

# NEWSLETTER

## KOSOVO



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## Reform proposals for a better business climate

**The business climate in Kosovo has improved continuously in recent years. This is reflected in a current survey of Kosovar and German investors, which shows that many companies plan to increase their investments in the country. However, the study also highlights areas that are in need of reform including further improving VAT refund procedures, making it easier to install solar panels, advancing data protection reforms, facilitating cross-border freight transportation and modernising education. The government has already taken important reform steps to address these issues. It is now crucial to keep up the momentum by fully implementing the reforms that have been initiated.**

### Introduction

Over the past decade, Kosovo's economy has grown significantly, with high growth rates of up to 10.5% in 2021. The country's growth model has been largely based on remittances to finance domestic consumption but has recently started to shift towards more investment and export-driven growth. In order to boost investment, it is crucial that companies have a positive perception of the business climate in general and the regulatory environment in particular.

A recent survey of Kosovar and German investors conducted by the German Economic Team, conducted in cooperation with the German-Kosovar Business Association (KDWV) and REX Consulting, revealed that the business climate is generally assessed positively. The majority of the companies surveyed are optimistic about their business' future and plan to expand their investments in Kosovo.

However, the study also identified areas that, from the business community's point of view, require urgent reform. Further research revealed that the government has already recognized these problems and has taken important reform steps. Judging from the results of the survey, however, these reforms have not yet had their full effect on businesses. The following sections highlight recent reform achievements and briefly outlines the next recommended steps.

### Increasing the effectiveness of VAT refund

The Tax Administration of Kosovo has implemented various measures to improve tax-related processes for businesses including the introduction of electronic filing

of tax declarations to reduce the time and administrative burden. The system includes a "refund management" tool to inform companies about the status of their VAT refund requests. The Tax Administration has also begun to process VAT refund requests using a risk-based approach, so that companies whose tax records have a low risk of error receive fewer audits and faster refunds. Data from January to November 2022 show that tax refund procedures have improved. Taxpayers classified as low risk wait an average of 15 days to receive their refund, while taxpayers with a high-risk classification wait an average of 38 days.

These reforms are a big step forward compared to the previous situation, but there is still room for further improvement. First, the time between VAT declaration and refund should be shortened even further. This would help businesses as less liquidity would be withdrawn from them.

Second, to encourage the development of small and medium-sized enterprises (SMEs), a cash flow-based VAT scheme should be considered. This would help SMEs which are particularly vulnerable to financial constraints and have inferior access to finance.

### Facilitating the installation of solar panels

The Ministry of Economy has drafted a new energy strategy for 2022-2031 with the goal of diversifying the generation mix by investing in renewable sources and reducing lignite-based generation. The Office of the Energy Regulator is currently working on a new feed-in regulation for so-called prosumers that includes raising the capacity limit for each solar installation. The new prosumer regulation would help businesses in Kosovo, as many of them are willing to invest in solar panels but need predictable long-term feed-in tariffs to make sound investment decisions.

Likewise important for investors is the standardisation of municipal permits for solar panels. The standardisation reform process is on hold but needs to be resumed quickly.

### Accelerating data protection reforms

Kosovo already adopted a law on personal data protection in 2016, in line with the EU's General Data Protection Regulation (GDPR). This modern data protection regulation is especially helpful for companies in the IT- and business process outsourcing sector, but only if potential outsourcing customers from the EU can rely on the effective enforcement of data protection in Kosovo.

However, the agency responsible for enforcing the law, the Information and Privacy Agency (IPA), had been inactive for nearly three years after its establishment and only recently became operational.

It is now important to catch up on the time lost and take swift action to ensure the proper implementation of data protection standards. Recommended measures include providing accurate information to citizens and businesses on data protection rights, improving private sector accountability as well as increased guidance from the IPA including through guidelines for data processing and model documents to facilitate businesses' implementation of data protection laws.

### Facilitating cross-border freight traffic

Up to now, cross-border car transportation has been difficult and cost-intensive for Kosovar companies. Kosovar exporters and importers have always had to rely on expensive foreign freight forwarding companies, as Kosovo has not yet succeeded in joining international agreements regulating the transport of goods and their insurance. The most important of these international agreements is the so-called Green Card membership. In a joint effort, several Kosovar government agencies have achieved the fulfilment of all technical requirements for Green Card membership. Recently, the Kosovar Insurance Bureau has announced that Green Card membership is expected soon.

This will support businesses as it will reduce costs, especially for SMEs exporting smaller quantities of goods to or importing from EU countries, as they would have the option of transporting small consignments with their own truck or van.

### Tackling long-term mammoth tasks

The study also reveals some fundamental problems for the business climate in Kosovo. Above all, there is a discrepancy between the education system and the qualifications required by companies. This leads to two effects that reinforce each other. Firstly, businesses are constrained in their growth because they cannot find enough or adequately qualified employees. Secondly, talented young people leave Kosovo because they cannot acquire the qualifications that are in demand on the domestic labour market. While there have been some small attempts at reform, particularly in the area of IT education, the problem remains large. Serious fundamental reforms are needed to bring the education system in line with the needs of the economy. Such reforms will have their impact on economic development only in the long term. Although quick successes are not to be expected here, tackling these reforms is crucial.

Other long-term reform challenges include addressing the lack of industrial sites with basic infrastructure and the unreliable energy supply.

### Communicating reform achievements

Reforms in the areas described have begun and some are already well advanced. Now it is important to keep up the momentum and fully implement the reforms, including the recommended measures. In contrast, slowing down these reforms, risks discouraging investment. In addition, it is crucial that policymakers effectively share information about improvements in the business environment. The aforementioned survey revealed a number of discrepancies between the status of legislative reforms and the level of information among companies. Therefore, policymakers in Kosovo should inform companies more effectively about reform plans and their progress, even if companies already consider investment conditions to be favourable. This will further improve the business climate by providing companies with an even more comprehensive picture of the positive outlook in Kosovo.

This newsletter is based on the Policy Study [“Improving the Business Climate – Boosting Investment. Proposals from German Business in Kosovo”](#).

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*\*Advisory activities in Belarus are currently suspended.*

#### Editor

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