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Commercial Legal and Institutional Reform (CLIR) Diagnostic Assessment Report for Albania



A USAID Initiative in Developing Countries

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I. INTRODUCTION

A. OVERVIEW

The Republic of Albania emerged nine years ago from over 44 years of isolation from the world economy and culture. Unlike its socialist neighbors from the former Yugoslavia, it did not interact with either the Western democracies or the former Soviet Union, but closed its borders and attempted to control the flow of information and ideas under a strict command government. Increasing access to information in the 1980s through international advances in broadcast and communications technology, along with the political changes in the Balkans and Eastern Europe occasioned by the break-up of the former Soviet Union and the collapse of communism, helped

Broad Indicator	Albania	Croatia	Kazakhstan	Macedonia	Poland	Romania	Ukraine
Population (millions) ¹	3.49	4.28	16.73	2.04	38.65	22.41	49.15
Area (km2)	28,748	56,538	2,717,300	25,333	312,685	237,500	603,700
1999 GDP Per Capita ²	\$1,650	\$5,100	\$3,200	\$3,800	\$7,200	\$3,900	\$2,200
% GDP Ave. Annual Growth (1990 – 1999) ³	2.3	-0.4	-5.9	1.9	4.7	-1.2	-10.8
% GDP - Agriculture	54	9	10	11	4	16	14
% GDP - Industry	25	32	30	28	33	40	34
% GDP - Manufacturing	--	21	23	--	20	30	29
% GDP - Services	21	59	60	60	63	44	51
Foreign Aid Per Capita ⁴	\$72.50	\$ 8.70	\$13.30	\$45.80	\$23.30	\$15.80	\$7.60
Corruption Index ⁵	N/A	3.7	3.0	N/A	4.1	2.9	1.5
Economic Freedom Index ⁶	3.70	3.50	3.70	N/A	2.80	3.30	3.60
Government Effectiveness Rating ⁷	-0.653	0.150	-0.824	-0.576	0.674	-0.570	-0.893
Regulatory Framework Rating	-0.700	0.236	-0.405	-0.312	0.565	0.199	-0.721

¹ CIA World Factbook, July 2000 estimate.

² CIA World Factbook; 1999 estimate.

³ World Development Report 2000/2001, published by The World Bank. Applies to GDP Growth and the agriculture, services, manufacturing, and industry composites of GDP.

⁴ The World Bank: <http://devdata.worldbank.org/query>. Figures are from 1998 and are in current US\$. As a point of comparison, foreign aid per capita in all developing countries is \$8.40.

⁵ Transparency International 2000. Scale = 1 - 10. Higher scores indicate less corruption.

⁶ 2000 Index of Economic Freedom Rankings, The Heritage Foundation (www.heritage.org). Scale: 1-1.95, free; 2-2.95, mostly free; 3-3.95, mostly not free; 4-5, repressed.

⁷ Worldwide Governance Research Indicators Dataset, The World Bank. Governance indicators reflect the statistical compilation of perceptions of the quality of governance of a large number of survey respondents in industrial and developing countries, as well as non-governmental organizations, commercial risk rating agencies, and think-tanks during 1997 and 1998. Governance indicators are measured in units ranging from about -2.5 to 2.5, with higher values corresponding to better governance outcomes. This footnote applies to the Government Effectiveness Rating, Regulatory Framework Rating, and Rule of Law Rating. Available at <http://www.worldbank.org/wbi/governance/datasets.htm#dataset>.

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Rule of Law Rating	-0.918	0.146	-0.590	-0.256	0.538	-0.088	-0.707
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to destroy the xenophobic myths used to enforce the isolation. With the death of President Hoxha in 1985 and the changes going on throughout Europe and the Balkans, the totalitarian Albanian state finally collapsed, leading to new approaches for the 1990s.

Emerging from its self-imposed cocoon, Albania entered the modern world with only minimal understanding of, and preparation for, democratic government and market economics. The international community was quick to supply aid and technical assistance as the formerly controlled economy fell apart and Albania began to find its way. In the nine years since the opening began, the country has made significant progress, but is still a long way from economic and political health and stability.

For the past several years, economic indicators have been positive, showing both increasing stabilization and much-needed growth. For the past five years, with the exception of 1997 when extensive national pyramid schemes collapsed and consumed 60% of the GDP, Albania has enjoyed annual growth rates of 7-8%. Last year, the currency moved from slow inflation to deflation, and has remained strong. The balance of trade, however, continues at unsustainable negative levels. Substantial investment will be needed in agriculture, industry and services in the short and long term to revive existing productive sectors and create new ones.

To enhance growth, Albania needs a modern legal system that permits investment and credit, and adequately provides for resolution of commercial conflict. Much of this system must be built from scratch, for Albania does not have an established history of commercial law to build upon. After gaining independence with the demise of the Ottoman Empire in 1912, the country had barely established a monarchy before becoming engulfed in World War I. A brief democratic experiment took place after the war, but was eventually extinguished with the advent of fascism in the 1930s. By the time of Hoxha's consolidation of power after World War II, totalitarian government had become the rule, and would stay so until 1991. Xenophobia, in great part inspired by the stated desires and actual attempts of its neighbors to acquire Albanian territory during the two World Wars, left the country opposed to Western and Soviet influence, and aligned with Communist China. The growth that might have taken place through relationships with its European neighbors was stunted almost at the outset, and is only now being addressed.

B. PROJECT BACKGROUND

The United States Agency for International Development has been providing assistance to the Republic of Albania since 1993, including substantial technical assistance in legal and judicial reform. In order to better understand the current status of commercial legal and institutional reform for strategic planning purposes, the USAID Mission in Tirana requested this diagnostic assessment.

The diagnostic methodology employed for this assessment was developed for USAID with the assistance of Booz·Allen & Hamilton in order to identify progress and problems in commercial legal and institutional reform (C-LIR) programs in Europe and Eurasia. The methodology was designed 1997-98, then field-tested in Kazakhstan, Poland, Romania and Ukraine from 1998-99.

At a workshop in Prague in December 1999, USAID and Booz·Allen submitted the results and methodology to a group of 50 legal reform professionals for their analysis and comment. The results were broadly affirmed, along with the overall approach. Revisions based on workshop input were made early this year, and two more assessments were performed, this time in Croatia and Macedonia. This is the third assessment done since with the revisions. In the coming months, some additional revisions will be made based on this new experience, and a handbook produced.

C. NOTES ON SCOPE & METHODOLOGY

The diagnostic assessment was designed to help achieve the following objectives:

1. To provide a factual basis for characterizing the degree of development and the status of commercial law reforms in Albania since its re-emergence into the world economy in 1991;
2. To provide a methodologically consistent foundation for identifying and describing the root causes of the "implementation/enforcement" gap; and,
3. To provide analytical and planning tools and metrics that will help USAID design new approaches to sustainable, cost-effective C-LIR interventions in Albania.

For the purposes of most assessments, "commercial law" is defined to include the following substantive legal areas:

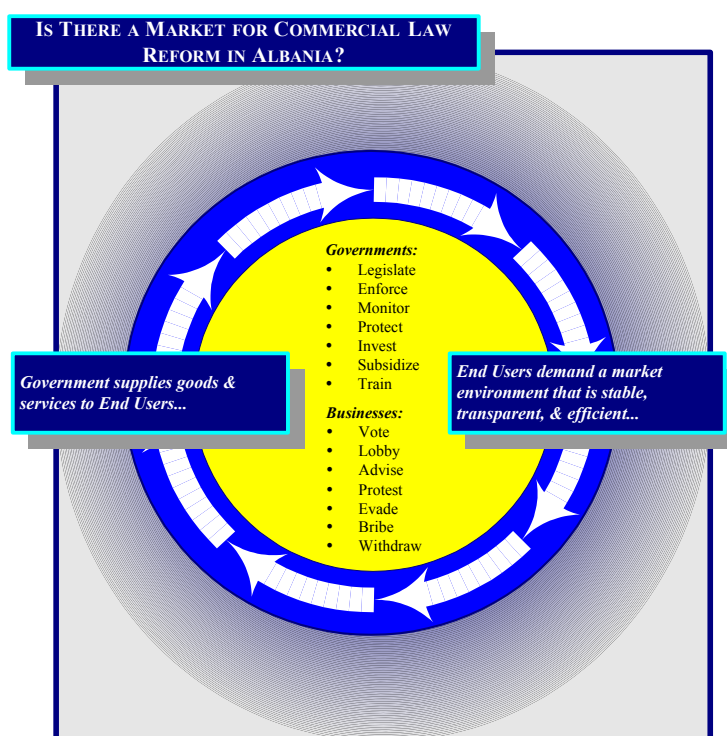
- **Bankruptcy** - Mechanisms intended to facilitate orderly market exit, liquidation of outstanding financial claims on assets, and rehabilitation of insolvent debtors.
- **Collateral** - Laws, procedures, and institutions designed to facilitate commerce by promoting transparency, predictability and simplicity in creating, identifying, and extinguishing security interests in assets.
- **Companies** - Legal regime(s) for market entry and operation that define norms for organization of formal commercial activities conducted by two or more individuals.
- **Competition** - Rules, policies and supporting institutions intended to help promote and protect open, fair, and economically efficient competition in the market.
- **Contract** - The legal regime and institutional framework for the creation, interpretation, and enforcement of commercial obligations between one or more parties.
- **Foreign Direct Investment** - The laws, procedures and institutions that regulate the treatment of foreign direct investment.
- **Trade** - The laws, procedures, and institutions governing cross-border sale of goods and services.

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For this assessment, however, only four areas have been examined: Bankruptcy, Collateral, Company and Contract. Although not studied in depth, a number of observations were possible for the other three areas (Competition, Foreign Direct Investment, and Trade), and brief comments are included in the report below.

Each of these substantive areas was assessed by collecting data in Tirana during a two-week period in September 2000. Within each of these substantive areas, four "dimensions" of C-LIR were examined as a conceptual framework for comparison. These include:

- *Framework Law(s)* - Basic legal documents that define and regulate the substantive rights, duties, and obligations of affected parties and provide the organizational mandate for implementing institutions (e.g., Law on Bankruptcy, Law on Competition);



- *Implementing Institution(s)* - Governmental, quasi-governmental or private institutions in which primary legal mandate to implement, administer, interpret, or enforce framework law(s) is vested (e.g., bankruptcy court, collateral registry);

- *Supporting Institution(s)* - Governmental, quasi-governmental or private institutions that either support or facilitate the implementation, administration, interpretation, or enforcement of framework law(s) (e.g., bankruptcy trustees, notaries); and,

- *"Market" For C-LIR* - The interplay of stakeholder interests within a given society, jurisdiction, or group that, in aggregate, exert an influence over the substance, pace, or direction of commercial law reform.

II. GENERAL COMMENTS ON THE STATUS OF ALBANIAN COMMERCIAL LAW

A. COMMON THEMES

Unlike a country such as Croatia, which had a strong legal tradition to build upon when emerging from socialism, Albania has no strong history of modern law. The *kanun*, an expression of traditional law that developed during the Middle Ages, still informs and influences many social arrangements, but there are few well accepted statutes from before 1991 to build upon for commercial activity.

The international community has helped address this legal abyss by assisting with substantial reforms in the past nine years. As a result, all of the commercial laws examined for this assessment are new, with the oldest (the Civil Code) adopted in 1992. As a further consequence, all of the laws are relatively modern and generally reflect modern European traditions and norms.

This is reflected in the comparative scores below taken from C-LIR assessments done in Macedonia, Poland, Romania, Ukraine, and Kazakhstan. Albania has the highest scores for legal framework (85%), better even than Poland (84%). For all other areas, however, Albania falls well below Poland, but compares favorably with Macedonia, Romania, and Kazakhstan, except in Implementing Institutions. Only Ukraine consistently performs below Albania.

	Albania	Mac	Pol	Rom	Ukr	Kzk
AGGREGATE TOTALS	53%	57%	77%	54%	41%	54%
1. Legal Framework	85%	79%	84%	69%	58%	67%
2. Implementing Institutions	52%	53%	79%	56%	42%	57%
3. Supporting Institutions	33%	47%	70%	50%	34%	46%
4. Market for Reform	44%	48%	74%	40%	28%	48%

In the other assessments done with this methodology, much attention has been paid to the need for revising laws and improving the legal framework. For Albania, this has not been the case. The complete newness of the laws and the legal traditions has led to an unusual situation in which most of the observations apply across the board to all areas of commercial law.

To address these broad areas, general comments are set forth below. In addition, analysis of the courts and most supporting institutions have been examined most thoroughly in part E - Contracts.

1. Legal Framework

Process. In extensive interviews with more than 50 people, the most frequently heard commentary on Albanian commercial legislation was that the laws are generally good enough, but need to be implemented. The team found this to be true in examining the framework laws. Revisions can certainly be made, and should be, but the focus of assistance at this point should be less on substantive issues and more on process.

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Judges, lawyers, businesspeople and even members of Parliament uniformly agreed that there is no formal mechanism for engaging stakeholders -- particularly the private sector -- in the formulation, revision, or adoption of legislation. Several government officials responsible for legislative drafting noted that they generally provided drafts to some groups for comments, but they cited personal conviction rather than mandatory regulations as their reason for doing this. This conviction leads to some private sector feedback, but the approach is not predictable and does not capture a broad enough section of those who will be affected by the laws.

ALBANIA	Aggregate	Bankruptcy	Collateral	Company	Contract
1. Legal Framework	85%	90%	91%	75%	84%
2. Implementing Institutions	52%	21%	80%	54%	51%
3. Supporting Institutions	33%	16%	58%	21%	35%
4. Market for Trade Liberalization	44%	24%	71%	32%	50%

There appears to be a window of opportunity for creating an interactive, participatory process for drafting legislation. First, a number of respondents responsible for or involved in legislative drafting noted their practice of seeking comment from private sector interest groups, suggesting that there is at least a core group of officials who understand the need for such input. Second, several members of Parliament interviewed indicated a desire for more assistance from the donor community, suggesting that there might be an increased sense of receptivity from Parliament for technical assistance. Third, the private sector, as well as the judges, indicated that they want and need a formal mechanism for communicating their interests and their findings on the need for new or revised laws. (The judges pointed out that although they deal with gaps in the law, they have no way of making sure the identified gaps are eventually filled.)

Creating such a mechanism will not only support the development and refinement of Albanian law, it will have a number of other important benefits. Meaningful involvement will help to remove the often heard complaint that these laws are German or French but not Albanian. Feedback and comment would allow the drafts to be adjusted to the Albanian context and to build a sense of ownership where little currently exists. This should provide greater support for implementation as the private sector has notice of new laws and accepts the laws as its own. In addition, the participatory process builds respect for and commitment to democracy itself by reinforcing the concept of accountability of government officials to the electing constituency in a culture where government by decree has been the rule. Finally, it increases socio-political stability by providing the private sector with a rational, formal system for voicing their needs. Though commercial law provides a context for creating such a system, it will be used for all law-making.

Education and Awareness. Another universal theme for all areas of law was ignorance of both law and commerce. Basic business concepts are not well understood or known among law makers, judges, lawyers or even much of the business community. With less than ten years in the modern world, Albanians face a bewildering array of new concepts, including modern commercial law. They still have little education or experience in these areas, and in many cases

are unable to absorb the plethora of new laws because they do not understand the underlying transactions that the laws regulate.

One of the best illustrations of the problem was presented by a lawyer who had assisted with the preparation of the 1994 bankruptcy law. When asked what he thought about the draft of the new bankruptcy law, he responded "What new law?" This level of (un)awareness was found throughout the legal community with respect to a wide variety of existing and proposed laws. It should be noted the system of relatively silent adoption of the existing commercial laws has worked against their implementation, and has left Albanians with a feeling that they have a set of foreign-imposed statutes, which they do not yet relate to effectively.

There is a crying need for education and awareness for all of groups before or in concert with the passage of any new laws. Simple "street laws" are being prepared by GTZ for broad publication and dissemination, but a focused campaign for priority areas such as credit and collateral will be needed before the country can effectively use or otherwise implement these laws. Without such assistance, new laws may even be counterproductive, like dragging a new swimmer into deeper and rougher water instead of teaching basic strokes.

Consolidation and approximation. Several legal professionals noted the need for a formal Commercial Code and for careful approximation of laws to European standards (for eventual membership in the European Union) and compliance with WTO requirements. If pursued in the manner of past legal reforms, these are not likely to be absorbable by the legal community, which cannot yet absorb the current changes. Even so, they express important issues.

The idea of a Commercial Code is more a preference than a need. Many civil law traditions do indeed set out their commercial laws in a separate Commercial Code, although many of the underlying concepts supporting commercial transactions are set forth in the Civil Code. On the other hand, many civil law countries have the approach currently employed in Albania of incorporating commercial laws within the Civil Code through specialized sections. It is hard to imagine a reason for replacing this perfectly acceptable system with another at this time. Perhaps it should be revisited in the long term, but should resisted in the near term.

Approximation and compliance are valid concerns. The issues are much more related to implementation than legislation, however. Most of the laws have been adopted in the shadow of WTO and the European Union, and if applied would generally harmonize. Recognizing this, support for harmonization and compliance at the legislative level should focus on a slower, deliberate process of identifying and addressing the areas of refinement on a biannual or other mid-term basis.

New laws. Despite the very conservative tone of this introductory section, it is recognized that some new laws will be needed from time to time as the existing laws are better applied. For example, one legal professional who works with foreign investors noted the need for a franchise law. In fact, the Civil Code covers franchise, but the respondent was correct that the nine articles do not provide sufficient coverage and need to be expanded through implementing or supplemental regulation.

But which new laws are needed? A supply side approach would compare Albania to a European country and start pumping in the new laws and regulations based on eventual investment and commercial needs. As already stated numerous times, the legal and business community cannot absorb such a project, which would have to be staffed and run by a team of foreign experts with little Albanian participatory capacity. A more effective approach would be to have the foreign and domestic business community, with input from the legal community, identify areas in which their existing or planned commercial activities are being constrained, and then identify which constraints are based on gaps in law rather than implementation or physical infrastructure. A national program of business roundtables or workshops could be used to identify and prioritize needs, and build the nascent business associations at the same time. Laws identified should then be fed into a formal mechanism of participatory legislative process.

2. Implementing Institutions

The courts are the principal implementing institution for contract and bankruptcy, a secondary implementing institution for collateral (in defining rights under collateral law), and a supporting institution for company, foreign investment, competition and trade. Clearly, they are fundamental to commercial legal and institutional reform. In Albania, they are fundamentally weak.

The courts were repeatedly cited for their lack of effectiveness in the tasks they are handling. This is understandable in light of Albanian history, but certainly not acceptable for Albania's future. The need for increased legal knowledge, increased transparency and reduced corruption were all noted. These are addressed in somewhat more detail in the section on Contract Law, below, but are mentioned here for emphasis.

The courts are undergoing positive change. USAID has helped to establish a Magistrates' School which is addressing the need for theoretical and practical training. The World Bank is about to commence a large scale project of administrative reform, including assistance in case management and court administration to help streamline and improve the process of justice. The European Commission, the Soros Foundation and others are also providing targeted assistance. Local leadership and commitment to reform are strong, so that the outlook for the judiciary is very good.

It is not clear, however, to what extent these projects will address the need for transparency through written, published judicial decisions. According to Albanian law, all judges must issue their final decisions in written form, but the practice of oral decisions, or written decisions without a legal basis is reported to be widespread. The newly established Courts Inspectorate may need assistance in learning to evaluate written decisions, and training will certainly be needed for judges who have never been trained in decision writing. Without strict enforcement of this law, it will be virtually impossible to turn the tide of reported corruption and establish confidence in the judiciary.

Assistance will be also be needed on a targeted basis as actual needs arise. For example, much of the education in bankruptcy will not be meaningful until some bankruptcy cases begin to filter through the courts. At that time, the business and legal communities could profit greatly from

direct assistance, using a bankruptcy case as a teaching opportunity, with expert assistance and public analysis, not unlike some highly publicized trials in the U.S. during the last decade.

3. Supporting Institutions

For all areas of law, the supporting institutions are generally weak, whether public or private. The specialized services, professional associations, special interest business associations, and other private sector associations found in a healthy civil society are generally weak or missing. One result is that any demand for change is difficult to coordinate or focus, and the actual changes are more difficult to supply.

Fortunately, a number of programs have begun to address some of the needs. World Bank is reported to have a program for the bailiffs and judicial enforcement agents, which will be critical in making commercial judgments meaningful. In education, there is also progress, including the Magistrates' School mentioned above and the Masters of Business Administration program being offered at the Faculty of Economics with funding from USAID through the University of Nebraska. Both of these have been very well received.

In addition, the World Bank will soon be instituting a program of assistance in legal publishing for the Official Gazette and others, with an emphasis on electronic publishing and internet dissemination. This will help fill the gap in available legal materials. Internet access will certainly increase the availability of much needed materials, but increases in comprehension of those materials will need additional effort.

Associations. The weakness of associations presents a critical problem and a critical opportunity. A number of national, local and bi-lateral business associations are forming and growing. Few have a clear understanding of how an association should be structured or operate, how it is funded, and what kinds of services can and should be provided to its members. A program of general association building would probably be a valuable investment over the next few years. The Albanian-American Chamber of Commerce, founded during the second week of this assessment, would be a natural leader and counterpart for providing general training in association building and association management. The newly revived Chamber of Trade and Industry also appears to have strong leadership potential as a sponsor or counterpart in association building activities. For lawyers, both the Chamber of Advocacy and the Association of Women Lawyers need assistance in organizing and improving the legal profession.

While such technical assistance to business associations may not immediately appear relevant to commercial law, it should be noted that business and professional associations are both counterparts and conduits in the development and dissemination of commercial laws. They provide a structure for representing special interests, and for collecting and communicating information on the impact of law on those interests. They also provide a transparent forum for government and private sector communication, strengthening the rule of law while weakening the capacity for hidden or corrupt influences. Moreover, there is demand for these services -- several thousand companies and individuals have joined new and existing associations in the past year.

Education. Strong associations serve a critical role in educating their members and the general public about legal issues, a role that extends beyond the need for educational institutions and their courses. Accordingly, public awareness and educational programs should include appropriate associations whenever possible, both as sponsors and counterparts. Such partnerships strengthen the associations while disseminating necessary information.

General "popular" or "street" education and awareness is needed in a number of areas. In addition to law generally, and even specific laws such as collateral, there is need for increasing awareness in virtually all areas of business, commerce, law and economics. Some of the topics which might be useful in the near term include:

- General business concepts
 - How companies operate
 - Profits, losses and revenues
 - Marketing and public relations
 - The nature of contracts and how they work
 - How credit works, including the need for foreclosure and repossession
- The economic impact of law
 - How enforcement of judgments strengthens the economy
 - The role of government in facilitating growth through commercial law
- Specific laws
 - Customs law and valuation
 - Collateral law -- how and why it works
 - Bankruptcy -- every aspect

While there are many experienced professionals and educated individuals who understand these areas, there is no group (other than banks and foreign accounting firms) with sufficient understanding to support Albanian economic development. Courses should be provided for lawmakers, government officials, judges, lawyers, notaries, and business people, recognizing that most have no practical business experience, and few have more than nine years of experience.

Continuing Legal Education. There is currently no program of Continuing Legal Education (CLE) for lawyers, notaries or judges. A retraining program is planned for existing judges who did not attend the Magistrates' School, but not for ongoing provision of relevant legal education. More troubling, however, is that no institution has yet been identified that appears ready to take responsibility for a CLE program.

For judges, it is likely that the Magistrates' School will eventually provide the necessary follow-on seminars and workshops as course materials are revised in light of changing laws and circumstances. The Association of Judges would be a natural vehicle for CLE programs. The team was unable to meet with the Association, but did find judges who are not members and do not value membership, relying on NGOs and projects for their needs. Clearly, the Association will need support if it is to become meaningful for its constituency.

The Chamber of Advocacy (formerly the Bar Association) is another natural candidate to develop and offer CLE courses for lawyers and notaries, many of which could also serve judges. Unfortunately, the Chamber has a well established history of inactivity, so that it does not currently enjoy the respect of the legal community necessary to function as a professional organization. Current leadership has expressed interest in change. This may be the hour in which assistance will bring lasting results, although this remains to be proven. On the other hand, the team heard high praise for the Association of Women Lawyers, which could serve as an additional or separate vehicle for development of CLE.

The Law Faculty would generally provide some support for CLE. In Albania, the Faculty simply has not shown interest. Several respondents noted that high politicization of Faculty leadership and appointments has led to a serious decrease in motivation and relevance of the professors in the past five years, while others noted that low salaries (based on hours taught, not on preparation time or research) and poor conditions leave little incentive for professors to develop new materials or take on additional responsibility. Faculty members have expressed an interest in change, and foreign specialists have noted that there are a number of potential reformers at the school. Opportunities should be provided for the Faculty to use technical assistance and improve its role and performance, if desired.

Accounting. Within the CLIR methodology, accountants and auditors have been identified as important supporting institutions, especially for companies, bankruptcy, and any legal action or transaction requiring valuation of a company. Albania does not currently have an accounting profession known to be capable of providing these services. This is not a function of insufficient use of International Accounting Standards (IAS), but a failure to use and apply the existing law on accounting and auditing.

Several specialists noted that IAS is needed only for certain kinds of entities and transactions, and these standards are being used there. Better standards would fill the vast majority of needs for Albanian accountants and accounting. This will be driven by banks which wish to make loans, businesses which wish to receive loans, and both businesses and tax authorities as they negotiate the proper level of taxes. Hence, improved accounting should be tied to programs in these areas, rather than placed in a vacuum of the theoretical (albeit accurate) need for proper accounting standards, with emphasis on enforcement, including civil or criminal liability for accountants and auditors who do not comply.

4. Market for Reform of Commercial Law

The demand side of the market equation is, as with any product or service, crucial for legal reform in Albania. Currently, demand is soft. Those interviewed almost unanimously voiced the opinion that the existing laws are good enough for now, and can be revised in a few years as needs arise. The demand, then, for framework laws does not seem sufficient to support any major initiatives at this time.

This does not mean, however, that there is no demand. The needs most frequently expressed were at the implementation level, where there appears to be substantial demand for change. The constant chorus of complaints regarding court performance made it quite clear that there is

popular and professional pressure that can be harnessed to support the changes underway. The new Magistrates' School attracts top students, with more applications than it can fill. The outlook for court reform is quite good. The supply of the reforms is coming primarily from the donor community, but with governmental and institutional support. By working closely with Albanians and Albanian institutions, such as the Magistrates' School, it should be possible to avoid the sense of "foreign" solutions that has tainted much of the legislative reform.

There is also demand for a better legislative mechanism, although it is less focused. Several government drafters expressed their own desire to include the private sector in review of laws. Private sector associations expressed frustration or confusion at how they could voice their interests to government in an effective manner. It will probably be necessary to help both the public and private sectors to better understand the purpose and impact of participatory lawmaking, and to help focus private sector demand into proposals or support for a transparent participatory mechanism. If the goodwill encountered among drafters is representative of the mood of the legislators, then the government is in a position to supply this change, with outside technical assistance. Unfortunately, the last national experience with democracy was more than 70 years ago.

At the level of supporting institutions, there is also growing demand for the organizations that undergird commercial law development and civil society. In the past year, a number of private sector business associations have been started or revitalized, and those which are not operating effectively are subject to rather open criticism from their members. Lawyers are frustrated with an ineffective bar association, and several complained that they did not even receive notice for the few meetings held by the bar this past year. There seems to be strong desire for something better, but it has not become effectively focused.

Supply for this part of the market should ultimately come from the private sector, although the government could theoretically support the development of associations, if it had the resources. Most of the new associations need help: they do not have a history of associations to draw upon, and are often uncertain about the form, role, services, and organizational structure that they should have. This is another area where outside technical assistance could be very effective in the short term.

It is worth noting that Albania has a population of 3.4 million relatively poor people (by European standards). There are approximately 900 lawyers and 350 judges. The overall commercial market is quite small, and there is no large group of investors waiting to come in. In fact, much disinvestment is currently taking place among foreign investors, some of whom are moving their money to Albania's neighbors. It is not clear to what extent policy makers understand that they must compete with their neighbors for investment, and that they must eventually integrate regionally in order to offer investors more substantial markets. There does seem to be a strong interest in European integration, and this will provide an important context for reforms.

Some of the demand for change, however, is offset by satisfaction among many with the intimate, small town society that has existed for decades. Small loans are made between friends and colleagues, and few people have found a need yet for bank loans or collateralized credit.

This is likely to change -- and may change quite rapidly with the advent of secured credit for farm equipment and machinery -- but the critical mass of those consciously demanding the benefits of globalization and modernization is quite small. Again, public awareness and public debate will be essential in bringing about lasting reforms.

B. OTHER COMMENTS

1. Roles of Donors.

Respondents occasionally commented generally on the role of donors in commercial law reform. Several themes appeared from these observations. The team was not in a position to critique or effectively analyze these comments, but felt it worthwhile to pass them on. They may not necessarily provide any basis for action; they do reflect some strongly held opinions. It should be noted these remarks were not aimed at USAID, but at the donor community in general.

First, several respondents noted that many donor efforts are directly with the government, but at the ministerial level. These individuals requested that the legislature also be included directly in donor projects -- not simply as a recipient, but as one of the counterparts in project development and evaluation. Others also mentioned that it greater private sector participation is needed in the same way -- not merely as recipients of assistance, but also as partners in the process, possibly through regular roundtables or other events involving public sector, private sector and donor representatives.

A variation on this theme of local counterparts was an observation and request that foreign consultants be teamed with local specialists when researching and doing assessments. The commentator expressed frustration with the frequency of foreign specialists interviewing local individuals for information that would go into a report that the respondents would never see. He did not feel necessarily that all reports should be made public, but that Albania would be better served if consultancies could be used to transfer the research and assessment technology through twinning. The respondent also felt that this would improve the quality of information and the sense of Albanian ownership in projects.

There was a strong feeling that much of the donor activity is not sufficiently coordinated. This view was held both by Albanians and donor representatives.

Finally, it was noted that the Albanian government was not strong or experienced enough to negotiate effectively with some of the donors, and thus not always able to modify or influence some of the aid to better suit socio-political concerns as well as the development needs of the country. One respondent felt that too much emphasis was given to "big picture" programs while what people really wanted was to learn how to earn a living, produce or do business better.

2. Local Government

Several business associations commented on work being done both inside and outside of Tirana with local governments to improve business conditions. (One project mentioned was funded by USAID.) While this area of analysis was outside the terms of reference for this project, it appears that there may be a good window of opportunity for building public/private partnerships at the local level. These can serve as a model for the national government.

3. Diagnostic Limitations

The team was able to meet with a wide range of business, professional, and government representatives, as well as foreign donors currently engaged in commercial legal and institutional reform projects. Even so, there were gaps. Most notably, the team was unable to meet with agricultural associations or other representatives of the agricultural community. Much, if not most, of the immediate growth in the Albanian economy is likely to come through producers and processors of agricultural goods, and thus they represent a very important segment of the business sector; programmatic decisions based on this assessment should be supplemented with interviews of the agricultural sector.

Second, the team was able to discuss notaries with judges, lawyers, and business people, but did not actually get to meet with any notaries. They should be included more directly in future legal studies.

Finally, the study was limited by time to the city of Tirana. It is unlikely that many significant differences would have been found elsewhere, but the team felt that it would have been beneficial to visit other towns. There are two reasons for this: first, it broadens the base of respondents and can avoid a somewhat skewed perspective often found in capital cities; and, second, such travel sends a message to the interviewees that their town matters to the donors and the government. In other countries where the team members have traveled, there is palpable resentment in the hinterlands of the capital, based in part on the sense that they are being forgotten or ignored. Geographically broad-based research helps to build ownership for national programs, even at the assessment stage.

III. RESULTS OF THE ASSESSMENT

A. BANKRUPTCY

On a comparative basis, Albania leads the other five countries analyzed under this methodology in terms of legal framework. This is not surprising, in light of initiatives that have produced two new bankruptcy codes in six years. Like Poland and Macedonia, Albania has received substantial support in updating its laws, and the scores reflect this assistance.

	Albania	Mac	Pol	Rom	Ukr	Kzk
A. BANKRUPTCY	38%	57%	78%	54%	37%	50%
1. Legal Framework*	90%	87%	80%	59%	41%	60%
2. Implementing Institutions	21%	57%	80%	62%	45%	51%
3. Supporting Institutions	16%	42%	76%	52%	33%	49%
4. Market for Effective Bankruptcy System	24%	41%	78%	45%	28%	41%

* The score for Albania bankruptcy framework is an estimate based on discussions regarding the new law.

For all other aspects, however, Albania has the lowest scores. As discussed further below, Albania's bankruptcy laws are essentially unused, in part due to the weaknesses in the implementing and supporting institutions, and in part due to the very low demand. The scores thoroughly reflect these findings.

1. Legal Framework

Bankruptcy practice in Albania is governed by the Law on Bankruptcy Procedure, No. 8017, dated 25 October 1995. The law was based on a former German bankruptcy law, but with insertion of some American concepts, which were felt to have been inadequately tailored to fit properly with the German system. The law provides discretion to the courts for determining when a debtor can be declared bankrupt, with little weight given to the creditors' committee, and triggering mechanisms are not sufficiently spelled out. However, none of this really matters, for two reasons.

First, the Bankruptcy Law has essentially never been used, at least not in Tirana. Several respondents believed that a bankruptcy case had been filed and prosecuted in Durrës several years ago, and there are rumors that perhaps one other case was prosecuted in another city. Several cases may have been begun, but none completed. Although the pyramid crisis could have produced a number of bankruptcy cases, it did not because a new law was passed to deal with the impact of the pyramid schemes.

Reasons given for not using the law varied. One lawyer felt that this was due in part to fear of retaliation if property is seized, while another noted that judges are unwilling to permit eviction of families from residential property. Yet another was convinced that the main obstacle has been

ignorance of the law and procedure, so that judges simply will not handle these claims. Whatever the reason, the Bankruptcy Law has not been employed, and may be the least understood law in Albania.

Second, the existing Bankruptcy Law has become irrelevant because it is going to be replaced. The new law is expected to be disseminated in draft for comment before the end of September, and to be passed by the end of November 2000. Drafting has been coordinated and led by GTZ, using German attorneys. The law is based on current German law, and is expected to be a thoroughly modern European bankruptcy law when passed. Efforts have been made to involve Albanians in the drafting and preparation of the law, within the limits of their knowledge of bankruptcy.

The team determined that the extreme flux of the current situation made it relatively meaningless to score either law for the diagnostic: one law has not been used and will soon be replaced, while the current draft has not yet been submitted for comments. The team has requested comments, however, from the German drafters, and may be able to obtain scores from them in a few weeks.

2. Implementing Institutions

The courts are the implementing institution for bankruptcy law in Albania. The District Courts have jurisdiction, where bankruptcy cases are assigned to the Commercial Section of the Civil Division. There are no separate bankruptcy courts, and no separate bankruptcy division. The Commercial Section currently has only six judges, so any significant appearance of bankruptcy claims could overwhelm the system.

As previously noted, the Bankruptcy Law has almost never been applied, so that there is almost no experience whatsoever with the application of the law. In fact, bankruptcy is not well understood by lawyers, judges or the business community, and presumably not by legislators and policy makers. Extensive assistance will be needed for the courts to handle bankruptcy proceedings effectively.

3. Supporting Institutions

Unfortunately, the supporting institutions for bankruptcy are no healthier than the courts, with limited exceptions.

The bailiffs are soon expected to receive assistance and training from the World Bank and the European Commission. At present, however, lawyers report that they are generally not effective in compelling payment or seizing property. There is no existing training program for the bailiffs, and no materials in Albanian to instruct or assist them. (The head bailiff, however, does have a respectable collection of legal materials in English.) When they need to rely upon the police for enforcement, they are generally unable to do so. The system simply does not work.

Notaries generally act as another supporting institution for bankruptcy in civil traditions. To the extent they must provide expertise, including any forms or agreements related to bankruptcy, the

notaries are no different than the rest of the legal community. They have virtually no experience with and no knowledge of bankruptcy law or practices.

The registries are not yet sufficient for bankruptcy purposes either. Most important is the collateral registry, which is not yet installed. The team did not evaluate the land registry, which is currently being assisted by the Land Tenure Center of the University of Wisconsin and appears to be very successful in identifying and registering land. This will be important when an operable bankruptcy system is installed, but currently there are no bankruptcy actions to test the system.

In the area of professional associations, the lawyers' association has no bankruptcy expertise and no bankruptcy support services at this time. It is not so clear where the accountants stand. In terms of local accounting practices, foreign professionals indicate that the practices do not generally provide an accurate picture of the financial situation of locally audited companies, and balance sheets are considered universally unreliable. One foreign professional felt strongly that this was due to a lack of enforcement of the existing accounting law, which he deemed adequate for Albanian needs, *if enforced*. Clearly, assistance will also need to be provided to the accounting profession once efforts are made to implement a bankruptcy system.

Rather than comment on each specialized service normally found in developing countries, it is sufficient to note that there are no satisfactory services at present. It is likely that foreign banks could take an important leadership role in developing practice and understanding, and should be encouraged to help promote public understanding of the purpose of bankruptcy. The Bankers Association should be considered as a potential counterpart in bankruptcy development.

4. Market for Reform of Bankruptcy Law

The team was unable to identify any source of local demand for the replacement of the existing Bankruptcy Law with a new law. Upon further investigation, it appears that the new law is being sponsored by an international financing institution as a condition precedent to financial assistance, with a set deadline in October or November. This observation is not intended to shed doubt on the quality of the new law, which is believed to be very good, but only to point out that the law is not being produced in response to local demand. Consequently, programs to apply it will probably take additional effort.

The demand for bankruptcy law and practice in general seems to be underdeveloped. Several possible reasons for this were suggested by a variety of respondents. First, with only nine years of participation in the international economy, Albania has no tradition of bankruptcy. Until 1991, there was no private property or secured financing and no private companies who might need to be reorganized or liquidated -- bankruptcy was not part of the vocabulary. Second, even after the socio-political opening, loans were often seen as some form of state largesse instead of financial obligations with consequences for non-payment. The pyramid schemes did not help to change this approach, because many saw the schemes as state-sponsored investments for which they should not have to pay the consequences through bankruptcy and foreclosure. Third, to the extent that bankruptcy will involve residential property, Albanians generally will not support eviction proceedings. Even foreclosure on real property in rural areas results in unmarketable

assets -- the local population continues to consider the property owned by the debtor and will not support a change in use or ownership. Finally, there is some suspicion that many existing Albanian companies are technically bankrupt, and that enforcement of bankruptcy law would create another collapse that the country could not handle. In short, there is not a deep-seated understanding of bankruptcy sufficient to challenge traditions and practices or to serve as the basis of bankruptcy implementation.

Moreover, bankruptcy is used as a reorganization or market exit tool for companies or individuals who cannot meet their debt obligations with existing revenues. Better stated, it is the handmaiden of credit, and is driven by financial difficulties. Albania certainly has financial difficulties, but the vast majority of its credit economy exists between friends, colleagues and family members on the basis of trust. Most loans are small, and most creditors are not interested in reorganization or liquidation in this intimate society. Most commercial banks are lending only to foreign companies, and most secured credit is issued to foreign companies. Non-performing loans at the Bank of Savings and Credit (currently 88% of the loans) are in part inherited from the privatized banks through restructuring of the state entities to improve privatization values, and in great part represent the aftermath of the pyramid collapse. Whether the debtors are solvent is not known, but assuming that many are not, it is unlikely that any government could support the political cost of putting thousands of citizens into bankruptcy.

The demand for bankruptcy reform does not have a critical mass. It will come as secured credit increases, which will depend on improved enforcement of contracts, debt, and secured transactions through the courts prior to reaching bankruptcy levels. These conditions do not currently exist, and much of the emphasis on bankruptcy law is based on preparation for future needs. This is appropriate, and the current legal reform does meet an important future need by laying the foundation and erecting the framework. Actual implementation will surely come, but for now that wave seems far from shore.

On the supply side, education, development and application of bankruptcy law and concepts will need to come from outside assistance, in partnership with appropriate Albanian stakeholders. Once cases begin to be prosecuted, it might be very helpful to build a public and professional education campaign around a few cases, with foreign experts to help guide and interpret the processes.

B. COLLATERAL

In the West, this formal property system begins to process assets into capital by describing and organizing the most economically and socially useful aspects about assets, preserving this information in a recording system . . . and then embodying them in a title. A set of detailed and precise legal rules governs this entire process. Formal property records and titles thus represent our shared concept of what is economically meaningful about any asset. They capture and organize all the relevant information required to conceptualize the potential value of an asset and so allow us to control it. . . This is the place where capital is born.

Hernando de Soto, *The Mystery of Capital*, pp 46-47

Collateral is poised to become one of the success stories of legal reform in Albania. The law is well thought out and structured, but, more importantly, substantial resources have been invested to insure that the collateral registry is properly designed and instituted. Progress in linking demand for goods susceptible of collateralized lending - such as agricultural machinery and construction equipment - will be critical if Albania wants to unleash the potential for economic development inherent in secured credit. The scores reflect the current strengths, but also the weaknesses.

	Albania	Mac	Pol	Rom	Ukr	Kzk
B. COLLATERAL	75%	74%	77%	32%	48%	35%
1. Legal Framework	91%	79%	90%	44%	76%	56%
2. Implementing Institutions	80%	87%	79%	13%	56%	23%
3. Supporting Institutions	58%	61%	65%	35%	31%	31%
4. Market for Modern Collateral System	71%	68%	75%	37%	30%	28%

1. Legal Framework

Lenders are more willing to lend when their risk is reduced. Another way of stating this is that the costs of borrowing will be reduced if the risk of lending is reduced. One way of reducing risk is to provide assurance that the loan will be repaid, or that there will be money to satisfy the loan. A method for providing this assurance is for lenders to put a lien or a charge on property. A prime type of such lien or charge is a *hypotek* or mortgage on real (or “immovable” property).

Along with many other Eastern European countries, Albania lacked a law which dealt with non-possessory liens or charges on “movable” property. A non-possessory lien is one in which the borrower does not have to part with possession of the asset serving as security. However, since the borrower keeps possession of the “charged” asset (i.e. the asset on which there is a lien), there must be a way to provide notice to third parties of the existence of the charge, and also mechanisms to protect the lender in the event of a default by the borrower in repaying the loan.

The Law on Securing Charges came into effect on June 1, 2000. It has a number of important features, including the following:⁸

- There is flexibility in the form of agreement to create the charge. No specific form of agreement is required.
- Charges are permitted on “future” property (e.g. replacement inventory and new accounts receivable, useful in cases where the chargor in the ordinary course of business sells inventory which is replaced by other inventory, or accounts are collected, but new sales are made and new accounts receivable are generated).
- The new Law on Securing Charges allows for the establishing of priorities between charges on the same property, either by virtue of law (see below) or by virtue of the order of registration. The registry plays an essential role in establishing a priority where the law does not otherwise mandate it, and also allows creditors to determine whether there are prior charges on the property.
- If there should be a default (as defined under the relevant securing agreement), the competent court can issue an order of enforcement to the execution officer to seize the collateral described in the securing agreement and deliver it to the creditor (chargee) without giving prior notice of seizure to the person in possession of the property. There is no requirement for a court hearing, thus making the procedure a speedy one. Where the collateral is an account, instrument or a security, the chargee may notify the debtor or the obligee to pay to the chargee the amount owing under the account, instrument or security.
- The law also contains protections for the chargor (the person whose property is charged as security) and other creditors who have taken an interest in the charged property. At least 10 days notice prior to any disposition of the seized property, notice is required to be given to the chargor and any other person with a charge on the property subordinate to that of the chargee. However, this can only be done if the securing charge is registered in the Registry before notice of disposition. Similarly, the chargee may propose to the chargor that the chargee keep the property in lieu of selling it. Notice must be given to the chargor and to persons with a subordinate charge, and if any person who is entitled to notice objects within 15 days, the chargee must dispose of the collateral.
- The chargor (and any subordinate chargee) also have the right, under certain conditions and at certain times, to redeem the collateral against fulfillment of the unpaid obligation.

The new law covers a wide variety of transactions, including consignments and leases of goods with terms of more than one year.

⁸ Source: Prof. Ronald C.C. Cuming, Q.C., *An Overview of the Albanian Law on Securing Charges*.

As mentioned above, the law and the registry provide for certain priorities. Article 605 of the Civil Code of Albania regulated priorities among creditors. The Civil Code was recently amended to deal with priorities of “unsecured” creditors.

A purchase money charge (PMC) is given the highest priority. A PMC is a charge given to a lender which advances funds to the borrower to acquire a particular asset. If this charge is registered, it has the highest priority with respect to the asset bought with the funds.⁹

Other priorities for unsecured creditors are given to claims of wage earners, claims for unpaid social security payments, awards because of death or health problems, and claims of authors for transfer of intellectual property rights within the prior two years (carried over from prior law).

A new provision has been added relating to government claims. These claims, if registered, get priority over unregistered charges and charges registered after the government registers its claim (except purchase money claims). One example of a government claim is for unpaid tax obligations. In many jurisdictions, tax obligations often present a “hidden charge.” This occurs by virtue of the fact that some laws give priority to a lien given to the State for tax obligations, even though the lien does not have to be registered, and there is thus no public notice of the lien. In such a situation, a lender may advance funds to a borrower, thinking that it has priority, only to be “pre-empted” by the tax authorities when trying to enforce the lien.

The “lowest” priority as between chargees (i.e. secured creditors) is determined under the Law on Securing Charges, and is generally determined by time of registration (with the proviso that PMCs take precedence over ordinary securing charges).

At the time of this Diagnostic, the Registry had not yet become operational. The legislative framework was thus in place, but actual implementation of the Law on Securing Charges must await the commencement of operation of the Registry.

2. Implementing Institutions

There are two implementing institutions for Collateral Law. First, the Collateral Registry provides the mechanism by which pledges on property can be recorded for the protection of creditors. Second, the courts interpret the validity of the agreements and laws on which claims to rights in property are founded.

The Collateral Registry could not be evaluated during this assessment because it had not yet been instituted. Although it was scheduled for implementation earlier in the year, the facilities needed were only recently maintained. At the time of the assessment, the actual opening of the registry was several weeks away. The team was told, however, that the registry system and equipment

⁹ To the extent that the lender has registered its security interest, it is a “secured” creditor with respect to the asset purchased with the borrowed funds. However, Civil Code Article 605 gives a PMC special status over the other claims covered by that Article.

are modern, accord with European standards, and will be able to function efficiently and effectively.

Although the system is not yet accessible by internet, registration can be done by fax, permitting substantial ease of transactions for creditors outside of Tirana. The system is designed, however, so that it can eventually be decentralized physically through a network or internet approach, if needed.

The courts as implementing institutions are more thoroughly covered under the Contracts section of this assessment. Due to the newness of the law, and the overall condition of the judiciary with respect to other commercial laws, judges will need substantial training in this area if they are to implement and support this vital reform effectively. Secured transactions constitute an essential part of the foundation for economic growth for most modern economies, and the courts will be an impediment to that growth if not trained and supported in this area.

3. Supporting Institutions

One of the most important supporting institutions for this reform is the Bankers' Association, and its individual members. The banks have been involved in the development of the law, the forms to be used under the law, and the design of the registry, and this involvement must continue to ensure success. Banks have the strongest institutional interest in seeing this law through, and will need to be ready to assist the public in understanding the purpose and function of the collateral system. Some of the foreign banks may be prepared to invest their own resources in developing or disseminating materials to this end.

Other supporting institutions are not so strong. The bailiffs, as noted in the discussion of Contract Law, are expected to obtain assistance soon from other donors. They will need it. Respondents noted that it was very difficult to attach or seize property in connection with debts, especially if the property is owned by an individual rather than a corporation. The ability to enforce such debts through seizure must be established for the system to work, and the bailiffs are currently a weak link in that chain.

The team was unable to interview evaluators, but understood that they are also weak, and that the auction system for seized property is not functioning effectively. This may be less troublesome than problems of attachment, because very little value is ever collected by the creditors in such proceedings. Indeed, in well developed collateral systems such as that in the U.S., creditors seldom recover more than 5% of the value of their property through repossession and auction. The strength of repossession is in the deterrent affect on debtors, who understand that they will lose their entire investment in the property if they do not continue to pay for it.

Creditors' rights, enforced through repossession, are just one side of the coin, however. On the other side is protection against abuse by unscrupulous creditors. Consumer advocacy groups help to balance the interests of debtors and creditors in a healthy system, both by negotiating culturally acceptable limits on repossession, and by legitimizing the laws. Albania does not seem to have such a group currently in place.

Public education and awareness will be required for the new system to take hold and provide the economic benefits of collateral lending. As noted under Contract Law, there are a number of trade and business associations that are improving and that could assist in such efforts, but substantial support will be needed. Likewise, courses will be needed for lawyers, judges and policymakers.

4. Market for Reform of Collateral Law

With the advent of a new collateral law and collateral registry, there will be little demand at this point for any ongoing reform, but great demand is expected for the implementation and use of the new law. This demand is unlikely to mature, however, without extensive education of the public.

Possessory pledges and surety are known and understood in Albania, and are even included in the *Kanun of Lek Dukagjini*. Non-possessory pledges are brand new as a concept, and even credit is poorly understood by many. There is therefore little existing experience or practice to build on, suggesting that successful implementation of the new collateral law will require a great deal of public awareness and education.

Demand for use of collateral law is expected to come in great part from the agricultural sector, as farmers learn that they can obtain equipment -- which is in short supply -- on credit. Likewise, the food processing industry is likely to understand quickly the benefits of collateral credit in order to purchase processing equipment and supplies. Other industries can also be expected to use credit. Consumer credit, however, may take longer, or at least until the courts are willing to consistently enforce agreements against individuals in accordance with their terms. Consequently, the initial focus for collateral credit should be on commercial transactions.

Agricultural and business associations could serve as the principle proponents of collateral borrowing, along with commercial banks, who can dramatically increase their lending activity. They will need substantial assistance, however, in raising awareness. Likewise, lawyers, judges, notaries, and bailiffs will need to be educated in the use and application of the law if it is to work effectively.

As the law is used, it is likely that additional reforms will be needed. Currently, there is no formal system for identifying, coordinating, or implementing reforms based on user experience. As noted elsewhere, such a system needs to be developed in the legislature. However, a program of assistance to business associations and banks in the development and implementation of collateral law also provides an opportunity for building the "demand" side of civil society, by creating a more formalized flow of information between users, who can then engage lawmakers in the future as problems appear.

C. COMPANY

Company Law is a work in progress for Albania. Once again, the recent introduction of modern European legislation results in a relatively high score for the framework law, second only to Macedonia, which has also received significant assistance in this area. Albania does not do as well comparatively in the other areas, finishing last for both supporting institutions and market. This is not surprising: Albania's isolation arrested development, leaving an intimate society with commerce based on contacts and relationships, with few large companies and little desire for corporate organization. Increased integration into the global marketplace will Entry into the global marketplace is likely to provide much of the impetus for growth in this area, as traditional forms of doing business show themselves insufficient for the demands of increased trade and commerce.

	Albania	Mac	Pol	Rom	Ukr	Kzk
C. COMPANY	46%	55%	76%	60%	42%	57%
1. Legal Framework	75%	76%	70%	53%	39%	53%
2. Implementing Institutions	54%	45%	76%	73%	52%	67%
3. Supporting Institutions	21%	52%	82%	70%	42%	58%
4. Market for Efficient Company Law	32%	47%	78%	43%	33%	48%

1. Legal Framework

Law 7638 on Commercial Companies (“LCC”), based in large measure on French and German company laws, was enacted in late 1992 and came into force on January 1, 1993. The law deals with four forms of doing business as a “company”, as follows:

- A) General Partnerships (Arts. 13-25) – In a general partnership all partners are jointly and severally liable for the partnership obligations, without limitation. There is no minimum capital required. Each partner can bind the partnership with respect to third parties.
- B) Limited Partnerships (Arts. 26-36) – In a limited partnership there are both general partners and limited partners. The limited partners are liable for partnership obligations only to the extent of their contributions to the partnership. General partners have unlimited liability (as in the case of the general partnership). Limited partners may not participate in management of the partnership.
- C) Limited Liability Companies (Arts.37-73) – This type of company is the form most commonly used by Albanian businesspeople. It is formed by one or more “partners”. The minimum capital is 100,000 lek (slightly more than US\$ 700, and “partners” are liable only up to the amount of their contribution to capital (i.e. the partners have limited liability).
- D) Joint Stock Companies (Arts. 74-88) – A joint stock company (“JSC”) has the ability to make a public offering of its shares. To do so, a JSC must have capital of at least 10 million lek (a little more than US\$ 70,000). If no public offering is intended, the JSC must have capital of at least 2 million lek (about US\$ 14,000). There are relatively few JSCs in Albania. Most

investors who have chosen this form were required to do so required by a particular law (e.g., banks must be JSCs).

In addition to defining each type of “company” and delineating its powers and rights and those of its members, the law also has general provisions applicable to more than one form of company (Arts. 1-12), and also provisions dealing with matters such as: management of JSC’s (Arts. 96-127), the General Meetings of Shareholders Arts. 128-149), provisions relating to capital (Arts. 150-166), mandatory audits (Art. 167-185), conversion of public companies (Arts. 186-188), dissolution of public companies (Arts. 189-190), requirements relating to shares (Arts. 197-210), and common provisions for all forms of companies, e.g. annual reports; affiliates, subsidiaries and controlling companies; mergers and splits, and liquidation and dissolution (Arts. 217-294). It is a very comprehensive law, comprising almost 300 articles.

The general view presented to the team was that the company law is adequate for Albania under current circumstances, with only minor changes needed. Problems most often cited related to the registry and other administrative matters surrounding registration. For example, comments were made that the law does not contain any time limit on approval of registration, and that the law should specify what requirements exist following registration (e.g. the obligation to register with the tax authority). Another complaint mentioned in the context of forming a company is the matter of other approvals, licenses, etc. which are required by the company. Obtaining these other approvals and licenses was deemed to be time consuming and burdensome.

Some practitioners complained that the fee structure for registering a foreign company was twice the amount required for a domestic company (40,000 Lek vs. 20,000 Lek). In addition, a different (and higher) fee structure prevailed for foreign firms.

Some of the problems in the area of company law stemmed from the same lack of knowledge, experience and information which afflicts other legal areas. Thus, some judges view an Albanian company formed by two foreigners as a foreign company, and thus ineligible to hold land.

2. Implementing Institutions

The Company Registry is housed within the courts and is responsible for initial registration and amendments. Lawyers representing local companies expressed general satisfaction with the services provided, and one claimed that he could generally register a company in a week or less, well within the standard for developing countries. Representatives of foreign companies were less satisfied, due to discriminatory fees and greater delays. These delays may be typical for joint stock companies, which are used relatively frequently by foreign investors and are substantially more complicated than the limited liability companies favored by local investors.

There is certainly room for improvement in the registry, especially through use of computerized, decentralized registration. Even so, there does not seem to be any significant demand for such improvements. Current problems were considered an inconvenience rather than a constraint to investment. If demand develops and funding is available, the business community is still small enough to address the need fairly easily, but the team would not place this as a top priority at present.

3. Supporting Institutions

Most comments made on supporting institutions under the section on Contract Law also apply to supporting institutions for Company Law. Specific comments are justified, however, for several matters.

First, the courts act as a supporting institution for companies in interpreting and applying laws relating to the formation and governance of companies. As in other areas, the judiciary is poorly trained in this regard. The team was told of at least one instance of a judge who was unable to distinguish between an Albanian company and its foreign shareholders, and thus refused to allow the company to own land. (Only Albanians are permitted to own land.) We were unable to determine how widespread such confusion might be, but respondents made it clear that they were often dissatisfied with rulings on company issues. As noted elsewhere, Albania has only a few years of experience with *any* type of corporate forms. Education in the nature and purpose of companies would be very useful for judges and the general business community.

Second, accountants and auditors provide an important support function for companies in developed economies by accurately portraying the financial condition of a company. This is useful both for corporate management, and in obtaining bank loans. Albania does not yet have a recognized cadre of accountants who apply reliable standards. If demand for credit grows, or if the tax collection system becomes more effective, there will be a greater need for such services. Currently, most companies are small and are not obtaining formal credit or complying with tax laws. It is, therefore, not surprising that accountancy has not developed sufficiently in this environment.

Finally, there are no independent corporate filing services such as those found in countries with more vibrant corporate registration. In many countries, entities or individuals specialize in handling all aspects of corporate filings, so that lawyers and notaries do not need to stand in line waiting for stamps and approvals. In Albania, the lawyers stand in line, spending as much as four hours obtaining various seals and signatures. They did not perceive this as a problem, however. The market for services can fill this need, but not until the economy -- and the demand for more efficient use of professional time -- reaches a critical mass.

4. Market for Reform of Company Law

The team was told that most Albanian firms are small, and therefore satisfied with the relatively simple procedures required for establishing a limited liability company. A lawyer specializing in formation and registration of Albanian companies stated that he could generally register a company within a week, or even as little as three days. He did not see any need for reform in the overall process. Foreign investors, however, complained of the complexities involved in creating a joint stock company, and felt that reform was needed to lower the cost and simplify the procedures for these companies.

The market for reform in the area of company law would seem, therefore, to be divided. For most local investors, the regime and timing are adequate. Thus, it seems unlikely that much local support could be generated for any extensive reform plan. This is not surprising -- as in

other areas, the laws are generally adequate for limited liability companies, having been adopted from European models only a few years ago.

If foreign investment opportunities improve, a higher demand can be expected for reform of the laws governing joint stock companies. Indeed, improvement in the foreign investment climate may require changes, especially for those investors who are more sensitive to costs and are comparing the regimes of Albania with neighboring countries. (Coca Cola, Peroni, foreign banks and some other larger international investors are often better able to absorb or overcome the costs and bureaucratic obstacles than smaller investors.) Based on these observations, demand for change can probably best be identified and focused through the institutions representing these investors, such as the Banking Association, Foreign Investors Association of Albania, and bi-lateral chambers of commerce. Associations of smaller, Albanian businesses are less likely to be concerned, although growth may increase the demand to move from limited liability to joint stock models.

The demand for development of capital markets and securities also appears to be rather limited at this time. Assuming that market size and economic growth are the principle economic drivers for capital markets, and that, in a country the size of Albania, capital markets do not yet significantly drive growth, any large projects in this area may be premature.

D. COMPETITION

No assessment was made of competition law. Several respondents commented on one aspect of competition, however, in the area of procurement. These individuals noted problems in transparency of the procurement process by the central government and felt that anti-competitive practices were common. They also cited interference by the national government in local procurement bids, including the disallowance of local bidders in favor of contractors normally used by the national government, often at higher cost. (These comments were made in the context of observations on the need for decentralization, another topic outside the terms of reference, but one mentioned by more than a few respondents.)

E. CONTRACT

Albania places fifth among the six countries studied in its overall scores for Contract Law, in spite of its tie for first in legal framework. Again, the foreign assistance in making laws has proven fruitful, putting Albania (84%) at the same level as Macedonia and Poland, well ahead of Romania, Ukraine, and Kazakhstan. Scores drop precipitously, however, upon examining the implementing institutions (51%), supporting institutions (35%) and market (50%).

	Albania	Mac	Pol	Rom	Ukr	Kzk
E. CONTRACT	55%	61%	80%	63%	45%	64%
1. Legal Framework	84%	84%	83%	74%	50%	73%
2. Implementing Institutions	51%	62%	83%	73%	49%	66%
3. Supporting Institutions	35%	50%	79%	66%	50%	54%
4. Market for Efficient Contract Law	50%	50%	75%	37%	30%	62%

As discussed below, the law is not supported by a sufficient court system nor a civil society enriched by appropriate supporting institutions. The current scores, however, are not as bleak as the picture indicates. There is substantial donor support for the courts, with complementary commitment from the government to improve performance, even as business and professional associations begin to develop. Indeed, the scores reflect a baseline, which future assessments will hopefully improve upon substantially.

1. Legal Framework

Contract law for Albania is embodied in the Civil Code of Albania, which sets forth the general principles of contractual (and other) obligations in the Obligations section of the Code (arts. 455-658), with specific forms of contract (such as leases, agency and franchising) in the title on Contracts (arts. 659-1161). The provisions for various forms of contract tend to be general (for example, franchise is covered in only nine articles [arts. 1056-64]), leaving specifics for implementing regulations, few of which have yet been passed.

The present Civil Code is based on European models. Adopted in the early 1990s, it is essentially a modern set of laws that can adequately serve the country in its goal of approximating European legislation for eventual membership in the European Union. It has a very flexible approach to contract, permitting parties to enter into contracts on any subject not prohibited by law. Thus it avoids the control-oriented mentality found in many transition countries of making illegal all activities that are not expressly permitted by law. In addition, most contracts do not have to be notarized to be legal (with the exception of real estate and a few other transactions). Notarization serves an evidentiary function, not a legalization function -- non-notarized contracts are fully enforceable, but are theoretically subject to challenges on the authenticity of signatures. As a result, contract law is not burdened by unnecessary formality or legal restrictions.

The provisions on contract formation are more than adequate to support continuing commercial development. Both natural and juridical persons are free to contract, and state-owned entities stand on an equal footing with private parties or entities for commercial agreements. There is

also no legal discrimination between foreigners and Albanians in contract law. Where law is silent, parties may rely on custom and trade usage to define their rights and obligations.

Parties also have the flexibility to adopt customized terms, including liquidated damages, choice of forum and choice of law, and may refer their conflicts to arbitration through dispute resolution clauses. (As noted below, arbitration and other alternative dispute resolution mechanisms are still rather nascent and ineffective, but the law permits such choices.) Albania is not a signatory to the UN Convention on Enforcement of Foreign Arbitral Awards, but the Code of Civil Procedure expressly recognizes such rights, and expressly permits enforcement under executory judgment proceedings without re-opening any consideration of the underlying merits.

The Code is also adequate with respect to damages. It provides for specific performance, money damages (including interest during the period of non-payment) and liquidated damages, and provides adequate guidelines for determination of damages. The procedural law permits the use of judgment on an executory title,¹⁰ with immediate enforcement, and the courts have the statutory authority to enforce their decisions. In practice, however, this breaks down significantly.

Those interviewed with respect to contract law voiced no serious concerns with existing legislation. All expressed satisfaction with the statutory framework, although some noted that more detailed regulations were needed for certain areas, such as franchises. One respondent stated that franchise is not covered by the law at all, even though it is expressly addressed (Arts. 1056-64). This comment highlighted a general view that few lawyers, judges, law professors, notaries or other legal professionals have a good knowledge of Albanian commercial law.

In conclusion, contract law at present is good enough, if not very good, for most transactions. There are no major gaps, and the overall flexibility permits the parties to determine their own needs within the terms of the contract. Implementation, however, is considered to be at a deplorable level, completely undermining the otherwise adequate statutory framework.

2. Implementing Institutions

The implementing institution for contract law is the courts. For Albania, this institution has suffered badly, but is in the process of repair.

The Albanian Court System is comprised of 30 courts, populated by 350 judges. The court of first instance for most commercial matters is the District Court. There are 22 of these courts, with 6 regional Appellate Courts and one Supreme Court. In addition, there is a Constitutional Court that hears only questions regarding interpretation of the constitution, which must be certified by the Supreme Court. All courts examine both criminal and civil matters, but with separate divisions for each. Within the civil division, there are also specialized sections:

¹⁰ Executory titles are loan documents or other documentation relating to non-payment of a stated amount that can be enforced rapidly through accelerated procedures in which the creditor simply proves non-payment, without any trial on the merits of the underlying transaction or any reason for non-payment. In the U.S., this normally takes the form of a confession of judgment, enforced through a motion for summary judgment.

administrative, commercial, family and civil. In theory, these sections will hear only those cases within their subject matter specialties, but, in practice, the lack of sufficient judges sometimes results in assignments across the specialties in order to avoid excessive backlogs.

The budget for courts is set aside from national revenues through the Ministry of Justice for allocation by the High Judicial Council. The Council is comprised of representatives from each level of the courts, as well as the Ministry of Justice. The budget is generally considered insufficient for the current and future growth needs of the courts.

Throughout the country, the court infrastructure is minimal. Most judges hear cases in their rather cramped chambers of perhaps 12 square meters, which must also house a secretary, if they have one. In Tirana, a few larger rooms are available for larger trials, but on the whole conditions are inadequate. Judges have few legal materials, and few have even a full set of Albanian legislation or the Supreme Court decisions that have recently been published. There is no systematic means of supplying laws or jurisprudential materials, and judges must often depend on lawyers to supply the necessary copies (assuming that the lawyers know and are using the law, which is not universally true).

The Tirana Court recently purchased and installed computers for its judges, which are replacing typewriters as the principle means of preparing decisions and orders. These are not yet networked, however, and only two have access to the internet. (A third will soon have access, but only because the judge personally purchased a modem, which he is installing.) According to court representatives, the money for this investment came from the overall court budget -- no donor agency was mentioned as having supported or supplied the initiative, but this has not been verified.

The Tirana District Courts have the heaviest case load. On the administrative side, they hear claims involving both local and national governments, while outlying courts hear only claims involving local government. In addition, Tirana is the country's largest city, with approximately 20% of the nation's population, and approximately 60% of Albanian businesses headquartered there. Tirana also has the largest number of District Court judges (50).

Respondents from all backgrounds were unanimous in their assessment that the courts have not functioned effectively in interpreting, applying or enforcing the law. Historical reasons for this include a lack of qualified candidates after the transition to an open society, and questionable selection practices by earlier governments. In order to staff the courts quickly after a "purge" of judges, minimal training was given (a six month course), and few judges hold law degrees. In fact, some have not received a college education. Moreover, almost all commercial law in place today has been passed since 1993, so that the practical application of these laws is entirely new even for those judges with a solid legal background; for the others, the profusion of new law tends to be overwhelming.

Court users paint a dismal picture of performance. Although required to do so by law, few judges consistently provide written decisions, or provide reasoning based on law. There is little transparency in the decision-making process, and, not surprisingly, the suspicion of corruption is very high. Domestic users estimate that as many as 50% of the current judges are corrupt; some

foreign businesspersons are not so optimistic. One respondent also noted that few of the local lawyers know or use the law sufficiently to argue their cases on a legal basis, and depend on bribery to obtain their desired results.

To the extent that the business community does use the courts in hopes of having claims assigned to a generally competent judge, they are usually dissatisfied with the outcome. Even when a judgment is obtained, it is frequently difficult to have the decision enforced if the loser does not wish to pay. While the overall responses were negative in this regard, several respondents noted that the situation is somewhat better where it involves commercial property (bank accounts or commercial office space) than residential or personal property. Indeed, one attorney reported substantial success in attaching such commercial assets, but reinforced the overall impression that is virtually impossible to obtain satisfaction against residential property.

Problems in enforcement were identified at several levels. First, some judges will simply not render a judgment against personal property, and many will not render judgments against political figures or "well connected" individuals. In fact, several legal professionals reported that a claim against the political elite is simply a waste of time and money. If a judgment issues, however, the bailiffs will not always assist in the attachment. At times this is because they are threatened with violence (one respondent cited the widespread use of Kalashnikov rifles for defense), and the police are not willing to intervene or assist when deadly force has been threatened. When bailiffs do in fact obtain property, they do not necessarily protect the value either during seizure or storage (for movable property), thus diminishing the market value at auction. (Auction is dealt with below, under supporting institutions.) Seizure of residential property is further complicated by legal tradition that prohibits eviction until the resident finds another abode.

On the other hand, an attorney who primarily represents foreign clients and creditors noted that it is relatively easy to attach commercial bank accounts in commercial proceedings by freezing the account at the beginning of the action and executing against it upon judgment. Success was also noted in the enforcement of foreign judgments. Although not a signatory to the U.N. Convention on the Enforcement of Foreign Arbitral Awards, the Code of Civil Procedure provides for homologation and enforcement of foreign judicial and arbitral awards. These are brought to the Court of Appeals, which has proven reliable in issuing executory judgments without reopening the case on the merits.

Another source of frustration frequently cited by attorneys was the failure of courts to honor executory titles. In theory, a creditor may sue upon these in an expedited proceeding, receive a judgement rapidly, and enforce the debt through execution on assets. Such a "yes or no" decision should be rapid and effective, with a minimal cost related to the litigation. In practice, few Albanian judges either understand or honor these mechanisms, and tend to open the entire transaction for trial. This defeats the purpose of the credit mechanism, raises the cost of credit, and ultimately lowers the amount of credit made available in Albania.

Aside from this area, lawyers and litigants generally felt that the speed of litigation was reasonable, but could be improved. Several respondents estimated that the average case took approximately one year from filing to judgment, and one noted a case that had gone all the way

to the Supreme Court in about 18 months. Another noted times of 3-4 years for a final decision. This difference is in part due to time added if a case is remanded for trial on appeal. Although by international standards this timeframe is admirable, Albanian stakeholders felt that it was too slow and suffered unnecessary bureaucratic delays. It is quite possible that the length of trial will increase, however, as judges are required to spend more time on application of law and preparation of decisions.

In ranking the different courts, user confidence was highest with the Constitutional Court, which was seen as completely competent. The Supreme Court was also considered to be generally trustworthy, especially with recent appointments and in light of their use of published opinions. The Court of Appeals was not often noted, suggesting that they are seen more as a stopping point on the way to the Supreme Court than fully important in their own right. The District Courts, as previously noted, command very little respect from the legal community at present.

The situation as presently evaluated would be quite bleak, except for a number of important changes underway.

A three-year Magistrates School has been established for the training and appointment of all new judges. With substantial assistance from USAID through a project with East-West Management Institute and through ABA/CEELI, the School is offering a very practical preparation for future judges, and entry into the school is highly competitive. Successful candidates, who must have a law degree, spend one year in classes, followed by two years of increasing responsibility as interns to judges or prosecutors, depending on their chosen field. The first graduation was held in August 2000, with 19 successful graduates, of which six are now employed in the Tirana District Court.

The Magistrates School also has a mandate to provide training for all judges with less than five years of experience. Short courses have been designed and are being delivered to improve the level of legal knowledge of these younger judges. There is not yet, however, a program in place to provide much needed legal training for the "older" judges, who have no better grasp of law than newer ones. A World Bank project should address this, but the issue should be monitored by the donor community as there is a great demand from the legal and business community for an improved judiciary, which will eventually require some form of continuing legal education.

Another positive sign is the establishment of an Inspectorate that is expected to rate the performance of each judge at least once every two years. This assessment will be given to the High Council of Justice, which has the power to remove judges for incompetence, malfeasance, and other standards relating to a judge's effectiveness or ability. It is reported that the Council has already removed a number of judges, and it is rumored that the former President of the Tirana Court was removed for bypassing the system for assigning cases. Another rumor counterclaims that he merely resigned. Although these rumors may not be useful as measures of truth and fact, they are important indicators of public impression, and the impression is that the Council is serious about integrity in the courtroom.

Additional assistance will be needed to upgrade the level of judges, and to remove those who are corrupt or incompetent. One tool to be seriously considered is the publication of legal decisions.

Existing law requires that the litigants be provided with a written decision, in which the legal basis for the decision is stated. Under current practice, decisions may be read in court, but are seldom provided in written form, and the quality of the written decisions is very low. As a result, transparency of the process has been substantially compromised.

Two reasons have been cited for this practice. First, many judges are uncomfortable with written decisions because they simply do not have training or understanding of what is required. Second, some judges do not produce decisions because the outcome is based on bribery rather than law.

A program in which judges are both trained and required to write decisions can have several positive results. First, the training will be valuable in itself. Second, well reasoned or well written opinions will have jurisprudential value -- even though the civil law tradition does not rely on precedent, each decision does provide information regarding the interpretation and application of law. Third, poorly reasoned or written decisions help to expose those judges who are either unqualified or corrupt. It is generally easier to prove incompetence than corruption, so that such a record provides a basis for removal of corrupt judges also. Fourth, it provides a record on which the litigants can appeal -- if the decisions based on bribery (combined with indefensible legal arguments) are overturned, then bribery becomes less profitable, and can be limited systemically. Current practice, on the other hand, is fertile ground for bribery and incompetence, and has led to widespread dissatisfaction with the judicial system.

Some changes have begun at the Supreme Court level in providing written decisions. Decisions of the Supreme Court issued in plenary session have been decreed legally binding as precedent. In addition, the Court can choose to hear cases for precedential value on its own motion, not only on appeal. Thus the Court can actively refine legal interpretation by choosing cases and publishing precedential decisions, and has begun to do so. Foreign legal experts have noted that the quality of judicial reasoning and writing has improved dramatically since this practice was instituted. With the advent of computerized decisions and the low cost of internet publication, it is possible for all decisions -- not just selected ones -- to be published electronically and economically; this is not the tradition of civil law jurisdictions, but the question should be raised whether this tradition should change.

Finally, in addition to the other positive changes taking place in the Albanian judiciary, the World Bank will soon begin implementing an extensive program of court reform. This includes administration of the courts and modern case-tracking techniques, which should help to improve both efficiency and quality of the decision-making process for commercial and all other cases. The project is also supposed to address the training needs of judges with more than five years of experience who are not included in the mandate of the Magistrates School, but this has not been confirmed.

3. Supporting Institutions

The diagnostic methodology for this assessment identifies the following as examples of supporting institutions to be examined:

USAID/EE/MT/ILE COMMERCIAL LAW REFORM ASSESSMENT FOR EUROPE AND EURASIA
Diagnostic Assessment Report for Albania

Government Entities:	Notaries
Professional Associations:	Lawyers/Bar Association
Specialized Services:	Certification and Inspection Services
	Specialized Publishers
	Universities, Foundations and Think Tanks
Trade and Special Interest Groups:	Banking Associations
	Business Associations
	Consumer Advocacy Associations
	Import/Export Associations
	News Media
	Self Regulatory Organizations
	Trade Groups

In simple terms, most of these groups can be described as either nascent or "not yet." With only nine years since Albania emerged from complete isolation, few of the groups or practices found in more developed transition economies yet exist. The good news is that some are growing and are likely to have a significant impact in the next few years.

a. Notaries

Notaries are regulated by law, and, as in most civil law countries, hold a special position as the sole agents for approval of certain types of transactions. Unlike some other countries, however, notarization is not required to make a transaction or contract legal (except for leases, mortgages, pledges and a few other specific acts), but provides evidence of authenticity as well as an air of authority. Documents to be registered are also notarized for purposes of authenticity, but lawyers are permitted to prepare the documents.

Lawyers indicated that they were generally satisfied with the quantity and quality of notaries, and that they generally used them only for authentication, not for drafting. One private sector entrepreneur with a substantial construction business uses them occasionally for loan contracts, but has only used them once to draft the contract, and thereafter has used the original form. Banks tend to have their own forms, or even their own notaries, and generally do not seek services from the broader pool of notaries.

Notary fees were judged to be generally reasonable, but unpredictable. According to one courthouse lawyer, fees for notarization of the same kind of document could change from week to week without notice. Although this respondent felt certain that a set fee schedule existed, he had never seen one, and intimated that this was deliberate in order to negotiate or change prices. This impression does not indicate truth, of course, but at least one instance of distrust of notarial ethics by a lawyer. Another case was cited of a notary who had forged signatures to support a fraudulent transaction. While this does not support any generalized conclusions, it can lower overall confidence in the system.

As with lawyers, no institution or organization was identified as being responsible for ongoing education of notaries in the changing legal environment. Having been initially educated at the law faculty, most notaries are consequently under-educated in current laws, and do not have an

organization that can be counted on to provide for additional education as new laws are passed and old ones amended.

At least some of the notaries have computerized their operations, but the team was not able to identify the extent to which this had taken place. One observational detail suggests that the status of notaries might not be as exalted as elsewhere in Europe -- a number of notaries also advertise photocopying services, with their storefronts suggesting that the latter service may be the principal one.

For notaries to improve their position, they will need to establish themselves as experts in the changing law, and provide services based on these laws. Collateral law will represent a new opportunity and challenge for them, especially if they can master the law quickly and provide high quality services at competitive prices. Whether they can do so remains to be seen.

b. The Bar Association

Albania has approximately 900 lawyers admitted to practice, with 500 (56%) in Tirana. Although the law has provided for a National Bar Association with mandatory membership, this has never materialized in any useful fashion. Recently, a Chamber of Advocacy was created to replace the Bar. At the outset it was reorganized from the previous design of 28 chapters (one for each administrative division), to 11 District Chambers under a National Chamber.

The leaders of this new Chamber foresee its evolution as an independent organization (although with mandatory fees) that can serve to license and discipline attorneys, administers admission to the practice through a bar exam, and serve as a traditional association with services for its members (training, workshops and others to be determined) while working actively for legal reform and improvement through drafting of laws. In addition, the leadership would like to have a legal requirement that all draft legislation must be submitted to the Chamber for comment and advice prior to adoption into law.

These leaders recognize that there is a serious lack of knowledge and practice in commercial law and are interested in providing or co-sponsoring seminars to address such needs. It is not clear yet whether the Chamber members are open to a mandatory continuing legal education (CLE) requirement as a condition to maintaining a license to practice, but the Chamber could certainly become a leader in providing such education.

Due to its recent creation (or re-creation to replace the defunct Bar), it is difficult to judge the potential effectiveness of this organization. A number of practitioners and other stakeholders expressed doubts based on the lack of activity so far, but it should also be noted that at least one of the leaders is currently preoccupied with an election campaign. The Chamber should be given a chance to respond to offers for assistance, and either take up the mantle of national leadership or follow its predecessor into oblivion.

The team also heard that there is a very active and vibrant Association of Women Lawyers. Several respondents felt that this group had the personality and drive to provide many of the support services, including seminars and workshops for all lawyers, normally provided by a

national bar association such as the new Chamber of Advocacy. The team did not have the opportunity to meet with representatives of this group, but notes that this Association should certainly be included in efforts to assist the legal profession.

c. Certification and Inspection Services

Certification and inspection services often serve to harmonize practices and develop standards with respect to import and export contracts. In Albania, no such services currently exist. This is in part due to the almost complete collapse of the export market during these transition years, as such services are generally used to establish the quality and quantity -- and therefore the price -- of manufactured items, especially in foods and processed oils. Albania's current level of export output in these areas is still quite low and unlikely to support such services for a while.

d. Specialized Publishers

There are no specialized publishers currently operating in Albania. In other jurisdictions, such institutions frequently provide standardized forms and contracts for use by the legal profession, as well as legal and jurisprudential books, pamphlets and other materials. There is also no legal press producing scholarly articles, legal journals or other regular periodicals upon which the legal community can rely to improve its knowledge of legal developments.

The Official Gazette is the only entity currently publishing. Its mandate, as a state organ, is to publish all new laws and regulations, as well as the decisions of the Supreme and Constitutional Courts selected for publication. Several respondents noted that it has not always produced enough copies of these laws for the legal community. The World Bank is reported to be providing support to the Gazette in upcoming projects, which hopefully will include internet access to the publication. If provided in electronic format, laws which are modified could easily incorporate the changes in the body of the electronic text. At present, changes are known only to those few professionals who track the changes in their own collections of laws. One respondent noted that lawyers frequently site laws without being aware that they have been changed.

In light of the very small market for legal publications in the Albanian language¹¹ it seems likely that the development of such publications will require donor support during the near term. This could be focused on creating a newsletter with an organization such as the Chamber of Advocacy, or perhaps a quarterly publication sponsored by the Supreme Court and providing a variety of commentaries, opinions on legal interpretation, practice notes and other useful information. If published primarily through the internet, costs could be kept low enough to permit subscription or membership fees to cover the actual costs of publication.

¹¹ *Assuming all lawyers, judges, notaries and politicians purchased each item published -- which is not a valid assumption -- there would still be no more than a few thousand potential purchasers for any publication offered.*

The lack of legal materials, especially jurisprudential materials, will continue to hinder the proper implementation of existing laws, as well as any new laws which may be adopted in the coming years.

e. Universities, Foundations and Think Tanks

There are currently only two institutions providing legal education and training. The Magistrates School, noted previously, serves the judiciary by providing updated instruction in theory and application of laws, including specialized commercial law courses. It is also providing training for magistrates who were appointed before the school was established, but plans are to discontinue this service once those judges have been trained. It is not clear whether the School will have a continuing legal education function after that time, but the progressive nature of the leadership there suggests that the school will adapt and respond to the needs of the market. It is certainly an appropriate place to concentrate assistance for judicial CLE. If the Judges Association eventually develops sufficiently such a role, it could also become an important agent for the development of judicial expertise in commercial law, including contract law.

The Law Faculty is, in most countries, the logical focal point of assistance efforts for improving the content and quality of legal expertise for both future and existing lawyers. It can produce scholarly articles, incorporate changes into its curriculum to ensure currency, and provide relevant seminars and training to practicing lawyers. At present, the Faculty fulfills none of these roles adequately.

A number of respondents, including some from the donor community, expressed doubts about the willingness of the Faculty to take on this role in a meaningful way. In their defense, one local expert noted that the teachers are not well paid and have little incentive to invest the time to develop new courses, new materials, or new training programs. Their salary is keyed to class hours delivered, not to time spent in preparation for class or invested in research. With no vehicle currently available for scholarly publication, there is not even the lure of professional esteem to inspire the normal scholarly advancement found in most faculties of law.

The team met with several adjunct and full time Law Faculty members, all of whom recognized that assistance is needed and that they are open to it. Attempts by some donors to date to involve the Faculty in reforms have not been fruitful, however. Additional effort will be needed to identify ways in which the Faculty can be motivated to become a leader in the development of commercial and other law for Albania, perhaps through the temporary funding of a Commercial Law Institute or other program. In the end, however, the Faculty members will have to choose whether they will become leaders or become irrelevant to the changing legal environment.

Under contract with USAID, the University of Nebraska is providing assistance to the Faculty of Economics for an MBA program. This program includes some material on business law, and thus provides additional resources to the overall commercial law community. It could possibly serve as the basis for seminars and workshops for the business and legal communities in specific areas of commercial law (such as bankruptcy), or for economic impact of commercial laws and practices. The government, legal, and business communities have a very low understanding of economics and commercial law, which is likely to hinder rational, demand-side legal reform and

refinement. Any institutions that can help to fill this gap should be considered candidates for additional technical assistance.

f. Banking Associations, Business Associations, and Trade Groups

Business associations are in a growth mode. Although there are no highly developed associations yet, there are a number that have begun to actively pursue a role in the business community.

The Banking Association includes both foreign and domestic banks. At present, it is not yet as strong as its component parts, so that the principle legal drafter in the Ministry of Justice felt it more important to communicate directly with banks than with their Association when considering changes to the banking law. Even so, the Association was respectfully cited by bankers and others as an important point of contact for the banking community.

The Team was unable to interview any Association representatives during this assessment, but recommends that the Association be included in any activities adopted to strengthen private sector associations. For the Bankers Association, this could include specific assistance in developing standard forms and contracts for banking, including loan documentation.

Several business associations are also growing. The Chamber of Commerce and Industry of Tirana appears to be developing dramatically at present. One year ago, the Chamber had 200 members, based on mandatory membership requirements for Tirana's 23,000 registered businesses. This year, the Chamber has over 2,000 members based on services being provided or to be provided. Donors that had attempted to work with the Chamber in the past found it moribund, and at least one was quite unaware of and surprised at the growth in the past year.

The Chamber sees itself becoming an important representative of the business community. In the past year, it has worked to obtain accelerated and improved visas for businesspersons travelling to neighboring countries. (Only Slovenia does not require a visa for business travelers.) It is currently organizing a trade fair in Tirana, and claims to have earned more than \$20,000 this year in protecting trademarks on behalf of its member, including the expulsion of an unlicensed Coca-Cola distributor at a trade fair in the north. The group has also stated that its mission is to "represent the business community of Tirana in its relationship with the state, to support and protect its legal economic interests and to encourage the development of trade and industry in the District according to these interests." Toward this end, it has established -- on paper at least -- a "Juridical Office" to follow legal issues and interface with lawmakers on legal reform. If it maintains the momentum of the current year, the Chamber could become a leading business organization.¹²

¹² Assistance to the Chamber should include, however, an emphasis on voluntary membership rather than state-mandated membership options. A local businessperson noted that in his experience, mandatory associations tend to have mandatory fees and no mandatory services for those fees. In the team's experience, such mandatory structures tend not to be sustainable on their own merits and have high membership dissatisfaction because they are not demand-based.

The team also met with the Albanian American Trade and Development Association (which now has 70 local members), the Foreign Investors Association of Albania and the Rotary Club. Respondents from the business community noted the existence of several other foreign and domestic associations, including bi-lateral chambers of commerce, and a brand new American-Albanian Chamber of Commerce. The demand for such associations, based on their growth and creation, appears to be quite high at this time.

Discussions with representatives of the various associations and the business community revealed that there is general belief that such associations should have a role in forming and refining commercial law, but the approach tends to be passive. Most respondents envisaged a situation in which they would respond to the government if asked for an opinion, but had not considered the possibility that they might *initiate* such communication or present a draft law for consideration. This attitude underscores the lack of a formal participatory mechanism for participation by the business and legal communities in the development of commercial law.

Despite this passive approach at the national level, several of the associations noted that they are working closely with local governments to improve the business climate in some of the outlying cities. Moreover, the Chamber of Trade and Industry was contacted by at least one candidate for mayor to organize a meeting with Tirana's business community, and then assembled 150 members to meet the candidate. This work at the local level might provide the foundation for public-private partnership initiatives at the national level, including legal initiatives.

g. Consumer Advocacy Associations

The team did not identify or speak with any consumer advocacy groups. With respect to contract law specifically and commercial law generally, consumer advocacy assistance could become very useful with implementation of the new collateral law. It is likely that initial use of the law will be for financing of farm and factory equipment, but also likely that there will be a rapid increase in consumer credit once the law is understood well and applied properly. In other countries (such as the United States), the history of consumer collateral lending has also been a history of abusive lending and collection practices. By working with an Albanian association from the outset, consumer interests could be negotiated from the outset. Such work at this time, however, may be premature. (See the discussion on Market for Collateral Law Reform, above.)

h. Import/Export Associations

There are currently no formal import/export, freight forwarding or transport associations in Albania. Increased economic activity, particularly in relation to the Corridor 8 initiative, may drive the demand for development of such organizations, but assistance is likely to be needed. There is no tradition of special interest associations in Albania, so that little is known about the structure, role or potential activities that these organizations can provide. For contract law, this means that there is not yet a body of stakeholders who can help to develop and harmonize contract practice in the import/export context. Current practices are highly varied, although standardized commercial documents are employed in import/export and shipping transactions.

i. News Media

Matters of commercial law are not generally covered by local news media. Respondents, including foreign professionals who work with local media, noted that the little legal coverage in the press and broadcast media focuses on high profile court cases, and is not generally of very high quality. It was believed by respondents that there are no journalists who specialize in commercial law matters, or even economic and business matters.

The press, like all other Albanian institutions, is still quite new. In interviews with business associations, it was noted that reporting is still quite political, and the respondents expressed reluctance to attempt to use the press through press releases or prepared articles. This could also be due partly to lack of experience by these associations with the press.

Assistance is certainly needed to develop reporting capacity in the areas of commercial law and commercial activity. This reporting gap makes it more difficult to catalyze demand for change based on knowledge of problems and available solutions. The team did not interview any media professionals, and thus cannot offer any opinions regarding the capacity or interest of the media in obtaining assistance. Business associations, on the other hand, expressed interest in support for their own newsletter-based reporting.

j. Self-Regulatory Organizations

The Albanian Institute of Authorized Chartered Accountants is responsible for monitoring the proper use of accounting standards required by Albanian laws. The Institute recognizes that there is a substantial lack of expertise in the area of international accounting standards (IAS), and estimates that no more than ten Albanian accountants can effectively apply IAS. Institute recognizes that the level of professional skills is insufficient for Albanian.

Comments from the private sector supported these conclusions. Several respondents opined that most accounts of local firms are unreliable. One respondent also noted that the auditing practice was also substandard, but felt that there would be little change until companies needed to obtain commercial loans, at which point they would have to apply proper standards. There were few respondents who felt the need for IAS, finding instead that the immediate need was simply to apply the existing Albanian standards, which are sufficient for most companies. IAS is currently required only for international investors, who have the resources to use international accounting firms.

The team did not interview or analyze any other self-regulatory organizations. (For purposes of this assessment, the Bar Association was considered separately as a professional association.) Trading houses and stock exchanges which regulate certain aspects of specialized contracts in other countries have not developed yet in Albania.

k. Trade Groups

The team did not identify or interview any trade groups during this assessment.

4. The Market for Reform of Contract Law

The demand for additional reforms in the area of contract law is essentially flat at this time. Indeed, the legal and business communities have been unable to absorb the legislation changed since 1993, and are generally overwhelmed by the amount of new law and new legal concepts. One attorney even noted that the passage of new commercial laws sometimes delays use of existing laws in all fields, and asked that no major new commercial laws be introduced for a few years. This opinion may be extreme, but the unanimous verdict from the legal community was that the laws are good enough for now, they simply need to be implemented.

There are a few exceptions to this saturated demand, however. First, several respondents noted that while contract law in general is sufficient under the existing Civil Code, some special areas need to be improved. Examples given were franchise, mortgage and pledge, which are contained in general terms in the Code, but are not adequately developed through regulations. On the other hand, it is unlikely that donors will find any generalized support for additional changes locally due to the excess, unimplemented supply of laws. Such special areas should be treated as niche markets, and perhaps addressed only as needed when actual demand exists based on identified investment opportunities or business conditions. In other words, even the identification of specific areas of reform appeared to be based on theoretical demand in case investors want to go into a certain area. Moreover, interested parties should be employed as the champions of such changes, such as banks for mortgage contracts, rather than government sponsors. There is a danger of creating resentment rather than partnership right now if large scale reform projects are mounted from the supply side.

Another exception to the lack of demand for additional reforms is the demand for a change in the way the laws are made. The business and legal communities -- including judges -- noted that when they identify problems or changes needed in the contract law, they have no formal mechanism for either introducing or pursuing these changes. A few respondents noted that there is a council or forum for government and private sector, but none felt that there was an institution representing their interests through a formal legislative mechanism. The team was unable to confirm the existence of this public/private forum, or to identify its make-up or membership.

In many countries, specific reforms are channeled through specialized committees of bar associations, business associations, and even parliamentary legislative reform committees. The infrastructure of these organizations is still weak in Albania, and the private sector in particular wants and needs help. Assistance to private sector organizations should be done in the context of identified needs -- such as collateral contracts once the law is passed -- in order to capture demand and provide motivation for building the specialized organizational structures.

On the supply side, there are several areas where assistance is needed. (It should be noted, however, as has been often repeated, most stakeholders feel that there are enough major laws for now, so that the supply of laws should be de-emphasized in most cases. For example, work on the system of lawmaking in order to obtain private sector input is greatly needed, as noted in in Section II.A.1 of this report (at page 5).

The supply of rational, relevant, commercially necessary laws and regulations is greatly hampered by widespread ignorance of business, commerce and economics. This is true for

businesses, legal professionals and law-makers. Basic education, therefore, is needed for all involved in the process. The country could benefit handsomely from assistance in training lawmakers and policy makers in the economic impact of law, or in simple principles of contract and other law before or simultaneously with the introduction of reform efforts.

As also noted, there is substantial demand for improvement in the judiciary and enforcement of judicial proceedings in contract. The World Bank program of support to the judiciary should provide the foundation for this, so that there seems to be much needed in this respect. Education of judges in contract law and business practices, however, would still be useful and is unlikely to be sufficiently covered by any existing programs.

F. FOREIGN DIRECT INVESTMENT

The team did not review foreign direct investment, but several notable observations were made by respondents during the course of interviews.

First, several respondents noted that foreign investors are often discriminated against in the enforcement of laws. Although the law generally provides for equal treatment, international investors found themselves unequally treated in matters of tax enforcement, with what was described as "harassment" by tax authorities. One respondent explained this as a natural consequence of a system in which tax authorities are expected to meet a quota for revenues collected, and very few companies are keeping books that show profit, so that those with good books and good sales are subject to continual pressure to pay more. The team was not in a position to determine whether the system works as described, but would note that if this is the case, the tax authorities should be encouraged to amend their incentive system by changing their agents' collection requirements to include the number of companies paying taxes, not just the number of taxes paid by a company.

Another example given of discriminatory enforcement was in the courts, where several respondents felt that foreigners could not hope to win or enforce a suit against a local defendant. One respondent cited a case in which the judge expressly recognized that the law was in favor of the foreign plaintiff, but refused to enforce the law against an Albanian. On the other hand, the team spoke with people who had successfully prosecuted suits by foreigners against Albanians, suggesting that this unequal treatment may reflect the uneven quality of the judiciary as much as any anti-foreign discrimination. Hopefully, the Judicial Inspectorate and the Magistrates' School will begin to address these problems.

Second, several respondents noted that there are separate fee schedules for foreign and domestic companies, including the cost of various administrative filings and taxes on labor. The amounts mentioned were not prohibitive, but those commenting on this practice felt it violated the rules of equality under the law guaranteed by the Albanian constitution.

Third, and perhaps most important for the future of investment, foreigners are not permitted to purchase land outright. One respondent also noted an instance in which an Albanian company, owned by foreigners, was not permitted to purchase real property because the judge reviewing the case would not distinguish between the legal person of the company and the individual nationalities of the owners. In any event, there is sufficient literature already in the development library to establish that this practice will inhibit foreign investment. It may even inhibit local investment when the local investors need foreign partners to supply necessary capital. Changing this position is likely to require substantial education of the public and policymakers on the economic impact of such a law, while also addressing the fears of foreign domination, loss of sovereignty or other concerns that may support the existing law.

Local investors also commented on discrimination, but on discrimination *against* them in favor of foreigners. They noted that bidding on many of the privatized state assets had disallowed the Albanian participation by requiring that all bidders have 10, 15 or more years of experience to qualify. In a country that has only permitted private enterprise for nine years, this is a de facto

elimination of all potential Albanian investors. Again, the team could not confirm whether the bids were in fact structured in this way, but noted that there is substantial resentment in some circles based on a perception that the playing field is not level.

Finally, foreign or local investors who produce or sell trademarked products must battle against a large amount of counterfeiting. In addition to a number of respondents who commented on this point, the team noted that even the local television station carried commercials regarding counterfeit vegetable oils. The newly enlivened Chamber of Trade and Industry noted that one of its functions is to help protect the copyrighted and trademarked property of its members, and related several cases in which they had successfully dealt with counterfeiters. Others, however, were not as positive, noting that even when counterfeiters have been identified and a case against them established, no meaningful sanctions are applied.

Albanian policy makers will need to understand and address the problems faced by investors before the situation changes. Respondents addressing the issue felt that policy makers did not generally understand that Albania had to compete with its neighbors and other developing countries for investment dollars. Significantly, one respondent who worked with foreign investors noted that more were now leaving Albania -- withdrawing their investments -- than coming in.

If policy makers decide to address these issues, it might be useful for someone to sponsor an "Investors' Roadmap" assessment, in which the costs of starting, setting up and running a business are benchmarked against international best practices and comparable economies. If followed by a program of eliminating unnecessary bureaucratic restraints, this can be a very effective tool for improving the investment environment.

G. TRADE

The team did not assess the trade environment, but prior familiarity with customs programs, plus a number of comments from respondents, provided some noteworthy observations.

A multi-donor effort is currently underway to assist customs officials in reducing the flow of smuggled goods and enforcing customs laws equitable. USAID-supported efforts were reported by a number of non-USAID respondents to be making substantial progress. However, much work is still needed.

The business community expressed frustration with the new system of customs evaluation in which reference prices are used to determine whether the stated value of a shipment is within established commercial pricing for similar shipments. Reference values have been employed due to the high degree of undervaluation on invoices. Respondents working in this area felt that there is insufficient information flow between the public and private sectors on the system, why it is employed, and how it works. There appears to be a clear need for additional information and communication in this area.

Unequal application of customs duties was cited as a problem, providing competitive advantages to those who are able to smuggle or understate the value of their goods. One respondent expressed hope that the situation was improving, citing the integrity of the new director of customs and the positive reaction of the customs service when he complained of problems at a specific post. The existing customs programs should continue to make progress in improving the application of duties, but it might still be worthwhile to assist with increasing public awareness of the customs laws, and the economic impact of thwarting the law.

IV. ANNEXES

ANNEX 1. CONTACTS

ANNEX 2. COMMERCIAL LEGAL AND REGULATORY REFORM (CLIR) INDICATORS:

Summary Scores
Implementing Institutions Matrix
Detailed Scores:

- A. Bankruptcy**
 - 1. Legal Framework (not scored)
 - 2. Implementing Institutions
 - 3. Supporting Institutions
 - 4. Market for Effective Bankruptcy System
- B. Collateral**
 - 1. Legal Framework
 - 2. Implementing Institutions
 - 3. Supporting Institutions
 - 4. Market for A Modern Collateral System
- C. Company**
 - 1. Legal Framework
 - 2. Implementing Institutions
 - 3. Supporting Institutions
 - 4. Market for Efficient Company Law
- D. Competition (not assessed)**
- E. Contract**
 - 1. Legal Framework
 - 2. Implementing Institutions
 - 3. Supporting Institutions
 - 4. Market for Efficient Contract Law
- F. FDI (not assessed)**
- G. Trade (not assessed)**

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ANNEX 2. COMMERCIAL LEGAL AND REGULATORY REFORM (CLIR) INDICATORS

Summary Scores

Implementing Institutions Matrix

Detailed Scores:

- A. Bankruptcy**
 - 1. Legal Framework (not scored)
 - 2. Implementing Institutions
 - 3. Supporting Institutions
 - 4. Market for Effective Bankruptcy System
- B. Collateral**
 - 1. Legal Framework
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- C. Company**
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 - 3. Supporting Institutions
 - 4. Market for Efficient Company Law
- D. Competition (not assessed)**
- E. Contract**
 - 1. Legal Framework
 - 2. Implementing Institutions
 - 3. Supporting Institutions
 - 4. Market for Efficient Contract Law
- F. FDI (not assessed)**
- G. Trade (not assessed)**