Creating a Favorable Business Environment: Case Study on Firm Registration Process in Uzbekistan

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Abstract: The development of national economy in many respects depends on conditions such as freedom and guarantees, privileges and preferences so that entrepreneurial activities prosper within a better entrepreneurial environment. While the development extent of entrepreneurial environment is defined by several indexes, the processes and documentation as a part of state registration of entrepreneurial activity have a special value among them. In this article, in consideration of exemplary entrepreneurial environment practices in different developed countries, the successes and shortcomings of Uzbek experience and some important theoretical rules on the creation of such favorable and friendly entrepreneurship conditions are discussed. We find that in order to increase the share of small business and entrepreneurship there is a need to systematically improve the mechanisms of state regulation of organization and registration processes of business entities. A system of incentives should be introduced in the registration process such as optimization of its time, increasing the number of business entities.

Key words: Entrepreneurship, Business Environment, Firm Registration Process, State Registration Bodies, Uzbekistan

1. Introduction

After the fall of the Soviet Union, Uzbekistan has entered a period of transition from socialist to market economy. Features and influences of the old socialist system still manifest itself in the current status of entrepreneurship, the attitudes of society toward entrepreneurship and the way economy is currently functioning (Smallbone and Welter, 2011). This is especially evident in the existence of “informal economy” characterized by non-registered entrepreneurial activity which occurs without the link to formal economic

and political structures (Rasanayagam, 2011). Non-registered businesses operations are taking place not only to avoid taxation, but also as a result of certain hindrances that occur in the process of establishing new business and company registration. However, in recent years, we can see the process of continuous economic liberalization in many emerging economies (Yiu et al. 2007). Uzbekistan authorities have also recognized entrepreneurship and small business formation as a significant driver of the economic development.

The world practice demonstrates that governments play a crucial role in the course of attracting small business and private entrepreneurship into modern production process (Yiu et al. 2007). Its functions include taking initiative of developing better conditions for businesses, preventing them from possible obstacles and encouraging fair competition as well as creating favorable entrepreneurial environment for the advancement of modern and technology-based manufacture. Among many problems hindering small business development in the country, complexity of firm registration process possesses considerable weight. To many potential entrepreneurs, the process of firm registration appears to be an unsurmountable obstacle. Complex rules and regulations, duration and expenses occurred when registering a company as well as insufficient understanding of the steps to be undertaken discourage potential entrepreneurs to start a new business venture. Making the firm registration process more straightforward, creating conditions which enables a quick and simple business start-up formation is one way to minimize the activity of informal economy. Therefore, a need for detailed discussion on the firm registration process and influencing factors should be conducted.

In the current study, we explore Uzbekistan business environment, more particularly, the rules and regulations for opening small and medium business with an objective of evaluating whether current rules and regulations impede or promote entrepreneurial activity. To begin with, a wider context of firm registration is examined and a comparison is drawn between Uzbekistan and other developing countries. Next a detailed case analysis is performed by examining the current status of entrepreneurship and the firm registration process. Finally we offer recommendations for making the registration process more effective.

2. Business environment in emerging economies

There is a strong positive relationship between role of SMEs and innovation, and through innovations, economic growth (Audretsch, 2004). There are many evidences in the literature which state the fact that small firms surpass large ones in job creation and innovation (Acs, 1992). Effective functioning of business, though, is impossible without an appropriate enabling environment (Shaikhutdinova, 2011). Favorable business environment in a country, in turn, drives the creation of new firms (Klapper et al, 2004). Prior studies have acknowledged favorable business environment and government support influence on businesses (Vorozhbit et. al., 2010; Shayhutdinova, 2011; Shikunova et. al., 2010; Filippov, 2011). A favorable business environment involves such socio-economic conditions that ensure independence of the entrepreneur, minimize the risk of business activities, give legal guarantees of responsibility and provide motivation for entrepreneur's work on the commercial success and social responsibility (Tsy-pin, 2007). The

report by Committee on Economic Cooperation and Integration notes that “Encouragement of innovation is particularly important in business. To let innovations prosper, though, business environment should be conducive to investment in research and development; not, to burden of over-regulation” (ECE, 2008).

Unstable hostile nature of the external environment and the scarcity of key resources, particularly capital, are characteristic to many developing countries. For example, Albania entrepreneurs state that they face unfair competition, changes in taxation procedures, lack of financial resources and problems related to public order (Bitzenis et al. 2003). In some countries, bureaucracy and corruption are also prevalent. In emerging economies, social business and political ties have a strong positive effect on organizational performance as well. Political ties lead to greater performance when general government support is weak and technological turbulence is low (Sheng et al., 2011). An environment that lacks stable structure relies mostly on informal networks to enable entrepreneurs to operate and expand their business, access resources, and surpass the bureaucratic barriers (Smallbone and Welter, 2001). It is a clear fact that bureaucratic entry regulations are neither welfare-improving nor benign (Klapper et al., 2004). Our study identifies a current state and specific alignments of Uzbekistan business environment. Given the political and economic history of Uzbekistan, the creation of environment which is conducive to business may present a challenge.

3. Methodology

In order to provide a detailed analysis of Uzbekistan business environment and registration process we applied a case study method. Secondary data from governmental documents as well as data from various organizations were used to provide a clear insight. We evaluated current status of Uzbekistan in terms of ease of doing business and entrepreneurship by accessing World Bank data. Process of state registration of enterprises in Uzbekistan with formation of legal entity was analyzed from the data extracted from Uzbekistan government agencies and their publicly available online and archival documents. Role of State Registration Bodies in establishment of registration periods of entrepreneurial units was assessed through observation and analysis of internal documents.

4. Case Study Analysis

4.1 Current state of ease of doing business and state registration processes of small businesses in Uzbekistan

When it comes to ease of doing business in Uzbekistan, positive changes are apparent. An increase of 8 spots has moved Uzbekistan to 141th place in the world in 2015, thus, continuing a positive trend of improvement in its status among world economies. The highest position in “ease of starting a business” scale was achieved in 2014 making Uzbekistan 65th out of 189 countries. However, in comparison to 2014, the ranking has dropped by 6 points in 2015.

REGION	Europe & Central Asia	DOING BUSINESS 2015 RANK	DOING BUSINESS 2014 RANK***	CHANGE IN RANK
INCOME CATEGORY	Lower middle income	141	149	↑ 8
POPULATION	30,241,100			
GNI PER CAPITA (US\$)	1,900	DOING BUSINESS 2015 DTF** (% POINTS)	DOING BUSINESS 2014 DTF** (% POINTS)	CHANGE IN DTF** (% POINTS)
CITY COVERED	Tashkent	54.26	50.02	↑ 4.24

Rankings	Distance to Frontier		
TOPICS	DB 2015 Rank	DB 2014 Rank	Change in Rank
Starting a Business	65	60	↓ -5
Dealing with Construction Permits	149	147	↓ -2
Getting Electricity	145	148	↑ 3
Registering Property	143	146	↑ 3
Getting Credit	104	99	↓ -5
Protecting Minority Investors ✓	100	118	↑ 18
Paying Taxes	118	179	↑ 61
Trading Across Borders ✓	189	189	No change
Enforcing Contracts	28	29	↑ 1
Resolving Insolvency	77	72	↓ -5

✓=Doing Business reform making it easier to do business. X=Change making it more difficult to do business.
Click here to see all reforms made by Uzbekistan.

Indicator	Uzbekistan	Europe & Central Asia	OECD
Procedures (number)	7.0	5.0	4.8
Time (days)	7.5	12.1	9.2
Cost (% of income per capita)	3.3	5.3	3.4
Paid-in min. capital (% of income per capita)	0.0	5.8	8.8

No.	Procedure	Time to Complete	Associated Costs
1	Register the name of the company	Less than one day (online procedure)	no charge
2	Make a company seal	1 day	UZS 30,000 to 50,000
3	Register with the local authority (khokimiyat) and obtain the certificate of state registration	2 days	UZS 96,105 (equal to one minimum wage salary)
4	Open a permanent bank account with a local bank	1 day	no charge
5	Register with the Tax Authority	1 day	no charge
* 6	Register with the Statistics Agency	1 day (simultaneous with previous procedure)	no charge
* 7	Register with the National Bank (Xalq Bank)	1 day (simultaneous with procedure 5)	no charge

* Takes place simultaneously with another procedure.

Table 4-1 Ease of doing and starting business in Uzbekistan

Source: World Bank, 2015

With the aim of increasing the share of small business and private entrepreneurship in the economy, Uzbekistan is paying special attention to the regulations in this regard. The government is taking wide-ranging measures to create favorable entrepreneurial atmosphere including optimization of the time needed to have businesses registered in the country (Entrepreneurial environment in Uzbekistan in the opinion of representatives of small and private entrepreneurship, 2011).

To illustrate and compare, we can state that in the early years of independence of the country, it took fifteen days to get a business registered in the country (The Law of Republic of Uzbekistan, 2011) and by 2003, the time required to this was reduced to seven days (The decision of Cabinet of Ministers of Republic of Uzbekistan, 2003) while in 2006 the very process started taking only two business days (The Decision of the President of Republic of Uzbekistan, 2007).

In addition to reduction of registration time of entrepreneurial units, several key entrepreneurship-friendly changes in registration procedure have been implemented. For example, in the early years, an entrepreneur had to address all registering bodies (Inspection of Entrepreneurial Units Registration, Tax Department, Statistics Department, Pension Fund, Road Fund, Employment Fund, etc.) personally and had to be listed on their registration books. However, as of September 2006, the notification procedure of state registration of businesses was established. Now, the state registration of businesses is carried out by Inspections of State Registration of Entrepreneurial Units at authorized judicial authorities or city (regional) administration and businesses can be registered in tax and statistics authorities simultaneously. Thus, the time from the date of application for registration to the delivery of Certificate of State Registration of Entrepreneurial Unit has reduced to no more than two working days.

We will below discuss procedure required to register business before 2006. The State Regulation on "Notification Procedure of State Registration and Registration of Businesses" stipulated that overall process of the state registration and statement on the account involve eight stages for entrepreneurial units with the formation of legal entity and seven stages for individual businessmen and farm entities without formation of legal entity. We can consider processes of state registration and statement on the account of entrepreneurial units with formation of legal entity in the table below (table 4-1).

Stages	Subjects	Actions	Terms
1	The Founder, Commercial and Industrial Chamber, Consulting Firms or other persons	1. Prepare necessary documents for the state registration of entrepreneurial units 2. Develop projects of constituent documents	At the discretion of founders
2	The founder or legally authorized person by founders	1. Represents documents to registering body for the state registration of entrepreneurial unit.	At the discretion of founders
3	The responsible party of registering body	1. Considers the documents presented for the state registration of entrepreneurial unit	No more than 3 working hours
4	The responsible party of registering body	1. Sets statistical codes of business units concerning property, territorial location and so on. 2. Directs inquiry about assignment of identification number of taxpayer to District (City) Tax Bureau 3. Conducts the permission documentation for making of seal and stamp.	*
5	The responsible employee of the state tax service	1. Appropriates a taxpayer ID to the entrepreneurial unit through the centralized ID base in real time mode. 2. Inserts corresponding record in the centralized ID base. 3. Directs ID assignment to the responsible employee of registering body by means of electronic post or fax.	No more than 8 working hours
6	The responsible employee of registering body	1. Inserts the data about state registration of the entrepreneurial units in the state register. 2. Grants the certificate of the state registration and other documents.	No more than 2 working days from the date of reception of documents

7	The responsible employee of registering body	1. Provides data from the state register and other documents to corresponding state bodies.	Within a day from the date of carrying out state registration
8	Corresponding state bodies	1. Carry out registration of entrepreneurial unit, including as payers of insurance payments in for Pension Fund, Employment Fund and Road Fund (for the units who have to pay for corresponding funds). 2. Includes the entrepreneurial unit in State Register of Enterprises and Organization List. 3. Provides permission for making seal and stamp.	No more than 2 working days from the date of reception of documents

Table 4-1 *Processes of state registration of enterprises in Uzbekistan with formation of legal entity*

As we can see from the table above, in the process of registration of the entrepreneurial units, each procedure or action entails certain amount of time depending on the level of complexity and quantity of activities. For example, the allocated time for consideration of the documents presented to obtain the state registration by entrepreneurial units (stage 3) is no more than 3 working hours, while the required time for entering data on registration in the state register and presentations of other documents (stage 6) takes up to two working days.

4.3 Inconsistent relations of “The State Registration Bodies” in establishment of registration periods of entrepreneurial units

It is important to note that the establishment of registration time of businesses is carried out under the influence of various inconsistent relations. On one hand, for example, with the aim of creating and strengthening healthy competition in the economy by increasing the share of small businesses, augmenting the volume of GDP and tax revenues and maximizing the employment of domestic resources and opportunities, the government may cut the time needed for the registration of businesses through legal acts and documents regulating entrepreneurship activities. In certain cases, though, such reductions can surpass the extremes of optimum limit. Such cases entail rational reduction of physical time on a particular activity.

On the other hand, responsible bodies directly engaged in the registration of entrepreneurial units (for example, State Chamber of Registration, State Tax Departments, State Statistics Departments, etc.) want this period to be longer despite because of the fact that it is their responsibility to ensure that the registration of businesses is duly accomplished with maximum care and concentration.

There are some other reasons why Registration Bodies are in favor of longer time frame for registration of businesses:

- Excessive workload arising from baseless time frame (less than real physical time required to this end) for registration processes;
- Risk increase of poor handling due to excessively accelerated actions to accomplish registration on time;
- Undesirable increase of the time spent on performing certain activities caused by ever-increasing volume of information and data pertaining to the registration of entrepreneurial units;
- Application of certain punishments (disciplinary, administrative, financial, etc.) in the event of inevitable failures to have businesses registered timely;

5. Discussion and implications for Uzbekistan

5.1 Importance of optimization of state registration time of entrepreneurial units

It is well-known that the restriction of monopolistic activities, creation of healthy competitive environment and full employment of internal possibilities in the spheres of industries depends on the share of small businesses in national economy (Radas and Bozic, 2007). The increase of small enterprises, micro firms, individual and private entrepreneurship significantly influences the increase of their share in GDP as well as an increase of total income and employment rates of the people of the country (Filippova, 2011). Therefore, fostering the development of small-business entities should always be the main tasks of the government of the given country.

Governments take different measures and actions with varying directions and characters to increase the number of small businesses in the national economy. One of them is simplification of registration process of entrepreneurial units, in particular, reduction of the time required for the registration (Tsypin, 2007). However, the possibility of such a reduction is limited within the constraints of technological advancements in the country. Therefore, it is imperative that the time required for the registration of businesses be reasonable and acceptable. From the theoretical point of view, the reduction of registration time of entrepreneurial units has relative character and could be expressed in establishment of optimal term that consists of the sum of required time needed to have a business registered:

$$OM_p = \sum_{i=1}^n OB_i,$$

OM_p - optimal registration time;

OB - optimal time required for solving certain problems or actions during the registration;

i - types of problems and actions which should be solved during the registration of entrepreneurial units.

However, operation time required for registration of enterprises does not always correspond to optimal terms. Because of different factors, duration of registration time is subject to some certain changes under certain influences. Optimality of relationships - interactions of "state - business environment" is the most important factor and it reflects the objective needs of both public authorities and the interests of business. The mechanism of the relationship of state authorities and business structures should be open and able to adapt to the constantly changing conditions of the economic situation. In this case, the effectiveness of the relationship is directly dependent on how much power and business structures integrate joint action to achieve economic growth (Filippova, 2014). In our opinion, reduction of registration time can only be attained by granting various compensatory measures, such as provision of additional highly qualified employees, creation of favorable conditions designed to augment labor productivity in registration process (necessary number of computers and other technologies, data storage equipment and data processing machines, vehicles and other communication facilities, etc.). However, by the same token, liberalization process of the economy entails reduction of administrative jobs in the state bodies of authority, which contradicts our proposition of more personnel in state registration bodies.

The above-stated cases can be displayed in a following formula:

$$BM_d \leq OM_p \leq TM_{pu}$$

BM_d – registration time of entrepreneurial units established by the government;

TM_{pu} - registration time needed by registration bodies of entrepreneurial units.

So, optimal time is formed under the influence of two inconsistent factors and any further reduction of operating time may bring about various negative consequences. The details provided above suggest that drawing a rational balance of state vs. registration bodies of authority is not sufficient by itself. In our opinion, in order to simplify the registration process and to reduce registration time required, it is important that we approach this issue from the angle of stimulating the quantitative increase of businesses which entails due consideration of some theoretical aspects in this regard.

5.2 Improvement of state regulation of organization and registration processes of entrepreneurial units

The organization and state registration of businesses cover the period from the moment of inception of organizing entrepreneurial activity, learning possibilities and preparing necessary documentation and contacting corresponding registering bodies to obtaining state registration certificate, which constitutes general period of organization and registration process of entrepreneurial activity (figure 5-1).

Figure 5-1 Regulation stages of organization and registration processes of businesses

General period of state regulation (establishment of certain periods for different stages) can be divided into two groups: regulated and unregulated stages. The unregulated stage involves measures and actions which are carried out at the discretion of an entrepreneur or a founder. In this stage, there is no influence of the government regulations in terms of setting certain registration time for entrepreneurial units. In order to prevent entrepreneurial units from bureaucracy, conceit and other obstacles in the registration process, all the tasks are carried out by the corresponding state bodies within the time frames established by the government.

If we consider the conditions in Uzbekistan based on the terms stated above in Table 3, we can see that realization of the said procedures and actions in the first and the second stages of state registration and statement on the account are at the sole discretion of the founder and it is not limited to any time period. This stage involves attending to such important issues as preparing necessary documents for the state registration of entrepreneurial units, working out projects of constituent documents, submitting them to state registration bodies. In certain cases, this whole process may last several months, which takes its toll on the quantity of the entrepreneurs wishing to open their own businesses.

Hence, in our opinion, it seems that government regulation is also needed in the process of document preparation and collection including constituent documents (charter agreement, statute), bank receipt on payment of the established State Tax, Single Login and Password confirming the name of firm, sketches of seal and stamps, decision of District Mayor (Hokim) on land allocation for business and other authorization documents. Additionally, the government should consider regulating the time spent on accomplishing these documentary necessities and take actions to help start-ups to finish this process as quickly as possible. The most convenient way is the institution of the state control over quality of services provided by Commercial and Industrial Chamber and other various consulting firms. The realization of such measures expands borders of state regulation of small business organization and registration processes and leads to its perfection. The figure below describes this process even more clearly (figure 5-2).

Abbreviations:

УДЧ - general periodic border of organization and registration of entrepreneurial units;

ТСЧ - regulated border of registration process of entrepreneurial units;

ДБМ - registration time of entrepreneurial units established by the government;

ОМ - optimal registration time of entrepreneurial units;

АБМ - actual registration time of entrepreneurial units.

Figure 5-2: Improvement of state regulation of organization and registration processes of entrepreneurial units

In the above-given figure, we can see two processes of different character. The first is the expansion of borders of state regulation of registration of businesses and once we reach it, improvement of these processes will bring about considerable increase in the number of entrepreneurial units.

The second - the formation of optimal registration time for enterprise represents the sum of minimal time expenses required to accomplish necessary operations and actions during the period of registration process, which is characterized by extreme border of registration time reduced by the government (Shaikhutdinova, 2011). However, from the point of time, this border is also relative and may narrow owing to social and economic development, particularly, expansion of technical possibilities.

As mentioned above, the government tries to reduce the time needed for registration of businesses as far as practical with the aim of encouraging the organization of entrepreneurial units (Shikunova and Drobysheva, 2011). In certain cases, however, this reduction, as specified in the figure above, can surpass even optimal border, which in turn contradicts with the possibilities of registration bodies of authority. To this end, registering bodies tend to prolong operating time or to keep optimal time on the border of operating time (Loginov and Murashova, 2010).

6. Conclusion

In many ways, support for small business and entrepreneurship from the state is manifested in the creation of favorable conditions for business. Assessing the ease of doing business indicators, we can see that along with many others, ease of organizing business sub index plays an important role. The degree of favorable conditions for business in the country is determined mainly with the number of procedures for registration of business entities, the time required for accomplishing set procedures, as well as expenses associated with registration. Hence, there is a need for optimization of these parameters for further development of business. There are contradictions between the state and the registration authorities in determining the registration period of business entities. As excessive reduction or increase of the registration period can lead to negative trends in business development. Optimization should be done considering the consequence and based on a combination of these two alternatives. In order to increase the share of small business and entrepreneurship there is a need to systematically improve the mechanisms of state regulation of organization and registration processes of business entities. A system of incentives should be introduced in the registration process such as optimization of its time, increasing the number of business entities.

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