

Incentives for Foreign Investments
– Case Study of Bosnia and Herzegovina

Workshop on Case Studies on overcoming barriers to
investments in energy efficiency and renewable energy
projects through policy reforms

Kiev, November 10.-11., 2009

General description of the case study

The aim of the case study is the establishment of a promotion agency and a support fund to improve the climate for foreign investments in the country

- In 1998, the Federation Law on Corporate Income Tax, and the Law on the Policy of Foreign Investment have been adopted and the Foreign Investment Promotion Agency (FIPA) was established as State Agency
- Key mission of the FIPA is to further develop and improve the business climate of the country
- In 2007, a support fund has been designed within the FIPA providing financial support for foreign investors (FISF with a yearly budget of 1mln EUR)

Country

- This case study has been implemented in Bosnia and Herzegovina

Timeframe

- The case study as described here starts with the adoption of the Law on the Policy of Foreign Investment in 1998
- The Foreign Investors' Support Fund (FISF) was established in 2007 and became operative in 2008

Objective

- To introduce financial incentives for the promotion of foreign investments and to address obstacles related to the limited availability of foreign and domestic investments for renewable energy and energy efficiency sources
- To open Bosnia and Herzegovina's economy to more foreign investments

Financing Institution

- The Council of Ministers of Bosnia and Herzegovina is the main cost-bearer as it established the Foreign Investment Promotion Agency (FIPA)
- The Government of the Federation of Bosnia and Herzegovina has also participated financially in the development and implementation of related laws

Removed barriers to investments in EE and RES

The case study contributes in removing legal and administrative barriers for foreign investments and is recommended for the Republic of Moldova and the Russian Federation

Republic of
Moldova

Kazakhstan

Russian
Federation

Ukraine

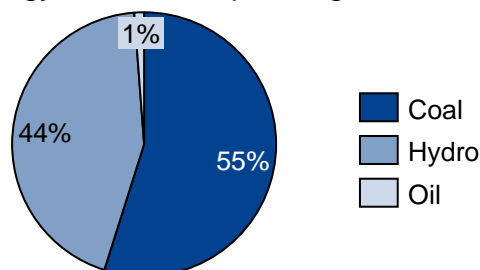
- **Currently, in the Republic of Moldova, the MIEPO (Moldovan Investment and Export Promotion Organization) is established in order to promote and support business development**
- **Similar agencies or investment promotion centers are present also in Kazakhstan (KAZINVEST), in the Russian Federation (National Investment Agency) and in Ukraine (InvestUkraine)**
- **However, these promotion centers do not have an established financial budgets and they are not enclosed in clear regulatory frameworks such as is the case of the FIPA**
- **The establishment of a clear financial budget, of target sectors for investments (e.g. in the area of energy efficiency and renewable energy sources) and of a clear regulatory framework for attracting foreign investors in the countries would foster the development of markets for energy efficiency services and renewable energy sources**

Background to the case study

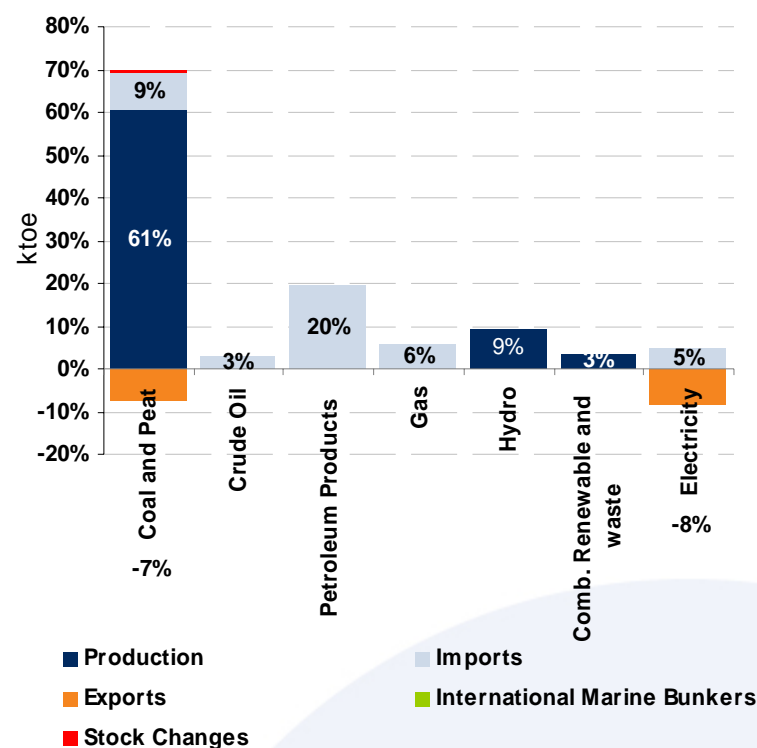
Bosnia and Herzegovina has a good potential for investments in EE and RES, but the investment climate of the country suffers from the administrative structure of the country

- Following the Dayton agreements, the state of Bosnia and Herzegovina has no competences regarding energy policy and national energy strategy, which is regulated at the entity level
- This has led to the establishment of parallel policies, authorization procedures and the presence of administrative and legal barriers for investors wanting to operate in both entities
- The establishment of the FIPA and of the related fund is a policy measure at the state level and therefore helps overcome the existing barriers related to the administrative structure

Energy sources for power generation¹⁾



Energy balance of Bosnia and Herzegovina in 2006¹⁾



1) Source: International Energy Agency (IEA). (2006), Energy Balance for Bosnia and Herzegovina.

Key players involved in the implementation of the case study

The implementation involved the **Council of Ministers**, the **Foreign Investment Promotion Agency (FIPA)**, and the **Government of Bosnia and Herzegovina**

Key Player	Description	Role
The Council of Ministers	The Council of Ministers of Bosnia and Herzegovina (including the Federal Minister of Finance)	Responsible for the establishment of the FIPA and the fund (provision of financial resources). The FIPA and the Fund apply for the entire Republic of Bosnia and Herzegovina.
FIPA	The Foreign Investment Promotion Agency	<p>The Foreign Investment Promotion Agency (FIPA) as main governmental organization for the promotion and the support of foreign investments and as manager of the fund. The FIPA has the mission to</p> <ol style="list-style-type: none"> 1) attract and maximize the flow of foreign direct investment into Bosnia and Herzegovina, and encourage existing foreign investors to further expand and develop their businesses in Bosnia and Herzegovina 2) facilitate the interaction between public and private sectors, and have an active role in policy advocacy in order to contribute to continually improving the environment for business investment and economic development 3) promote a positive image of Bosnia and Herzegovina as a country that is attractive to foreign investors
The Parliament	The Parliament of the Federation of Bosnia and Herzegovina	Responsible for the definition and adoption of Laws

Approach for case study implementation

While the FIPA was established and became operative in 1998, its regulatory framework was only approved in 2004 – establishment of the FISF followed in 2007

Phases	Phase 1	Phase 2	Phase 3	Phase 4
Timescale	1998		2004	2007
Milestones	Adoption of the Law on the Policy of Foreign Investments	Establishment of the FIPA	Adoption of the Law on FIPA of Bosnia and Herzegovina	Establishment of the Foreign Investor Support Fund (FISF)
Responsible Key Player	The Federal Minister of Finance	The Council of the Ministers	The Government of Bosnia and Herzegovina	FIPA
Results	<p>Establishment and implementation of</p> <ul style="list-style-type: none"> •The Law on the Policy of Foreign Direct Investment (FDI Law) • The Law on Corporate Income Tax (CIT Law) including exemptions and appliance (see Annex for details on the law) 	<p>Establishment of the FIPA based on the decision regulating the main competences and objectives of the FIPA:</p> <ul style="list-style-type: none"> •Directs the investors towards potential investment projects •Presents the advantages and characteristics relating to the projects (e.g. legal, economic and financial framework, tax system) •Organizes and/or participates at seminars, exhibitions and conferences on promotion of the state; •Proposes legislation and legal measures aimed at promoting investment conditions 	<p>Adoption of the Law on Foreign Investment Promotion Agency based on the decision approved in 1998, the law regulates the main competences and objectives of the FIPA</p>	<ul style="list-style-type: none"> • In June 2007, the Foreign Investors' Support Fund (FISF) was established • The FISF became operative as of February 2008 • The FISF distributes its funds to eligible foreign investors • Foreign investors must follow the procedures determined in the Rule Book on the Manner of Distributing Resources for the Support of Foreign Investors
End result	Establishment of FIPA and FIPA regulatory framework and establishment of FISF			

Impact of case study implementation

The most important impact of the implementation of FIPA and FISF is the maximization of the inflow of foreign investments which strengthens the economy of Bosnia and Herzegovina

Economical Impact	Environmental Impact	Social impact
<ul style="list-style-type: none"> • The introduction of the Foreign Investors Support Fund (FISF) and additional fiscal incentives (taxation) mainly had an economical impact: <ul style="list-style-type: none"> • It attracted and maximized the flow of foreign direct investment into Bosnia and Herzegovina (in 2007 direct foreign investments reached EUR 1'628 mln an all-time high) • It encourages existing foreign investors to further expand and develop their businesses • It facilitates the interaction between public and private sectors through joint actions • It contributes to continually improving the environment for business investments and economic development • It promotes a positive image of Bosnia and Herzegovina as a country that is attractive to foreign investors 	<p>An indirect impact is the increased deployment of renewable energy sources through the development and implementation of energy projects</p>	<p>An indirect impact is the creation of employment if projects are setup in Bosnia and Herzegovina</p>

Overall impact
<ul style="list-style-type: none"> • The establishment of the FIPA led to an effective networking with both the public and private sectors. It provides a link between governmental and non-governmental institutions (i.e. foreign investment agencies of Balkans) in order to facilitate investment and business development through the signature of MoU's (memorandum of understanding) • Furthermore, the cooperation between local, regional and international organizations (i.e. World Bank, EU Commission) to promote and enhance the investment environment in Bosnia and Herzegovina has been strengthened and shall be expanded in the future

Costs of case study implementation

The costs for implementation of the Foreign Investor Support Fund amount to at least 8-10 mln EUR, without the yearly budget of 1 mln EUR

	Costs	Comments
Phase 1-3	n.a.	<ul style="list-style-type: none"> The implementation of the Case Study required financial resources for the setting-up of the Foreign Investor Support Fund (FISF) which amount to approximately EUR 8-10 mln. A detailed breakdown of these costs is not available. The annual budget of the FISF is EUR 1 mln, with a maximum of 150'000 EUR provided per applicant The Council of Ministers is the main cost-bearer <ul style="list-style-type: none"> Establishment of FIPA Provision of the required financial resources for the establishment and operation of the FISF The Government of the Federation of Bosnia and Herzegovina has also participated financially in the development and implementation of related laws (i.e. law on taxation)
Phase 4 Establishment of FISF	8-10 mln EUR	
Yearly budget FISF	1 mln EUR	

1) Source: United Nations. (2007). Case Studies of Market Transformation: Energy Efficiency and Renewable Energy.



Regulatory preconditions

Regulation on foreign investors rights and obligations, tax incentives, and bilateral agreements are necessary for establishing an attractive climate for foreign investments

Solid legal basis

- Solid legal groundwork to provide transparency and free access in the country (e.g. bankruptcy, collateral, and enforcement laws)

FDI Law

- The Law on the Policy of Foreign Direct Investment
- The law ensures the national treatment of foreign investors: Foreign investors have the same rights and obligations as residents of Bosnia and Herzegovina

CIT Law

- The Federation Law on Corporate Income Tax
- The law ensures tax incentives for foreign investors

FIPA Law

- The Law on Foreign Investment Promotion Agency
- The law regulates the main competences and objectives of the FIPA

Bilateral agreements

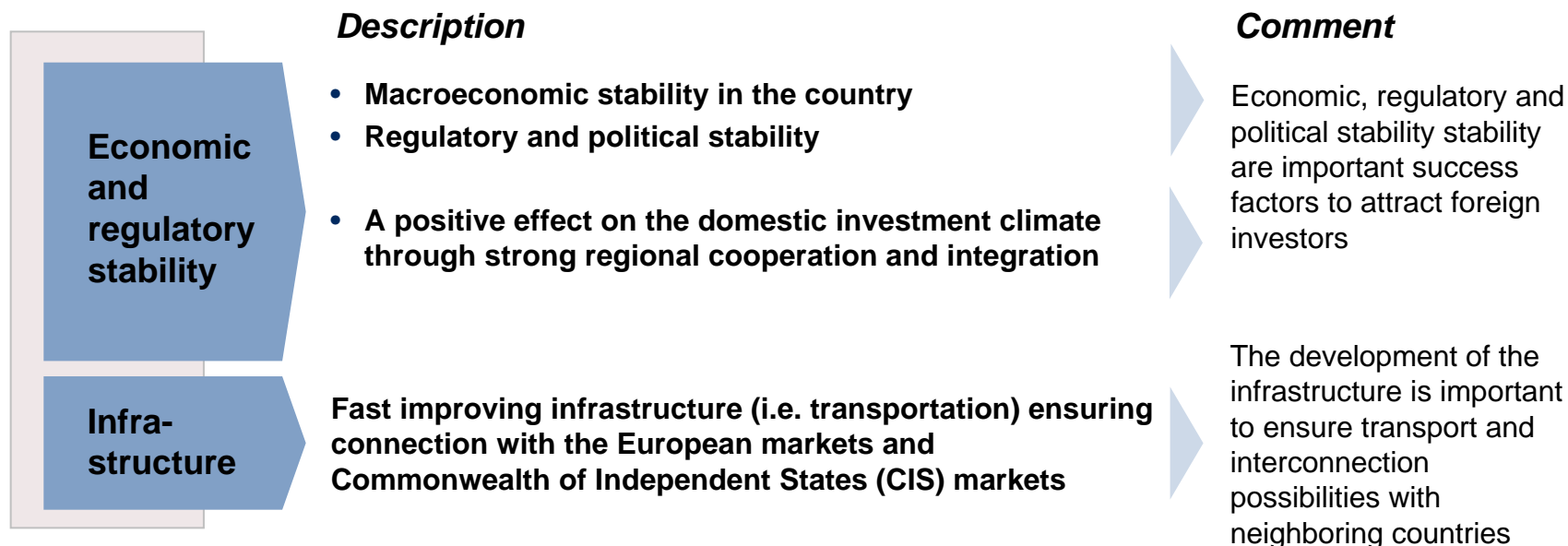
- Bilateral agreements and treaties avoiding double taxation
- Bilateral agreements for mutual promotion and protection of capital investments

Regional investment policies

- Regional investment policies enabling the development of infrastructure projects
- Regional investment policies enabling the development of power generation projects

Critical success factors

The economical stability and the regional cooperation with foreign investors are most important for a successful case study implementation



Most critical among the success factors is the economical and regulatory stability → As such investors can find a stable and transparent investment environment and minimize risks

Risks

Main risks to the successful implementation still lie within an intransparent bureaucracy and regulation – Risks from the case study are neglect of developing domestic companies and the energy sector

	Risk factors	Risks	Possible effects	Comments / Recommendations
Risk for Implementation	Bureaucracy / Regulation	<ul style="list-style-type: none"> The general situation is still not transparent enough for foreign investors, inefficient bureaucracy can still undermine investments A complex legal and regulatory framework and non-transparent business procedures (e.g. public procurement tenders) 	<ul style="list-style-type: none"> Foreign investments cannot be attracted Foreign investors are not able to win projects 	<ul style="list-style-type: none"> Close cooperation between FIPA and foreign investors to overcome administrative burdens Additional information on the regulation and conditions for tenders should be added in several languages (e.g. English, French)
		<p>Foreign investors do not share their know-how</p>	<p>Domestic companies do not improve their know-how within the industry sectors, particularly in matters of renewable energy sources and energy efficiency</p>	<p>Cooperation between foreign investors and domestic companies should be added as a precondition to foreign investment in Bosnia and Herzegovina</p>
Risk from Implementation	Energy sector	<p>The energy sector, particularly energy efficiency and renewable energies are not developed with projects supported by the FISF</p>	<p>FISF capital does not support the energy sector</p>	<p>Assign a certain percentage of FISF supported projects to renewable energy and energy efficiency related projects</p>

General recommendations for replication

When replicating the case study, besides setting up a national investment agency, foreign investment should be attracted by strong cooperation at the regional and national level

Several “lessons learned” from the implementation of the Case Study should be considered for successful replication of the Case Study in other countries

- The formulation of a national and regional investment promotion strategy and the establishment of a coordinating National Investment Agency have a beneficial influence
- Strong regional cooperation and integration have a positive effect on the national investment climate
- Attractive financial laws for foreign investors can successfully break new ground and profoundly improve general conditions for foreign investments
- Joint-Presentations of national and regional institutions and authorities are the most effective in attracting foreign direct investments

Recommendations for replication: concrete actions

Concrete recommendations for replication include the setup of laws for the promotion of foreign investments, the establishment of a FIPA, and the setup of a FISF

Recommendation	
Pre-condition	1 Establish a solid legal basis and bilateral agreements (e.g. regarding double taxation)
	2 Establish regional investment policies, enabling the development of infrastructure, and power generation projects
Recommendation for implementation	3 Establish a law on the Policy of Foreign Direct Investment
	4 Establish a law on Corporate Income Tax
	5 Establish a law on the objectives and the conduct of an agency for promotion of foreign investment
	6 Consult experts on project financing for setting up the financial aspects of the project
	7 Establish an agency for promotion of foreign investments (FIPA) with the objectives to inform and support foreign investors
	8 Find financial support for a Foreign Investor Support Fund, either national (e.g. government) or international (e.g. international donor organizations)
	9 Setup a Foreign Investor Support Fund and the according requirements for applying for the fund's resources
	10 Inform foreign investors about the project developing possibilities and the incentives in the according country
	11 Establish procedures for foreign investors interested in applying for the FISF's resources
	12 Monitor the projects setup with the resources of the FISF and make sure that they comply to the according rules

Conclusions

By implementing a proper regulatory framework and setting up an agency as contact for foreign investors, Bosnia and Herzegovina has made significant efforts to attract foreign investors

- **By implementing the laws and concept presented in this case study Bosnia and Herzegovina has made significant efforts to open its economy to foreign investment**
- **One of the most important step in attracting foreign investments is the State-level "Law on Foreign Direct Investment", which provides a broad framework for foreign investment:**
 - **The law accords foreign investors the same rights as domestic investors**
 - **With a few exceptions, there are no restrictions on investment**
 - **Investors are also protected from changes in laws regarding foreign investment. Should the government make changes, the investor may choose the most favorable set of rules to apply.**
 - **The law prohibits expropriation and nationalization of assets, except under special circumstances and not without due compensation**
 - **Finally, because of the requirement for equal treatment, the law also treats foreign investors the same as domestic investors with respect to bidding on privatization tenders**
- **Additionally, the Foreign Investment Promotion Agency acts as main contact for foreign investors and help to overcome bureaucratic and regulatory burdens still existing in Bosnia and Herzegovina**

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The background of the slide features a close-up, artistic photograph of a green plant stem with a small globe of the Earth resting on it. The lighting is dramatic, highlighting the textures of the plant and the globe. At the bottom of the slide, the word "PÖYRY" is written in a large, bold, light-colored sans-serif font, with a double slash symbol above the 'Y'.

PÖYRY

Annex: Sources

List of sources used for case study elaboration

- **Law on the Policy of Foreign Investment in Bosnia and Herzegovina (1998). Official Gazette of Bosnia and Herzegovina, 17/98 and 13/03. Retrieved September 29, 2009, from <http://www.fipa.gov.ba/>**
- **Federation Law on Corporate Income Tax (December, 2007). FBiH Official gazette no. 97/07. Retrieved, September 29, 2009, from <http://www.fipa.gov.ba/>**
- **Bakic, T. & Theiss, W. (2008). Bosnia. Foreign investors' rights. Retrieved September 29, 2009, from <http://www.iflr1000.com/LegislationGuide/47/Foreign-investors-rights.html>**
- **Law on the Foreign Investment Promotion Agency of Bosnia and Herzegovina (December, 2004). Retrieved, September 29, 2009, from <http://www.fipa.gov.ba/page.asp?id=10>**

Annex: FDI Law

The FDI Law was implemented by the Federal Minister of Finance to strengthen the protection of foreign investment

Law	Titel	Description
FDI Law	The Law on the Policy of Foreign Direct Investment	<p>The FDI Law ensures the national treatment of foreign investors: foreign investors have the same rights and obligations as residents of Bosnia and Herzegovina. The FDI Law specifically stipulates that foreign investors have the following rights and benefits:</p> <ul style="list-style-type: none"> (a) the right to invest and reinvest the profits of such investments into all sectors of the economy under the same conditions as any Bosnia and Herzegovina resident, with the exception of the armament and media sectors, where foreign control of a legal entity is limited to 49% (b) if the foreign investment represents a contribution in kind into a company already established or to be established by a foreign investor or jointly by a foreign investor and domestic physical persons or legal entities, the contribution shall be exempted from paying customs (with the exception of passenger cars, slot and gambling machines, and parts of them), provided that the conditions below are fulfilled (c) the right to transfer abroad, freely, without delay, and in any currency, the profit resulting from investment in Bosnia and Herzegovina (d) the right to be entitled to the same ownership rights over real estate (once registered as the owner) as domestic nationals and resident legal entities <p>The FDI Law strengthens the protection of foreign investments, stipulating that foreign investments shall not be subject to any act of nationalization, expropriation, or measures with similar effects, except when in the public interest in accordance with applicable laws and regulations, and against the payment of appropriate compensation. The FDI Law states that the rights and benefits of foreign investors and the obligations imposed on them by the FDI Law cannot be terminated or overruled by subsequent Laws and regulations. Should a subsequent Law or regulation be more favorable to foreign investors, the investor will have the right to choose the regime according to which the investment will be regulated</p>

Annex: CIT Law

The CIT Law was implemented to generate tax incentives for foreign investments

Law	Titel	Description
CIT Law	The Federation Law on Corporate Income Tax	<p>The Federation Law on Corporate Income Tax (CIT) of the Federation of Bosnia and Herzegovina states that a taxpayer that generates more than 30% of its total turnover from export activities within one calendar year is exempt from paying CIT for that year (Article 31)</p> <p>A taxpayer that invests at least BAM 20 mln (USD 16 mln) in the territory of the Federation of Bosnia and Herzegovina within a period of five consecutive years is exempt from paying CIT for five years, starting with the first year of the investment; at least BAM 4 million must be invested in this first year (Article 32)</p> <p>Taxpayers must undertake certain actions and provide the competent tax authorities with evidence proving their entitlement to these CIT exemptions</p>