products is 50% to 70% when produced in Albania and 100% to 105% when imported. Alcoholic drinks have an excise tax of 40% to 105% when produced in Albania and an additional of 25% when imported. For derivatives of petroleum the excise tax is in the range of 25% to 85% and for some special derivatives up to 300%. Normally the excise tax stimulates the domestic production of goods rather than import of goods

Custom duties

The "Harmonized Goods Classification System" have been in force in Albania since 1992. The main body of legal acts concerning customs is

comprised by: Law nr. 7599, dated 2.9.1992 " On Custom Code" Law nr. 7609, dated 22.9.1992 " On Custom Duties", and a series of amendments updating it as well as a number of Council of Ministers Decisions and Circulators of the Ministry of Finance . According to the Custom Code, the management, organization and the control of the custom activity in Albania is realized by the General Directory of the Customs. Normally the custom value includes the price of the good, and transport and insurance expenses. There are four levels of custom duties for imported goods: 5 %,10 % 30 % and 40% Some indications about custom tariffs are provided on the annexes of this guide.

Tax on small business

This tax is applied on individuals exercising private economic activities. It includes learned professions as well as small scale individual ambulatory trade activity. It is calculated on the bases of the total revenues and varies from 2% to about 10% depending on the type of activity.

Investment incentives in Albania

In order to respond to investment expectations and the need to promote growth, a system of incentives is implemented in Albania. These incentives apply equally to foreign investors and Albanian investors. The most important incentives are the followings:

There is a four years tax holiday for all companies that exercise for at least 10 years economic activity in manufacturing or production sector.

There is a 60% reimbursement on tax on profit for re-invested profits in production sector.

There is a five years tax holiday for companies that exercise "promoted activity" in a tourism development zones, in accordance with the Law No. '7665, dated 21.1.1993 "On priority tourism development zone".

There is a package of tax incentives for companies operating in a free zones or entering a concession contract

There is no limit on debt/equity ratio

Losses can be carried on for three consecutive years in addition to the year the loss occurred.

Albania does not levy a withholding tax on outgoing dividends.

To help investors in recovering losses due to the damages of the recent political and social unrest, a law was adapted by March, 1997 on the Temporary exemption from custom duties and VAT on importation of machineries, equipments and necessary materials for their assembly, which are imported for investments on manufacturing, construction and services in telecommunication, banking as well as in water supply and electric energy. The law will have effects till December 31,1997.

Accounting

The regulations governing the accounting records to be kept by businesses in Albania are contained in the Accounting Law, (law nr. 7661, dated 19.1.1993) in force since 1993. According to this Law, all the enterprises must keep orderly accounts, appropriate to their activity, without prejudice to the requirements of special laws or regulations.

Bookkeeping practices vary, from companies which have their accounts computerized and bind the computer sheets in sequential order to form their obligatory accountings records, to companies that keep their official records by hand. In the later case, entries are often posted monthly summarizing the transactions of the month, one month being the maximum period permitted for transactions to be grouped together for recording purposes. Accounting entries must be posted in Albanian currency, lek. The accounting principles which aim to ensure that a company's annual financial statements are clear and present a true and fair view of its financial position, are much in line with those used in EU countries:

- Prudence
- Going-concern
- Recording
- Cost bases
- Accrual bases
- Matching the revenues and expenses
- Consistency
- Materiality

Principles of calculation include among others the followings: Fixed assets and circulating assets are estimated according to the consignment or production cost. Depreciation schedules are determined by the Ministry of Finance. Intangibles are depreciated within a five years period, unless it is otherwise determined in the General Accounting Plan or in the absence of such a determination, a different schedule of depreciation is approved by the Ministry of Finance. A general assembly can only distribute a dividend after having approved the financial statements and having taken note of the existence of distributable earnings. Distributable earnings are defined as net earnings of the financial year minus prior losses and allocation; the legal reserve or a reserve made mandatory by the articles, increased by any earnings carried over. The minimum balance for the legal reserve can not be distributed.

Annual financial statements include the balance sheet, profit and loss account and an annex with the disclosure requirements. The presentation of cash flow statement is not obligatory. Normally the financial year correspond to the calendar year. Normally the annual financial statements must be audited before presenting them to the tax offices. Auditing is not obligatory for companies that do not exceed two of the three following indices:

- a balance of 6 million of lek at the end of the respective year
- 12 million lek in total revenues
- an average of 10 employees during the financial year

The majority of the companies must present their financial statements in the relevant tax office within March 31 of the next year.

LABOR LAW

The basic legislation is the Labor Code approved by the Parliament in 12.7.1995. Other important acts related with labor are: law nr.7995, dated 20.9.1995 " On the promotion of employment", law nr 7939, dated 25.5.1995 "On migration", law nr. 7986, dated 13.9.1995 " On state inspectoriate for labor' and a number of Council of Minister's Decisions.

Labor contracts are normally bargained at two levels: at factory level for the so called collective labor contract and at individual level for the so called individual labor contract.

The collective contract contains dispositions concerning the employment conditions, individual labor contracts, professional education as well as mutual obligations of the contracting parties. The parties in a collective contract are one or more employers on one side and one or more trade union on the other side. The collective contract is settled at enterprise level or branch level as the parties agree.

The written labor contract must include in particular:

- identity of the parties
- place of the work
- general description of the work
- the initial date of the work
- duration if the contract is a contract with a fixed duration
- duration of the paid vacancies
- the time period of notification for contract resolution
- the constitutive elements of the wage and the date of payment
- the normal duration of the working hours of the week
- the labor contract must include also the collective contract in force

The labor contract can be settfed:

- without a fixed duration
- with a fixed duration

The first three months of the work are considered as test period. During the test period each party can withdraw from the contract by notifying the other party at least five days before.

The working hours

Daily working hours are fixed in the collective labor contract or individual labor contract. The normal working time in a day is 8 hours. This can be longer or shorter only within the limits of the maximal weekly working time. Employees under 18 years old have a daily working time of no more than 6 hours.

Night shift begins at 22 o'clock and ends at 6 o'clock in the morning.

For any working hour from 19 o'clock up to 22 o'clock the additional hour wage shall be no less than 20 %.

For any working hour from 22 o'clock up to 6 o'clock in the morning the additional hour wage shall be no less than 50 %.

The maximal weekly working time is 48 hours.

The weekly unpayable holiday is 36 hours and normally includes Sunday.

For the work done during a holiday the additional payment is at least 25 % or it will be compensated with another holiday.

The maximum additional working hours are fixed in collective labor contract or individual labor contract. The employee can not be asked for additional working hours if he has worked 50 hours during that week. The additional working hours are compensated either by holidays or by an additional payment of at least 25 % more than the normal rate.

Annual vacation

The duration of paid annual vacation shall be fixed in the collective labor contract or individual labor contract. It can not be less than 3 weeks. Special protection for underage and women are foreseen by the labor legislation. These are mainly related with night shifts, heavy weights, special working conditions during pregnancy etc.

Wages

The wage can not be less than the minimum wage fixed by the decision of the Council of Ministers.

The employer pays regularly the employees every two weeks if the wage is calculated based on hours, days or weeks worked or by the end of each month if it is calculated on monthly base.

The employer deducts from the payroll of employees the individual income tax and social insurance payments.

Procedure for dismissal

For the period after the test period, if the employer wants to dismiss the employee, he must inform him in a written form at least 72 hours before discussing the problem with him. The employer presents his reasons for the dismissal. The decision can be taken only 48 hours after the discussion with the employee. It must be in a written form. This procedure is not applied in case of massive dismissal. A dismissal is qualified as a massive dismissal when the number of employees dismissed within 90 days is at least 20, independently from the total number of the employees in the enterprise. In such a case the employer must discuss first with the trade union that represent the employees or in the absence of such trade union with the employees.

The duration of consultation must be at least 20 days. The employer must inform in a written form the competent authorities for any massive dismissal. A copy of the project of massive dismissal must be sent to the Ministry of Labor. The Ministry of Labor helps the parties to achieve an agreement but does not have the right to forbid a massive dismissal.

Social security system.

All employers, their employees, self-employed persons, civil servants etc. must be registered with and pay contributions to the Albanian social security system. Under this system, social security contributions are paid partly by the employer and partly by the employee. There is a minimum and

a maximum wage used for the calculation of social security calculations, which are ordinarily revised from time to time. Employees whose total compensation or wage exceeds the maximum base, pay their social security contribution according to this base. For 1996 the minimum wage and the maximum one were respectively 4100 lek/month and 12300 lek/month.

FDI IN ALBANIA

Albania may not be the first country that sprang to mind when you decide to invest abroad, but there are good reasons why it should be top of your list. Albania offers:

- Strong commitment of the government to a market economy, supported by stable social climate and friendly, liberal legislation.
- Rapid GDP growth rate.
- Wide and quick privatization and widespread of private property
- Availability of skilled labor coupled with low labor costs
- Market proximity and rich natural resources including tourism

Basic legal principles of foreign investment in Albania

Foreign investment in Albania can be classified in the following categories:

- direct investment, including green field investment-participation in Albanian companies
- portfolio investment
- other forms of investment as specified in the Foreign Investment law.

The rationale behind the legal principles of foreign investments is the fundamental truth that open regimes with respect to foreign investment and trade are necessary for enhancing international competitiveness and integration into the global economy. Albania has adopted the national treatment clause, that is foreign investments are treated on a bases no less favorable that that accorded in like situations to Albanian investments. This principle is bases on the general premise that equal treatment of investors in similar circumstances and free competition among them are prerequisite of a positive investment environment. Foreign investments in the Republic of Albania are not conditioned by any preliminary authorization.

Albania offers in ali cases and at all times a fair and equitable treatments to foreign investments. They enjoy full protection and security in accordance with the basic principles of International Economic law. The foreign investor has a wide variety of options to be considered when decides to make an investment in Albania. Practically Albanian legislation provides room for all internationally accepted forms of FDI.

It should be stressed that practically all kind of assets can be freely transferred outside Albania subject to the payment of taxes and the satisfaction of claims and adjudicatory judgments. No withholding tax is applied on such transfers.

A liberal attitude is adopted by Albania also in matters concerning expropriation, discrimination, compensation and transfer of money; Albania consents to the submission of the dispute for resolution to the International Center for Settlement of Investment Disputes to be treated in accordance with the Convention on the Settlement of Investment Disputes between States and Nationals of Other States.

SUMMARY OF ALBANIAN COMPANY LAW

The law no. 7638, dated 19.11.1992 “On commercial companies” established the legal bases of any Albanian company. The main principles are organized around two axes, the company as a contract among its associates and the company as a legal entity distinct from its owners.

There are four forms of companies according to Albanian company law.: PARTNERSHIPS, LIMITED PARTNERSHIPS, LIMITED LIABILITY COMPANIES and JOINTSTOCK COMPANIES.

The Legal Foundation of any Albanian company rests on its articles of association and by-laws (the articles). In general the articles may be in notaries form or simply signed by the associates as a private document. The form, name ,duration, company designation, principal place of business, purpose and amount of capital must be indicated in the articles. Additional items are required of a limited liability company or a joint stock company.

A company generally can be created when two or more persons associate and agree to create a company. However according to the Albanian company law, limited liability companies or joint stock companies can exist also as one - man company.

Each associate must make a capital contribution. Capital contributions can take a number of forms: cash, in kind contribution or use of property. The essential condition for a capital contribution is that it must have an ascertainable value. The capital contribution by an individual of his technical knowledge or services for an interest in the company is rarely permitted in any company form since service can not be subject to a forced sale to satisfy the company’s creditors.

PARTNERSHIPS In Albanian company law, the general partnership is considered an entity (i.e. with legal personality) distinct from its partners, who themselves may be individuals or legal entities. All partners in a general partnership are considered merchants and are jointly and severally liable for company debts. The minimum number of partners is two. No minimum capital is required. Interests in a partnership can not be represented by negotiable share certificates. No securities can be issued by the partnership.

THE LIMITED PARTNERSHIP has two classes of partners, general partners and limited partners. The general partners are deemed merchants and have unlimited personal liability. The limited partners are only liable for debts to the extent of their interest in the company’s capital.

LIMITED LIABILITY COMPANY The associates are not considered merchants as such. They are liable for the company's debts only to the extent of their interest in the company's capital. There is no limit on the maximum number of associates. A limited liability company is managed by one or more managers.

THE MINIMUM CAPITAL required for the establishment of a limited liability company is 100 000 lek (roughly the equivalent of about USD 1000 calculated at the rate of exchange of January 1993).

The capital is divided into interest - shares of equal nominal value. The minimum nominal value is set at 1000 lek. Cash or any property, real or personal, tangible or intangible, can be contributed to a limited liability company's capital, either its use or total ownership. No contribution in service is permitted.

ALL THE CAPITAL must be subscribed to and paid up before organization of the company and the articles must state that the capital is all paid in. Interest - shares in a limited liability company are not freely negotiable and cannot be represented by share certificates. Nothing prohibits certain interest - shares from having a larger or priority share on the profits.

THE LIMITED LIABILITY COMPANY is administered by one or more managers. The identity of the first original managers must be mentioned in the articles filed for registration. In the absence of a contrary close in the articles, a manager has the power to perform any managerial act in the company's interest.

ANY decision that amends the articles is considered "extraordinary" and requires a greater majority than "ordinary" decisions.

Extraordinary decisions must be approved by at least three quarters of the capital. This is also applied in case of decrease or increase of the capital or transfer of an interest - share to a non - associate. Subject to the transformation being nullifiable, all the associates must agree to the operation of transforming a limited liability company to a partnership.

A limited liability company's management's generally is supervised by the Assembly. Two other management supervisory mechanism exist: the self - dealing procedure and the rules requiring use of an official auditor.

JOINTSTOCK COMPANIES The Albanian jointstock company is deemed commercial by form. The Albanian company law makes a distinction between jointstock companies that have offered their shares for sale to the public and those that have not. A jointstock company is deemed to make a public offering of its securities when they are listed in the stock exchange, are sold through banks, brokers or other types of financial institutions or their sale is publicized in any other form. Normally it is quite rare for a jointstock company to make a public offering while it is being organized. This way no public offering is made during incorporation and the formalities are simpler.

MINIMUM CAPITAL required for a public jointstock company is 10.000.000 lek (the equivalent of about USD 100 000 calculated at the rate of exchange of January 1993), for a private jointstock company the minimum capital required is 2 000 000 lek (the equivalent of about USD 20 000 calculated at

the rate of exchange of January 1993). The par value of the shares can be freely fixed in the articles.

DURING organization of a jointstock company, all authorized shares must be subscribed, but only one fourth of par value need be paid in immediately and the remaining portion must be paid up within five years of company's registration. Normally, a privately - held jointstock company will not use subscription bulletins. Shareholders must share in earnings but not necessarily in proportion to their rights to capital. Their share in losses is limited to their share in jointstock company's capital, however.

MANAGEMENT The management form comprises a directorate, which manages the jointstock company and a supervisory board that controls the directorate. Members of the directorate need not be shareholders, but they must be physical persons. The supervisory board must have no less than three members and no more than twenty one. One third of the members of supervisory board must be from employees.

THERE ARE two types of general shareholder's meetings, termed ordinary and extraordinary. The extraordinary Assembly decides with the approval of three - fourth of the voting shares present or represented. The ordinary Assembly decides with the majority of shares presented or represented.

THE NUMBER of votes per share must be proportional to the proportion of the capital it represent.

Fraction of shares are not taken into account.

SHAREHOLDERS are accorded a preferential right to subscribe to new shares resulting from cash increase in capital pro rata to their current interests in the company. The company's capital must be completely paid up before new shares may be authorized to compensate cash contribution by shareholders.

SHARES A jointstock company can issue different types of shares: ordinary, preferred shares, voting or non - voting shares, registered or bearer shares. A jointstock company is not allowed to purchase its own shares, except to cancel them and thus reduce its capital when not motivated by losses.

Institution to promote foreign investment

ALBANIAN ECONOMIC DEVELOPMENT AGENCY

AEDA was founded in August, 1998 with the initiative of the Albanian Government, in the context of implementation of new policies to increase investments and exports, as well as in the context of reformation of public institutions. It plays the role of an operational branch which actively helps fulfilment of programs of the government.

AEDA's legal responsibility as joint stock company offers an operational and flexible activity like all other private companies, while by being a state company 100%, it has all the necessary facilities and authority to surpass bureaucracy hinders in protecting businessmen in Albania.

The main aim of AEDA is to incite economic development in the country, and in accordance with this, it has chosen well developed forms, backed by a well-prepared staff of professionals and a wide network of outside authoritative experts in the field of economy, finance, business, legislation and others.

In order to organise and reconstruct in Albania the bases of industry, agriculture and services, in the context of the market economy, which will enable Albania's integration in the global markets, it is necessary to develop a quick exchange of qualitative, serious and professional information.

AEDA is engaged with its Information Department to gather, process and deliver all standard information taken by state or private bodies as well as every other kind of information of economic value collected during implementation of different projects, from monitoring or specific study by every other serious and credible source.

Materials published by this agency include a daily newspaper, electronic newspaper in the Internet, publishing in the different sectors or enterprise profiles. The newspaper is specialised in economy, which will give information to businessmen in a simple journalist like way, the economic and juridical possibilities in setting up a business, it will publicly offer the strategy and the ways of privatisation, economic policy of the government, operational data of the economic development in Albania, of public and local economy and be helpful with information on currency exchange rate and markets of goods, on customs and fiscal regime, as well as on financial instruments and programs.

Creation of a favourable environment for investments in Republic of Albania, which will result in opening of new jobs, is the main aim of the Promotion Department activity, which will be able to offer suggestions and recommendations to the government in improvement of its legislation and procedures in process of development of economy in general and of specific sectors.

The Promotion Department's most important job is promotion of investments from Albanians and foreigners, promotion of exports and commercial exchange, promotion of the privatisation program for state owned sectors of economy, study of potential possibilities of different branches of economy to attract private capital. It will also realise complete and professional services towards local and foreign investors by offering them information, specialised consultancy, a study of the market and study on the credibility of a business, etc.

AEDA develops its specialised activity according the formula "one stop", in service of private and public subject of international organisation or the NGOs. It co-operates with its counterpart organisations and institutions. AEDA's engagement in projects, contracts, conferences, seminars, fairs, round tables and other activities with foreign international financing bodies, with donors, as well as private subject enables realisation of a wide program, in favour of economic development of Albania.

Albanian SME-s and foreign businessmen, public and private institutions, international organisations and every subject interested in Albanian market and economy will profit by realisation of AEDA-s programs.

Programs of international bodies, its publishing activity, specialised and professional consultation, specific studies, different advertisement and

logistics services, will make up the financial mechanisms which will secure the activity of the Agency and will create possibilities of fund accumulation for promotion of new initiatives.