



LOCAL ECONOMIC DEVELOPMENT IN KOSOVA

**Research Report
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SUMMARY

Local Economic Development in Kosova

Objective

This Research Report (“Report”) addresses the current problems related to the management of Local Economic Development (LED) in Kosova.

The Report recommends the possible ways:

- to expand the role of local government in the promotion of economic development;
- to re-direct LED’s efforts to develop a market economy and to create public-private partnerships that will encourage active stakeholder participation.

The Report is written with the understanding that the participation of stakeholders is critical to LED in its development in strategy and policies, as well as for implementation.

Organization of Kosova local government

- In August 2000, UNMIK published Regulation 2000/45, entitled “Municipal Self-Government in Kosova” (“2000/45”) that provides the legal foundation for the provisional democratic self-government in post-war Kosova. 2000/45 is intended to address specific needs of Kosova, and establishes a single-level local government comprising 30 separate local municipalities. 2000/45 specifically allocates certain activities and responsibilities to municipal governments. Under 2000/45 the municipality of Pristhina enjoys no special status, despite the fact that it is Kosova’s administrative and political center.
- Under 2000/45 the institution known as the Municipal Assembly is the highest body of municipal government. The CEO and the Board of Directors of the Municipal Assembly comprise the Executive bodies. It was the intention of the drafters of 2000/45 that the executive bodies be closely overseen and monitored by an UNMIK-appointed Municipal Administrator. 2000/45 is not dispositive, however, as the U. N. Special Representative of the Secretary General (SRSG) holds ultimate power over municipalities and their activities.
- Although the newly elected municipal assemblies faced difficult challenges as a result of poor technical skills and extended staff training periods, municipalities have made progress and addressed numerous important issues. Municipalities have begun the process of establishing their own revenue sources by improving their collection of fees and charges. In all municipalities, the departments in charge of LED activities such as the Department for Economy and Finance, the Department for Reconstruction and Development and the Department for Urban Planning play key roles.

Role of local government in LED

- Local governments assume primary responsibility for community development. They are also responsible to provide for public utilities and services. However, Kosova's local administrations need to improve their communication with private business owners and work harder to build effective public-private partnerships.
- Local governments should assume a larger role in supporting businesses in their region. In a recent survey by Riinvest, ("SME 2001"), 619 private business owners (SMEs) were asked to evaluate their local government's support to the local businesses. The multiple-choice answer consisted of "good," "unsatisfactory" and "bad." 36% of the businesses surveyed had a positive view of the support, while 68% had a negative view. Of these, 38% reported the quality of support as "unsatisfactory" and 25% reported it as "bad."
- Approximately 30 percent of the rural population has migrated to urban areas, and the resulting strain on public utilities and services has been tremendous. This strain can be alleviated if local governments work improve the living conditions in rural areas thereby attracting migrants to return.
- Local governments should have a larger role in the development of Kosova's SME network.
- Local governments should contribute to improving the quality of public infrastructure and services consistent with emerging economic development needs. There is an urgent need to modernize urban plans and to target top priority sectors such as power, roads, water, business zones, transport, parking and public hygiene.

Challenge of capacity building in the municipal administration

- Absorbing the new structure: The new working environment that continues to develop presents numerous challenges for administrative personnel in Kosova municipalities. Local government administrations must react to the changing environment and implement programs that will result in improved skills and competencies required to effectively operate the new administrative organs.
- Low wages and little training: At the present time, municipal personnel in Kosova, which number 5,446, earn approximately 129 Euros per month. As a result, the skills and motivation to improve are low. In order to increase capacity and effectively raise personnel management within municipal organizations, it will be necessary to develop a pool of human resources possessing adequate skills, strong work ethics, and a positive attitude. Adequately trained personnel are most critical in the areas of budgeting, public finance, legislation, public services management, SME support and strategic planning.

- I.T. strategy: In order to effectively utilize Information Technology, it will be essential to assess the current attitude of municipal staff and recruitment personnel that are responsible to communicate with new applicants who are by and large, technology-trained. There is a need for developing an overarching information technology architecture and implementing specific technology solutions in a phased manner throughout the municipal administration.

Power-sharing between the central and local governments

- Despite all efforts to build the required legal framework and judicial system, a stable environment for sustainable public finance structure is still not in place. In the aftermath of the elections it has become clear that the legal uncertainty and inability to self-finance that exist as a result of the incomplete legal framework plague municipal budgets. 2000/45 represents an important, though insufficient, first step toward the definition of the structure and function of municipal authorities. Specifically, the necessary budget instruments and revenue/expenditure policies remain to be clearly defined.
- Municipalities are authorized to collect and appropriately allocate revenue from municipal charges and fees. Notably, several Municipalities will apply the property tax during 2002 within a pilot project.
- Recent Riinvest survey results indicate that although a variety of local taxes have been levied on businesses, only a small percentage of them have actually been collected. This failure can be attributed to inadequate administrative policies within local governments that would cause market inequality.
- Expenditure demands coupled with the limited revenue potential that exists in many municipalities results in their facing large 'revenue gaps' or vertical fiscal imbalance. The responsibilities assigned to the municipalities are considerably large as compared to their authority and capacity to raise and manage their own source revenues.
- The proposed share of the municipalities in the Kosova Consolidated Budget for 2002 is 83.69 million Euros (nearly 11%). Of these, 10.31 million Euros have been allocated for the salaries of the municipal staff. The estimated municipal revenues for 2002 are 9.13 million Euros.
- During the years 1999-2001 international donor funding provided for most of the expenditure needs for the municipal public utilities. However, according to budget projections for 2002, these expenditures will be funded by the Kosova Consolidated Budget and increasingly, through municipal revenues.
- The people of Kosova are increasingly coming to expect more from their local governments. This is especially true with respect to services that impact quality of life, local amenities, basic infrastructure, public health services, recreation parks and

green spaces, public markets and local transport. Meeting these expectations will require local governments to develop integrated strategies and action plans.

Municipal public services

- Riinvest's SME 2001 survey asked the businesses to indicate their views on the quality of public utilities and services such as power, water, telecommunications, roads, hygiene, health and education provided by the local governments. 95% of those surveyed were highly dissatisfied. Power supply rated the highest in terms of dissatisfaction. Other services such as water supply (51%), hygiene (50%), roads (37%) and health and education (22%) were rated as "bad."
- In the immediate post-war period, UNMIK authorities prohibited utility-providing institutions from collecting fees for their services. Even after they were allowed to collect, the rate of collection was very low and law enforcement mechanisms were inefficient. The Kosova Consolidated Budget for 2002 allocated funds for the subvention of the water, central heating and other municipal utilities in the amount of 9.4 million Euros.
- 2000/45 outlines the responsibilities of the municipalities. However, it fails to address certain important responsibilities. As a result, conflicts between central authorities and local governments are not uncommon. The issue that has yet to be resolved relates to the locus of authority to appoint directors to manage public utilities. This has resulted in unnecessary strain among utility staff and management. As a result, the people suffer the consequences.
- The public utilities services can improve only when the management function and the regulatory function work in harmony with laws to clearly govern them. Several activities and arrangements are in progress for defining the role and relationship of Public Utility Service Providers and the municipalities with the establishment of the Kosova Trust Authority and the Public Utilities Regulatory Commission. (Details in Annex 5)

Environmental and natural resources protection

- To date, local governments have not developed capacities and mechanisms to protect natural resources from unregulated, and often illegal, exploitation. There is no effective structure for awarding rights to mining areas and zones. In addition, the regulation of environmental protection issues is not yet legally established. Kosovars again suffer the consequences of the fact that Kosova has no pollution control or environmental protection regulation or education programs

Establishing coalitions and partnership networks

- Successful implementation of LED depends upon the combined effort of three basic groups: the public sector (government), the private sector (businesses) and the Non-

governmental sector (NGOs, community organizations, trade unions, and religious associations).

- Riinvest is currently implementing a program to enable municipalities to enhance SME development. This program is designed to assist local governments and the business community to provide leadership and guidance to SMEs and to foster public-private partnerships.
- Although business associations are working hard to establish initial contact with local governments, they lack both logistic capacity and sufficient expertise to successfully engage in policy advocacy and related lobbying effort. The sustainable contacts and partnerships with local governments and NGOs have not yet been created.
- Partnerships of local governments with civil society and NGOs, another important vehicle for solving community problems, have not yet proved successful in Kosova. On one hand, municipalities have helped little to create the local alliances necessary to support such partnerships. On the other hand, however, NGOs have been equally unable to create liaison systems within their own community.
- The post-war period and the local elections have seen the first real efforts to establish local partnerships and to develop know-how in Kosova. Currently, several actors are actively building on these efforts for the purpose of creating and implementing sustainable strategies for local economic development.
- The municipalities are moving in the right direction and are beginning to develop strategic priorities. All the actors are becoming increasingly aware of the importance of joint and coordinated efforts as the only option for achieving the common goals. It is hoped that the next phase will include the creation of a sustainable and comprehensive LED strategy.

RECOMMENDATIONS

1. A coordinated effort on behalf of local governments, private businesses, the donor community and civil society is required in order to develop a strong LED strategy. This is also required in order to promote participation of all stakeholders, ensure effective use of local resources, strengthen democratic institutions and improve overall quality of life. An integrated process should lead to:
 - LED strategies and action plans in municipalities;
 - Project identification and development based on LED strategies; and
 - Public-private partnerships for strategy and project implementation.

2. Appropriate legislation should be developed on the basis of a reconsideration of 2000/45 and its subsidiary and related regulations. New legislation should foster:
 - Progress in transfer of more powers and competencies to local administration (commensurate with their capacity to take them on) and with more consistency and clearer definition regarding authorizations and decision-making responsibilities. This will also result in a clearer definition of an appropriate role for international administrators.
 - Evaluation of the necessity for improving the organization of the municipalities in order to better address their needs, especially for Prishtina, which deserves special status in view of its size and importance for economic and social advancement.

3. Local governments should act within the framework established under existing legislation to determine the tax base and tax rates, and ensure equal opportunity for all businesses in the market. Municipal fees and charges should be fair. Municipal budgets should take into consideration the interests of those citizens earning higher incomes. Within the process of fiscal devolution, several sources for municipal revenues, based on fees and charges and potential avenues for taxes, should be considered.

4. There is an urgent need to improve the quality of municipal public services and utilities. This can be accomplished by:
 - defining full responsibility of the municipalities in managing public services and utilities;
 - increasing managerial capacities within municipal administration and public enterprises, including needed funds for their modernization; and
 - improving collection systems for fees and charges for services delivered to citizens.

5. Local governments should further develop their capacities for promoting modern LED. It can be done through :

- Providing a satisfactory business environment for family businesses and SMEs; promoting local products and services, such as food processing, tourism and handicrafts; boosting the high technology sector and protecting the environment;
 - Improving systems for information exchange; encourage cooperation between research institutes, businesses and local governments; Creating security and safe conditions that are vital for the business activities and entrepreneurs;
 - Reducing administrative charges and improving procedures and facilities for business registration; facilitating investment, training and consulting; Improving urban conditions and locations for attracting business; Offering incentives to local businesses and foreign investors; and promoting fair competition with transparency in public tenders.
 - Adopting modern human resources management practices for recruitment, selection and continuous development of staff skills, especially for budgeting and public finance, legislation, public services management, computerization of municipal administration; giving priority to SME support and strategic planning in the municipal administration. It is necessary to analyze and consider possibilities to rationalize personnel within the municipal administration in order to improve efficiency. There is a need for developing an overarching Information Technology architecture and to implement the technology solutions through clearly defined phases.
6. Institutional support is critical to build partnerships that will lead to successful LED strategies. The coordination of all participants in the process is the key. Local administrative institutions, such as Department Finance and Economics, Department of Development and Department of Urban Planning should take active roles. Other actors should include business associations, local agencies for SME support, employment offices, financial institutions, local bank and non-bank institutions, insurance companies, training institutions and civil society. On this basis, the creation of broad coalitions for the promotion and support of local and economic development can be achieved.

Local Economic Development in Kosova

1. Introduction

This Research Report (“Report”) on Local Economic Development (“LED”) is prepared as part of the Project entitled "Promotion of Economic Development through Civil Society" that is implemented by the Riinvest Institute for Development Research (“Riinvest”) in partnership with the Center for International Private Enterprise (“CIPE”), Washington, D.C. and supported by the USAID Mission in Pristina.

This Report is intended to address current problems in the management of LED in Kosova and to recommend an effective approach for the creation of public-private partnerships to promote active stakeholder participation in the development and implementation of LED policies.

This report will be presented in Prishtina at the International Roundtable Forum (IRTF), an important project vehicle designed to facilitate deliberation on key economic policy issues. During the past year Riinvest has presented the following research reports at IRTF meetings:

1. Socially Owned Enterprises and their Transformation/ Privatization;
2. Key Issues in Building a Taxation Policy in Kosova;
3. SME Financing and Development; and
4. Selected Aspects of the Social Situation and Development of the Pension System in Kosova.

Each of these IRTF sessions discussed the issues and presented the policy recommendations found in each of the above-described reports in the context of policy priorities for economic reform in Kosova. The IRTF sessions facilitated open and professional discussions among both local and international policy experts, members of the business community, international administrators and representatives of Kosovar civil society. Riinvest liaised and networked with relevant organizations, banks and other financial institutions as well as with international donor institutions. IRTF has continued to advocate the implementation of the research recommendations.

Riinvest hereby presents to IRTF its fifth module on LED. This Report examines the role of the local government in the development of LED strategies and policies as well as the instruments that could be employed to facilitate sustainable local economic development in Kosova.

Taking into consideration the emerging role of local governments, and the devolution of functions and fiscal responsibilities to municipal government in Kosova, the report has attempted to identify priorities and to outline activities required to increase the role of

local governments in the development and implementation of LED policies within the context of a market economy.

1.1 Objectives

This Report is intended to identify current problems related to local economic development in Kosova and to make recommendations that will serve as the basis for the establishment of policy priorities that will enhance the role of local governments in economic development in a way that is compatible with the development of a market economy and thereby help to:

1. Integrate local economic and social development activities within the context of the local environment so as to improve the quality of life of the population in the municipal areas;
2. Support local businesses in their efforts to grow and to increase investments [attract new capital investment];
3. Ensure optimal use of local resources at the local, regional and national levels of government;
4. Increase the efficacy and quality of provision of local public services;
5. Promote SME development and a culture of entrepreneurship;
6. Promote the creation of local economic development coalitions which would include the public and private sectors, NGOs and civil society; and
7. Foster a dialogue among stakeholders that will advance LED activities.

1.2 Contents

This report highlights several problems affecting the role of local governments related to economic development and the relationship of LEDs with the central government. Taking into consideration the experiences of LEDs in transition and developed economies throughout the world, the research and analysis found in this Report addresses the following issues:

1. The Role of the local government in LED in respect of:
 - Problems and issues in enhancing their role in LED;
 - Business attitudes towards LED issues; and
 - Developing human resources and capacities to manage LED.
2. Power sharing between local and central authorities in respect of:
 - Finance and public services; and
 - Natural resources and environment protection.
3. Opportunities for public-private partnerships and coalition building with participation of NGOs, business associations, trade unions, citizen communities, local banks and donors.

This report also provides by way of Annexure the following related information:

- a brief historical overview of LED in Kosova;
- USAID - Community Infrastructure and Services Program;
- Community Development Fund (CDF) of World Bank;
- Legal relationships between the PUSPs, the Regulator and the municipalities;
- Experience of countries in transition on issues of local finance;
- Statistical Information derived from Riinvest's SME survey 2001 and
- Map of municipalities in Kosova.

1.3 Methodology

This Report is based on the RIINVEST database and research reports that comprise, *inter alia*:

- Establishment and Functioning of the Local Institutions in Kosova 2000;
- Post War Reconstruction - Strategies and Policies 2000;
- Surveys of 300 Private Enterprises, 1997, 1999, 2000;
- Survey of 619 Private Businesses, 2001;
- Surveys of 192 Socially Owned Enterprises, 2000 and 2002;
- Survey of 3500 households, 1999;
- Surveys with 24 municipal government staff, 2001; and
- Surveys with 36 SMEs in 12 municipalities of Kosova, 2002.

This report also has employed reference materials from, *inter alia*:

- The World Bank;
- Transitional Department for Finance and Economy;
- Central Fiscal Authority (CFA);
- Institute for Statistical Office of Kosova (SoK);
- Banking and Payments Authority of Kosova (BPK);
- Internet based information sources; and
- Experience of countries in transition.

The project staff conducted visits and interviews in the municipalities of Suhareka, Prizren, Podujeva, Vushtrri, Ferizaj, Gjilan, Kacanik, Viti, Peja, Klina and Istog during the preliminary stage with the goal of liaising with the senior local staff and receiving their inputs regarding the local government's role in the LED. Inputs from independent and international experts have also been used.

II. ROLE OF LOCAL GOVERNMENTS IN LOCAL ECONOMIC DEVELOPMENT

2.1 Organization of local governments in Kosova

Following the emergency period in Kosova, UNMIK embarked on the next steps toward sustainable development with efforts to provide for greater Kosovar participation in decision-making processes. Kosovar society and its political parties began the process of establishing the first democratic institutions when municipal elections were held in the second quarter of 2000. The local elections held in October 2000 in 28 municipalities marked an important milestone in the transfer of responsibility from the international community to local institutions. Another important contribution had already been established in August 2000 when UNMIK Regulation 2000/45 (“2000/45”) was promulgated. This landmark legislative act, modeled on the European union’s “Charter on Local Self-Government”, invests Kosova’s democratically elected local governments in general with the functions and responsibilities typical for municipalities.

2000/45 establishes a single level of local government with 30 municipalities, which is different from the two-level government structure in other transition economies.

With the experience of the new structure for self-governance, the option of better organization of municipalities may be evaluated in future and especially for the Prishtina municipality. The experience of many countries indicates that the political and administrative centers are endowed with specific legal refinements in order to better address their organizational and other needs. In view of the size and the importance of Prishtina for economic and social advancement it deserves to have a special status in the near future.

Section 3 of 2000/45 lists the Government functions to be devolved to the municipal governments and the activities for which municipal governments are responsible. Some of the important activities of municipalities include:

- Providing basic local conditions for sustainable economic development;
- Urban and rural planning and land use;
- Licensing of building and other development;
- Local environmental protection;
- The implementation of building regulations and building control standards;
- Service provision of local public utilities and infrastructure;
- Primary health care;
- Primary and secondary education; and
- Licensing of services and facilities.

Generally speaking, the authorities and responsibilities vested in Kosova municipalities are similar to those found in the municipalities of most market economies.

2000/45 provides that the highest representative body in the municipality is the Municipal Assembly. The CEO and the Board of Directors establish executive bodies within the municipality. The UNMIK-appointed Municipal Administrator (the “Municipal Administrator”) is itself vested with significant powers related to the supervision and monitoring of the municipal assembly’s activities, as well as those of the Mayor, the CEO and the municipal civil service. The Municipal Administrator approves each appointment or dismissal of senior municipal staff and ensures adequate representation of all communities within the municipal structure. No appointment or dismissal can enter into force without prior authorization of the Municipal Administrator. Similarly, no expenditures can be incurred without the Municipal Administrator’s prior authorization. After the municipal elections, the constitutions for the municipal assemblies was smoothly promulgated, although some problems were encountered in respect of procedures and execution deadlines. In some municipalities it was impossible to approve the municipal statutes during the timelines given for appointment of the CEOs and the Boards of Directors.

Generally speaking, the delays were caused by the fact that the newly elected municipal bodies were inadequately prepared to efficiently execute appointments. It was also due to the lack of practical experience in negotiating solutions with opposing interests. The value and importance of distinguishing between administrative functions and their political content was not adequately understood and the professional standards and transparency in recruitment procedures were inadequately understood and applied. This negatively affected the quality standards of the municipal administration and as a result, of the services rendered.

Although the new institutions faced difficult challenges owing to lack of expertise and a longer longer staff learning curve than had been anticipated, municipalities progressed in the right direction and successfully dealt with some important issues such as building own revenue sources through more efficient collection of fees and charges.

With the assistance of Department of Local Administration, CFA, Directorate for local and regional coordination of MoFE and the former Department for Reconstruction, municipalities have drafted a working document entitled “Assessment of the Strategic Development of Municipalities”. This document has enabled the Municipalities to set goals which are consistent with their strategic framework, and thus allowed them to enjoy a more sustainable support from the international donor community.

The U. N. Special Representative of Secretary General (“SRSG”) retains broad powers in respect of local decision making. The SRSG has the ultimate decision-making authority on all the provisions of 2000/45. The SRSG may overrule any municipal decision that is considered to be non-compliant with Resolution 1244, the UNMIK regulations, the applicable law, or if the decision is found to infringe on the rights and interests of the communities. The SRSG has also reserved the right to replace members in the municipal assembly if it is considered necessary to ensure adequate representation of minorities. The SRSG also has the right to dismiss the municipal assembly or its members.

The powers currently held by the SRSG fully reflect his authority under UNSCR 1244. The SRSG's powers are considered adequate to ensure the first developmental phase of local government in Kosovo, taking into consideration the post-conflict situation, the lack of experience at the local level and the transition currently underway. Increasingly, however, as Kosovo's Municipal governments gain experience, the powers held by the SRSG and the UNMIK Municipal Administrator are perceived as obstacles to the independent and autonomous functioning of the local governments in Kosovo. It is frequently asserted that delineation of responsibility between the Municipal Administrator and municipal officials is not as clear as it should be and that this has led to confusion and conflicts between those bodies.

This problem has been exacerbated by frequent changes in the regulations related to the appointment of public utilities directors and municipal management responsibilities generally. This, in turn, has led to conflicts between the local authorities and the corresponding departments in the central government. These conflicts are also reflected in the relationship between local authorities and the personnel of the municipal utilities which has negatively affected the adequacy of public service delivery.

The time has come to review the competencies and authorization of the international administrators and to effectively transfer more powers to local administration. In so doing, a clearer definition of the advisory role of international administrators should also be developed.

2.2 Role of local government in LED

Local governments are assigned a primary role in promoting LED for community development to improve the quality of life. This is a development-oriented approach to meet the needs of citizens by encouraging public-private partnerships to capitalize on the development energy and interest of the community. To achieve this goal, local government should be open to the citizens' initiatives and transcend beyond their bureaucratic role. Such a stakeholder-oriented approach has the potential to bring about a new dimension to democratic governance for LED.

Strengthening of such a role implies the need to advance the participatory capacity of the population in these processes and to create institutional relationships for LED consistent with development of market economy.

2000/45 gives local governments a very important role in the delivery of public services. This role is inextricably linked to the important function of facilitating and encouraging economic development on the local level. Local governments face major challenges in providing public services and fostering economic development. These challenges are of very different types:

- Public Infrastructure and Public Utilities: Much public infrastructure was severely damaged during the conflict. Prior to that time it suffered from a decade

of financial and technical neglect. A well functioning system of water and sewer, local roads, streets and bridges, efficient removal of solid waste and the provision of reliable electric power are fundamental to the attraction of foreign investment and the encouragement of domestic SMEs. Unfortunately, in many municipalities the role of local government in the delivery of public services is has not developed adequately and faces several limitations. In addition, most municipalities lack a sufficient revenue base, either own sourced or from intergovernmental transfers, to properly fulfill their infrastructure and public utility obligations. Clarifying the role of municipal government in these areas is essential if they are to properly perform their functions. Ensuring that they have sufficient revenue, and the authority to collect it is also essential. The importance of resolving this issue cannot be overstated.

- Municipal Privatization: Municipalities exercise defacto ownership or effective control over significant amounts of buildings, real property and even enterprises. The inability to privatize is a huge barrier to economic development. It should also be recognized that governmental involvement in economic activities at any level confuses and dilutes the proper role of government in society. Municipalities have to play the primary role of organizing proper records of property rights especially by updating the Cadastral Registry.
- Rural Urban Migration and High Unemployment: Several municipalities have also suffered the negative economic impact caused by high levels of rural-urban migration. It is estimated that 30% of the rural population has moved into a few of the larger towns. The OSCE estimates that the population of Prishtina has grown to 545,477, approximately 23% of the population of Kosova. Prizren has grown to now comprise 10% of Kosova's population, and it is followed by Gjakova and Podujeva with 5% and Ferizaj with 4%. This migration has created serious problems for those municipalities, particularly with respect to the provision of municipal infrastructure, basic public services, and the expansion of public utilities. The rapid increase of unemployed people in Kosova is due in part to migration. In 2001, the number of registered unemployed persons increased by 14% with highest increase in Gjilan (22%) followed by Mitrovica (21%) and Prishtina (16%).
- Uneven Management Capacity and Uneven Economic Development: Some municipalities have significantly greater endowments than others. Proximity to good roads or productive mineral deposits as well as to foreign centers of commerce are clear examples. In addition, some municipalities have significantly better management capacity than others. Enhancing the institutional and management capacity of municipal administrations to address these challenges will be critical to eventual success.

2.3 Findings from the 2001 SME Survey

Local governments in Kosova need more and better channels of communication with private businesses. Existing contacts are mostly on an individual basis and related to administrative issues. These should be formalized through the establishment of contacts with various bodies such as business associations and NGOs. The recent Riinvest SME 2001 survey of 619 private businesses has generated some useful information with respect to the business community's perception of local governments.

In that survey respondents were asked to evaluate the support of local governments to their businesses by choosing one of the three options, "good", "unsatisfactory" and "bad". As explained in more detail in Annex 4, the results indicate that 36% of the businesses had a positive view of the support and 68% had a negative view of support and of these 38% reported the support as "unsatisfactory" and 25% reported the support as "bad".

The analysis of responses by size of enterprise indicates that micro and small enterprises are most overlooked by local governments. The manufacturers, however, have a more favorable view of such support. The services sector holds a less favorable view.

The evaluation of response by regions indicates that the most positive view of support was in Prishtina, Gjakova and Peja at around 39% in relation to an average of 36%. The least favorable view was found in Ferizaj, Mitrovica and Gjilan, ranging between 29% to 36%.

The research also tested the opinion of businesses on six requirements for which local governments provided support related to:

1. Assistance regarding business location;
2. Assistance to establish contacts with potential investors;
3. Reconstruction of public infrastructure and utilities;
4. Providing access to business information;
5. Fostering efficient administrative procedures within the municipal bodies; and
6. Assistance with respect to business registration procedures.

Overall response to the above query indicates a negative response with 57% of the respondents stating that they did not receive *any* support. Requirements #5 ranked as most favorable, where the business owners recognized the local government's effort in improving the administrative procedures and the facilitation for setting up of new businesses: 51% to 68% expressing a positive view. This response reflects a recent introduction of a provisional and simplified registration procedure in the UNMIK offices in municipalities.

The most positive view was on Requirement #6, the support received for establishing new companies, at 62%, favorable fees and charges at 58% and administrative procedures at 51%.

Business owners expressed a high level of dissatisfaction with public utilities and services, including power, water, telecommunications, roads, hygiene, health and education provided by the local governments, with 95% having most negative view about the power supply. “Bad” was marked for water supply by 51%, for hygiene by 50%, for roads by 37% and for health and education by 22%.

Opinions on utilities varied regionally. The most positive view of water supply was found in Gjakova and of telecommunications in Gjakova and Prizren. The most positive view on education was found in Peja and Gjilan and very negative in Prishtina. Business owners in Prishtina indicated a very negative view of public hygiene.

The question regarding equality of treatment of businesses by the local administration, elicited the following responses: 49% had no view, 18% had a positive view and 28% viewed treatment as “not equal.” Compared to micro enterprises, SMEs had relatively negative view regarding equality of treatment. By regions, the most negative view of equal treatment was in Gjilan and more positive view was in Mitrovica.

Business owners’ responses to questions regarding local governments in general confirms the reality that there is substantial need for improvement in many areas of public services.

The post-war situation is characterized also by several social and economic problems. There has been a large migration to urban areas with about 30% of rural population moving to cities and towns. This has created a major problem for local governments in providing public utilities and services. OSCE estimates that the population of Prishtina has grown to 545,477 that is 23% of the population of Kosova, followed by Prizren with 10%, Gjakova 5%, Podujeva 5% and Ferizaj 4%.

The high urban population density causes tremendous strain on the ability of local governments to provide economic and social infrastructure. This condition also encumbers the creation of better living conditions outside the urban area to encourage the recent migrants to return to their origin.

Rapid increase of unemployment in Kosova is partly due to migration from rural areas, with current unemployment level estimated at 50%. In 2001, the number of registered unemployed persons increased by 14% with highest increase in Gjilan (22%) followed by Mitrovica (21%) and Prishtina (16%).

2.4 Dispersion of private business and LED

In 2001, Kosova had 40.924 registered businesses, an increase from 29.564 businesses in 2000, (38%). The dispersion of businesses by regions and municipalities (Annex 4, Statistical Information) can be seen by ratio of 'inhabitants to registered businesses' and 'employees to registered businesses'. The table below illustrates the ratio of inhabitants per registered business and employees by regions. According to these figures, Prishtina

and Prizren have the most inhabitants per registered business, while this ratio is most adverse for Mitrovica, and is better for Ferizaj, Gjilan, Gjakova and Peja. While one would expect more businesses in the developed regions like Prishtina and Prizren and this reflects that these regions in post-war period have been under greater pressure from migration from rural areas.

Table 1: Ratio of inhabitants to businesses and employees to businesses by regions.

Region	Inhabitants / Businesses	Inhabitants / Employees
Pristina	62.2	16.0
Prizren	60.7	15.4
Peja	48.4	10.7
Gjakova	54.9	11.3
Mitrovica	73.4	19.3
Ferizaj	41.9	12.3
Gjilan	48.6	13.6
Average	55.7	13.9

Source: Statistical Office of Kosova

In the above table, it is worth noting that the SMEs mainly located in larger towns have not received adequate support of banks and non-bank financial institutions or municipalities. The relationship between SMEs and municipalities was limited to administrative issues like licencing and tax collection. However, the level of awareness of the municipal officials regarding the need for SME support as an important element in local economic development is gradually improving.

Expanding the banking system is vital for the support to business in the regional and municipal centers. There are 7 commercial banks operating in Kosova under a BPK license. In addition, 15 non-bank financial institutions are in operation of which 10 are micro-finance institutions and 9 credit and savings organizations. These institutions have better presence in the regional centers and in the small municipalities like Klina, Vushtrri and Dragash. Commercial banks have expanded their operations to many municipal centers. MEB and The New Bank of Kosova have established their branches in 7 regional centers, The Bank of Private Business in 4 regional centers, The Economic Bank in 2 centers, while The Kasa Bank, The American Bank and The Credit Bank are currently operating in Prishtina region.

Development of the SME network throughout Kosova has been mainly on the initiative of entrepreneurs. The local governments' contribution for development of local businesses has not been significant.

2.5 New role of municipalities in LED

Similar to advanced practices in other countries, the local governments should support the businesses in the following important areas:

- Lower administrative charges for the registration of the businesses;
- Facilitate investment, training and consulting;
- Promote better locations for local businesses and foreign investors;
- Offer special incentives to new businesses by way of lower fees, charges; and
- Promote fair competition with transparency in the public tender process.

Local governments should pay greater attention to developing strategies to further develop a favorable environment for businesses and support them with reasonable policies (e.g. reasonable fees and charges and modern urban development). The businesses are still perceived as a source of budget revenues and less as potential partners in the development of the community they live in.

LED strategies should focus not only on attracting foreign direct investment (FDI), but also on capitalizing on the local resources and local business initiatives. Local government should support the improvement of local enterprises so as to enable them to look beyond the local market and strive to be competitive in the Kosovar and export markets. Resources for LED are available, but they should be effectively harnessed especially for the sectors like services, food processing, tourism and handicrafts.

The role of the local government should be more consistent through creation of enabling business environment for:

- The development of family businesses and SMEs
- Better urban planning for business development
- Promotion of local products and services
- Promotion of high technology sector and services
- Environmental protection

Local governments should also play an active role in other important areas, such as:

- Creation of partnerships based on common interest among the local stakeholders,
- Support partnerships with international donor community in preparation and implementation of LED plans,
- Institutional involvement in the preparation of privatization plans for socially owned enterprises and public utilities at the municipal level,
- Promotion of LED through an improved exchange of information,
- Encourage cooperation between research institutes, businesses and local governments,
- Ensuring secure and safe conditions that are vital for the business activities and entrepreneurs.

One can conclude that local governments can contribute especially to improvement of the quality of public infrastructure and services consistent with emerging economic development needs. There is an urgent need to update city and urban plans and to identify the real needs of the community and the businesses regarding urban development. It is also important to target the top priority sectors: power, roads, water, business zones, transport, parking and public hygiene through specific programs.

The devolution of functions and responsibilities to local governments accompanied by an enabled legislative base will create conditions conducive to the advancement of local business initiatives and partnerships among the local stakeholders. This process of decentralization will serve as a conduit for the municipalities to become an important partner for promoting institutional environment in the interest of the business community.

Establishment of local funds for supporting local businesses is an important part of LED in many other countries, though the experience of such funds is uneven. The establishment of such funds in Kosovo could be a possibility for supporting business promotion and improvement of utilities and infrastructure.

It is important to stress that local governments should endeavour to play a more active role in the privatization of the socially owned enterprises and assist local businesses especially by providing adequate cadastral basis for the assets subject to privatization.

The exclusion of local governments from the commercialization of the socially owned enterprises, in the municipalities of Ferizaj, Peja, Prizren, Mitrovica, Podujeva, Prishtina, Lipjan and Gjilan has had a negative impact throughout this process, particularly in regard to the fulfillment of the obligations of the firms in terms of environment, infrastructure and employment. In the post-war period, some municipalities attempted to manage and control SOEs though it was certainly outside their authorization.

2.6 Challenges of capacity building in municipal administration

Municipal governments in Kosovo face a number of serious challenges in developing a well trained highly motivated staff. A higher level of skill and capacity at the municipal level is necessary because municipalities are facing a new environment comprised of the new pluralist system in municipal assemblies, new expectations from the emerging business community, a pressing need for transformation of the socially owned property, a growing demand for public services, an imperative to support and promote public-private partnerships and greater involvement of civil society in local economic development.

The level of organization and the smooth functioning of the local governments depend greatly on the overall competence of the human resources of the municipal administration including the management capabilities and the administrative skills of staff. This requires efficient management of personnel and capacity building in all the relevant municipal

departments in order to develop a pool of administrative professionals with a high degree of work ethics and positive attitude.

Human resources is the most valuable asset of local governments. Hence, for the development of the local administration, adoption of modern human resources management practices for recruitment, selection and continuous development of staff skills should become one of the top priorities in the municipal administration. The need to improve the personnel management function in the municipal administration and continuous development effort call for building a close relationship between the personnel department and other operating departments through regular interaction.

Development of personnel in the municipal administration deserves a very high degree of attention. Training needs are most striking in areas of budgeting and public finance, legislation, public services management, SME support and strategic planning. The municipal administration system of Kosova presently employs 5.446¹ staff, with an average monthly salary of 129 Euros (CFA, January 2002). Under these circumstances, with obvious budget constraints, there are very limited possibilities of staff motivation.

In light of this background, it is necessary to analyze and consider the possibilities to rationalize personnel within municipal administrations. Such rationalization entails a thorough analysis of the functions and work processes in the municipal administration that will lead to improved efficiency and the reduced costs within the re-organization.

The rationalization should also reflect the importance of having new staff with up-to-date administrative and management skills. These plans, supported by in-depth analysis, should form the basis for the effort to win support within the administration at all levels, as well as external support and favorable public opinion for the re-organization of personnel. In order to achieve this, the following steps are proposed:

- Set goals on requirements of staff, including training and development of the current staff and recruitment of new staff with appropriate skills set for each department of the municipal administration;
- Determine the staffing needs and developing an effective staffing plan;
- Develop the municipal administration staff rationalization formula;
- Train the staff in important functions of budgeting and public finance, legislation, taxation and planning to achieve a critical mass for rapid improvement of efficiency. Such staff training and development should serve as the base for taking up the responsibility of Local Economic Development; and
- IT training for the general administration.

The process of application of Information Technology in municipal administrations call for a change in the attitude of the municipal staff. It also implies recruitment of new IT staff with relevant training. There is a need for developing an overarching information technology architecture and implementing specific technology solutions in a phased

¹ Department of Local Administration

manner throughout the municipal administration. Though some staff is equipped with computers, currently, most municipal administration is performed in the old ways using typewriters and writing by hand. This highlights the need for staff training in using technology. The application of IT with appropriate software solutions is important for development of the LED database and promotion of SMEs that will also help increase the administrative efficiency.

III. POWER-SHARING BETWEEN THE CENTRAL AND LOCAL GOVERNMENTS

3.1 Local finances

It was impossible during the immediate post-war period to establish structures for self-government or to put into place a revenue system that would allow for self-financing of budgetary needs, either at the central or the local government levels. During that time UNMIK's primary focus was to use donor funding to finance the major part of central and municipal government administration, and public services.

During this period some municipalities stepped into the institutional vacuum and arrogated the power to establish and use a wide variety of fiscal instruments as their own revenue sources. In some instances municipalities levied very high fiscal charges, allegedly to cover administrative costs associated with the issuance of various types of business permits, and annual taxes on businesses classified by their size. Sometimes, under the pretext of a tax, municipal administrations charged specific businesses with monthly levies that were in fact higher than the presumptive tax. A variety of factors were responsible for the levying of such taxes and fees, including:

- Limited possibilities within the existing legal framework to define own revenue sources for self-financing;
- Lack of precision in the legal framework that defined the authority of municipalities;
- Undefined upper and lower limits for the applicable fiscal burdens.

Municipalities also established varying tax and fee policies for the SME sector. Some taxes and fees were levied by some municipalities and not by others. The analysis in the RIINVEST's 2001 survey of 619 SMEs reflects that businesses have paid various kinds of local taxes, including:

- 33.6% of those surveyed paid property tax;
- 6.8% paid tax on cadastral revenue;
- 13.8% paid tax on urban land utilization;
- 11.2% paid tax on business activity;
- 16.8% paid tax on rent of premises;
- 16.4% paid advertisement tax; and
- 1.4% paid other taxes.

Although the local governments levied a variety of taxes, only a small percentage of businesses actually paid them. This is one more example of the low collection capacity of local governments.

It soon became clear that the municipal revenue practices described above were not conducive to business development and inadequate to the task of funding municipal

expenditure. An intergovernmental fiscal reform process was initiated to address these issues and their work has not yet been completed. The first major step in the reform process was the promulgation of 2000/45 that served to clarify the role of municipal governments in the provision of public services. In practice, this meant that many functions such as primary and secondary education and primary health care, then performed by the central government, were identified as being municipal responsibilities.

Although it was intended that these responsibilities would be devolved to the municipalities during 2001, the process was delayed due to the fact that the municipalities possessed insufficient financial resources to properly handle these new responsibilities. The problem was exacerbated by the fact that by even as late as the first quarter of 2001, municipalities had no clear understanding what the level and composition of central government revenues were going to be. There was a need to design and implement a fiscal infrastructure that would provide for real, responsible devolution to the municipalities, having conceptually the three major components as follows:

The first component was to implement a system of modern taxes to generate a significant volume of revenue without causing economic distortion. These taxes include a VAT, a payroll tax, and a corporate income tax. On January 1, 2001, none of these taxes had yet been implemented. By August, 2001 each of these taxes were either fully in place or in an advanced state of design. By that time, it was clear that Central Government revenues increased substantially.

The second component involved the development of municipal own-source revenue bases. This component itself had two parts: designing, enacting and implementing a modern property tax system and the establishment of a modern system of user charges based on the principal of cost recovery.

The third and final component was the design and implementation of a system for intergovernmental transfers. This required the design and implementation of two components:

- a general or equalizing “block grant” based on relative measures of fiscal need and fiscal capacity between municipalities; and
- a set of special purpose grants, one for elementary and secondary education and one for primary health care.

Many of the key elements of intergovernmental financial reform were accomplished during the second half of 2001 and were integrated into the 2002 budget. Four of the most striking features of the 2002 budget are:

- Donor funding now comprises only a small portion of the recurrent budget (7%). Most revenues are raised from centrally administered broad-based taxes.
- The public services designated as local functions under 2000/45 have in fact been devolved to municipalities.

- Municipalities would now have the ability to finance a significant portion of their budgets after full implementation of modern systems of broad-based property taxes and user fees and charges.
- A system of intergovernmental transfers based on objective criteria has been developed.

Kosova Consolidated Budget and related issues: The proposed share of the municipalities in the Kosova Consolidated Budget for 2002 is 83.69 million Euros. Of these, 10.31 million Euros are provided for the salaries of the municipal staff while the estimated municipal revenues for 2002 amount to 9.13 million Euros.

Table 2: The structure of budget revenues in municipalities in Euros

Year	2000	2001	2002	2000	2001	2002
Central Grants	9,713,700	14,069,500	74,563,000	86.36 %	82.1 %	89.1 %
Own sources	1,533,740	3,067,480	9,126,560	13.64 %	17.9 %	10.9 %
Total	11,247,440	17,136,980	83,689,560	100.00 %	100.0 %	100.0 %

Source: Kosova consolidated budget

Despite all efforts to build the required legal framework and judicial system, a stable environment for sustainable public finance structure is still not in place. The uncertainty and lack of clarity of sources for self-financing of municipal budgets for functioning of the Local Government Institutions became evident after the elections.

The Regulation on Municipal Self-Government passed in August 2000 represents an important, but still insufficient endeavor for definition of authority of municipal governments particularly relating to budget instruments and revenue/expenditure policies.

3.2 Ongoing factors relevant to the devolution of fiscal responsibilities to local governments

The above discussion makes clear that the process of intergovernmental fiscal reform has taken major steps forward in 2002 and would increase possibilities of municipal governments to establish an environment conducive to local economic development. However, it must be emphasized that these are only the first steps. A great deal more work remains to be accomplished, both at the level of policy design and implementation. The following is a non-inclusive list of some of the most urgent tasks to be addressed during the remainder of 2002.

- Public Utilities: The role of municipal governments with respect to providing public utilities must be clearly defined and understood. Any remaining ambiguity on this important topic is, by this point in time, unnecessary and destructive to economic development..

- Budget Transparency: Much of the achievement of the intergovernmental fiscal reform of 2002 has already been diminished by the fact that as of late March, 2002 no municipality has been given a final and definitive schedule for all of the transfers that it is intended to receive during the year. Although functional responsibility has been devolved and a revenue system for municipalities has been developed and made an integral part of the 2002 budget, in order for municipalities to effectively carry out their responsibilities, they will require all relevant information related to the revenues at their disposal and the timing of dispersals that they can expect.
- Intergovernmental Transfers: As mentioned, the establishment of a new system for transferring finances from the central government to municipal governments is a significant achievement. In order for municipalities to properly execute their functions they will have to have a reasonably clear understanding of what their revenues from all sources are likely to be over a three- to four-year period. However, the fact that nothing has been communicated to municipalities on this important topic is a serious omission that should be addressed as soon as possible.
- Property Tax: The pilot property tax law is a good one, but progress in implementation has been slow. Implementation should be significantly accelerated with the objective that in the very near future, the property tax is one of the most important sources of local revenue. As part of this process it will be important to move from a pilot law to a full-fledged law. The final version of the law should fully define the enforcement and collection powers possessed by the municipalities.
- Fees and Charges: Municipalities are required under DLA/CFA Administrative Instruction 2001/1(2) (“AI 2001/1(2)”) to make significant modifications to their systems of fees and charges. The situation in the immediate post-war period where municipalities levied a wide assortment of fees and charges with little regard for the establishment of a healthy environment for business development or for correct revenue policy has already been discussed. AI 2001/1(2) requires municipalities to levy fees and charges based on the principle of cost recovery and it provides useful guidance on what that means in practice and how such a system should be designed. AI 2001/1(2) also requires municipalities to submit their revised system of fees and charges to DLA and CFA for review and approval. It is clear, therefore, that the problem will not lie with the development, but rather the implementation. Although municipalities began the process of revising their fees and charges in September of 2001, to date, only half of the revisions submitted have been approved by the DLA and CFA. The importance of finalizing this process and of implementing the new system of fees and charges cannot be exaggerated.
- Public Service Financing: As mentioned, Kosova’s municipalities face severe problems in the delivery of basic public services such as water, sewerage, municipal street construction and maintenance. A decade of neglect prior to the

war, often severe damage during the conflict, together with an influx of rural migrants to many urban areas have combined produce a genuine crisis in this area. These complex issues will remain until such time as issues related to municipal privatization and the status of Public Utility Service Providers (“PUSPs”) and the role of the municipality in the provision of utility services have been resolved. However, other aspects of the problem are less complex and should be immediately addressed. Specifically, the central government urgently needs to provide guidance to municipalities on the design of a fee structure and financing system for developing residential or commercial/industrial land. The absence of well-designed system has already resulted in insufficient municipal revenues to expand the urbanized zone and in levels of illegal construction that have already reached epidemic proportions in some municipalities.

- A Budget System Law: Many countries have a law or an organized set of laws governing the development and execution of public budgets, reporting on public spending through public financial reports, and all other aspects of fiscal accountability. Such laws typically regulate the rights and responsibilities of all of the parties in the process and the rights and responsibilities of the different levels of government. Kosova does not yet have such a legislative framework. Developing such a law would be a major step forward the process and clarify the role of municipal governments and in strengthening municipalities and making them more able to properly execute their responsibilities and to play their proper role in encouraging local economic development.

The experience of some countries in Eastern Europe that have addressed the transition process and determination of central and local taxation and their priorities is detailed in Annex 4.

3.3 Municipal public services

The overall status of the municipal infrastructure in Kosova in the late 1980s was inadequate to fulfill the citizens' needs; it deteriorated further due to mismanagement and politicization of administration during the years of colonialist repressive acts of the Serbian regime that followed in the 1990s. They inflicted heavy penalties on the municipal capacity to provide public services, especially in terms of human resources, impoverishment and neglect of management development and technology applications. During the past three post-war years, endeavor has been made for enhancement of the technical capacities of some public services through appropriate investment.

In the last decade, no efforts were made to improve the water infrastructure in the artificial and natural lakes of Kosova. This includes water resources, water levels, water filtering and purification equipment and systems. The main water pipeline systems have received no repair or maintenance in years, resulting in water loss of up to 40%. In terms of water availability, only 62% of the population receives regular water supply of potable quality, 7% receive very poor supply, and 31% do not receive potable water from the

supply system. Up to 51% of the population does not have access to the water supply system at all.

The regions that have relatively good access to better quality water services are Zvecan, Zubin Potok, Mitrovica, Prishtina and Peja. The worst access is found in the municipalities of Vitia, Klina, Lipjan, Glogovc, Skenderaj and Kamenica.

Riinvest research indicates that the general condition of the sewerage transmission and disposal system is very precarious. Only 23% of the population of Kosova is connected to the public sewers systems as per the data of the year 2000. Only 23% of the population of Kosova is connected to the public sewers as per data of the year 2000. This is partly explained by the low level of urbanization, whereby the 1 million rural population of Kosova has almost no connection to public sewer system. However, the urban areas seem to be better served, by comparison. The share of urban population with access to the public sewers is 69.72%; only in the town of Peja 100% of the population has such access and two other towns that provide access to the public sewers to over 50% of the population are Prishtina (80%) and Prizren (53%).

During the immediate post-war period, municipal PUSPs were not allowed to collect the fees for their services. Although UNMIK's policy on this issue has changed and now approves fee collections, the lack of legal enforcement mechanisms continue to mean low collection rates and financial crisis for the PUSPs.

During the recent elections the local authorities assumed many responsibilities under pressure of promises to electorate though some of them did not have a local character. While on the other hand, the expectations of people from the local government increased significantly in respect of quality of life, local amenities, basic infrastructure, public health services, recreation parks and green spaces, public markets and local transport. For meeting all such expectations would require a major strategy and planning effort by the municipal governments with an integrated approach for all the functions.

The Kosova Consolidated Budget for 2002 has allocated 9.4 million Euros for the subvention of water, central heating and other municipal utilities. The international donor community has also provided substantial amounts by way of grants to fund the utilities. The most important among such donors are DFID, USAID, GTZ, KFOR, ABD and OXFAM. Donors with the potential to provide larger amounts of support include UNMIK, FAO, EU, SDC of Sweden, and Government agencies including KOCKS, THW IRC, KFW and TURING of Germany, ACT of Norway and VIVENDI of France.

Two examples of international donor support to municipalities and communities for the purpose of improving infrastructure and public utilities are provided in Annex 2 - USAID - Community Infrastructure and Services Program and Annex 3 - Community Development Fund, A World Bank initiative.

3.4. Management and regulation of public utilities

Effective management and regulation of the public utilities of Kosova goes to the very heart of the UNMIK mandate and the work of all international institutions and donors in Kosova. Article 3 of 2000/45 provides that services related to local public utilities and infrastructure, including water supply, sewage treatment, waste management, local roads, local transport services and local heating systems is to be devolved to from the central to the municipal governments. The respective municipal assemblies must approve municipal budgets for public utilities and services. 2000/45 also provides that municipalities may make cooperative arrangements among themselves to execute their powers and fulfill their responsibilities related to the provision of these services.

Although Article 3 of 2000/45 gives a clear indication of the kinds of government services that are to be municipal responsibilities, the picture it paints is incomplete. There are numerous pieces of legislation currently pending that will to govern the management and regulation of all PUSPs in the power, water and solid waste sectors (the “Sectors”). When enacted, these laws should more clearly define the relationship that is intended to exist between the central government and the municipalities regarding the delivery of these public utility services. The new legislation would be important for providing a solid foundation for more effective management within the PUSPs and for the delivery of higher quality services to customers.

Important activities are in progress for establishment of institutions and related legislation for management and regulation of Public Utility Service Providers. Creation of the Kosova Trust Agency (KTA) and the Public Utilities Regulatory Commission (PURCK) have been contemplated. The objective is to define responsibilities, authorization, sector specific regulations and relationships between all actors, namely, the following:

- Public Utility Service Providers
- Kosova Trust Agency
- Public Utilities Regulatory Commission
- Supervisory Boards of PUSPs
- Municipalities
- Customers

A brief review of the legal relationships between PUSPs, the regulator, and the municipalities that is outlined in the pending legislation is provided in the Annex 5.

3.5 Environmental and natural resources protection

The exploitation of abundant natural resources in some municipalities is of critical importance for local development in the regional context. Among these natural resources the availability of minerals and coal is deemed to be of greatest importance for Kosova.

These resources have played a significant role in the development of some areas. However, the decisions related to their exploitation were heavily influenced by political

considerations. Currently, local governments are not in a position to protect the resources from unregulated and often illegal exploitation. This problem is closely related to the absence of planning in awarding rights and licenses to mining areas and zones. Also, there is inadequate regulation for environmental protection in the exploitation of resources.

Rural areas offer great potential for the development of rural enterprises such as animal husbandry and cultivation of fruits and vegetables. The large grazing lands in the Sharri highlands and the neighboring areas are ideally suited for dairy farming and milk processing. The increase in supply of animal and agro-based products would result in opportunities for industries such as post harvest handling and processing of the agro and dairy products. The considerable variety of medicinal plants available in these areas has the potential for developing marketable products. These activities would offer opportunities for rural development.

The relatively large arable land surface and the established cultivation practices offer limitless opportunities for development of agriculture and agro products and particularly vegetables, particularly for municipalities in the Dukagjini valley. The Municipal governments need to develop plans for the agro-based and rural industry in order to increase production and rural incomes. There is also a need to develop legislation to safeguard the arable land.

Electric power generation, the metallurgy industry, particularly the heavy metals sub-sectors, and chemical industry have been most responsible for the high level of pollution and environmental degradation in some areas, particularly in Mitrovica and Obiliq.

The industrial areas in the Mitrovica region having lead and zinc mining and processing and related chemical industry, the coal based power plant at Obiliq near Prishtina with the cluster of surface coal mining and chemical industry and the cement plant at Han i Elezit in south Kosova are the main polluters in Kosova. In addition to air pollution, these industries have generated industrial waste and residue that is dumped in large unregulated landfills.

The volume of chemically contaminated water discharged in the main rivers, particularly in Sitnica (91%) virtually transforms the confluent system in Sitnica-Iber region into an open-air industrial waste disposal site. The wastewater discharge of the power plants and the chemical industry in Obiliq and the Trepca industrial complex further add contaminants to these rivers. In the past, inorganic substances generated by some industries heavily polluted Kosova's hydro system. Currently, these industries are abandoned. The other contributors to environmental pollution in Kosova are industrial activities like leather processing, textile, paper and construction material that are scattered all over Kosova.

The normal garbage and waste generated by the households as well as certain waste generated by increase in the SME activity in the post-conflict period are causing waste management problems that exacerbate the pollution problem described above. The

dumping of rubble and waste generated by construction activities and uncontrolled sewage discharge into water bodies and open lands add further to the environmental pollution. Agriculture, transport and residential heating all contribute to deterioration of air quality and increase pollution.

The industrial and urban waste is a serious problem for Kosova's environment. In 1996, the overall land surface covered with waste disposal sites was larger than 12,000 hectares. The largest industrial waste disposal sites are in Obiliq and Zvecan. Due to the poor design and lack of maintenance of the Obiliq site, there is a clear and imminent risk that phenol and other noxious substances will pollute underground waters. The situation is similar at the waste disposal sites in Mitrovica. Until now, at none of these sites any waste recycling has been done resulting in high risk of the wind spreading the toxic wastes over a large areas.

Urban solid waste management has already become one of the most intractable environmental problems in Kosova. The latest estimates indicate that the daily solid waste generation in Kosova amounts to 1.2 kg per capita amounting to daily generation of 750 tons in Prishtina alone. The garbage collection and disposal facilities are woefully inadequate to cope with this volume. During the year 2001 some international donor organizations have funded projects for development of some modern disposal sites for urban solid waste. Long term planning in the solid waste sector is in its infancy. Due to the low content of recyclable materials currently there is no solid waste recycling activity.

At present Kosova has not developed any pollution control or environmental protection legislation. There is very little in the way of organized education programs to address these issues and as a result, the Kosovars have to suffer the consequences of health problems, and in extreme conditions, slow demise.

Municipalities must have wider authority for pollution control and environment protection. Municipalities need grant funding of carrying out this responsibility that would require training of municipal staff in technology and management of environment and related regulation and services. These responsibilities have to be integrated with the full range of devolution of the Government functions, while monitoring and facilitating enacting regulation and law enforcement relating to all the responsibilities that potentially may constitute managing environmental risks.

IV. ESTABLISHING COALITIONS AND PARTNERSHIP NETWORKS FOR LOCAL ECONOMIC DEVELOPMENT

Local Economic Development has a greater chance of success through the joint efforts of the public sector (government), private sector (businesses) and the non-governmental sector (NGOs, community organizations, trade unions, religious associations). The first step in the strategic planning for LED should always be the identification of the real partners those with strong motivation and are capable of establishing a solid long-term partnership based on common goals and expectations. The creation of such partnerships involves participation of public institutions, businesses, industries, civil society organizations, business and professional associations, groups of experts, and training institutions that share common interests in the local economy.

The first joint LED efforts in Kosova took place immediately after the war. All participants (representatives of local authorities, UNMIK and many international organizations) were focused on overcoming the consequences of the war and paving the way for reconstruction. The UN pillars at the central level, together with the international organizations with the highest implementation capacities, such as USAID, DFID, GTZ, Swiss Contact, SIDA, in conjunction with a large number of humanitarian agencies began the process of identifying potential partners within the existing local administration structures, civil society representatives and local communities.

The goal of this activity was to identify the problems in the field, to set priorities and to design and implement relevant projects. Unfortunately, these activities did not lead to the development of sustainable long-term partnerships, which is a precondition for the development of sound LED strategies. During this phase, the urgent needs and short-term solutions prevailed.

(i) Progress in the establishment of public private partnerships

After the first elections in the post-war period, the establishment of local institutions was a cornerstone for further joint and coordinated LED activities and for the first time after many years the conditions exist for development of institutional partnerships. The UNDP- supported LOGO Project, aimed at enabling municipalities of the Prizren region for the creation of development plans, was a significant contribution in this direction.

(ii) Enabling municipalities for SME development in Kosova (Delta Program)

The Delta Program is a joint project of Riinvest, Open Society Institute (OSI), the International Finance Corporation and the World Bank. The program is designed to assist members of local governments and business communities to provide leadership and guidance in the process of fostering SMEs in their communities, while assist them in building public – private partnership.

The program commenced in December 2001 and is in its pilot phase that includes seven municipalities, with the perspective to incorporate other Kosovar municipalities in a later phase. Municipalities of Prizren, Istog, Klina, Kaçanik, Viti, Vushtrri, and Podujeva are participating in a one-year program, which consists of integrated components intended to support them in the design and implementation of Local Economic Development strategies and action plans, in particular for SME development. The program will be mainly focused on the following:

- Training on action plan design for SME support, creation and retention, facilitation of the work with stakeholders at the municipal level in the process of local economic development strategy design;
- Facilitating group work that allows municipal teams of participants to develop local economic development plans and implementation strategies;
- Mentoring municipalities in the design and implementation of action plans;
- A Study tour to Hungary, familiarising a selected group that participating in training with practices and instruments applied by municipalities from a more advanced neighbouring transition country.

The training and facilitation is being provided by topical experts and training facilitators with relevant experience in Central and Eastern Europe. Additionally, a training of trainers component will ensure the sustainability of the program, and the future replication of the project's pilot stage to the other Kosovar municipalities.

Another important component in the organization of the efforts to support genuine local economic development is the assessment of the number of the existing SMEs, their geographical distribution and the quality of their economic activities. The emerging banking system could play a key role in providing for a better access to the capital and financing options for the SMEs within a comprehensive LED strategy.

Public-private partnerships need strong organization from both sides: as a matter of fact, the business community has to be better organized, in order to serve as a valid counterpart for the municipal administration. During the previous two years, CIPE and Riinvest have assisted and supported the establishment of 14 business associations in the following municipalities: Mitrovica, Kacanik, Prizren (2), Ferizaj, Viti, Rahovec, Gjakova, Peja, Gjilan, Suhareka, and Prishtina (2).

The establishment of the business associations is a good opportunity to better articulate and channel the interests of the private sector while creating partnerships with the municipalities. The business associations have already begun to establish their first contacts with the local authorities, but they lack the necessary capacities in terms of logistic and expertise for policy advocacy and related lobbying effort. The sustainable contacts and partnerships with local governments and NGOs have yet not been created.

For strengthening the Business Associations Riinvest and CIPE conducted a training event for their leaders on association development. It also organized founding assembly meetings of associations in several cities, facilitated greater involvement of individual

associations in the policy development process encouraging their participation in the policy forums and provided equipment grants to use technology more effectively.

In December 2001, Riinvest conducted two surveys in 12 municipalities that had submitted applications for participation in the Delta Program. The first survey targeted 24 municipal officials, whereas the second was conducted with 36 SMEs. The participating municipalities were Prizren; Suhareka; Ferizaj; Gilan; Kaçanik; Vitia; Peja; Istog; Klina; Podujeva; Vushtrri and Fushë Kosova. The surveys were designed for the purpose of assessment of the relationships between SMEs and local authorities, and the opportunities to enhance them.

The 24 municipal officials were selected from the Municipal Departments of Finance and Economy or alternatively from the Departments of Reconstruction and Development. The SMEs were chosen at random samples among the active businesses. The results from the surveys are as follows:

- All municipalities surveyed have completed the establishment of the institutions for local administration, such as the Municipal Assembly, the Municipal Government and the pertaining Departments. Most of the posts in the staffing tables were filled in accordance with the new structures. The most of the Majors, CEOs and Directors of the Departments laid stress on the need for training and technical assistance.
- None of the municipalities surveyed has drafted any LED strategy. In the previous years, efforts were undertaken to set development priorities in the municipalities, but this didn't result in the creation of any sustainable strategy for local development. In these efforts, municipalities were supported by the Department for Local Administration, Department for Reconstruction and by LOGO project staff.
- 2001 has brought about improvements in the attitude of municipal officials towards business community and civil society. They are providing greater attention to their role for the creation of favorable conditions for the local businesses that may prove to be a relevant contribution for the municipalities to the efforts for economic growth. The officials have taken an important first step in the right direction, but nonetheless it seems they still lack the capability to coordinate the efforts of many actors that should be involved in the process.
- Representatives from the donor community are cooperating with the local governments and community members with the objective of identifying suitable projects based on priorities.
- The commercial banks and the non-bank financial institutions have established their offices in the seven major towns in Kosova and are in the process of serving the towns in the smaller municipalities.

- The conditions necessary for strategic cooperation between local governments and the business community are in place and there is need for efforts to make them sustainable.

The survey of SMEs in the same municipalities revealed a slightly different situation. Two thirds of the entrepreneurs gave high ranking for their own contribution to cooperation, while one third affirmed that the level of cooperation was not at the desirable level. This response accentuates the fact that both recognize the need for cooperation and their willingness will have bearing on building partnerships that currently are at initial stage.

The level of cooperation between the private businesses and the NGOs is not satisfactory. More than 81% of the businesses have never collaborated with NGOs, though the SMEs have performed better than microbusinesses in such cooperation. The cooperation also has an uneven geographic spread; Gjakova and Prizren regions are above average in cooperation while Peja is well below the average. The cooperation where exists is mostly for trade in products and services and to a lesser extent it is the exchange of information and in coordination of activities.

4.1. Institutional support to partnerships for LED

Building partnerships for local economic development needs institutional support and coordination of activities of the actors involved in the process. The departments in the local administration like Finance and Economics, Development, Urban Planning etc. should take active interest in such coordination. From the private sector business associations, local agencies for SME support, employment offices, financial institutions, local banks, and non-bank institutions, insurance companies and the training institutions could equally take up the coordination function. Such coordinated effort will go a long way in the creation of a favorable environment for local economic development.

The regional and local agencies for the support of entrepreneurship and development could be established in some municipalities on the basis of the demand for coordination in the private sector initiatives. Their activity should be primary focused on two issues:

1. Coordination of initiatives at the regional level with the central level programmes.
2. Mobilisation of local and regional capacities and advancement of human resources for successful establishment of local and regional development coalitions.

One of the most important functions the Business Associations and Agencies for SME support can perform is to assist in the creation of coalitions for the promotion of local and regional economic development. Such coalitions were quite successful in Poland. They help integrate local institutions, regional tiers of government, public utilities, business associations, trade unions, farmers medias and NGOs, while promoting the spirit of

partnership among all actors involved in the development process. By the means of these coalitions a positive configuration can be built to serve as a starting point for creation of favorable conditions for the businesses. In several countries businesses have been provided support in various forms like incubators, construction zones, business zones, technology parks. It is necessary to critically evaluate the feasibility of such programs in the Kosovar conditions and analyse their cost-benefits. Programs to support development in rural areas of the handicrafts, family businesses and farms could be seriously considered. It is essential to identify the sectors and businesses that such coalitions can stimulate and also determine the specific capacities, interests and demands of the local and regional stakeholders.

The other potential building block for establishment of partnerships is the NGO community and the civil society. After the war between 300 and 500 international NGOs were engaged in Kosova. Their work, along with the coordination efforts of OSCE, has stimulated establishment of several local NGOs. Today it is estimated that there are about 1,000 registered NGOs in Kosova. The NGO community is not evenly spread in the municipalities of Kosova and their existing capacities are insufficient to meet the LED needs at many locations. However, there is a very low level of awareness among the municipal officials regarding the role that NGOs could play in the civil society. It is necessary to raise such awareness to generate a more articulated interest in civil society for participating in local economic development.

The Association of the Municipalities in Kosova was established in 2001 and is developing coordination and lobbying activities. The Association is also engaged in developing cooperation with similar organizations and municipalities in other countries. The activities of this Association could play an important role in promoting modern LED.

The municipal administrations have not helped create local alliances that would support them in solving problems within their communities. The responsibility for building such cooperation is not of NGOs alone. However, sometimes there is an impression that the newly elected bodies adopt a distrustful attitude towards civil society, which they incorrectly perceive as a possible threat. At the same time, the NGOs have not been able to create an adequate liaisons structure within their own community. Although OSCE has provided considerable support for the coordination of the NGO sector much remains to be done in this regard.

In conclusion, in the post-war period and especially after the local elections, initial efforts were made in Kosova to establish local partnerships and for building related know-how. Currently, several actors are active in building upon these efforts, aimed at the creation and implementation of sustainable strategies for local economic development. The municipalities seem to be moving in the right direction in developing their strategic priorities. It is hoped that in the next phase they should be able to have a sustainable and comprehensive LED strategy. All the actors are becoming increasingly aware of the importance of joint and coordinated efforts as the only option for achieving their common goals.

ANNEX 1

Brief Historical Overview of Local Economic Development in Kosova

Generally speaking, the role of municipalities and/or local governments in LED has depended to a large extent on the overall social and economic system. During the first phase of the communist regime after the World War II, local authorities were subject to rigorous supervision from highly politicized central authorities and the so-called "people's councils".

The Constitution of 1963 greatly increased municipal competencies by accentuating the status of the municipality as a socio-political entity entitled to have a greater role both in strategic planning and the delivery of services.

The constitutional reform of 1974 was a decisive step forward in the advancement of the municipal competencies. That reform greatly expanded the competencies of municipalities and gave them a much larger role in higher-level decision-making. Municipal territory and jurisdiction was defined by law and could be altered only by referendum. In addition, full local autonomy was granted in areas such as budget making, financial management and public services within the existing legal framework. After the constitutional reform of 1974, Kosova had 22 municipalities that were shaped according to the new criteria. The average territory for a municipality was 496 square kilometers; the average population was approximately 90,000 inhabitants. The smallest municipality was Glllogovc with 291 square kilometers, and the municipality with the lowest population density was Leposavic with 16,1000 inhabitants. The largest municipality was Prishtina, which comprised 854 square kilometers and 289,000 inhabitants.

According to the Constitution of 1974, local governments were arranged in a single level (municipalities) and those municipalities were endowed with identical competencies regardless of their size or population. Municipalities were vested with political, organizational, integrative, coordination and planning responsibilities in the spheres of economy, finance, social assistance, health care, human resources, education and other related municipal activities.

It should be noted that with respect to the competencies and the range of activities of municipal authorities, the functions the local governments had in terms of economic development planning; emphasis was placed on the economy as one of the top responsibilities for every municipal government. Yet another important function for the local economic development, the right to levy municipal fees and taxes and to use tax and budgeting instruments also pertained to the municipal competencies.

Municipalities had also the right and the obligation to prepare their own urban plan and to outline an overall development plan for the improvement of the welfare of the population including the social insurance schemes, education and health care. The municipalities

were entitled to manage the obligatory education (elementary school) and to manage projects related to further in-service to additional education of adults.

This period was marked by an active development policy that targeted the most undeveloped municipalities. The balanced regional development was one of the primary medium term goals as laid out in the development policy. Accordingly, the measures and indicators for the monitoring of the performance and achievements were defined. The subsequent law on less developed municipalities established the criteria to be applied in each medium term.

Specific programs for the less developed municipalities, such as investment incentives, economic restructuring, capital investment for the modernization of the production capacities, especially in the agricultural sector, infrastructure and the support for farming and tourism activities, were put into effect. One of the best success stories was the project for the development of the agriculture in the 12 less developed municipalities of Kosova.

In order to support the less developed municipalities, an appropriate fund was created, with the perspective to be used in a later stage for the establishment of an agency for development.

During the period of 1986-90, the following municipalities were considered as less developed, according to the above-mentioned law: Viti, Vushtrri, Glogoc, Deçan, Dragash, Klina, Istog, Kamenica, Podujeva, Skenderaj, Malisheva and Rahovec.

Table 3: The level of economic development of municipalities in relation to the average of Kosova (Kosovo=100) for the year 1988

No.	Municipality	GDP per capita	No. of employed (In 1000 inhabitants)	Capital Assets
1.	Vitia	48,7	50,8	13,0
2.	Vushtrri	71,6	61,2	33,4
3.	Gllgovc	163,0	68,5	228,3
4.	Deçan	56,6	54,0	13,5
5.	Dragash	54,8	40,3	27,0
6.	Istog	52,8	54,8	18,8
7.	Klina	69,3	51,6	31,2
8.	Kamenica	71,1	68,5	39,8
9.	Lipjan	59,3	76,6	41,8
10.	Rahovec	88,0	58,8	51,4
11.	Podujeva	37,9	35,4	15,1
12.	Skenderaj	44,9	43,5	18,9
13.	Malisheva	35,1	37,9	3,9
14.	Kaçanik	71,8	81,4	99,7
15.	Gjilan	113,6	102,4	73,8
16.	Gjakova	134,4	154,8	96,0
17.	Mitrovica	167,9	158,8	124,7
18.	Leposaviç	152,0	191,9	203,1
19.	Peja	98,0	72,5	91,4
20.	Prizren	92,1	98,3	64,2
21.	Prishtina	176,5	199,1	313,4
22.	Ferizaj	114,1	85,4	65,0
23.	Suhareka	87,7	65,3	55,0
24.	Z.Potok	43,3	87,0	-
	Kosova	100,0	100,0	100,0

Source: Statistical Office of Kosova

After 1989, some new municipalities were created, mainly for political reasons (regions with significant number of Serbian population: Zubin Potok, Shterpece, and Novo Brdo).

On the other side, after the autonomy of Kosova was suppressed by violence, the Serbian regime also suppressed some of the municipalities mostly inhabited by Albanians. (Malisheva, Opoja)

The relationship between the central and local government levels during this period was characterized by direct interventions from Belgrade, which did much harm to the local authorities, in practical and legal terms. The appointment of Serbian mayors, the proclamation of the emergency situation in the municipalities mostly inhabited by Albanians, the continuous deprivations the local governments were subject to because of the immediate and unstoppable transfer of core municipal competencies to Belgrade, diminished in a great extent the range of effectual activities in the local level until the year 1999.

This situation created by illegal, violent and discriminatory measures, had provoked the total boycott of these authorities by the Albanian population, which proclaimed their own constitution and organized their own parallel central and local government structures. The municipal tier of the government was coordinated by the Coordination Council of the Municipalities of Kosova, which was formed by the legal of the municipalities. This was a structured form of non-violent resistance and self –government. It carried out some basic governmental functions in the local level and provided limited public services (budget, education, science, culture, sports, and social welfare).

ANNEX 2

USAID Community Infrastructure and Services Program (CISP)

USAID is effectively promoting the initiatives of communities in Kosovo to restore normalcy and encourage self-determination and self-reliance. One of the principle interventions under this strategic objective is the Community Infrastructure and Services Program (CISP). By supporting the rehabilitation of infrastructure prioritized by communities, it contributes to the reestablishment of the necessary conditions for normalcy, and future economic and social development. Community participation and “buy-in” in the infrastructure projects, and commitments for ongoing maintenance and operations helps to develop a sense of ownership and responsibility. The program also develops administrative and managerial skills in communities, municipalities, and distribution utilities to help Kosovars effectively exercise the objectives of self-determination and self-reliance.

The CISP project cycle starts with the identification of potential projects, in conjunction with community representatives, and collaborating NGOs, utility companies, Kosovo Force (KFOR), and United Nations Mission in Kosovo (UNMIK) counterparts. Those projects demonstrating high levels of community participation and support, community commitment to cover operational costs after the project is completed, and significant socioeconomic impacts then go through a collaborative design and implementation planning process.

Community participation and “buy-in” commitments are specified in memoranda of understanding, which outline co-financing arrangements, community contributions, the ongoing operational and maintenance support requirements, and the sources of support. All projects also carry the requirement to develop “business plans”, an exercise which compels the community to consider management, budget, customer service, and cost recovery issues, and the steps necessary to resolve them.

The rehabilitation activities then are implemented through competitively selected local contractors, overseen by implementing partners. Projects include electricity and water distribution system upgrades, feeder roads, bridges, schools, health facilities, and to a lesser extent, community centers, libraries, and sports facilities. All projects are focused on facilities that suffered damage during the conflict, or are dysfunctional from years of neglect. The rehabilitation efforts result in tangible improvements in levels of service for the communities, leading to restored conditions of normalcy.

To date, 132 projects have been completed, serving the priorities needs of over 700,000 people with improved levels of service. The average cost per project is \$42,500. 55 projects have been completed in ethnic enclaves or mixed communities. An additional 82 projects are under construction or in the planning stages for implementation in calendar year 2002. USAID’s objective through the end of 2003 is to rehabilitate a total of 300 sustainable community infrastructure projects throughout the province.

To foster even stronger community buy-in and to promote greater degrees of self-reliance, projects under development in 2002 will carry with them the requirement for a minimum community contribution (15 percent of project value) prior to undertaking rehabilitation work. More rigorous business planning will be required as well, to ensure operational and financial sustainability. This will further encourage communities to adopt participatory planning, budgeting, and revenue enhancement mechanisms and foster greater degrees of self-reliance and determination.

The effective provision of public utilities, primarily electricity and water distribution services, is widely recognized as the sine qua non of “normalcy” in the province. Yet, the viability of utilities is seriously constrained by uncontrolled technical and commercial losses; poor billing and collection rates; limited financing capacity to rehabilitate, maintain or expand service delivery; and weak managerial and administrative capacity. Over the past year, the CISP program has initiated a broad-based institutional strengthening effort for these utilities, whose service mandates cover 100 percent of the electricity and 60 percent of water consumers in the province.

Management capacity in utility companies was just as “decapitalized” following the conflict as was the physical infrastructure itself, so an important emphasis of the institutional strengthening effort was focused on establishing the requisite management, administrative, and operational skills (human capital) in these utilities. To date, structured and targeted training courses have been delivered to 84 water utility and 173 electric distribution utility managers in the areas of supervisory skills, management planning, accounting, financial management, and customer service. Additional courses in accounting, billing and collection procedures, and meter reading have been provided to non-managerial staff. 15 municipal water distribution utilities and all 7 electric distribution utility companies now have core management and technical staff with enhanced knowledge and skills in the operational and financial management aspects of utility management.

USAID also has supported accounting reforms in the electric distribution utilities to appropriately account for levels of service, customer invoicing and receivables, cash collections, and customer debt, and to institute controls to eliminate abuses in cash receipts. It also has supported an intensive effort to reconstruct customer databases in order to enable financial staff and management to properly track individual and collective levels of service, receivables, customer debt, and revenues.

The accounting reforms and databases will be automated in all electric distribution utilities in calendar year 2002. This automation will contribute to reduced commercial losses, improved collection rates, and improved financial viability of the utilities. It will enable the utilities themselves to assume the appropriate responsibilities for infrastructure rehabilitation, maintenance, and expansion in the future.

While the full impact of the reforms and institutional strengthening measures has yet to be felt, revenues of the electric utilities increased from approximately \$20 million in

calendar year 2000 to over \$45 million in the first 11 months of 2001. This impact, clearly the most significant impact brought about by the CISP program in 2001, will be deepened in 2002. The focus in the coming year will be on identifying and eliminating commercial losses, by significantly improving the billing rates (bills issued on distributed energy were a mere 55 percent in 2001), and continuing collection improvements (collections against billed energy increased from 36 percent in 2000 to 51 percent in 2001).

ANNEX 3

COMMUNITY DEVELOPMENT FUND (CDF)

The Community Development Fund is a World Bank initiative that channels investment to local communities for small-scale projects on a grant basis in a transparent and demand-driven manner. It has the status of a non-profit Foundation, and operates as an independent NGO under the supervision of the World Bank and its Board, composed of prominent members of Kosovar society selected for their professional expertise and their understanding of social problems in Kosova.

The CDF has 13 members of the professional staff and 5 ancillary staff. By qualifications, 11 have university degrees and 7 have high school qualifications. By gender, the professional staff has 8 women and 5 men. All staff is Kosovar.

Objectives

The objectives of the CDF are:

- To improve the quality and availability of community infrastructure and services in poor and conflict-affected communities.
- To support institutional capacity building at the community and municipal level so as to improve the quality and sustainability of service delivery and increase civic participation in local development.

Activities

The CDF finances small-scale infrastructure projects identified as priorities by communities themselves on a grant basis. The community is obliged to participate in the investment with minimum 15% of the value of the project. The total community contribution, however, will always depend on the size of the project.

CDF also gives grants to local NGOs and/or groups of citizens that identify projects of their priority and that are implemented to fulfill the needs of people with disabilities; women, especially those heading families, youth, and children.

Ever since inception, the CDF has completed a total of 98 projects in 24 municipalities. Of these,

- 72 are infrastructure projects (18 water supply networks, 12 sewerage networks, 13 school constructions, 4 school rehabilitations, 1 school gym, 2 cultural centers, 2 heating systems, 1 playground, 1 kindergarten, 8 road reconstructions, 1 irrigation canal reconstruction, 2 storm-water drainage systems, etc.) and

- 26 are social services projects (health education, literacy courses for children with disabilities and women, computers courses for children with disabilities, health education through puppet theater, anti-drugs and anti-AIDS campaign, civic education, youth programs, young ecologists' programs, etc.).
- Currently, there are 39 infrastructure and 22 social services projects under implementation.

It is CDF's strong conviction that the communities, if given a chance, can self-organize and find solutions to their problems. In a Kosova that ended up devastated by war, with over 700 villages almost completely destroyed, and without any investment in rural infrastructure for over 40 years, finding communities that need assistance in order to upgrade their living standard is not that hard. Yet, in these circumstances, and in view of the limited availability of funds, priorities need to be set.

CDF initially approached the communities that had been most damaged in terms of housing. Always insisting on the financial participation of the communities in the realization of the projects, CDF triggered a process, which had been put aside following the end of the war. It indirectly forced the communities to self-organize, create a local committee, or make use of the old structure of the local communities from the past, in order to decide upon a priority for the village.

In the vast majority of the cases, there was clear agreement among members of different families (or clans), or even neighborhoods, when deciding what would the village profit from, if there were a donor to help them. In cases when there were disagreements, CDF would usually give the community a second chance to sit down and discuss how to come to the solution of their problem. If there were no agreement after the second round of talks, CDF would withdraw from the eventual project.

CDF's approach towards communities' meetings was to let the community self-organize the way they wish. Insisting on a participating percentage of women or youth in these meetings was not CDF's approach. If it would be ascertained that women, in fact, didn't participate in the meeting, separate, informal talks would be made at the village level, in order to sense the feeling of the rest of the community. Generally, in cases of water supply, sewerage and schools, there was absolutely no objection from one single member of the community.

The prioritization of projects by the community led to the organization of contribution gathering around the village, household by household. In most cases, the village committees are organized in such way, that they have a clear idea on how much each household can contribute, and would go for the option of scaling the contribution, based on the economic situation of each individual household. This led to the creation of an internal control mechanism among the villagers, in order to assure that the collected funds will end up invested in a project.

The second step to that was to make the community think about sustaining the project in the future. The fact that the community needed to contribute financially to the project, ensured ownership of the community over the project. Second, a team of, usually, more educated people, would then sit around and discuss how to organize an informal user's association to further sustain the project – either by sorting out a fee-payment scheme, or having the capacity to intervene, on an ad-hoc basis, whenever necessary.

Last but not least, was establishing a connection between the communities and the local governments. Not one single project implemented by the CDF has been executed without proper municipal documentation and permits. Construction and other types of permits needed to be requested by the community, whose representatives approached the Municipality in order to obtain them. The effect here was double-fold: one, the communities could request the realization of their rights by approaching the municipalities and requesting them the fulfillment of a technical requirement that would solve their problem, and thus inform the municipality of their intentions, and two, the municipalities got direct information from the communities of the infrastructure investments done in their area, and could exercise their quality control over the works.

What CDF assumes is that from this working process, the communities have learned -

- To democratically decide upon their priorities;
- To push for the realization of their project, even when the Municipality was reluctant to issue corresponding permits;
- That a tender process can be fair, if rules set are fully respected;
- That they can freely express their dissatisfaction if the quality of works is not acceptable;
- That they need to take care of a project granted to them, because there will be no CDF that will take care of it, once the project is finished.

On the other hand, during its two years long experience, the CDF has also had to deal with Municipalities. At first, it was in times prior to local elections, when international staff administered the municipalities. Later, it was after the assemblies were constituted that CDF started establishing contacts with elected local governments.

The experiences were different, but could be summarized like this:

- Wherever there were municipal administrators that had a clear vision of development, the projects went smoothly;
- Wherever there were municipal officers that had a developmental vision, regardless of political and local sympathies, the projects went smoothly;
- Often, elected municipal officers tend to try to impose the priorities drafted by the elected officials on CDF, without taking into account the opinion of the local communities;
- There is no unique mechanism, procedure or system by which the municipalities will collect data on the needs of the communities, based on the list of priorities that each

single community might be setting. This will always be an obstacle to achieve something by communities that have no representation in the municipal assemblies;

- Patterns of the former municipality structures – bureaucracy, laziness and corruption, are visible in many municipalities CDF had to deal with. Trying to evade the strict WB procurement rules, by trying to push for contractors known to municipal structures or officers, is an often, repeating, phenomenon.
- If clever, both pragmatically and politically, municipal officers will authorize financial contribution to CDF projects, because with a small usage of revenue funds, the Municipality will profit from substantial projects that will improve living conditions in, mainly, rural areas.

One of the main conclusions that could be drawn from what was said above is that communities that fight for the implementation of such projects are determined to stay in their villages – in one way or the other, they see their prospects there. Now, in order for rural development to function, such communities need to be offered other types of assistance – employment, first of all. Will this be employment in the agricultural sector or small or medium production-enterprises that is another issue – and depends on availability of funds, planning and market orientation. Bearing in mind the congestion of towns with huge fluxes of rural population with little or no chances for employment, developing the rural areas would be a good solution for Kosova.

And, development starts with basics – education, health, culture, access to markets and jobs: a starting point for self-sustainability.

ANNEX 4

EXPERIENCE OF COUNTRIES IN TRANSITION ON ISSUES OF LOCAL FINANCE

A number of municipal functions are for the benefit of local population and therefore they are the responsibility of the municipalities because they can be most efficiently performed at that level. Most often the total cost of those expenditure responsibilities typically exceeds the revenue capacity of the local government. Therefore, in the Local Self-Governments world over, some difference between local revenues and local expenditure needs is almost universal.

Devolution of important fiscal responsibilities to municipal governments in Kosova represents a major step in turning over responsibility for managing their own affairs to the citizens of Kosova. The fiscal aspect of the devolution has led to the need for the design of a system of grants from the central to the local level of Government.

The experience of countries that have addressed the transition process shows that municipal governments should really identify and define their own priorities in respect of economic and social development. But that, however, does not imply that they should be at variance with the national priorities. Rather local priorities should be subordinated to the national priorities thereby avoiding any conflict in the links with the higher tiers of the government.

The local governments take the functions and responsibilities that result in their large expenditure responsibilities that correspond what municipalities are typically responsible for throughout the world and what they should be responsible for according to the generally accepted principles of public finance. The cost of providing the public services and the availability of own source revenues of municipalities to finance those expenditures are the difficult questions even in a developed economy.

The interest of the local authorities to have discretionary power in determining the budget issues is reflected in the following four basic elements that are related to the process of devolution:

- Local autonomy for the fulfillment of public needs often unique to local environment,
- The generic character of local government in relation to the needs it has to address,
- The democratic character of local government representing the local community, and
- The managerial character of the economic infrastructure that is intertwined with local government

In the above background, it is interesting to note the characteristics of the taxation systems of some transition economies in Eastern Europe as listed in the table below:

Table 4: Local and Central Taxation in some countries in Eastern Europe

	Czech Republic	Estonia	Hungary	Romania
Local taxes: share in overall taxes (%)	12	14	9	10
Taxation Structure at the Central Level				
Income and profit tax	14	18	21	31
Tax on domestic products and services	36	5	37	27
Social insurance contribution	46	36	33	31
Other taxes	4	41	9	11
Taxation Structure at Local Level				
Income and profit tax	90	90	50	8
Property tax	5	9	11	15
Other taxes	5	1	39	77

Source: LGI Studies: Local and Regional Tax Administration in Transition Countries, Edited by Mihaly Hoge, Budapest 2000, page 60

In some of the transition countries both pension and unemployment costs were partially transferred to local governments including central government subventions (e.g. Albania, Bulgaria, Hungary, Russia, Ukraine) ¹. In other transition economies these costs were accounted for by the social insurance schemes for assisting the poor families. There are numerous examples of the transfer of the administration of some state enterprises from the central to the local governments that reflect greater participation of the local governments in the privatization process.

However, most of the local governments did not succeed enough in accomplishing the given tasks. Therefore, even now they heavily rely on the government transfers.

¹ Riinvest: Key Issues in Building Taxation Policy in Kosova, 2001.

Table 5: Central and Local Expenditures in some transition countries

Country	Share of governmental expenditure in the GDP			Share of local expenditure in overall government expenditure (%)
	Overall	Central	Local	
Albania	44.00	-	-	-
Bulgaria	41.2	-	9.9	24.1
Hungary	57.2	31.9	17.4	30.4
Poland	48.1	31.8	5.9	12.3
Romania	35.6	21.7	3.7	10.4
Russia	39.6	20.3	17	42.9
Ukraine	73.4	57.5	20.9	28.5

Source: Riinvest, Key Issues in Building Taxation Policy in Kosova, June 2001

The share of the local government expenditure in the state budgets of some Central European countries over five years is presented below. It indicates that in most countries it has remained constant or declined marginally except in Poland where it has increased considerably.

Table 6: Share of local government expenditure in state budgets of some countries of Central Europe

Country	1994	1995	1996	1997	1998
Estonia	33.1	31.4	29.8	28.1	30.6
Latvia	26.0	26.2	26.2	24.2	25.2
Lithuania	32.7	31.8	28.7	22.9	-
Poland	19.0	19.1	24.6	26.8	34.0
Czech R.	20.6	20.8	18.8	16.6	-
Slovakia	11.8	11.0	12.0	12.2	13.9
Hungary	26.7	26.6	27.2	25.5	24
Slovenia	11.5	10.1	10.8	10.5	9.2

Source: LGI Books: DECENTRALIZATION: Experiments and Reforms, Edited by Tomas M. Horvath, Budapest, 2000, pg. 54.

ANNEX 5

LEGAL RELATIONSHIPS BETWEEN THE PUSPs, THE REGULATOR, AND THE MUNICIPALITIES

The role of the KTA and the PURCK in the functioning of public utilities

The following is a brief review of the legal relationships between PUSPs, the regulator, and the municipalities that is outlined in the pending legislation.

The power to manage and regulate state and socially owned enterprises in Kosova lies with the SRSG as part of his reserved powers. Today, all PUSPs in Kosova are state-owned enterprises. As such, the SRSG, not the provisional institutions of self-government controls the development of all sectors and govern the relationship between PUSPs and the municipalities where services are delivered.

In the area of public utilities, management and regulation are two sides of the same coin. Only when the management function and the regulatory function work in harmony can public utility services be improved. Only when laws clearly govern each function can management and regulation work. Although management of the PUSPs falls within the control of the Kosova Trust Agency (the “KTA”), the regulation of these enterprises lies within the purview of the Public Utilities Regulatory Commission (the “PURCK”).

The regulation establishing the Public Utilities Regulatory Commission of Kosova (the “Regulator”) and the sector specific regulations that sit under the Regulator’s “umbrella” provide specific rules for each sector controlled by the Regulator. The PURCK regulation and the Sector specific laws provide for the restructuring and corporatization of all existing PUSPs and for public tenders for private sector participation to provide the services in each sector on a rigid time frame.

The Regulator does not run companies. It merely establishes rules and requirements that each PUSP must fulfill and which are intended to improve customer services. The functions of the Regulator in Kosova are modeled on international best practices and include all of the above activities:

1. granting license and permits for service providers in each sector pursuant to the applicable regulations;
2. levying charges and fees for Licenses, permits and authorizations; and for other services provided by the Regulator;
3. regulating the setting of tariffs, rates, charges and fees levied by PUSPs;
4. establishing standards and codes of practice for PUSPs;
5. establishing a system of fines, penalties and other remedial measures in the event that PUSPs breach their obligations under either their licenses or applicable law;
6. advising the SRSG on Sector specific matters as requested;

7. monitoring PUSPs in respect of technical and economic standards and establishing reporting procedures that facilitate that process;
8. establishing rules that promote market access on a non-discriminatory basis and the development of a competitive markets in the utilities sectors, including rules related to the conduct of public tenders for new market entries;
9. developing and implementing a system for receiving and responding to complaints by customers, PUSPs, and, as applicable, municipalities;
10. promoting the development and introduction of new technologies within each Sector; and
11. developing a system for conducting hearings and investigations necessary to collect the information required to accomplish all of the duties set out above.

Under the draft regulations, the Regulator is specifically required to coordinate its activities with other state organs having jurisdiction over certain aspects of the service provider's activities, including ministries or agencies responsible for competition, environmental protection and consumer protection, and with the municipalities.

For its part, the KTA will also undertake the task of making all PUSPs more efficient, both technically and financially. Under these new laws, all existing PUSPs will be restructured according to their core competencies. Water companies will be separated from waste companies (18 of the existing 31 water companies also provide solid waste services), and each new company will be required to obtain a license from the Regulator to provide its services.

The Role of the Municipalities in the Functioning of Public Utilities

The role and function of the SRSG and its emanations, the KTA and the PURCK, have been clearly identified. It is clear, however, that the delivery of public utility services is in many cases a municipally based activity and heavily involved with municipal governments that are obligated to provide municipal services to its citizens. The legislative framework has taken all of these facts into consideration in developing the future architecture for each of the Sectors. It is envisioned that the municipalities will have a close working relationship with all public utility service providers, whatever their ownership structures may be.

The PURCK regulation and the Sector specific regulations will require restructuring and corporatization of each PUSP. They will also require unbundling of functions, separation of assets according to function, and financial unbundling to reflect economic reality. Cross subsidization will be closely scrutinized. These activities will be accomplished by the KTA as custodians of the existing PUSPs and the PURCK will monitor the KTA to ensure that these activities occur within the time frames specified in the relevant Sector regulation. Licensing requirements for all PUSPs will require openness and transparency in the conduct of all of these issues. The PURCK will also require that the PUSPs and the municipalities that they serve operate openly, transparently and commercially.

PUSPs will work closely with the municipality in the following areas:

- Municipalities shall hold voting positions on the Supervisory Boards of each publicly owned PUSP, together with appointees of the KTA. As such municipalities will be voting members and decision makers within the respective PUSPs.
- Municipalities and PUSPs will conclude service agreements approved by the PURCK that clearly define the rights and obligations of each party.
- Municipalities will participate in the tariff setting processes of the PURCK that effectively establish the tariffs which will be charged by a PUSP for the delivery of the services established in the service contracts.
- Municipalities and PUSPs will work together to create development plans for the respective municipality, and the costs of expanding services pursuant to the development plans will also be reflected in the tariffs approved by the regulator.
- In many instances municipalities and PUSPs will cooperate in the collection of fees related to the delivery of Sector services within the municipal service area.
- Municipalities and PUSPs, will work together under the guidance and monitoring of the Regulator to deliver improved quality services to municipal customers, and to address customer complaints, directed first to the PUSP, then to the Municipality, and finally to the Regulator.
- The municipality will have the power to request that the Regulator call public tenders for the purpose of attracting new market entries into the Sector and the municipality's service area.
- The municipality will have the right to invoke the dispute settlement procedures established under law for the resolution of disputes between municipalities and service providers, and to seek recourse through the courts in the event that the decision of the Regulator fails to satisfy the particular claim of the municipality.

The foregoing discussion clearly reflects the partnership relationship that is intended to exist between the Regulator, the PUSPs and their managers, and the Municipalities. Each of the parties has obligations to deliver services under the tri-partite arrangement, and the laws that soon will govern and regulate the Sectors effectively provides that each party will be adequately and fairly represented in the process of delivering PUSP Sector services.

ANNEX 6

STATISTICAL INFORMATION ON LOCAL ECONOMIC DEVELOPMENT

SME RESPONSE TO LED ISSUES

Extracts from the results of Riinvest SME Survey 2001

Background

One of the important survey and research activities of Riinvest has been for supporting the development of Small and Medium size Enterprises (SMEs) in Kosova. In order to develop understanding of the current situation and elicit views of the owners/managers of SMEs, Riinvest earlier carried out three SME surveys during the years 1997, 1999 and 2000. The fourth survey was recently carried out in December 2001. The survey results are very useful for Riinvest to make policy recommendations that will facilitate SME and entrepreneurship development.

SME response to LED issues

SME survey 2001 collected information relating to Local Economic Development. The business enterprises were asked to give opinion regarding the quality of support they receive from the local governments. The questions in the survey were as follows:

1. How would you evaluate the support of the local government for your business?
 - a) Good
 - b) Unsatisfactory
 - c) Bad

2. In which field do you receive support of the local government?
 - Facilitation in finding the right location
 - Support to create new contacts with potential investors
 - Building the infrastructure (roads, power, communication etc.)
 - Providing with important information that is relevant for business
 - Benefits for conducting administration procedures
 - Benefits for establishing new companies
 - Favorable policy for fees and charges

2. Do you have any cooperation with NGO in your municipality?

- a) Yes b) No

4. If yes, what kind of cooperation do you have:

- a) Coordination that is related to decision-making activities in your municipality;
- b) You sell your products to them;
- c) You receive information from them for improving your activities.

5. Does municipal government have the same approach to all SMEs

- a) Yes
- b) No
- c) I do not know

The results of the response to these questions are provided in the tables that follow. The methodology followed for composition of survey sample size and selection of companies for the survey is explained below.

Survey Sample

The first three SME surveys of Riinvest had a sample size of 300 enterprises and the same enterprises were surveyed every time. For SME 2001, Riinvest doubled the sample size and the selection of businesses was made on the following basis:

- Total sample size of 600 enterprises
- 200 companies were selected from the previous sample that included 300 companies
- 300 new companies were selected by random sample
- 100 sole proprietors were selected by random sample

The selection of 300 new companies was made on proportional basis by sector of activity and stratified by size-class. The size-class was defined on the basis of number of employees in the enterprise, as follows:

Micro Enterprise - 1 to 9 employees;
Small Enterprise - 10 to 49 employees;
Medium Enterprise - 50 to 250 employees; and
Large Enterprise - Over 250 employees.

Since the sample base comprises 1.9% small sized and 0.3% medium sized enterprises and 97.9% micro enterprises, it was necessary to do the stratification to ensure that the sample has enough small and medium sized companies.

Sample Selection procedure

1) Established the full sample base by creating a database of 29,564 enterprises in the Register of Companies published by Statistical Office of Kosovo. The Register provided the information for all the enterprises by sector, by size-class, by number of employees, location, address and phone number.

2) Out of the 29,564 enterprises 13,628 are the companies that were selected as the relevant sample base for the Survey. The information available in the register for these companies was then coded and recorded by using four size-classes, namely, micro, small, medium and large and by three sectors, namely, production, services and trade.

3) On Analysis of the characteristics of a full random sample important variables were determined as sector, size-class and location. It was found that there are very few companies in the sample base that are in the class of medium and small enterprises and more than 97% of these companies were micro enterprises.

The number and distribution of these companies in the register by sector and size-class is as follows:

Sector/Size-class	Micro	Small	Medium	Large	Total	% in Total
Production	3,676	137	19		3,832	28.1 %
Services	2,354	55	5	1	2,415	17.7 %
Trade	7,303	67	11		7,381	54.2 %
Total	13,333	259	35	1	13,628	100.0 %
% in Total	97.8 %	1.9 %	0.3 %	0.0		100.0 %

If the sample selection was made in proportion to size-class, the number of companies, it would have the following composition:

Micro Enterprises - 294
 Small Enterprises - 6
 Medium Enterprises - 1

4) Thus the sample selection on the above basis would have led to have an insignificantly small number of small and medium sized enterprises. It was, therefore, decided to take a stratified sample by size-class and in proportion to sector and location. The purpose was to have enough companies in each size-class comprising micro 55%, small 40%, and medium 5%.

6) Thereafter the decision was made about how many companies should be in the sample size when compared to the sample base. Since a part of the businesses in the register were not available to access at the address recorded in the register, it was decided to select a sample of 600 enterprises, which is double the number of enterprises in the earlier survey that had sample of 300 enterprises. Thus, the number of companies selected from the register by size-class and sector is as follows:

Sector/Size-class	Micro	Small	Medium	Total
Production	91	127	16	234
Services	58	51	4	114
Trade	181	62	9	252
Total	330	240	30	600

7) For selecting a sample of 600 enterprises, first a sample was drawn by size-class, then a random number was assigned to each company and the data was sorted in an ascending (or descending) order and then the first appropriate number of enterprises was included in the sample.

8) The proportions in the selected sample were checked and compared with those in the sample base.

9) The above procedure resulted in selection of 600 enterprises as the sample for survey. A separate file with the names and other information about these 600 enterprises was created and the survey questionnaire was administered on all them.

10) For random selection of the sample of 100 sole proprietorships, the sample was taken from the registers of local registration offices. The sample was in proportion to the sole proprietorships in seven main regions of Kosova. Using sample base of the Statistical Office of Kosova, the proportion of sole proprietorships was calculated and the sample size of 100 sole proprietorships was distributed accordingly among the seven regions.