Changes in Business Environment to the Benefit of SMEs Development in Slovakia after the Year 2004

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Abstract: Development of small and medium enterprises is among the priorities of the economic development in Slovakia. The most important development factor is the establishment of a favourable business environment, requiring simplification and a more transparent legislation, reduction of administrative and tax burden, reduction of contribution to funds, strengthening of the supporting infrastructure, as well as an easier access to capital. In the article are presented the main changes in business environment in Slovakia after the year 2004 and are identified main areas of the business environment to be improved to the benefit of further SMEs development in our country.

Keywords: Small and medium enterprises, business environment in Slovakia, legislative framework, administrative framework, access to capital, development of small and medium enterprises

1 Development of the Business Environment in Slovakia after the Year 2004

Small and medium enterprises play a significant role in all market economies. Their development is among the priorities in our country. The development of the business environment to the benefit of SMEs in 2004 provided evidence for gradual improvement of legislation and administrative structures in the interest of the strengthening of the competitiveness of business entities, being a principal prerequisite for an improved performance of the economy of our country.

Seen from the aspect of changes in business environment, the year 2004 was even more important than the preceding ones. The accession to the European Union on 1 May 2004 represented a culmination of the integration process of several years. Although the adoption of changes in the legislative and regulatory frameworks
associated with the enlargement was spread over several years, the significant amount of the new legislation was the result of our EU accession.

The most significant factors influencing the business environment of Slovakia in 2004 included the implementation of the new tax system, implementation of more efficient administrative procedures which are required by business start up, change in the previous system of social security to become the system of social insurance, making communication with tax offices more efficient and adoption of legislation to make bankruptcy proceedings more flexible.

The new act No 595/2003 Coll. LL. on income tax effective as of 1 January 2004, introduced so-called flat-rate tax, i.e. a single linear rate of 19% to be applied to all types of income of both legal entities and natural persons, thus abolishing a wide scope of various exceptions. The Act introduced deductibles at 25% (or even 60% for a specified handicrafts). There is no more tax on dividends.

Discrimination against entrepreneurs – self-employed small trade licensees came to an end on 1 November, 2004. Pursuant to Act No 539/2004 Coll. LL., which amends and supplements Act No 595/2003 on income tax (adopted in October 2004), self employed small trade licensees may deduct certain expenses spent in connection with business trips from their tax base (pocket money, per diem). Where an own motor car is used for the transportation, the small trade licensees may now (similarly as other employees), deduct costs of fuels and replacement costs.

Act No 255/2003 which amends and supplements Act No 289/1995 Coll. LL. on value added tax, took effect on 1 August 2003, with some of its provisions, such as the flat rate of 19%, which replaced the reduced 14% and the standard 20% rates, taking effect in January 2004.

The new Act on added value tax effective as of 1 May 2004, was based on the need to access the single internal market of the European Union. After 1 May 2004, the application of VAT became extended to the whole territory of the Union, goods, persons and money enjoy now free movement between the countries. In specified cases, the function of the border customs offices between Union Member States was now assumed by tax payers. The most important modification of the Act has been the change of the turnover threshold for mandatory registration: it became reduced from Sk 750 000 per quarter to Sk 1,5 mil. per year. Pursuant to the new act, companies are liable to register in respect of the tax, although not as payers, if the acquire goods from other Member States of the Union as part of their business activities worth in excess of Sk 420 000 in a calendar year.

Additional extensive amendments to tax legislation were prepared during the year 2004. Act 582/2004 Coll. LL. on local taxes and local fees on municipal wastes and small construction wastes took effect on 1 January, 2005. The local fees were abolished since January 2005 (except for the fees on municipal wastes), or were
transformed into local taxes, eight in number. Towns and villages are now free to
determine their taxes, as they are not restricted by the state setting the upper limit.
This concerns all the three components of the property tax (land, buildings,
apartments).

Act No 461/2003 Coll. LL. on social insurance, which took effect on 1 January,
2004 changed the previous system of social security into the system of social
insurance and also changed the calculation base of the levies. The standard has
also introduced changes in health insurance and unemployment insurance. The
minimum calculation base was raised for self-employed persons, and the new
obligation of paying insurance premium to Reserve Fund was introduced. The
principal changes from the viewpoint of business included the amendment in
respect of the payments of sickness benefits by the Social Insurance Company
starting as late as on day 11 sickness leave. For the first ten days, the
compensation for income shall be paid by the employer pursuant to the separate
law.

Act 462/2003 Col. LL. on compensation for income during sickness leave and on
amendments and additions to some laws provided, effective January 2004, for the
obligation of the employer to pay the employees during the first ten days of their
sickness leave; the benefits amount to 25% and 55% of the daily calculation base
during the first three days and during days 4 – 10, respectively.

The purpose of the new Act No 530/2003 Coll. LL. on register of companies and
on amendments and additions to some law, which took effect on 1 February, 2004,
was to make the operations of the register of companies more efficient, and to
speed up the registration procedure. The Act left the keeping of the register of
companies to courts, it however changed the nature of the procedure, from civil
court procedure to registration procedure. It comprehensively regulated the list of
data which are entered into the register of companies. The introduction of
standardised forms has a pronounced effect on making the registration procedure
simple and shorter. The speeding up of the proceeding at the register of companies
was achieved thanks to the prescribed forms as well as the setting of a relatively
short period of 5 days for the entering of the record and the subsequent publishing
in Commercial Bulletin of the data. The shortening of the entering of records thus
eliminated one of the reasons for corruption.

Act No 411/2004 Coll. LL. which amends and supplements Act No 328/1991
Coll. on bankruptcy and settlement introduced a significant extensibility to the course
of bankruptcy proceedings as it enabled the meeting of creditors to make decisions
on matters under their powers not falling under the decision-making powers of
judges, even in the case where the plea of prejudice is applied against the judge.
The above mentioned Act on bankruptcy was rather intricate. Although having
been amended almost 20 times, some frequently critised problems could not be
resolved, such as the tediousness of the bankruptcy procedure, the poor position of
creditors or the unambiguous nature of the assessment of whether the
entrepreneur in question meets the bankruptcy procedure opening criteria. Consequently, Ministry of Justice of the Slovak Republic undertook in mid-2004 to draft an entirely new law Act No 7/2005 Col. LL. on bankruptcy and restructuring on amendments and additions to some laws, which took effect on 1 July, 2005.

Act No 353/2003 and 549/2003 Coll. LL. on Civil Court Procedure and on judicial officers (taking effect on 1 January 2004) were enacted in the effort to making court proceedings more efficient and to eliminate unreasonable delays. The strengthening of the position of judicial officers is expected to speed up court proceedings.

The majority of the above changes in the legislation made a contribution towards further improvements of the business environment. Two documents were drawn up in respect of the economic strategy, determining the medium-term and long-term direction of Slovakia’s economy.

Slovakia’s Convergence Programme for 2004-2010 sets the medium-term and long-term goals of economic policy. The major objective of the economic policy is to achieve a high and sustainable growth of the economy and thus a more rapid improvement of the standard of live in Slovakia. Also, Development Strategy of Slovakia’s Competitiveness through 2010 was developed. The major objective of the Strategy is to make Slovakia catch up with the standard of live of the most developed EU Member States. This goal can only be achieved through a rapid and long-term economic growth. In a market economy, this goal may only be supported by creating favourable conditions for a growth of the economic competitiveness of the country. The development section of the Strategy has focused on four areas considered as the most significant ones from this aspect. All the four areas make up a single whole, with each of them being of the same importance: 1. Information society, 2. Science, research and innovations, 3. Business environment, and 4. Education and employment.

Regarding access to funds, the conditions improved due to the developments in the financial market (drop of interest rates, high liquidity), a more widespread utilisation of the right to pledge and the pointed competition in the banking sector. The application of the right to pledge under the new regulation adopted in 2003 and the utilisation of the register of such rights on the Internet reinforced the opportunities of small and medium enterprises to acquire financing through a simplification of the registration procedure of pledges, and through enabling securitisation of loans by chattels or other property values.

After the year 2004, the orientation of banks towards the financing of the small enterprises segment slowly turned from verbal into real action: several new loan products were introduced to the market. The products were of the micro-loan nature and the banks extend them under simplified administrative procedures, thus reducing the time needed for the assessment of application and the costs connected with the acquisition of a loan. In assessing applications for loans, the banks place
increasingly more emphasis on guarantees than on the quality of the business plan. The main problems concerning a better access to loans for small enterprises however remain the shortage of adequate securities whose requirements exceed the resources. Ranking first among the problems is the acquisition of the seed capital. Loans in the SME segment bear higher interest rates, and this represents an increased financial burden to be borne by the enterprises. This situation could improve in the future by the utilisation of the recently launched loan register of natural persons, provided that it will collect also information on natural persons – entrepreneurs.

In addition to the above mentioned aspects, the following problems were considered by organisations associating enterprises and by professional organisations to be the major barriers:

- unreasonably high taxes and fees imposed by towns and villages,
- unreasonably high fees for services of bank institutions which keep increasing,
- the prevailing bureaucracy of officers at any level, the long dealing times, obligation to produce certificates and documents providing evidence for facts which can be derived from official register, obligation to present numerous statistical reports,
- still the long time of court proceedings, thus reducing the change to enforce justified claims from creditors, even in the case of a favourable award,
- the pure legislative standard of some newly enacted laws, which is then reflected in the need of frequent amendments,
- intricate and poorly transparent system of project assistance from structural funds.

It can be stated, that the business environment in Slovakia gets gradually improved, with an acceleration after the year 2004. The quality of business environment is principally influenced by such factors as political stability, stability of the economy and its growth, the standard of the legislation and the real law enforcement. From the aspects of these factors, there is still strong criticism on the part of the business entities concerning the quality of the business environment, although a positive shift in this respect has been achieved.
2 Recommendations for Further Improvement of the Business Environment

Favourable business environment is the basic prerequisite for long-term competitiveness and growth of any market economy. It is in such an environment in which the state promotes and protects private property and competition: it creates clear-cut and stable rules for them, secures their compliance by all market stakeholders and, at the same time, minimizes administrative barriers and requirements on entrepreneurs.

The business environment in our country markedly improved in several aspects, mainly due to the application of reform measures during the recent five years: this concerns establishment of new companies, labour market legislation, up to the bankruptcy and settlement process. As the result, there are no more serious barriers to business in Slovakia today.

In the interest of further improvement of the business environment quality and to establish conditions for a long-term sustainable growth of Slovakia’s economy it is recommended in respect of legislative and administrative frameworks to focus on the following aspects:

- a mandatory system of impact analysis on the business sector should be introduced as part of the drafting procedure of legislative standards, to assess probable costs; this will result in a better quality of legislative drafts,
- the institution of the short-cut approval procedure at the National Council of the Slovak Republik should only be used occasionally, thus securing a good quality of the drafting and assessing of draft laws. The draft laws presented should be simple and easy to understand. The laws should be adopted in a comprehensive manner and if one law is amended, subsequent effects on other relevant laws should be addressed,
- elimination of unreasonable delays, aiming at improving the quality and the performance of the judicial system,
- to improve law enforcement by expedient amendment to the Rules of Civil Court Procedure, including the setting the period within which the competent court is obliged to act in the matter,
- to amend the Act on Local Taxes and Local Fees, so as to prevent, by its application, uncontrolled increase of the financial burden on SMEs by municipalities,
- to establish one-stop-shopping system, a site where starting business people may handle all necessary procedures,
- the principal prerequisite for full electronisation of information exchange on businesses between the different public institutions should be created,
• the system of electronic procurement should be implemented to gradually replace the conventional system of public procurement of goods by public service,
• corruption should be aggressively fought,
• the system of payments to funds should be simplified,
• companies not meeting the equity criterion as provided for by law, companies with negative equity and companies unable to meet their financial liabilities should be excluded from business by enacting relevant legal standards.

Conclusions
The existence of a stimulating business environment represents the basis for a successful development of the small and medium enterprises sector. The improvement of the business environment in recent years has gradually projected into positive characteristics of the SMEs sector. An in-depth analysis of the SME sector status allows to identify prevailing trends and to respond to changes needed to secure a desirable situation. In the article were presented the main positive changes in the business environment in Slovakia after the year 2004 and were identified the main areas of the business environment to be improved to the benefit of further SMEs development in our country.

References