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FORGING PARTNERSHIPS FOR LEGAL REFORM

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ABOUT THE EBRD

The EBRD is a multilateral bank that promotes the development of the private sector and entrepreneurial initiative in 36 economies across three continents. The Bank is owned by 73 countries as well as the EU and the EIB. EBRD investments are aimed at making the economies in its regions competitive, well-governed, green, inclusive, resilient and integrated.

ABOUT THIS JOURNAL

Legal reform is a unique dimension of the EBRD's work. Legal reform activities focus on the development of the legal rules, institutions and culture on which a vibrant market-oriented economy depends. Published once a year by the Office of the General Counsel, the *Law in Transition* journal covers legal developments in the region, and by sharing lessons learned aims to stimulate debate on legal reform in transition economies.

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FORGING PARTNERSHIPS FOR LEGAL REFORM

FORGING PARTNERSHIPS TO DELIVER LEGAL REFORM

Since the publication of the last issue of this journal, the EBRD has, through its Legal Transition Programme (LTP), continued to advocate legal reform in the countries where it invests. The underlying philosophy, promoted over the last three decades, is that "good laws make for good economies". There have been many significant achievements over the last year, some of which are showcased in this issue of the *Law in Transition* journal.

In particular, the LTP has provided continued support to Ukraine, which is a key priority for the EBRD. Among other things, the Bank drew up a detailed concept, technical specifications and an implementation plan for an online small claims court, which were endorsed by Ukraine's Supreme Court and High Council of Justice. The proposed platform aims to use guidance tools and digital access to the courts to help small and medium-sized enterprises in Ukraine (including displaced businesses) to enforce payments and contracts. Meanwhile, in a different sector, the Bank also helped the Ukraine Geology Service to undertake the collection, processing and digitisation of approximately 6,000 geological documents. Sixty-five per cent of those scanned documents related to deposits that are expected to contain minerals on the EU's list of critical raw materials – minerals that are needed for technologies driving the digital transition and the shift to green energy. In addition, the team supported the development of a dedicated online platform for that scanned geological information, helping to make it easily accessible to investors, reducing investors' risks and preventing significant unnecessary costs. We expect Ukraine to remain a top priority for policy dialogue and technical cooperation on legal matters.

This is a special time for the EBRD, with the Bank likely to begin investing in a number of new countries, subject to fulfilment of the necessary legal requirements. In addition to Iraq, the Bank also plans to start operating in six countries in sub-Saharan Africa: Benin, Côte d'Ivoire, Ghana, Kenya, Nigeria and Senegal. Alongside investment in these countries, the Bank will also begin delivering policy advice and technical cooperation. This will, of course, include LTP services, which will be delivered in close collaboration with other EBRD units working on policy dialogue. The objective will be to help these countries to create a predictable, transparent and investor-friendly legal framework for business.

While we will doubtless face significant challenges in these new countries, we believe that many of the skills and lessons we have learned from economies where we currently operate will be transferable. One of those lessons, which is the theme of this issue of the *Law in Transition* journal, is about the need to forge strong partnerships in order to deliver reforms.

The stories in this journal showcase the various types of partnership that the LTP establishes through its work, using examples from the recent past. These range from partnerships with other international organisations (such as the World Bank, the Asian Development Bank, the International Development Law Organization and the World Trade Organization) to collaborations with donors, national authorities, non-governmental organisations (NGOs) and private-sector organisations. One overarching message emerges from all of these stories: the impact of our technical cooperation programme is always much stronger when it involves collaboration with others. Our lawyers can achieve much more in partnership with others than they could if they worked in isolation. Over the years, they have developed strong relationships with partners, yielding substantial synergies and significant results.

One emblematic example of this approach is the first story in this issue, which is about railway sector reforms in the Western Balkans. This project involves investment by both the EBRD and the European Investment Bank, while the policy agenda is closely linked to the adoption of the EU's acquis communautaire and entails coordination with EU delegations in the Western Balkans, as well as members of the Transport Community. The project also involves collaboration with the International Monetary Fund, the World Bank and Agence Française de Développement. In other words, this project has resulted in the establishment of a very wide and diverse network of relationships, which have pushed the reform agenda and further developed the railway sectors of the relevant countries. This is the type of multi-partner arrangement that boosts the Bank's policy dialogue and achieves optimum results.

Other stories also contain valuable lessons, particularly on the need to have strong local stakeholders within national authorities who can champion the proposed reforms in the relevant jurisdiction. There is also a need to call on the immense expertise of the private sector and NGOs to deliver key messages. Lastly, those working on legal reforms need to convince donors to allocate funds to support deserving initiatives, since it is no secret that good projects require funding.

I hope that the stories in this journal will inspire others to enter into partnerships with relevant stakeholders and promote reforms, supporting progress towards the achievement of the United Nations' Sustainable Development Goals in the EBRD regions and beyond.

Enjoy the issue!

MICHAEL STRAUSS
GENERAL COUNSEL, EBRD

UNITED WE STAND

I am delighted to present the 2024 edition of the *Law in Transition* journal. This journal showcases the work of the EBRD's Legal Transition Programme, which seeks to improve the legal framework for investment in the economies where the Bank operates. This year, the various articles highlight the "partnership" element of our work, since each of the EBRD's success stories is a real team effort, involving other international organisations, donors, national authorities, NGOs and/or private-sector actors.

Each article demonstrates that a particular partnership has been instrumental in delivering outcomes and impact on the ground. The overarching lesson is that we need to establish strong relationships with key stakeholders in order to achieve the United Nations' Sustainable Development Goals. "United we stand, divided we fall," as the saying goes.

In the first story, Pavle Djuric, Duncan Kernohan and Jelena Cirkovic explore the links between investment in Western Balkans railways and institutional and governance reforms in that sector. This story is an excellent illustration of the role that partnerships play in our work, showing how national and international development organisations are working with political entities at regional and national level to improve the railway sector in the Western Balkans.

The second article, by Eliza Niewiadomska and Michael Strauss, looks at how the EBRD and the World Trade Organization are working to promote open markets for public procurement in economies where the Bank operates – a win-win scenario that primarily benefits small and medium-sized enterprises (SMEs) in those areas.

The next story, by Anar Aliyev, Nikolay Angelov and Marcel Schlobach, showcases an EBRD programme that is helping SMEs to make improvements in the area of ESG in partnership with the Swiss State Secretariat for Economic Affairs and a number of banks in Central Asia and the Caucasus.

In the fourth article, Gian Piero Cigna explores the role of governance – the "G" in ESG. He argues that establishing appropriate governance is essential in order to realise ESG ambitions and prevent greenwashing, providing plenty of examples from recent practice.

The fifth story, by Veronica Bradautanu, Yulia Shapovalova and Patricia Zghibarta (with contributions from Lizaveta Trakhalina), looks at the EBRD's efforts to improve law enforcement in Moldova, which have involved promoting mediation as an alternative dispute resolution mechanism and enhancing the practices of enforcement officers. The key partners in this project have been Moldovan authorities, the International Development Law Organization, relevant private-sector actors and donor countries (namely, Luxembourg, the United Kingdom and the United States of America).

In the next article, Catherine Bridge Zoller takes stock of two decades of cooperation between the EBRD and Serbia's Bankruptcy Supervision Agency (BSA) – a partnership that has, in recent years, also involved the provision of advice on the BSA's digital tools. That piece also contains an interview with Dragisa Petrovic, Director of the BSA.

Next, Paul Moffatt and Julia Anderson take us to Azerbaijan for a story showing how the country is using the internet to shape its future. The Bank has been working with the Azerbaijani authorities on an ambitious digitalisation programme encompassing both investment and technical cooperation.

The eighth article, by Vesselina Haralampieva and Divya Chawla (with additional input from Khalid Hamza and Solomiia Petryna), looks at the contribution that company boards and independent directors can make to the green transition process in the EBRD regions. It showcases the Bank's collaboration with the Climate Governance Initiative and contains input from that organisation as well.

The last piece, by Milot Ahma and Liubov Skoryk (with contributions from Markus Renfert, Serhiy Savchuk and Neal Harm), highlights the EBRD's efforts to promote factoring as an alternative source of finance for SMEs. It also reflects on the partnerships that the Bank has forged with professional associations promoting factoring, as well as the EBRD's recent collaboration with Ukrainian authorities aimed at modernising the legal framework for factoring in that country.

We hope that, by sharing the EBRD's experiences in this area, these stories will encourage policymakers, donors and other stakeholders working on legal reforms to come together and pool their efforts in pursuit of the Sustainable Development Goals.

As usual, all feedback on the journal is welcome.

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SECTOR AND GOVERNANCE REFORMS IN SUPPORT OF SUSTAINABLE, INTEGRATED AND WELL-GOVERNED RAILWAYS

“Railway transport stands as a pivotal infrastructure for modern economies, providing a vital mode of connectivity for freight, urban and intercity passenger transport, which is growing in importance across Europe.”


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As part of its transition mandate, the EBRD leverages investments to achieve policy results that enable the development of fully functioning market economies. In the Western Balkans, these investments contribute to integration with the EU single market and support regional connectivity. This article explores the link between investments in Western Balkans railways and institutional and governance reforms in this sector.

INTRODUCTION

Railway transport stands as a pivotal infrastructure for modern economies, providing a vital mode of connectivity for freight, urban and intercity passenger transport, which is growing in importance across Europe. A well-integrated and efficient rail network can provide major advantages for economic development by lowering transport costs, increasing connectivity and expanding labour markets.

Rail is particularly valuable in efforts to support greening of the economy as it is generally a more sustainable transport mode than road or air transport. This is largely due to its lower carbon footprint and potential for electrification, as well as its much greater spatial efficiency for transporting larger volumes of goods and people. The growing use of renewable energy sources further diminishes the environmental impact of railway transport, aligning with global objectives to reduce greenhouse gas emissions.

For the private sector, using railways for freight and passenger transport fits with increasingly stringent environmental regulations, but also meets growing consumer demand for sustainable transport practices. Yet rail services often struggle to be competitive with alternative modes of transport, which generally offer greater access and flexibility for most types of users.

The European Union's (EU) investment and reform packages (via the creation of the Single European Rail Area and Trans European Transport Network) are helping to address these challenges – with a broad objective of doubling high-speed rail traffic by 2030.[1] Increasingly, this creates new opportunities for direct investment and operation of rail services in European countries that can provide a valuable stimulus for new connections and competition in incumbent-led markets. For example, the requirement for mandatory competitive tendering of public service obligations that became effective from the start of 2024 is likely to create many new opportunities.[2]

The potential for growth in commercial activities in and around stations and wider rail sector assets is also a growing theme – with, for example, the sale of Network Rail railway arches in the United Kingdom achieving GBP 1.5 billion (€1.74 billion) in 2018, capitalising on the growth and potential in this area with the formation of the Arch Company.

While the private sector is vital to the growth and expansion of rail services, the public sector will continue to play a crucial role by providing infrastructure, supporting socially beneficial services, regulating access and use of the network and, in many cases, operating services through state-owned enterprises (SOEs). Developing an effective balance between public-sector interests and the harnessing of private innovation and efficiency will continue to be an important feature of the rail sector.

EBRD INVESTMENTS IN WESTERN BALKANS RAILWAYS – A PUSH FOR GREATER INTEGRATION

Given the historic underinvestment in railways in many of the jurisdictions where the EBRD invests, including the Western Balkans, it is clear that the shift to rail envisioned in European objectives and elsewhere cannot be achieved without substantial investments, together with operational and governance improvements of key actors in the sector, which are in state ownership.

This backdrop provides fertile ground for linking the EBRD's investments with governance improvements in relevant railway SOEs and sector reforms – especially those related to liberalising the sector and introducing independent economic regulation to increase competition and improve use of the railway infrastructure.

1 See European Commission (2021).
2 Under EU Regulation (EC) 1370/2007.

Typical features of SOEs – such as unclear strategies, lack of proper business and investment planning, inadequate asset management and internal controls, poor monitoring of business delivery and reliance on scarce government financing – are made worse by the fact that most railway sector companies in the region are monopolies. This further weakens incentives for efficiency, customer responsiveness and efficient pricing, creating adverse outcomes for citizens and economies.

In response to this challenge, the EU has long promoted structural reform of the sector through interoperability, competition and wider sectoral efficiency. This is primarily achieved through four consecutive rail packages that create requirements for: (i) formal separation of infrastructure and rail operations; (ii) introduction of rules on open access and track access charges; (iii) technical harmonisation; and (iv) formation of an independent regulatory body to oversee key interactions in the sector.

“Given the historic underinvestment in railways in many of the jurisdictions where the EBRD invests, including the Western Balkans, it is clear that the shift to rail envisioned in European objectives and elsewhere cannot be achieved without substantial investments, together with operational and governance improvements of key actors in the sector, which are in state ownership.”

Recognising the critical role of sustainable transport for economic growth and regional integration of the Western Balkans, the EBRD supports EU objectives for the sector's development and has been investing considerable resources into revitalisation and better rail connectedness in the region.

Furthermore, the EBRD is the key strategic partner of the Western Balkans countries, supporting their efforts to rebuild railways and promoting the shift from road to rail as a greener mode of transport. The Bank provides investment finance and comprehensive policy support aimed at improving the governance and management of national railway companies. To date, the Bank has lent more than €1.6 billion to Western Balkans countries to finance investments in the rail sector.

In Serbia, for instance, the EBRD is providing significant funding to upgrade the railway infrastructure as part of the pan-European Corridor X, which is vital for linking Western Europe to the Balkans and potentially further to Bulgaria and Greece, making it a key trade route for the region. In particular, the funding of €2.2 billion is jointly provided by the EBRD (investment loan of €550 million), the European Union (investment grant of €598 million) and the European Investment Bank (investment loan of €1.1 billion) to modernise the 230-kilometre high-speed rail link connecting Belgrade to the country's second-largest city, Niš.[3]

In North Macedonia, the EBRD is financing construction of the line on Corridor VIII that connects the Adriatic Sea to the Black Sea with a €175 million loan that is part of a total financing package of up to €560 million.[4] In Albania, the Bank is supporting the rehabilitation of the country's rail network with €136 million invested in the upgrade of two of the main lines between Tirana and Durres and Vore and Hani i Hotit.[5]

In addition to the construction and rehabilitation of the railway lines, the EBRD also provides financing as part of other important investments in the railway sector, such as the passenger and freight operators' renewal of rolling stock, construction of depots and purchase of critical maintenance equipment.

3 See EBRD (2023a).

4 See EBRD (2023b).

5 See EBRD (2024).

> The Bank has lent more than €1.6 billion to Western Balkans countries to finance investments in the rail sector.

REFORM SUPPORT FOR AUTHORITIES AND RAILWAY COMPANIES

All these critical investments are supported by important policy techical assistance projects that aim to further develop the market, support private-sector participants and commercialise the SOEs to capitalise on the extensive assets of the rail sector. In late 2023, for example, the EBRD launched a comprehensive reform programme to support Serbian rail development. The package includes:

- supporting the capacity and independence of the Serbian rail regulator to oversee the rapidly growing market by developing a forecast scenario of the future structure of the market, capacity building in key areas required for market function and a reform plan based on comparisons with Organisation for Economic Co-operation and Development (OECD) indicators for the governance of sector regulators and selected peers
- supporting Serbian Railways Infrastructure to improve its corporate governance practices and operational efficiency. This includes implementation of best OECD and international principles and standards in corporate governance, as well as identifying opportunities to increase commercial revenues, developing and implementing best practices for asset managment (linked to ISO 55,001 and ISO 9,001), together with training in project management, procurement and the use of International Federation of Consulting Engineers contracts.

Technical assistance to Serbia's railway sector also played a part in ensuring a platform for engagement with the authorities on an overarching reform of state ownership and corporate governance standards for SOEs. This engagement produced a gap analysis in relation to the relevant global standards (such as the OECD Guidelines on Corporate Governance of SOEs) and best practices, while providing clarity to the government on priority actions needed to strengthen the regulatory and institutional frameworks horizontally across SOEs. This, in turn, informed a state-wide Strategy of State Ownership and Management of Companies Owned by the Republic of Serbia 2021-2027, and a new law (adopted in September 2023) for governance of SOEs developed pursuant to it, which introduces a centralisation of the state's ownership function and improvements to SOE corporate governance standards.

This important reform also features in the stand-by arrangement between the International Monetary Fund and Serbia that reinforces the importance of its timely and diligent implementation.[6] Looking ahead to the implementation of the new legislative framework, railway SOEs will also be among the

“Recognising the critical role of sustainable transport for economic growth and regional integration of the Western Balkans, the EBRD supports EU objectives for the sector's development and has been investing considerable resources into revitalisation and better rail connectedness in the region.”

6 See International Monetary Fund (2024).

first to implement the new requirements and will serve as an example to be followed by other companies owned by the Serbian state.

Similar examples can be seen in Albania, where the financing and technical support from the EBRD and the European Investment Bank will push forward the country's reform agenda by helping the railway company prepare for the operational phase of new lines by developing a framework public-service obligation in line with international best practice. The same is true in Montenegro, where financing to the infrastructure management company comes with support for improving its corporate governance and developing partnerships with vocational training schools to attract more young workers to the railway sector.

The EBRD seeks to support the implementation of the Transport Community action plans as the foundation for the reform of the rail sector and to promote "transition" in wider related areas such as the governance, operational efficiency and regulation of SOEs.

STRENGTHENING EXTERNAL PARTNERSHIPS THROUGH POLICY DIALOGUE

A core objective for the EBRD is promoting transition within its countries of operation (and clients) towards a more competitive, integrated and well-governed economic model. A key aspect of this objective is ensuring alignment and complementarity with wider institutional objectives such as the implementation of the EU acquis communautaire in candidate countries and supporting related wider policy initiatives from key stakeholders. Within the Western Balkans rail (and wider transport) sector, this is primarily guided by the Transport Community Treaty[7] signed in 2017 and broader supporting institutions and policies – such as the Transport Community and Western Balkans Growth Plan.

The EBRD seeks to support the implementation of the Transport Community action plans as the foundation for the reform of the rail sector and to promote "transition" in wider related areas such as the governance, operational efficiency and regulation of SOEs. It also aims to provide capacity building and support for the reform of key market-building institutions such as the sector regulator.

Making a strong case for reforms and finding the right level of ambition and complementarity requires close collaboration with external partners such as the International Monetary Fund, the European Investment Bank, local EU delegations, the World Bank and Agence Française de Développement, which also play a key role in terms of financing and parallel technical support. The EBRD relies on all these important partnerships to identify and pursue the most useful and impactful reforms attached to its indispensable financing in the Western Balkans.

7 The Transport Community is an international body involving the EU and the Western Balkans, designed to extend the EU's transport policies and market integration to its south-eastern neighbours. Its main goal is to integrate the Western Balkans' transport markets with the EU's, enhancing connectivity and compliance with EU standards, which facilitates not only regional but also continental cohesion. This integration covers all major modes of transport, including rail, which is a critical component for sustainable development and regional cooperation. Key actions are defined and monitored with the Transport Community action plans across partner countries.

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BRINGING INVESTMENT-SENSITIVE GOVERNMENT PROCUREMENT UNDER INTERNATIONAL TRADE RULES

> "Explicit discrimination in government procurement against foreign suppliers remains a barrier to international trade."

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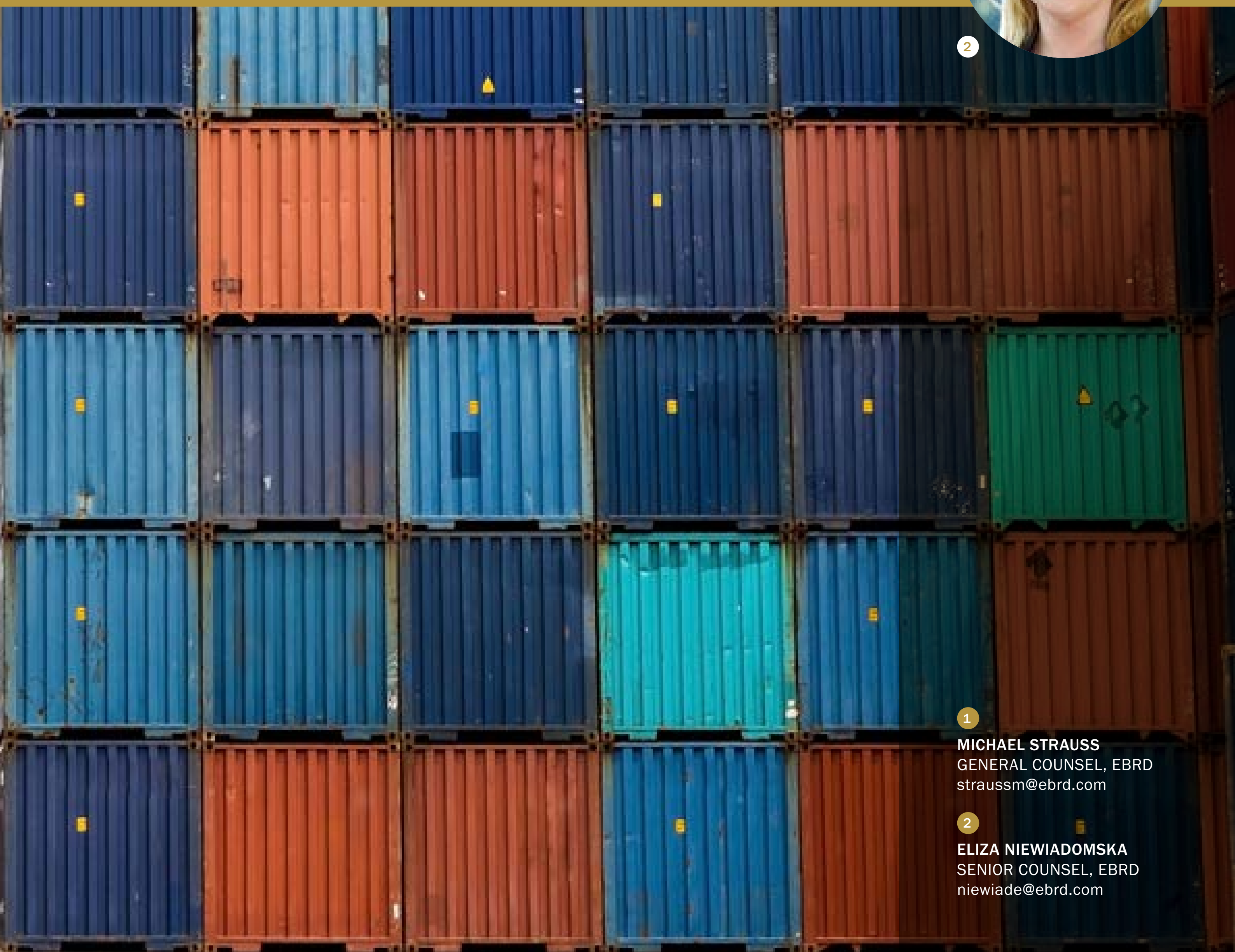

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The WTO's Agreement on Government Procurement (GPA), revised in 2012, is the main global legal instrument for regulating trade in government procurement markets. The EBRD GPA Technical Cooperation Facility helps the transition economies of the EBRD regions accede to the agreement. In the process, it opens new markets to cross-border trade and generates regulatory reforms that make national public procurement systems more transparent, competitive and efficient.

INTRODUCTION

Standard World Trade Organization (WTO) rules do not apply directly to government procurement markets of WTO members. Instead, the WTO's revised Agreement on Government Procurement (WTO GPA 2012), which came into force on 6 April 2014, is open for WTO members to join and provides a regulatory framework for ensuring that the government procurement covered by the agreement is handled in a competitive, non-discriminatory and transparent manner.

The WTO GPA 2012 allows government procurement markets to be open to cross-border trade and international competition. The binding procurement policy standards on contract awards, suppliers' qualifications and the conditions of the procurement process ensure transparency and non-discriminatory conditions of competition between suppliers, resulting in cost savings for the procuring governments. Thus, the agreement is expected to bring about lower prices, better quality and efficiency gains, while also reducing corruption and collusion risks.

The WTO GPA 2012 can play a key role in extending global trade rules to government procurement markets to help deliver legal certainty, efficiency and predictability in the infrastructure sector, boosting confidence and helping attract foreign direct investment. In collaboration with the WTO Secretariat, the EBRD set up a technical cooperation (TC) programme (EBRD GPA Technical Cooperation Facility) to encourage the EBRD's transition economies to accede to the 2012 agreement. This EBRD-funded technical cooperation has already supported the accessions of Armenia, Moldova, Montenegro, Ukraine and North Macedonia. The EBRD also joined the WTO's Government Procurement Committee as an observer in 2023.

BACKGROUND

The WTO operates a global system of trade rules and provides a forum for negotiating trade agreements and settling trade disputes between members. WTO rules aim to lower trade costs by reducing tariffs and non-tariff barriers and enhancing the transparency and predictability (standardisation) of cross-border trade. The WTO's trading system gives members an opportunity to increase economic productivity and cut the costs of doing business, thanks to important principles enshrined in WTO rules.

These aspects of the WTO's work are perhaps well known. What is less known is that the WTO global multilateral trading system supports the needs of all economies by monitoring national trade policies. Examples of WTO rules along these lines include commitments to announce trade policy changes, limit restrictive technical regulations and cut export subsidies in agriculture or other markets, all designed to reduce the uncertainty of trade policy and benefiting members and non-members. WTO rules promote competition in trade by building on key principles of:

- transparency (clear information about policies, rules and regulations)
- greater certainty about trading conditions (commitments to lower trade barriers and increase other countries' access to domestic markets, which are legally binding)
- trade facilitation, including the simplification and standardisation of customs procedures, the removal of red tape and the establishment of centralised databases to simplify trade. The economic savings from streamlining commercial exchange have been estimated at between 2 and 15 per cent of the value of the goods traded, according to the Organisation

for Economic Co-operation and Development (OECD).[1] The World Bank estimated in 2017 that every dollar of assistance provided to support trade facilitation reform in developing economies could generate economic benefits of up to US$ 70.

The WTO has 164 members, with 18 other countries negotiating membership. Joining the WTO trading system has required important regulatory changes in the domestic and trade policies of many countries. Besides reducing tariffs, WTO membership involves commitments to remove regulatory non-tariff barriers and improve transparency.

DEVELOPMENT IMPACT OF THE WTO GLOBAL TRADING SYSTEM

The WTO's role in promoting global trade is supported by economic theory and the latest academic research. Studies analysing total and disaggregated trade flows from 1995 to 2014 and looking into bilateral imports from 133 countries in the primary, textile and industrial sectors provided compelling evidence that the WTO has promoted new member trade, but developed countries continue to benefit more. The latest liberalisations, however, have boosted exports of least developed countries' primary products. Besides market access, the WTO agreements provide greater transparency and predictability that benefit members and non-members alike. Chang et al. (2011) reported a large and positive effect on the trade of GATT and WTO membership (74-277 per cent for countries in both the GATT and WTO). Dutt et al. (2013) found that WTO membership boosted the extensive margin of exports by 25 per cent and had no negative impact on the intensive margin. Larch et al. (2019) examined both domestic and international trade flows to estimate the effects of GATT/WTO membership. On average, joining either has expanded the international trade of a country relative to its domestic sales (dataset covering 178 trading partners in 1980-2016) by about 72 per cent, while GATT/WTO membership has elevated trade between member countries by 171 per cent. Joining the GATT/WTO has led to an average 88 per cent increase in international trade between member and non-member countries.[2]

1 See Gourdon et al. (2017).

2 See Niggli and Osei-Lah (2014).

It is now accepted that the creation of GATT/WTO rules has generated significant trade gains for WTO members as well as non-members. These benefits are even more important because 75 per cent of world merchandise trade today still takes place on a non-discriminatory, most-favoured nation (MFN) basis. According to WTO statistics,[3] the volume of world trade today is about 45 times the level recorded in the early days of the GATT (4,500 per cent growth from 1950 to 2022) and almost 400 times above 1950 levels. Between 1995, when the WTO was first established, and 2022, despite the Covid-19 pandemic, the volume and value of world trade expanded 4 per cent and 6 per cent, respectively, each year. Current tariffs applied between countries that grant MFN status average 9 per cent.

THE SPECIAL CASE OF GOVERNMENT PROCUREMENT MARKETS

WTO rules do not cover all sectors, markets or economies of WTO members. Investments and spending from state budgets and by state-owned enterprises (SOEs) in the utilities sector, defined together as government or public procurement, are not directly subject to standard WTO trade rules primarily aimed at commercial exchanges between private enterprises.

As a result, explicit discrimination in government procurement against foreign suppliers remains a barrier to international trade. Unlike most WTO agreements, the MFN principle does not apply automatically to the government procurement markets of WTO members. Governments maintain discrimination through government procurement laws, administrative guidelines and/or tacit understandings between government and industry. In addition, as traditional forms of trade discrimination have declined, policies containing local content requirements have emerged in the last decade. The 2017 OECD taxonomy of measures affecting trade in government procurement processes[4] describes several categories of direct and indirect trade barriers in government procurement.

Direct and indirect trade barriers in government procurement rules and practices affect important development priorities aimed at promoting sustainable growth. The consistent availability of and access to efficient public services are fundamental to the performance of national economies, social cohesion and national safety and security. Poor or inefficient infrastructure imposes huge economic costs, both visible and hidden, on businesses. Not only does it boost transport costs, but it also raises other costs in an economy, such as higher inventory levels, lower productivity and higher prices for consumers, with implications for the international competitiveness of domestic firms forced to operate in this environment. Some key prerequisite infrastructure for better economic performance – affordable, efficient and accessible public infrastructure and services (public transport systems, information and communications technology infrastructure, quality water supply, drainage and sanitation systems, a reliable and stable energy supply) – is absent in many regions.

Transport constraints can have a severe impact on an economy, resulting for instance, in a 7 per cent reduction in export volumes and a 16 per cent delay in shipment of goods – costs that are higher still in the case of time-sensitive goods.[5] Effectively resolving supply chain and transport constraints could mean a six-fold rise in world gross domestic product compared with tariff reductions, yielding added benefits in terms of jobs, lower prices and greater balance in the distribution of the gains of trade both in-country and internationally.[6]

Efficient global supply chains constitute an essential prerequisite for global growth, and these supply chains themselves depend on accessible and reliable infrastructure and public services. Citizens and businesses depend on this, in turn relying on national government procurement laws and procurement practices that typically remain outside the WTO system. Economic globalisation in the 21st century is more complex than the case of imports crossing borders. The combination of technological advances and economic reforms facilitating new types of commerce means that goods, services, employees, customers, investments and intellectual property cross borders at an ever-increasing rate. In a world of substantial flows of foreign direct and indirect investment, and where regional production networks and supply chains have extended their reach across many sectors and countries (as demonstrated by the pandemic), government procurement markets benefit only indirectly from borders open to international trade and foreign direct investment.

3 See World Bank Group and World Trade Organization (2018).

4 See Gourdon et al. (2017).

5 See Tas et al. (2018).

6 Ibid.

Development economists highlight the importance of liberalising government procurement markets for a good reason. The 12 largest, most complex and technically advanced infrastructure projects in the world, as presented in Table 1 below, are not at all commercial. Commercial investors fund just three of these projects: Dholera Solar Power Plant (India), the Thames Tideway Tunnel (United Kingdom) and Madison Square Garden Sphere (United States of America). The other projects are commissioned by public-sector clients, with investors ranging from the government of China to a subsidiary of Transport for London in the United Kingdom and international financial organisations. Governments execute different levels of control over SOEs, but effectively a final bill for the SOEs' public infrastructure projects goes to the taxpayer.

> “In a world of substantial flows of foreign direct and indirect investment, and where regional production networks and supply chains have extended their reach across many sectors and countries (as demonstrated by the pandemic), government procurement markets benefit only indirectly from borders open to international trade and foreign direct investment.”

Table 1. Largest infrastructure projects in the world, January 2024

Infrastructure project	Estimated budget	Client
NEOM City	US$ 500 billion	Public Investment Fund, Saudi Arabia
The Gulf Railway	US$ 250 billion	Governments of Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates
Dholera Solar Power Plant	US$ 169 billion	Adani Green Energy (commercial)
International Space Station	US$ 150 billion	European Space Agency, NASA, JAXA, CSA and Roscosmos
South-North Water Transfer Project	US$ 62 billion	Government of China
Grand Paris Express	US$ 47.7 billion	Société du Grand Paris, SOE
Beijing Daxing International Airport	US$ 46.2 billion	Government of China
Al Maktoum International Airport	US$ 33 billion	Dubai South, government of Dubai
London Crossrail Project	US$ 23.6 billion	Crossrail Limited, subsidiary of Transport for London, SOE
Chuo Shinkansen	US$ 13.7 billion	Japan Railways, SOE
Thames Tideway Tunnel	US$ 6.3 billion	Thames Water (commercial)
Madison Square Garden Sphere	US$ 2.3 billion	Vici Properties (commercial)

Source: V. Davies (2023) and F. Farhadi (2023).

HOW THE WTO GPA 2012 INTEGRATES PROCUREMENT INTO THE GLOBAL TRADING SYSTEM

Given the importance of government procurement markets for the development potential of both advanced and transition economies, most modern bilateral and regional free trade agreements include government procurement-related commitments. However, these are inherently fragmented and do not ensure globally standardised rules for government procurement markets. This is the benefit of the WTO's "code of fair practices on government purchases",[7] the Agreement on Government Procurement, signed under GATT in 1994 and revised in 2012. The WTO GPA 2012 is binding on 49 WTO members and is the main legal instrument in the WTO framework globally regulating trade in government procurement markets. It is underpinned by WTO principles of transparency and non-discrimination. The agreement aims to liberalise and expand international trade, facilitate integrity in government procurement systems and foster the efficient and effective management of public resources.

The WTO GPA 2012 is not part of standard WTO rules and is not binding on countries that join the WTO. It is voluntary and plurilateral. Members negotiate their terms of accession to the agreement and those that accede must adopt procurement policies and practices ensuring that the treatment of the goods, services and suppliers of other GPA parties is "no less favourable" than that given to their domestic goods, services and suppliers. In other words, only accession to the WTO GPA 2012 extends the WTO standard global trading rules of competition and transparency to the national regulation of public contracts. In this regard, the WTO GPA 2012 brings legal certainty, transparency and good governance into government procurement markets covered by the agreement.

The WTO GPA 2012 governs procurement by public-sector clients by any contractual means, including concessions and public-private partnerships. It applies to laws, regulations and purchasing practices regarding any covered public contract. The agreement does not cover every sector or market; upon joining, parties negotiate market access commitments with new acceding countries on a reciprocal basis. It may thus cover procurement by central and subcentral government entities, as well as utilities and other government enterprises that a party designates. Each GPA party's commitments specify public-sector entities – as well as categories of goods, services and works of estimated value equal to or above specified minimum financial threshold values – that are open to procurement bids by companies from other GPA parties.

Goods are covered in general, services that are covered are explicitly specified, and all GPA parties cover construction services in full. In addition, the WTO GPA 2012 provides for binding public procurement policy standards on tendering, selection and awarding requirements, qualification of suppliers, offsets and complaint mechanisms. The agreement also contains exceptions, excluding defence and national security contracts, as well as set-asides for small and minority-owned businesses.

BENEFITS AND CHALLENGES OF WTO GPA 2012 ACCESSION

The procurement market covered by the WTO GPA 2012 is worth more than US$ 1.7 trillion, according to WTO estimates.[8] Recent empirical evidence suggests that the agreement promotes competition by boosting the probability that a contract will be awarded to a foreign firm. It also fosters cost-effective public procurement by lowering the probability that the procurement price is higher than estimated contracts with single bidders and by decreasing the total number of wins by a single company and/or its subsidiaries. Research has also found that compliance with the WTO GPA 2012 does not translate to higher costs of procurement.[9]

7 See Baldwin and Richardson (1972).

8 See Tas et al. (2018).

9 Ibid.

The list of challenges differs from accession to accession. However, they are typically related to the domestic market's overall openness to international trade and quality of national government procurement laws. Timing and political circumstances of negotiations also play a role.

Political risks of withdrawal from negotiations/ affiliation. Some GPA parties criticise the WTO GPA 2012 as "imbalanced" and "too extensive". Others support the idea of more extensive coverage of government procurement markets and promote incorporation of the revised GPA text directly into the WTO's standard global trading system rules, which would then be binding upon securing WTO membership.

Separate bilateral market access negotiations. The GPA is open to all WTO members and is negotiated individually and administered by the Committee on Government Procurement, composed of all the parties to the agreement. Any member may accede on terms agreed between that member and all GPA parties. The accession process is based on bilateral negotiations with the acceding party on the procurement that it will cover and a determination by the GPA parties that its national government procurement regime complies with the mandatory policy standards of the WTO GPA 2012.

Regulatory compliance check. Unique among WTO trade agreements, the GPA sets the basic policy standards for transparency and competition in cross-border public procurement, in addition to market access. Upon accession, GPA parties incorporate the agreement's mandatory policy requirements in their national public procurement laws.

Potential new procurement practices and digital tools to implement. GPA parties need to ensure that their procurement procedures do not preclude competition or create unnecessary obstacles to international trade, including the procurement of SOEs in the utilities sector. The WTO GPA 2012 establishes general rules on permitted procurement methods (that is, open, selective and limited tendering procedures) and the electronic systems through which suppliers engage in competitive bidding for cross-border government procurement contracts.

HELPING TRANSITION ECONOMIES NAVIGATE WTO GPA 2012 NEGOTIATION, ACCESSION AND IMPLEMENTATION

As a part of the EBRD's mandate to improve the investment climate of the economies where the Bank works, the EBRD's Legal Transition Programme (LTP) helps these governments improve the way they manage public-sector contracting, making procurement systems more transparent, effective and competitive. Building on the Bank's procurement expertise and experience, the LTP started collaborating with the GPA Secretariat in 2011 in a bid to encourage EBRD economies to modernise their national public procurement laws to meet WTO public procurement policy standards, and to consider opening GPA negotiations. Accession to the WTO GPA 2012 is perhaps the most notable milestone in achieving these goals, as it promotes meeting and maintaining international standards for public procurement regulatory frameworks.

Upon revision of the GPA in 2012, the Bank set up a dedicated technical cooperation programme, the EBRD GPA Technical Cooperation Facility, to promote GPA accession among transition countries in the EBRD regions, in collaboration with the WTO Secretariat.

The revised WTO GPA 2012 motivated several such economies to consider accession as a step in their public procurement reforms. Building on this momentum, the EBRD GPA Technical Cooperation Facility has enjoyed considerable success in assisting transition economies' breakthrough in their GPA negotiations. Since its launch, this facility has supported all transition economies that acceded to the WTO GPA 2012 – notably Armenia, Moldova, Montenegro, North Macedonia and Ukraine (all other GPA signatories are highly developed economies).

Box 1. **North Macedonia: support with WTO GPA 2012 negotiations**

Counterpart:
North Macedonia, Public Procurement Bureau. WTO GPA 2012 accession process initiated in February 2018.

Background:
North Macedonia has been reforming its public procurement system since 2009. By 2018, substantial progress on regulatory reforms had been achieved and the government decided to open WTO GPA 2012 negotiations. Also a candidate country for EU accession, North Macedonia opted to negotiate the GPA to gain access to EU member states' public procurement markets before finalising its EU accession process.

Aim:
The main objective of GPA accession is to enable domestic business of North Macedonia to fully access the public procurement markets of other GPA parties, in particular those of EU member states, and to improve the competitiveness and transparency of domestic public procurement markets.

Approach:
Following North Macedonia's request for technical assistance, the EBRD has actively supported the country's GPA accession process, including bilateral negotiations with GPA parties. Technical experts of the EBRD GPA Technical Cooperation Facility have provided capacity building and proactive support with structuring and conducting bilateral negotiations, as well as on drafting the subsequent market access offers. In addition, the experts provided policy advice to guide the development of primary and secondary public procurement legislation and ensure the compliance of domestic laws with WTO GPA 2012 procurement policy standards.

Results:

- In January 2019, the Parliament of North Macedonia adopted a new public procurement law, transposing the 2014 EU Directives on Public Procurement and achieving compliance with WTO GPA 2012 standards. Likewise, the ratification of the Prespa Agreement in January 2019 positively contributed to the progress of WTO GPA 2012 negotiations.
- Twelve rounds of bilateral negotiations with GPA parties over five years were necessary to agree a WTO GPA 2012 market access offer for North Macedonia.
- In spring 2023, the WTO Committee accepted North Macedonia's accession to the WTO GPA 2012. The Parliament ratified this international agreement in autumn 2023 and it entered into force.
- Today, companies of North Macedonia have full access to the public procurement markets of GPA parties. This includes access to public procurement markets of EU member states, which otherwise would be achieved only when North Macedonia accedes to the European Union.

The EBRD GPA Technical Cooperation Facility provides regulatory advice and technical support to governments seeking accession to the agreement by providing (1) capacity-building activities, (2) country-specific technical cooperation and (3) accession negotiation assistance to economies in the EBRD regions that wish to accede. Most importantly, the Bank helps transition economies overcome any institutional, legal and/or trade policy challenges related to WTO GPA 2012 accession they may face during the negotiations and after the accession.

The Bank helps transition economies overcome any institutional, legal and/or trade policy challenges related to WTO GPA 2012 accession they may face during the negotiations and after the accession.

Box 2. **Moldova: e-procurement for WTO GPA 2012 compliance**

Counterpart:
Moldova, Ministry of Finance, Ministry of Economy and Infrastructure, from June 2019.

Background:
Moldova joined the WTO GPA 2012 on 16 July 2016. To implement WTO GPA 2012 standards and accession commitments, as well as achieve the targets of the roadmaps for the Association Agreement with the European Union, the Ministry of Finance of Moldova and the Ministry of Economy and Infrastructure of Moldova worked with the EBRD TC project to develop new digital procurement policies compliant with WTO standards and launch a national-level comprehensive electronic public procurement (e-procurement) system, MTender.

Aim:
Upon WTO GPA 2012 accession, the Ministry of Economy and Infrastructure became responsible for implementing WTO GPA 2012 policy standards. This specifically included introducing WTO GPA 2012 public procurement policy standards to entities in the utilities sector (GPA Annex III entities).

At the point of Moldova's accession to the GPA, national public procurement laws did not cover utilities sector entities, which became obliged by WTO GPA 2012 standards to adopt new procurement practices based on the ratification of this international agreement by the Moldovan Parliament.

Digital transition:
MTender is a multi-platform networking digital procurement service. It consists of a government-operated open data central database and portal and a network of a public and commercial electronic platforms certified to support electronic tendering for the public sector. MTender is a technologically advanced solution built using emerging technologies for automation. It is deeply integrated with e-government services and implements the Open Contracting Data Standard for data interoperability, as well as for open public online access to information on public procurement in Moldova. To comply with WTO GPA 2012 standards for utilities, MTender workflows were upgraded/developed to meet GPA requirements and brought the transparency and competition of public procurements in Moldova to a new level.

Results:
- Experts delivered capacity-building assistance to raise awareness of new obligations and standards to utilities sector entities in November and December 2019, training more than 80 procurement officers of key Moldovan utilities.
- WTO GPA 2012 procedural standards for utilities' public procurement were tailored to local needs, as reported by Moldovan utilities sector entities in a survey (February 2020), and prepared for implementation in the national e-procurement system.
- A new digital "GPA procedure" tool for MTender was developed, tested in the Moldovan context and transferred to the Centre for Information Technologies in Finance, an operator of MTender for the Ministry of Finance of Moldova.
- The MTender pilot implemented GPA/EU public procurement policy standards within 26 months and reached 3,000 public buyers (almost 95 per cent of the market) and about 4,500 sellers (a 30 per cent increase in new suppliers brought to the market and, overall, 30 per cent of local SMEs).

Perhaps the most valuable TC support entails help with designing the negotiation strategy, support during parallel bilateral negotiations and post-accession technical assistance with implementation of WTO GPA 2012 policy standards and commitments in national legislation and local procurement practice. Under the EBRD GPA Technical Cooperation Facility, the LTP enjoys an excellent working relationship with the WTO Secretariat. It has developed strong links with key GPA parties (Canada, the European Union, Japan, the United States) and effectively promotes innovative public procurement policy thinking to GPA working groups (SMEs, Market Statistics).

Box 3. **Ukraine: GPA cross-border bidding capacity building for suppliers**

Counterpart:
Ministry of Economic Development, Trade and Agriculture (MEDTA), Ukraine, from August 2019.

Background:
Ukraine has been a GPA party since 2016 and is well known for its advanced e-procurement system PROZORRO, implemented with the strong support of the EBRD. Since Ukraine's GPA accession, businesses from GPA countries have increased their participation in Ukrainian public procurement markets. However, Ukrainian companies were not very successful when it came to public tenders conducted by GPA parties. As such, the government requested technical support from the EBRD to help Ukrainian companies benefit from new business opportunities in the GPA countries.

Aim:
Technical cooperation facilitated GPA implementation in Ukraine by identifying bottlenecks hindering the effective participation of domestic suppliers in public procurement markets of GPA countries and designing and testing support mechanisms for MEDTA to increase Ukrainian business participation in public procurement markets covered by the GPA and cross-border bidding for public contracts.

Approach:
TC experts helped to develop different methodological tools, including online surveys, training resources and awareness activities for Ukrainian suppliers. MEDTA published dedicated online resources to provide practical tools for improving the effectiveness and success of Ukrainian suppliers in cross-border government procurement.

Results:
Within 12 months, a team of TC experts:

- conducted a survey among Ukrainian businesses to identify bottlenecks/non-regulatory barriers to cross-border trade with GPA countries, with findings and recommendations presented to MEDTA
- designed and delivered training and awareness-raising activities, with two country-level seminars and 18 smaller outreach events
- researched and analysed cases of successful participation by Ukrainian businesses in the cross-border tenders of GPA countries in 2019-20, with a report published online by MEDTA
- developed a set of guidelines on public procurement rules and practices in seven GPA countries most attractive to Ukrainian firms
- actively advised about 375 Ukrainian companies interested in bidding in GPA public tenders abroad
- assisted selected Ukrainian suppliers participating in GPA tenders, with 18 cases of Ukrainian companies winning a contract in a GPA country.

CONCLUSIONS

The WTO GPA 2012 crystallises current best practices in government procurement, approved and accepted by WTO members. It is harmonised with other relevant international legal instruments, including the 2014/2017 European Union directives on public procurement and the 2011 UNCITRAL Model Law on Public Procurement. It therefore complements other efforts by developing and transition economies to reform their government procurement systems.

The advantages of more countries in the EBRD regions joining the GPA are evident: EBRD economies would work towards more open and globally harmonised procurement rules for public contracts. The harmonised procurement policies, combined with access to the markets of the GPA parties, are expected to create new international trade opportunities: the WTO estimates the value of GPA market access commitments under the agreement at more than US $1.7 trillion a year. Results of the latest empirical studies suggest that joining the WTO GPA 2012 has a positive impact on the trade of both goods and services between parties, as well as on outward foreign affiliate service sales. The number of GPA parties has a small marginal negative effect on trade in goods. Service exports also rise slightly when more parties participate in the GPA. The growth of government procurement contracts above the threshold under the GPA also fosters service imports, exports and outward foreign affiliate sales.

The role of the WTO GPA 2012 in supporting development is to provide transparent, predictable and non-discriminatory government procurement regimes that foster good governance, attract investment, promote competitiveness and contribute to economic transformation. Accession to the WTO GPA 2012 can create market access opportunities for developing and transition economies, build trade capacity, align their government procurement policies with international best practice and extend WTO international trade rules to government procurement markets. This can lead to more cross-border trade, job creation, infrastructure development and integration into global value chains, contributing to sustainable growth.

The experience of the EBRD GPA Technical Cooperation Facility in terms of TC with the WTO Secretariat and technical assistance and capacity building provided to transition economies spotlights the potentially critical role that international organisations may play to help bring investment-sensitive government procurement markets under the WTO system of international trade rules.

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LEVERAGING OUTCOME-LINKED LOANS TO IMPROVE THE ESG PERFORMANCE OF SMALL FIRMS

> "The most compelling reason for SMEs to improve their ESG performance is to ensure their long-term viability and competitiveness in a rapidly changing marketplace."


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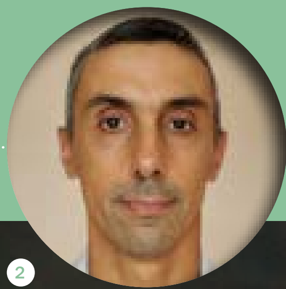
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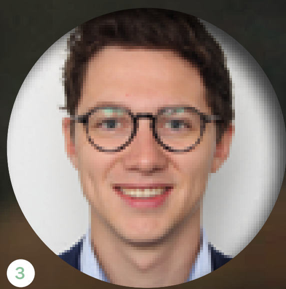
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SMEs play a key role in national economies, but often fail to address their environmental, social and governance (ESG) risks and opportunities adequately. Strong governance, as a key pillar of ESG, helps these businesses boost their competitiveness, integrate better into supply chains and access suitable finance. The EBRD's outcome-linked loan programme helps SMEs to implement crucial ESG improvements and adopt sustainable business practices.

INTRODUCTION

Small and medium-sized enterprises (SMEs) play an important role in both developed and developing economies and serve as a major source of new jobs. However, they face many difficulties, notably in attracting financing through commercial banks or accessing capital markets. Growing evidence suggests that inadequate corporate governance (including in relation to environmental and social risks) is among the top challenges hindering the access of SMEs to suitable medium- and long-term financing.[1] This affects their survival, competitiveness and growth prospects, with the associated negative impact at the macroeconomic level.

The EBRD's outcome-linked loan (OLL) programme is part of the Bank's efforts to support the development of a sustainable SME sector across its economies. The OLL programme is implemented in partnership with the Swiss State Secretariat for Economic Affairs (SECO) and several commercial banks in Central Asia and the Caucasus. This initiative is aligned with the efforts of the EBRD's corporate governance team within the Legal Transition Programme (LTP) to improve corporate governance in the Bank's regions and across sectors.

While SMEs in the EBRD regions are becoming more aware of the positive impact of adopting better environmental, social and governance (ESG) practices, most small businesses have limited capacity and willingness to make such improvements. This is primarily due to a lack of financial resources and expertise. The objective of the OLL programme is thus twofold:

- **Generate impact** by enabling SMEs to improve their ESG practices, thus accelerating their transition to becoming greener, more inclusive and better-governed businesses.
- **Improve competitiveness** by boosting the financial performance and growth prospects of SMEs through implementing relevant and ambitious ESG improvements. This would result in improved access to funding, better integration into supply chains, reduced operating costs and enhanced compliance with local and international regulations.

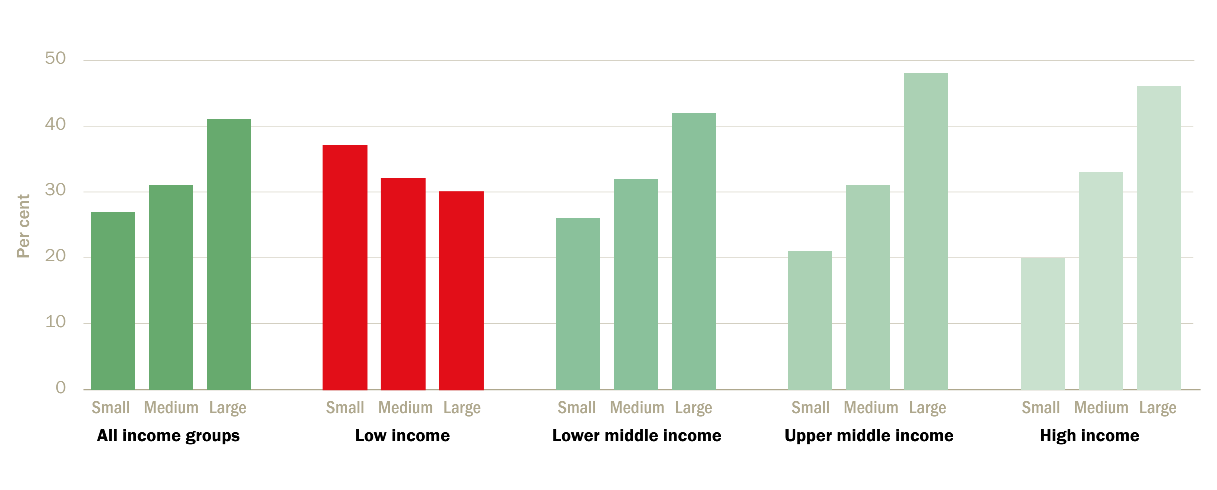
WHAT ARE SMEs AND WHAT ROLE DO THEY PLAY IN NATIONAL ECONOMIES?

Supporting the SME sector is a strategic priority for governments, development finance institutions, donors and international organisations. The main reason SMEs receive so much attention is that, although individually small, their collective contribution is large: the World Bank estimates that SMEs account for about 90 per cent of businesses and more than 50 per cent of employment worldwide.[2]

Due to their sheer numbers, SMEs are often referred to as the "backbone" of the economies and "engines" of job creation and economic growth. This is especially relevant in low-income countries, where these firms account for 7 of every 10 jobs (see Figure 1). Moreover, formal SMEs contribute up to 40 per cent of national income in emerging economies. These numbers are significantly higher when informal SMEs are included.[3] SMEs also play a vital role in regional economic and social development, as they often operate in areas outside capitals and urban centres where large enterprises are less present.

1. International Finance Corporation (2019).
2. World Bank (2024a).
3. The International Labour Organization estimates that SMEs are responsible for two-thirds of global employment. See ILO (2024).

Figure 1. Share of employment by firm size and country income group



Source: World Bank Enterprise Surveys (2024b).

> “The governance solutions for SMEs should aim to: (i) improve strategic decision-making; (ii) oversee the performance of management (from overview of expenditures to strategy implementation);(iii) establish strong management controls that also help to ensure the integrity of the company’s financial reports; and (iv) build a strong internal culture and staff morale.”

ESG CHALLENGES FOR SMEs

Many studies clearly demonstrate the link between good corporate governance and benefits such as improved firm performance, better access to capital and greater sustainability. Failure to enact good corporate governance practices may result in underperformance or, in extreme cases, the failure of the business. Common SME weaknesses include the lack of established strategy and business planning, non-formalised practices and weak internal controls.

In addition, SMEs often fail to recognise and integrate environmental and social (E&S) risks and opportunities in their strategies and have limited capacity to develop and implement appropriate E&S risk management practices. The situation in many SMEs is complicated even further by the succession risk and the increased role of extended family in the affairs of family-owned firms.

Due to their smaller size and various stages of development, SMEs have their own unique characteristics and challenges. Consequently, the governance and broader ESG guidance for SMEs should not be a simplified version of the governance requirements applicable to listed companies or banks. For example, SMEs often do not have the separation between owners and managers typical of larger companies. Instead, the ownership of SMEs is usually highly concentrated, and the owners are involved in both the strategic decision-making and day-to-day management. They usually oversee the relevant areas of the company’s work (including finance, operations, marketing and sales).

The most compelling reason for SMEs to improve their ESG performance is to ensure their long-term viability and competitiveness in a rapidly changing marketplace. To do so, SMEs should put in place suitable arrangements to direct and control the company effectively. This can be achieved by establishing internal functions and governance bodies as well as developing policies on topics ranging from cash management, budgeting and financial reporting to health and safety and sustainability, as appropriate for the size, sector and stage of development of the company (that is, start-up, active growth, organisational development and business expansion).[4]

The governance solutions for SMEs should aim to: (i) improve strategic decision-making; (ii) oversee the performance of management (from overview of expenditures to strategy implementation); (iii) establish strong management controls that also help to ensure the integrity of the company's financial reports; and (iv) build a strong internal culture and staff morale.

In the current environment, sustainability issues represent major risks and opportunities for all companies. In this context, the corporate governance frameworks should be designed to support the sustainability of firms. On the one hand, the larger ones face more complex challenges, but often have sophisticated governance structures and sufficient capacity to understand and manage the sustainability issues. SMEs, on the other hand, frequently lack sufficient awareness and expertise to analyse their material ESG areas and need to put in place a suitable governance framework to help them develop solutions to mitigate any significant E&S risks and adapt to the effects of climate change. Given their growing importance, sustainability issues should be integrated into the SME strategy-setting process and risk management. SMEs should also develop capacity to regularly produce the additional non-financial reporting, including on ESG performance, that many financial institutions and supply-chain participants increasingly require.

4 International Finance Corporation (2019).

OLL PROGRAMME: WHAT HAS BEEN DONE SO FAR AND NEXT STEPS

Enhancing corporate governance practices among SMEs is an important priority for the SME Finance and Development team at the EBRD. For instance, 51 per cent of the recently initiated 254 international advisory projects with SMEs explicitly incorporate corporate governance as either a core or a secondary objective. Such advisory support helps small businesses establish robust organisational frameworks, ensuring their long-term sustainability and growth.

As part of its efforts to improve the ESG practices of small firms, the EBRD and SECO launched a pilot OLL programme in 2023. An OLL is a financing instrument that combines an ordinary loan with a commitment of the borrower to achieve certain outcomes in the form of specific ESG performance improvements. The direct reward that the borrower receives is an incentive payment, which effectively lowers the interest rate on the loan and is proportionate to the achieved impact. The proceeds from an OLL could be used for capital expenditure (for example, new facilities and equipment), working capital or other legitimate business purposes.

The outcome-linked loan programme targets SMEs aiming to address their ESG risks and opportunities, regardless of whether they already have internal capacity to adopt ESG improvements on their own.

There does not need to be a direct link with the ESG outcomes that the borrower aims to achieve (for example, the procurement and installation of solar photovoltaic panels on the company premises). Instead, the outcomes must focus on areas that are material, given the sector and business model of the borrower. The level of ambition in terms of the magnitude of the improvements needs to be substantial (usually going beyond the applicable local regulations). On this basis, the OLL programme supports companies seeking to become ESG champions and provide positive demonstration effects in the local market.

The structuring of an OLL involves the following steps:

1) **ESG diagnostic:** Aims to establish the main ESG risks and opportunities that the borrower faces and is usually carried out by an expert in the field.
2) **ESG action plan:** Specifies up to 10 key performance indicators (KPIs) that the borrower intends to tackle as part of the OLL, together with the applicable baseline values, the agreed ambitious targets and a timeline for their achievement.
3) **Implementation arrangements:** Specify the mechanics of the OLL structure, including the reduction in the interest payment to which the borrower would be entitled, if and when it achieves the targets stipulated in the ESG action plan. These also define appropriate advisory support (if any) that the EBRD would provide to the borrower to achieve the stipulated outcomes.
4) **Reporting and verification:** Define the features of the periodic (usually annual) reporting to the lender on the implementation of the ESG action plan and the performance against the KPIs. The lender verifies this performance by using its in-house resources or with the help of an external verification consultant.

The OLL programme targets SMEs aiming to address their ESG risks and opportunities, regardless of whether they already have internal capacity to adopt ESG improvements on their own. As most SMEs lack sufficient resources to tackle their ESG challenges on their own, the programme provides both external advisory support and a suitable financial incentive to engage in such activities. At this stage, the incentive needs to be significant (up to 10 per cent of the loan principal) and is frequently paid out of grant funding provided by various donors (in this case, by SECO). As the markets develop, the amount of the incentive will be reduced and gradually phased out.

Box 1. **Case study: Multimodal Trans Terminal**

In April 2024, the EBRD signed the first OLL with Multimodal Trans Terminal (MTT), a provider of logistical and warehousing services in Uzbekistan. The loan of US$ 1.1 million will finance the modernisation of MTT's railway logistics terminal in Tashkent and is complemented by a comprehensive ESG action plan developed jointly by the EBRD and the company.

During the initial discussions about the potential OLL structure, MTT demonstrated strong commitment to the adoption of ESG standards. While the company had already initiated some measures on its own, the ESG diagnostic revealed important gaps compared to industry best practices. For example, on the environmental side, the company does not use any renewable energy sources and lacks water and waste management strategies. On the social side, women make up only 11 per cent of the MTT workforce and there is no formal strategy to promote the active participation of women, youth or individuals from underrepresented or marginalised communities. On the governance side, the company lacks a succession plan for key leadership roles and does not engage in any ESG reporting practices.

The ESG action plan entails a commitment to 10 material ESG improvements and outlines specific steps to address the identified challenges. These steps include:

- decreasing energy consumption by more than 20 per cent
- increasing the share of materials or waste stored and recycled to 90 per cent
- setting up an internship programme for young people, at least 25 per cent of whom will be women, in partnership with a local educational institution
- integrating ESG reporting into annual management reports.

These ESG measures represent uncharted territory for MTT and the EBRD will provide support for their implementation through technical assistance. The first ESG improvements are expected to be achieved in February 2025.

The external advisory support is used not only to identify the main areas for potential ESG improvements, but also to help the company develop internal capabilities to design and implement suitable solutions. In our experience, the success of this programme depends not only on the quality of the consultant, but also on the commitment of the company.

Given the low starting position of most SMEs, the ESG diagnostic could identify many “easy wins” – that is, measures that could be implemented easily and without incurring significant costs. Such easy wins typically involve adopting processes to collect data and introducing policies to facilitate the implementation of best ESG practices. Once these are in place, the next steps focus on ESG measures that require greater preparation and may involve certain investments/costs. To help with these, the EBRD often offers the borrower assistance through its International Advisory programme.

Awareness and understanding of various ESG-related topics among SMEs in the EBRD regions are growing, but still relatively limited. Therefore, maximising the impact of an outcome-linked loan requires the lender to lead the design of the ESG action plan and to provide suitable technical assistance in the implementation phase, so the borrower can apply the agreed measures and report on the achieved impact.

By their very nature, OLL instruments are more complex to structure and monitor than conventional EBRD loans. This implies that they are a niche product that is attractive mainly to aspiring ESG champions. Making outcome-linked loans a mainstream product would require:

- increasing the quality and quantity of data on the ESG performance of SMEs – to make it easier to establish the baseline and set the level of ambition for each KPI
- streamlining and standardising the loan terms – to reduce the cost

> “The initial experiences with the outcome-linked loan programme in Central Asia are encouraging and would enable the EBRD to streamline the operational modalities further and scale the programme in other regions.”

- developing capacity among local commercial banks to implement such a product – to increase their ability to structure such loans without the involvement of a development finance institution like the EBRD
- recognising that such instruments can be supported with donor funding only in the beginning – that is, until the adoption gathers momentum. Once that is the case, the level of incentive would gradually decline and the OLLs will play the signalling role for which they were originally intended.

The initial experiences with the OLL programme in Central Asia are encouraging and would enable the EBRD to streamline the operational modalities further and scale the programme in other regions.[5] As these loans become more popular and awareness of ESG improvements increases, the level of ambition of borrowers should rise while the need to provide incentives and technical assistance would diminish. This would gradually allow for ESG elements to be embedded in more financing instruments and would position those SMEs keen to use them on a more sustainable footing.

5 SECO is providing technical assistance to the EBRD to develop a robust and scalable OLL framework in partnership with iGravity, a Swiss consultancy.

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STEERING THE SHIP: HOW GOVERNANCE SHAPES ESG OUTCOMES

> “Litigation regarding climate-related disclosures is expected to increase as more firms begin to report these details and regulatory requirements tighten.”

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The environmental, social and governance (ESG) framework, which is crucial for promoting sustainability and ethics in corporate behaviour, often fails owing to a siloed approach separating environmental, social and governance-related aspects. Effective ESG requires a foundational focus on governance to enable environmental and social goals to be achieved. Building the right structure, culture and accountability (in one word, governance) is essential in order to realise true ESG ambitions and prevent greenwashing.

INTRODUCTION

The environmental, social and governance framework has emerged in recent years as a pivotal strategy for assessing and influencing corporate attitudes towards sustainability and ethical practices. This evolution stems from growing global demand for change.

Ideally, the ESG approach should be cross-cutting, with governance acting as an access code for the integration of environmental and social considerations into corporate dynamics. This "horizontal" approach is uncommon, though, with ESG rating providers and corporations often finding it easier to consider the three aspects vertically and separately. This approach increases the risk of creating silos and has proven to be suboptimal, however.

The first crucial step towards enhancing the efficacy of the ESG approach should be to recalibrate the focus to build the right governance. Governance should be the enabler that allows environmental and social ambitions to emerge through corporate dynamics. However, it often acts as a bottleneck in that regard. In this journey, building the right structure, culture and accountability is key to realising environmental and social ambitions and closing the door to greenwashing.

THE ORIGINS OF ESG

ESG considerations can be traced back to the socially responsible investment movements of the 1960s and 1970s, which stressed ethical and moral criteria in investment decisions, primarily in opposition to the Vietnam War and apartheid in South Africa. These movements laid the groundwork for considering non-financial factors in investment decisions. However, the concept of ESG as we know it today took on a more defined shape in the early 2000s, with a series of initiatives and reports that emphasised the integration of environmental, social and governance issues into financial analysis.

A landmark moment was the publication in 2004 of a report entitled *Who Cares Wins: Connecting Financial Markets to a Changing World*.[1] Commissioned by then United Nations Secretary-General Kofi Annan, the report was the outcome of a joint endeavour by the United Nations Environment Programme's Finance Initiative and the United Nations Global Compact.[2] It involved more than 20 financial institutions from across the globe. The *Who Cares Wins* initiative proposed that integrating ESG factors into investment analysis and decision-making processes could enhance traditional financial analysis by highlighting potential risks and opportunities that are not apparent through conventional financial analysis alone. This proposition marked a paradigm shift, suggesting that ESG factors were not just ethical considerations – tangential to business operations – but critical to financial performance and risk management.

1 See United Nations (2004).

2 The United Nations Global Compact is a voluntary initiative whereby chief executives commit to implementing universal sustainability principles and taking steps to support United Nations goals.

THE INTEGRATION OF ESG INTO MAINSTREAM INVESTMENT

Following the publication of the *Who Cares Wins* report, there was a notable move to integrate ESG considerations into mainstream investment practices. One of the most significant developments was the establishment of the Principles for Responsible Investment (PRI) in 2006.[3] Endorsed by the United Nations, the PRI provided a framework for incorporating ESG factors into investment decision-making, further cementing the importance of ESG in the financial sector. The PRI encourages investors to regard the three aspects of ESG as interconnected elements that can materially impact the financial performance of investments. The six principles promoted by the PRI do not look at environmental, social and governance-related factors as entirely separate aspects; rather, they encourage a cohesive approach which recognises that these factors can overlap and affect each other. The supporting framework and guidance[4] emphasise the interconnectedness of these aspects, rather than addressing them in silos.

Another pioneering endeavour is the Global Reporting Initiative (GRI)[5] – again, established in partnership with the United Nations Environment Programme – which issued the first set of sustainability reporting guidelines. These guidelines were developed to provide a framework for organisations to report on their ESG performance. Both frameworks underscore the importance of stakeholder engagement, which is a novelty in the rigid world of vertical "shareholders-board-management" hierarchies.[6] In practice, the GRI provides guidelines for disclosing how an organisation engages with its stakeholders, while the PRI focuses on the importance of incorporating stakeholder concerns into investment practices.

The business case for such initiatives was compelling. Organisations that adhere to GRI standards may find it easier to attract investment from PRI signatories, who seek out companies with strong ESG records as part of their investment criteria. Conversely, investors who are committed to the principles of the PRI may leverage GRI reports to monitor and assess the sustainability performance of their investment portfolios.

The PRI and the GRI have thus established an initial ESG "structure", whereby corporations can voluntarily adhere to agreed standards and report to the market, providing opportunities for investors who are keen to enhance their ESG exposure.

The six principles promoted by the Principles for Responsible Investment do not look at environmental, social and governance-related factors as entirely separate aspects; rather, they encourage a cohesive approach which recognises that these factors can overlap and affect each other.

3 See www.unpri.org. The PRI has more than 4,500 signatories globally, including asset owners, investment managers and service providers, who are committed to integrating ESG principles into their investment practices. The number of signatories is continuing to grow as awareness of and commitment to sustainable investing increases.

4 The PRI provides resources (including case studies, guidelines and tools) that help with the understanding and implementation of ESG integration. These principles often address complex scenarios where multiple factors interact, thus reinforcing an integrated perspective.

5 See www.globalreporting.org.

6 The first Organisation for Economic Co-operation and Development (OECD) Principles of Corporate Governance were issued in 1999. These acknowledged the role of stakeholders in corporate governance, emphasising the importance of recognising stakeholders' rights under the law and the benefits of active cooperation between corporations and stakeholders. The principles were revised in 2004, and the new version further highlighted the importance of going beyond legal compliance and fostering active cooperation with stakeholders to create wealth, jobs and sustainability. A 2015 revision provided additional guidance on how corporations can engage with stakeholders effectively. This led the way to the latest revision in 2023 and the addition of a new chapter on sustainability, where engagement with stakeholders is key.

Unfortunately, the limited oversight on how rigorously practices are applied has led to some "box ticking", whereby firms formally commit to those standards without meaningful implementation. This has raised concerns that some organisations may be using their signatory status to suggest a commitment to sustainability that is not matched by their investment practices.

Environmental groups and climate activists – jointly with academia – play a major role in fighting this approach and pushing for more accountability by raising awareness, engaging in direct advocacy, influencing policy and collaborating with corporations to improve sustainability. They often leverage media campaigns to influence public opinion and corporate reputations, potentially leading to divestment and the boycotting of companies with poor environmental practices. Activists have also taken legal action to enforce compliance with environmental regulations. By pushing for more detailed ESG disclosures and better practices, they play a crucial role in creating a culture and steering companies towards sustainable operations. Their efforts help to align corporate actions with global sustainability goals, contributing greatly to the broader fight against climate change and environmental degradation.

DIESELGATE

The scandal commonly referred to as "Dieselgate" was uncovered thanks to investigative work by researchers and subsequent regulatory action.

In 2014, a group of researchers from West Virginia University, funded by the International Council on Clean Transportation (ICCT), conducted tests to compare the emissions from European and American models of diesel cars. They intended to prove that diesel vehicles could meet emission standards effectively. The cars chosen for the tests included a Volkswagen Jetta, a Volkswagen Passat and a BMW X5. During on-road testing, the researchers discovered that the nitrogen oxide emissions of Volkswagen vehicles were up to 40 times the level allowed in the United States of America. The ICCT, surprised by the findings, reported the results to the Environmental Protection Agency and the California Air Resources Board, urging them to investigate further. In September 2015, after being confronted with evidence, Volkswagen admitted to installing software in diesel engines that could detect when they were being tested, changing the performance accordingly to improve results. This software had been installed in about 11 million cars worldwide from 2009 to 2015.

DISCLOSURE MATTERS

At the time of the Dieselgate scandal in 2015, Volkswagen was regarded as a leader in the field of sustainability, and its ESG disclosures were generally considered to be of high quality. The company regularly published detailed sustainability reports that followed GRI guidelines and indicated a commitment to transparency and environmental concerns. These reports covered a wide range of ESG topics, including emissions, energy efficiency and corporate governance.

This case underscored the importance of the quality and integrity of reporting, showing that misleading disclosures could have far-reaching negative consequences for a company and its stakeholders. The trust and credibility that had been established through Volkswagen's sustainability reporting were severely damaged.

Dieselgate led to huge reputational, legal and financial consequences for Volkswagen (estimated at around US$ 30 billion) and contributed to heightened public awareness and distrust around corporate environmental practices and greater awareness of the environmental impacts of corporate activities. The scandal acted as a catalyst for environmental activists, providing a clear, compelling example of corporate malfeasance that could be used to rally support for stricter environmental regulations and corporate accountability. It served as a stark reminder of the urgency and importance of addressing climate change, ensuring corporate responsibility and establishing robust regulatory frameworks.

Volkswagen's 2014 annual report says: "Compliance is a cornerstone of sustainable business – a view expressly shared by the Company's management." Indeed, the case served, for many corporations, as a reminder that the requirement to disclose certain practices in accordance with an agreed methodology pursuant to a disclosed commitment is a matter of compliance. Because compliance is a risk function, the reputational risk derived from inconsistent disclosure suddenly became high. To mitigate such risk, a number of corporations turned to "greenhushing", silencing their disclosure practices.

A NEW APPROACH

As the urgency and economic costs of climate change became more apparent, governments began to consider the serious risks that a changing climate posed to the environment, economies and individual businesses. This led to global policy shifts, including international accords such as the Paris Agreement[7] and the 2030 Agenda for Sustainable Development,[8] which underscored the need for concerted action to mitigate climate change and adapt to its impacts.

A milestone was reached in December 2015 – the same year as Dieselgate – when the Financial Stability Board,[9] in response to a request from G20 finance ministers and central bank governors for more transparent financial reporting of climate-related risks and opportunities, created the Task Force on Climate-related Financial Disclosures (TCFD). The primary objective of the TCFD is to help companies to understand what financial markets want from disclosure in order to measure and respond to climate change risks, and to encourage firms to align their disclosures with investors' needs.

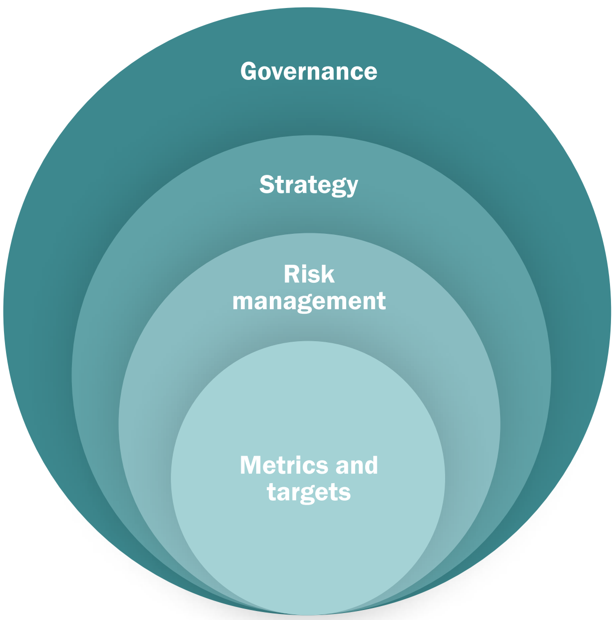
TCFD recommendations are structured around four thematic areas that represent core elements of how organisations operate (see Figure 1).

7 See https://unfccc.int/process-and-meetings/the-paris-agreement.

8 See https://sdgs.un.org/2030agenda.

9 See www.fsb.org. The Financial Stability Board is an international body that monitors and makes recommendations about the global financial system. It was established in April 2009 as a successor to the Financial Stability Forum after the G20 summit in London. Membership consists of all G20 economies, the European Commission and other key financial centres.

Figure 1. Core elements of recommended climate-related financial disclosures



- **Governance:** disclosure of the organisation's governance around climate-related risks and opportunities.
- **Strategy:** the actual and potential impacts of climate-related risks and opportunities on the organisation's business, strategy and financial planning.
- **Risk management:** the processes used by the organisation to identify, assess and manage climate-related risks.
- **Metrics and targets:** the metrics and targets used to assess and manage relevant climate-related risks and opportunities.

Source: TCFD (2017).

The central role of governance – as an enabler of all thematic areas – is clear from Figure 1. Each TCFD thematic area is, in itself, a governance aspect, where climate considerations are plugged in and shape the specific purpose of governance, thereby becoming the "enabler" for such climate considerations.

Generally, governance refers to the system of rules, practices and processes through which a firm is directed and controlled. It involves behaviours and encompasses the mechanisms through which executives – and, in turn, the company as a whole – are held accountable. This applies to performance, risk mitigation and environmental and social ambitions.

The TCFD approach is a horizontal approach, not a vertical one. It implies that effective interaction between shareholders, the board, management and stakeholders (first thematic area) is a precondition for developing an effective strategy (second thematic area), which, in turn, requires a solid structure for the assessment of risks and opportunities (third thematic area), which are to be disclosed using credible metrics (fourth thematic area). The linking of the four dimensions is key.

TCFD[10] reporting – while largely voluntary – is increasingly being monitored and incorporated into jurisdictions' regulatory frameworks. This shift makes companies more accountable for their climate-related financial disclosures and can potentially have legal implications if these disclosures – and the governance behind them – are found to be misleading or inadequate.

In some countries and regions, financial regulators, stock exchanges and industry groups are starting to encourage and require financial institutions and large companies to include TCFD-aligned information in their annual financial reports. Some stock exchanges, such as those in London, New York, Tokyo and Hong Kong, encourage or require listed companies to report in line with TCFD guidelines as part of their listing requirements.

On 6 March 2024, the US Securities and Exchange Commission (SEC) adopted final rules on the enhancement and standardisation of climate-related disclosures for investors, requiring corporations to disclose certain climate-related information in registration statements and annual reports.[11] Those rules are aligned with many of the TCFD's principles and recommendations. In particular, the SEC's rules highlight the importance of disclosing how the board and management oversee climate-related risks and opportunities. This includes descriptions of the governance framework and the processes for identifying, assessing and managing climate-related risks.

10 Following the release of its 2023 status report on 12 October 2023, the TCFD was disbanded, having fulfilled its remit. The Financial Stability Board has asked the IFRS Foundation to take over the monitoring of the progress of companies' climate-related disclosures. On 3 November 2021 at COP26 in Glasgow, the Trustees of the IFRS Foundation announced the formation of the International Sustainability Standards Board (ISSB), which has developed "IFRS S1: General Requirements for Disclosure of Sustainability-related Financial Information" and "IFRS S2: Climate-related Disclosures", incorporating the TCFD recommendations into the ISSB's standards.

11 See SEC (2024).

Figure 2. TCFD recommendations: the horizontal approach

Governance	Strategy	Risk management	Metrics and target
Disclose the organisation's governance around climate-related risks and opportunities.	Disclose the actual and potential impacts of climate-related risks and opportunities on the organisation's business, strategy and financial planning where such information is material.	Disclose how the organisation identifies, assesses and manages climate-related risks.	Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.

Source: TCFD (2017).

> “In jurisdictions where TCFD reporting has become mandatory, companies are legally accountable for the accuracy and adequacy of their disclosures.”

A WAVE OF NEW LEGISLATION AND LITIGATION

The United Kingdom was the first G20 country to enshrine mandatory TCFD disclosure in law. The legislation, adopted on 6 April 2022, requires more than 1,300 of the largest UK-registered firms and financial institutions to disclose climate-related financial information. This new requirement goes hand in hand with the United Kingdom's Companies Act 2006, Section 172 of which requires directors to act in a way that they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole. This includes, among other factors, the need to consider the impact of the company's operations on the community and the environment. Increasing shareholder activism and public pressure have led companies to integrate more detailed environmental considerations into their strategic decisions, potentially under the ambit of Section 172 obligations.[12]

In the European Union (EU), the new Corporate Sustainability Reporting Directive (CSRD)[13] – an extension and revision of the earlier Non-Financial Reporting Directive (NFRD) – was adopted by the European Parliament in November 2022 and represents a significant step forward in the EU's commitment to sustainable finance and corporate responsibility.

The new directive covers all large companies – whether they are publicly listed or not – as well as all companies listed on regulated markets. This means that around 50,000 companies in the EU will now need to comply, up from around 11,000 under the NFRD.

12 This avenue started to be explored in 2023, when ClientEarth filed a derivative claim in the High Court of England and Wales against Shell's board of directors for alleged breaches of their duties under the Companies Act 2006. Despite the lack of solid legal grounds for ClientEarth's derivative claim, this case may serve to advance climate related goals under Section 172 of the Companies Act.

13 See European Commission (n.d.).

Companies are required to report on their impact on people and the environment. The directive will use mandatory EU sustainability reporting standards, which the European Financial Reporting Advisory Group is developing. Those reporting standards are expected to incorporate the principles and recommendations of the TCFD. Reporting will include detailed information on; (i) companies' business models, strategies and targets; (ii) the roles of the administration, management and supervisory bodies as regards sustainability; and (iii) the principal adverse impacts connected with the company and its value chain. For the first time, an external auditor or certifier must audit or check the sustainability information reported under the CSRD.

In jurisdictions where TCFD reporting has become mandatory, companies are legally accountable for the accuracy and adequacy of their disclosures. Failure to comply can result in fines, sanctions and other regulatory action. Furthermore, investors are increasingly demanding reliable and standardised climate-related disclosures to assess risks associated with their investments. Companies that fail to provide meaningful and accurate data may face shareholder activism and reputational risks, potentially leading to divestment and challenges in raising capital.

These reforms have started to create a system of accountability for disclosures. There have been instances where companies have been sued for allegedly misleading investors about their exposure to climate-related risks or the robustness of their climate strategies. In this process, courts are pivotal in upholding ESG standards and adjudicating on disputes related to environmental and social issues. Litigation regarding climate-related disclosures is expected to increase as more firms begin to report these details and regulatory requirements tighten.

> "The EBRD is helping its clients to systematically integrate climate considerations into their decision-making, risk management, investment and operational plans and targets through its Corporate Climate Governance Facility."

Notable cases include the proceedings that were brought in the United States against the oil and gas giant ExxonMobil, which was accused of misleading investors about the risks climate change posed to its business. Though ExxonMobil prevailed in this case,[14] it highlighted the potential legal risks associated with climate-related disclosures. In another case filed in the Netherlands, ClientEarth initiated legal action against Shell's board of directors. The group of shareholder activists alleged that Shell's climate transition plan was inadequate and that the company's directors had failed to adequately prepare for a transition to a low-carbon economy. In May 2021, The Hague District Court ordered Shell to reduce its carbon dioxide emissions by 45 per cent by 2030 relative to 2019 levels. This reduction pertains to the entirety of Shell's operations and the energy products it sells, reflecting a substantial increase in the ambition of the company's existing sustainability policies.

Litigation is not limited to corporations, either. The landmark case of Urgenda Foundation versus The State of the Netherlands,[15] where the Dutch Supreme Court ordered the government to reduce its greenhouse gas emissions, exemplifies the role of the judiciary in enforcing environmental commitments. Courts can thus reinforce governance frameworks by ensuring legal accountability for ESG commitments and claims.

14 See People of the State of New York v. ExxonMobil Corp., filed on 24 October 2018 at the New York Supreme Court.

15 For more information, see https://climatecasechart.com/non-us-case/urgenda-foundation-v-kingdom-of-the-netherlands.

CONCLUSIONS

To sum up, the development of ESG has demonstrated the increasing role of governance in facilitating the transition to environmental and social sustainability. This "enabling" role is a cornerstone of the transition to sustainability. It requires horizontal integration of the ESG dimensions, with governance being the entry point and the glue that keeps the three together. Thus, in order to tackle climate risks, for instance, investors should be assured that the company has a sound risk management function in place where climate risks can be duly identified and analysed along with other operational risks. This does not go well with a vertical siloed approach, where environmental, social and governance-related elements are analysed and rated separately. Evidence shows that where ESG ambitions are siloed, they may not translate into tangible results.

Instead, an effective governance structure allows environmental and social goals to become corporate strategic priorities, while social and environmental challenges and risks are analysed holistically so they can, ideally, be turned into opportunities. This requires strong interaction between internal and external stakeholders, supported by a regulatory system that allows accountability and trust. The structure, culture and accountability that are required for this to happen are growing fast, but they still face some bottlenecks (for example, when it comes to the inclusion of stakeholders in decision-making, reliable disclosure and oversight) – especially in transition countries, where the ESG journey has only recently started and governance practices and frameworks may not yet follow best practices. The EBRD is helping its clients to systematically integrate climate considerations into their decision-making, risk management, investment and operational plans and targets through its CCG Facility.[16] The CCG methodology is based on the TCFD and is regularly updated to reflect emerging international standards and good practices.

Corporate performance has, historically, been measured using globally agreed, monitored and regulated financial indicators, whereby management informs the board, shareholders and stakeholders of profits and losses. A robust, standardised and evolving governance framework supports the preparation, verification and disclosure processes, ensuring confidence and trust. The same approach should eventually apply to environmental and social considerations as well.

16 In 2022, the EBRD officially launched its Corporate Climate Governance Facility, which aims to transform the way corporate clients do business by building their capacity to manage climate-related risks and opportunities and unlocking green investment. For more information on the CCG Facility, see www.ebrd.com/ccg-facility. For information on a pilot case study, see EBRD (2021).

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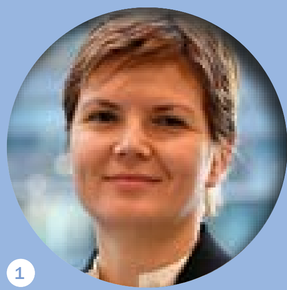
PARTNERING FOR GOOD IMPLEMENTATION OF LAW IN MOLDOVA

> “Poor dispute resolution and enforcement is a broad issue affecting society, the economy and politics, and impacting younger and smaller companies in particular.”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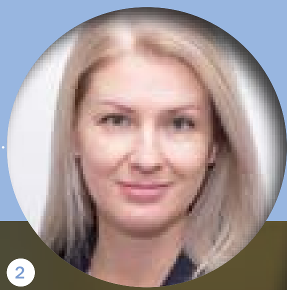
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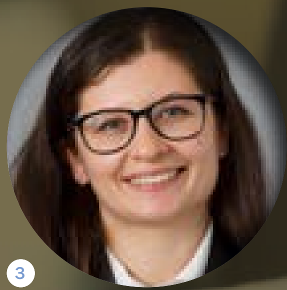
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The development and implementation of robust commercial legal frameworks is essential for well-functioning markets in the EBRD economies. As with any reform, it requires local stakeholders to become the champions and key drivers of change. In Moldova, the EBRD has built a strong partnership with the authorities to deliver better dispute resolution and enforcement services and EU accession reforms.

WHAT IS GOOD IMPLEMENTATION OF LAW AND WHY DOES IT MATTER?

The EBRD often hears from its economies that they have a good law, but it does not work – regardless of whether it is a law on secured transactions, public-private partnerships or companies. This typically means that the public institutions entrusted with regulating and monitoring these areas lack the necessary knowledge, people or financial resources. Ultimately, laws work if society is confident that the courts or other dispute resolution forums will uphold the law and protect party rights, and that court decisions will be enforced.

The courts and law enforcement face the same challenges as public institutions, with an added complication: due to the principles of independence of justice, reforming legal institutions is not an easy or quick fix. A further compounding factor in many EBRD economies is the perception of corruption and abusive practice. For instance, a 2022 European Commission report on Moldova noted that the low stock of foreign direct investment was "reflecting weaknesses in the business environment and continuing problems with corruption and the protection of property rights".[1] Poor dispute resolution and enforcement is a broad issue affecting society, the economy and politics, and impacting younger and smaller companies in particular.[2]

When focusing on good implementation of commercial laws, it is important to use all the available tools – such as alternative dispute resolution (ADR) and simplified court proceedings – for enforcing contractual rights.

1 See European Commission (2023).

2 See OECD (2017), p. 49.

3 See US Department of State (2023).

A country that enjoys investor and business confidence in its justice system also enjoys trust in the economy.

IMPACT OF GOOD DISPUTE RESOLUTION AND THE LTP'S ROLE

The Bank's Legal Transition Programme (LTP) focuses on various topics to help EBRD economies improve their implementation of commercial laws. These include expanding the use of commercial mediation by businesses in EBRD economies, leveraging technology to increase access to dispute resolution mechanisms for small and medium-sized enterprises (SMEs) by developing online courts, and bringing more transparency and efficiency to the enforcement of commercial court decisions.

The value of this work lies not only in offering solutions once the debtor refuses or is incapable of paying its debt or providing services or goods. Its greatest value is preventive. A country that enjoys investor and business confidence in its justice system also enjoys trust in the economy. An example of this is the United Kingdom, whose "procedurally competent, fair and reliable" judicial process[3] makes it an attractive hub for dispute resolution services and contributes to its reliable and investment-friendly environment.

One demotivating factor in reforming public institutions – including courts and enforcement – or training professionals is that it takes a long time to show results, which are also difficult to measure. However, there are attempts to estimate the benefits of legal reform. Recent research from the UK Law Commission on the value of law reform shows that estimated economic gains from the five highest value projects completed since 2019 is about £670 million (€778 million) over 10 years.

Another notable example is electronic trade document reform, where the UK Law Commission recommended "[allowing] for legal recognition of trade documents in electronic form to be used in the same way as their paper counterparts. The government's economic impact assessment established that the benefit of this reform over the course of 10 years would exceed £1 billion [€1.2 billion]".[4]

The quality of justice and enforcement in a country is fundamental to a well-governed economy – one of the Bank's key transition qualities of a sustainable market economy.

> "Building strong, long-term relationships is key to successfully reforming the justice system in Moldova. Working with the EBRD has been crucial in digitalising legal services and promoting alternatives to courts, such as commercial mediation and arbitration. Implementing these solutions while considering the needs of litigants, lawyers and businesses brings Moldova closer to the European community."
>
> **VERONICA MIHAILOV-MORARU**
> MINISTER OF JUSTICE
> OF MOLDOVA

PARTNERS FOR REFORM IN COMMERCIAL DISPUTE RESOLUTION

When it comes to justice reform, the focus in many EBRD economies is on anticorruption, criminal and prosecution law. Examples include Georgia, Moldova and Ukraine, which are all gearing up for accession to the European Union (EU) since being awarded candidate status and need to get their justice houses in order. Investing most of the resources into a fight against corruption may leave commercial justice and enforcement reform on the sidelines.

The Bank is among the handful of development institutions that continue to be a partner in business law reform, reminding countries about the huge need for such reform. The EBRD has a unique position in the markets in which it operates owing to a direct connection with businesses. No other stakeholders in the EBRD economies are both an investor in the private sector and a development partner, with the Bank's expertise and access to governments. The Bank's unique position to support the private sector, including SMEs, and to enhance the environment for businesses through policy engagement is very well explained as a key feature of the EBRD's business model and position within the multilateral development bank (MDB) system.[5]

It is therefore the role of the Bank to act as a partner to governments in assisting with good commercial law implementation, dispute resolution and enforcement. The EBRD's key partner in this reform in Moldova is the Ministry of Justice (MoJ) and connected agencies.

This reform requires partnering with multiple stakeholders. In Moldova, the Bank works on alternatives to courts with the MoJ and its Mediation Council, the Mediation Centre at the Chamber of Commerce and Industry, the Superior Council of Magistracy and legal professionals. In the area of digitalisation of the enforcement process, the EBRD collaborates closely with the Ministry of Justice, the banking community, the Association of Moldovan Banks and the National Union of Enforcement Officers.

4 See EBRD (n.d.).

5 Ibid.

AN ALTERNATIVE TO COURTS IN MOLDOVA

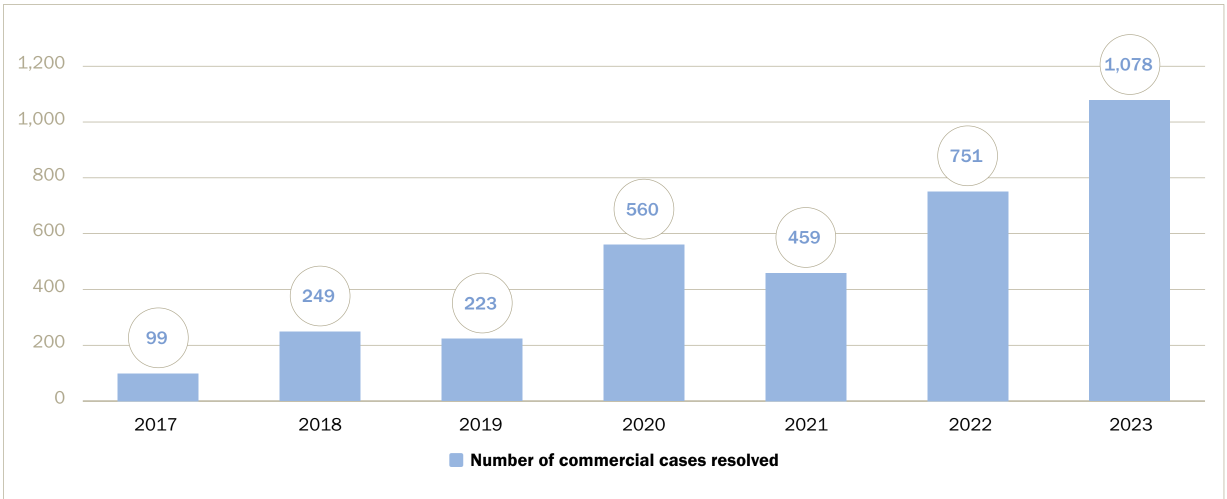
Since 2013, the LTP has actively supported the MoJ, the Mediation Council and the Mediation Centre at the Chamber of Commerce and Industry in the development of alternative dispute resolution (ADR) in Moldova via the Commercial Mediation and Arbitration Project. This project is being implemented in four phases.

The use of mediation was limited when the project began in late 2013. The Law on Mediation of 14 June 2007 was ineffective due to a lack of clarity, and the only realistic path to resolving commercial disputes was through the court system. At the same time, the backlog of pending cases in the courts was significant and, coupled with litigation costs, this restricted access to justice. This had an adverse impact on the general business environment in Moldova.

Thanks to the project, which is set to end in 2024, mediation is slowly but surely becoming more available and a credible alternative to courts in Moldova on commercial cases. The number of commercial mediation cases resolved through mediation increased 10 times – from 99 to 1,078 – from 2017 to 2023.

“Thanks to the project, which is set to end in 2024, mediation is slowly but surely becoming more available and a credible alternative to courts in Moldova on commercial cases.”

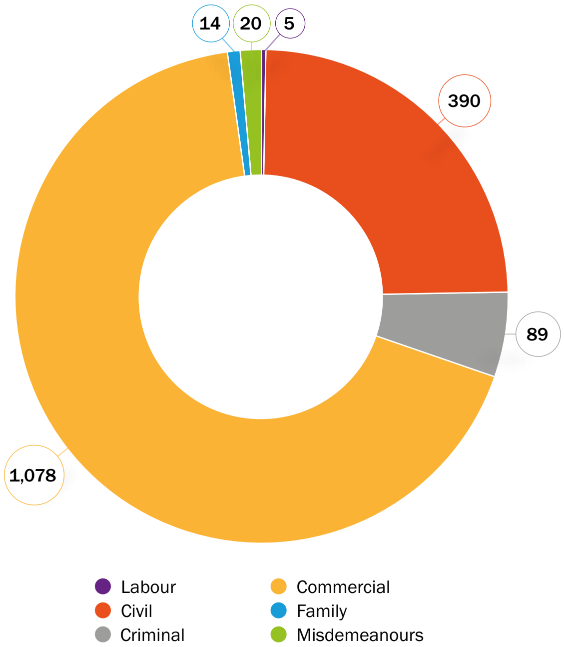
Figure 1. The number of commercial cases resolved through mediation has climbed



Source: Mediation Council of the Republic of Moldova.

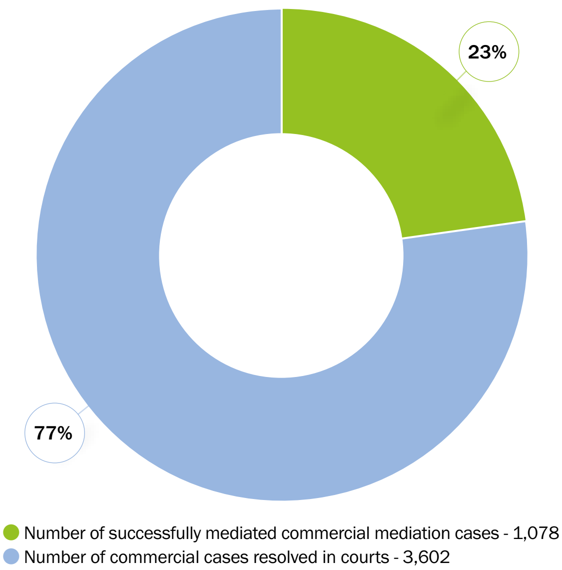
During the 2016-18 phase of the project, the Mediation Centre at the Chamber of Commerce successfully mediated a case involving a large Moldovan glass manufacturing company (also a client of the EBRD) against the largest utility company in Moldova, which saved both companies considerable expense and time compared to the court route.

Figure 2. Number and distribution of mediated cases, by type of case



Source: Mediation Council of the Republic of Moldova.

Figure 3. Number and ratio of mediated commercial disputes and commercial cases examined by courts in 2023



Source: Mediation Council of the Republic of Moldova.

The project also proposed improvements to the Moldovan arbitration framework. This was achieved by the EBRD partnering with:

- the Ministry of Justice and its Mediation Council for **policy and law reform**, as well as for **digital governance**
- the Mediation Council and the Mediation Centre at the Chamber of Commerce and Industry to **train mediators to provide qualitative service**
- with all three and the National Institute of Justice and courts to launch a **continuous awareness campaign to promote ADR**.

This would not have been possible without the support, including financial, from various donors: the government of Luxembourg, the UK government and the United States Agency for International Development (USAID). More partnerships were required to help with the expertise on mediation by the UK Centre for Effective Dispute Resolution and logistical implementation by the International Development Law Organisation.

Box 1. **Key achievements of the EBRD project on the implementation of law in Moldova (2013-24)**

Policy advice and legislation:

- Contributed to the development of the new Mediation Law that was adopted in 2015.
- A draft new law on arbitration with explanatory note was developed and submitted to the MoJ in May 2023, based on the assessment of the arbitration framework with recommendations. Public consultations were conducted in June 2023 and the Moldovan parliament is expected to adopt the new law in 2024.
- A study with recommendations on the introduction of mandatory pre-litigation mediation session was presented to the MoJ, the Mediation Council and mediation practitioners in April 2023.
- Legislative amendments required to achieve sustainability and independence of the Mediation Council, the self-governing body in the area of mediation in Moldova, were developed in 2020.
- Developed a Strategy and Action Plan for 2020-2024 for the Mediation Council that was approved by its decision in August 2020.
- The Mediation Council approved the first rules on quality standards for mediation services in 2020, and rules on the competence, training and functioning of specialised committees within the Mediation Council were approved in 2022. Forms and templates required for the activity of the Mediation Council were developed in 2020.
- The concept for the e-registry and case management system for mediators was adopted by a government decision in February 2024.

Institutional capacity:

- Successfully piloted a court-annexed mediation system in four courts in 2013-16 and a national case referral system by the courts was launched in 2018.
- The first Mediation Centre at the Chamber of Commerce and Industry in Chisinau was established in 2016, and its facilities for mediation and training services were renovated in 2020.
- Two regional mediation centres of the Mediation Centre were opened in the northern region of Moldova in December 2022 and in the southern region in March 2023.
- The business model with recommendations for positioning in the Moldovan mediation market, collaboration with public authorities and ensuring long-term financial sustainability of the Mediation Centre was approved by its decision in July 2021.
- A Mediation Lab at Moldova State University was opened in December 2021, in partnership with the Mediation Council and the MoJ. The lab serves as a hub for practical training and exchanges for current and future mediation practitioners.

Training and awareness raising:

- The United Kingdom-based Centre for Effective Dispute Resolution accredited 52 people as mediators in 2014-16.
- A course on ADR as part of the curriculum at the Faculty of Law of Moldova State University was introduced in 2018.
- The training programme of the Mediation Centre was improved to ensure compliance with the standards of the International Mediation Institute. The institute accredited the Mediation Centre in April 2024.
- An e-training module on mediation referral for judges was developed in partnership with the National Institute of Justice of Moldova and 50 judges improved their knowledge on mediation in September 2023.
- The project has reached more than 3,400 people since 2013 through its awareness-raising efforts. A total of 835 people increased their knowledge and skills on mediation through the project's training activities on mediation. These include 165 mediators, 176 attorneys, 60 arbitrators, 167 judges, 60 notaries, 186 businesspeople and 21 academics.

Digitalisation:

- An e-register of legal professionals, including mediators and a case management system for mediators, with an automatic electronic statistical module, was developed and integrated with governmental e-services. It has been operational since February 2024.

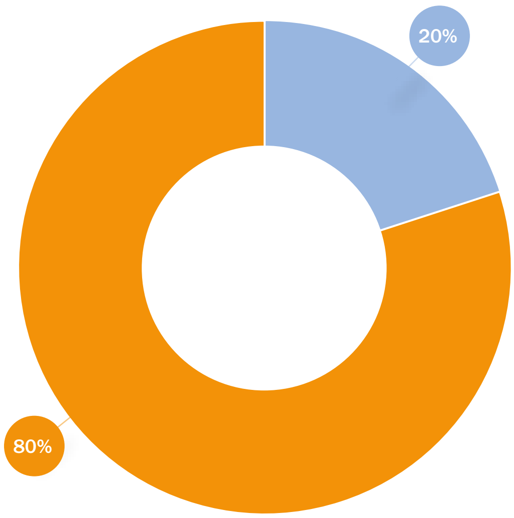
From 2017 to 2023, the number of commercial mediation cases resolved through mediation rose in 10 times, from 99 to 1,078.

HELPING THE BANKING SECTOR SAVE ON ENFORCEMENT COSTS

The enforcement of a court judgment is essential to protect creditors' rights and an indispensable element of a business-friendly market. In Moldova, the time and costs associated with the exchange of communication between enforcement officers and commercial banks results in significant enforcement costs.

To address these issues, the EBRD partnered with the Association of Banks in Moldova, the National Union of Enforcement Officers and the Ministry of Justice to launch the Project on Streamlining Enforcement Procedures – Digitisation of Debt Enforcement by Bailiffs from Debtor Bank Accounts. This project seeks to identify and implement the best model for digitising the communication between enforcement officers and commercial banks in the process of debt collection.

Figure 4. Moldovan banks processed tens of thousands of requests for information about debtors' bank accounts in 2023



Clients of Moldovan banks - 26,110
Non-clients - 104,438

Source: National Union of Enforcement Officers of Moldova.

Box 2. **Cost of paper-based enforcement from debtors' accounts in Moldova**

Every day, enforcement officers process an average of 516 requests for information about the existence of a debtor's bank account, according to the Association of Moldovan Banks. As about 80 per cent of these requests concern people who are not bank clients, most of the time banks give enforcement officers negative answers to such requests. About 500,000 paper documents circulate every year between the banks and the enforcement authorities.

PROMOTING DIGITALISATION AS A SOLUTION

In its five-year Strategic and Capital Framework for 2021-25, the EBRD emphasised the role of digital solutions as enablers of transition,[6] noting that "[e]ffective partnerships will be crucial to success". Indeed, identifying digital champions and maintaining strong and effective partnerships during the planning, delivery and use of digital solutions are vital for the ultimate acceptance and use of such solutions.

Like many EBRD economies transitioning to digital governance, Moldova has been keen to expand the role of digital tools in justice systems. In response to this need, the Bank in 2023 developed guidance for the Moldovan authorities and 16 other EBRD economies on how to provide better access to commercial justice services, with a focus on SMEs. The guidance is based on the results of an assessment that evaluated the degree to which 17 EBRD economies were ready to introduce,[7] or had already developed, online courts[8] for commercial disputes.

6 See EBRD (2020), p. 6.

7 For the purposes of this assessment, online courts are defined as dispute resolution mechanisms conducted by default online, starting from the submission of the claim and ending with the delivery of the judgment, accessible directly to litigants and their representatives and augmented by services and tools to ease access to justice and litigant participation. For the results of the assessment, the Guide and compiling your own action plan to build online courts, see https://ecourts.ebrd.com/report.

8 For more details on the Legal Transition Programme's work in the area of online courts, see *Law in Transition 2023* (lit-ebrd.com).

Digital tools are especially suitable in commercial justice where, usually, participants in proceedings have better digital skills and where the costs and speed of court cases directly affect the economic environment and its attractiveness to investors. The findings from the assessment and the guidance have been shared with the Moldovan authorities and will, hopefully, inform decisions on ongoing reforms in digital justice.

The promises of digital tools go beyond the improvement of court proceedings, however. More efforts are needed to ensure that businesses can effectively enforce judgments and ultimately recover their money. Such processes often entail the need to sell debtors' assets. While the Moldovan government has committed to improving the framework on enforcement, a transparent, fast and effective electronic system for the sale of assets (property) is still needed.

This is an area where the Bank could leverage its experience in the development of MTender (Moldova) and ProZorro.Sale (Ukraine) to design and implement a digital solution that caters to the auctioning of assets by Moldovan actors, including commercial banks, enforcement officers and insolvency administrators. The expected impact of this solution is to prevent abuse, ensure equal access to sales data, increase the efficiency and cost-effectiveness of the recovery of debt in the country, and boost the number of potential buyers. It is likely that effective and transparent debt recovery would tremendously improve the resilience of the financial sector.

> “Partnerships established by the EBRD with the Moldovan authorities were the driving force behind these reforms. These partnerships play a crucial role in ensuring that efforts to make Moldovan laws effective and its investment climate more attractive and trusted are truly impactful.”

EMPOWERING THE GOVERNMENT TO ADOPT QUALITY LEGISLATION

While the quality of legislation does not guarantee good implementation, it remains a crucial component. This is especially true for countries that pursue European aspirations and make significant efforts to transpose EU laws into their domestic legislation. The transposition requires considerable emphasis on adaptation of legal norms rather than their replication from one legal system to another. Yet, this is not always feasible, for a variety of reasons. It has been reported that the shortcomings of the EU acquis transposition – experienced by the latest EU members – result mainly from the lack of administrative capacity and pre-accession policy alignment.[10]

The EBRD *Transition Report* country assessment for Moldova 2023-24 identified the same challenges in Moldova and prioritised the need to strengthen administrative and institutional capacities ahead of EU accession negotiations.[11] To minimise EU law transposition shortcomings in the post-accession period, the EBRD's Competitiveness, Governance and Political Affairs team has rolled out its flagship Reform Support Teams programme in Moldova with the support of the government of France and the European Union to increase the capacity of the key ministries and agencies to deliver on major EU accession reforms.

Drawing on the EBRD's experience – especially in Georgia, Ukraine and Uzbekistan – the Bank is embedding almost 40 reform experts for up to three years in the State Chancellery, the Ministry of Energy,

10 See Knill and Tosun (2009).
11 See EBRD (2023b).

the Ministry of Infrastructure and Regional Development, the Ministry of Environment, the Ministry of Economic Development and Digitisation, the Agency of Public Property and the Ministry of Agriculture and Food Industry.

The experts provide strategic advisory and day-to-day operational support with the EU chapter-screening process and the development of normative acts, with a primary focus on transposing the EU acquis into national legislation. The Reform Support Teams programme helps to build capacity within the government administration through a comprehensive, coherent and coordinated approach to reform implementation. The advantages of the programme go beyond capacity improvement. Recruitment campaigns target members of Moldova's diaspora community and young specialists who choose to return to Moldova with a wealth of international experience to contribute to the European future of their country. It is also expected that the programme's roles will be integrated into the government administration in the longer term as part of the wider public administration reform.

CONCLUSION

The EBRD has developed a unique role as both a major investor and development partner in Moldova. This has allowed the Bank to leverage its expertise in supporting much-needed reforms in the areas of commercial justice, enforcement of creditor rights, digital transformation and alignment with EU legislation. Partnerships established by the EBRD with the Moldovan authorities were the driving force behind these reforms. These partnerships play a crucial role in ensuring that efforts to make Moldovan laws effective and its investment climate more attractive and trusted are truly impactful.

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VISION, DETERMINATION AND SUSTAINED EFFORT: WORKING WITH SERBIA'S BANKRUPTCY SUPERVISION AGENCY

> "The vision, determination and sustained effort by the Serbian authorities to invest in their insolvency framework has brought demonstrable results."

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It has been 20 years since the EBRD's Legal Transition Programme began working with the newly created insolvency regulator in Serbia, the Bankruptcy Supervision Agency (BSA) and its supervising authority, the Ministry of Economy. The Bank's aim from the outset has been to help the BSA regulate and develop a specialist professional body of insolvency practitioners.

INTRODUCTION

Insolvency practitioners, variously called trustees, administrators, receivers or liquidators, are at the heart of insolvency systems around the world. A court typically appoints them to oversee an insolvency proceeding. As a result, insolvency practitioners frequently control or monitor the debtor's operations and have considerable influence on the continuation of the debtor's business, as well as on how any assets belonging to the debtor are sold and how any proceeds are distributed to creditors.

As a regulator, the BSA performs an essential function in maintaining a strong insolvency framework. Using continuous supervision, regular inspections and developing risk-based supervision, the BSA and its supervisors ensure that insolvency practitioners (known as bankruptcy administrators in Serbia) act honestly and professionally. The BSA also collaborates with donors to deliver an official training programme on topics of interest for the profession every year. Now a leading regulator for the Western Balkans region, the BSA has a close and successful partnership with the EBRD. Key achievements include the development of national standards and a code of ethics for insolvency practitioners which underpin the BSA's supervisory function.

1 See Law on Bankruptcy Supervision Agency (Official Gazette of the Republic of Serbia Nos. 84/2004, 104/2009, 18/2005 and 89/2015), effective as of 1 August 2004.

In 2004, Serbia enacted the Law on the Bankruptcy Supervision Agency.[1] This law established a new single regulatory body for insolvency practitioners, responsible for issuing licences and supervising licensed insolvency practitioners. The EBRD, acting through its Legal Transition Programme (LTP), began working with the Agency from its inception a year later, in 2005. The Bank's engagement was aimed at strengthening the BSA's regulatory capacity and contributing to a better investment climate in Serbia, by increasing both the confidence of the investment community in insolvency procedures and the insolvency practitioner profession. The BSA collaborated with other donors in parallel, especially the United States Agency for International Development (USAID), which provided critical support to the BSA by establishing an electronic system for reporting and supervision of insolvency practitioners.

ESTABLISHING NATIONAL STANDARDS AND A CODE OF ETHICS

In the early days, the EBRD's working relationship with the BSA proceeded in stages. First, the Bank helped the ministry to develop a set of official national standards and a code of ethics for the profession, with the assistance of Professor Ron Harmer and British insolvency practitioner Neil Cooper. These were initially adopted in 2004 and slightly revised with input from the BSA in 2009. The standards established, for the first time, rules and guidelines for insolvency practitioners in the day-to-day conduct of insolvency cases, in line with international best practice.

Second, the EBRD contributed to the substantive reform of the Law on Bankruptcy, completed in 2009.[2] This was an important reform and has been the basis of Serbian insolvency legislation ever since, with amendments from time to time. Thereafter, the Bank worked with the BSA and its partners to develop a manual, published in 2010, to guide stakeholders on the application of the national standards and the related code of ethics. This helped the Agency to carry out its disciplinary functions, which were launched in April 2011 by legislative changes that empowered a newly created disciplinary board of the BSA to examine cases of professional misconduct involving a breach of national standards and/or the code of ethics.

“Professional standards and ethics are, therefore, among the most important issues to be addressed for the proper implementation of any country's insolvency framework.”

Often considered by stakeholders in the EBRD regions to be the weakest area of performance of the insolvency practitioner profession, national standards and codes of ethics help to define common rules with respect to professional behaviour. In so doing, they also support the performance of regulatory functions, in particular the investigation of allegations of misconduct by practitioners and, if necessary, the initiation of disciplinary procedures. Professional standards and ethics are, therefore, among the most important issues to be addressed for the proper implementation of any country's insolvency framework.[3]

In Serbia, the national standards cover the practical administration of the insolvency practitioners' duties. These include matters such as the administration of the insolvent debtor's bank accounts and monetary assets (National Standard 1) and the practitioner's report on the economic and financial position of the bankrupt debtor (National Standard 3). The code of ethics provides complementary rules on ethical conduct and an overarching framework regarding the behaviour of insolvency practitioners in the performance of their duties and responsibilities. A critical rule is that insolvency practitioners must be objective, impartial and independent when performing their professional duties.

In September 2012 the EBRD surveyed insolvency practitioners and BSA staff on the impact of the Bank's project with the BSA on the national standards and the code of ethics. There was a clear perception that the standards, while new at the time, had had a major, positive effect on the working practices of insolvency practitioners. The code of ethics, which prescribes an expected standard of professional behaviour and conduct, was considered more difficult to assess than the national standards, but the two documents – national standards and the code of ethics – were considered to be closely interlinked. Today, these are an established part of the Serbian regulatory framework for insolvency and a major achievement that has consolidated Serbia's leadership in the insolvency field.

There was a pause in the EBRD's active partnership with the BSA after 2012, although it continued to engage in the field of insolvency in Serbia through the LTP and remained in regular contact with the BSA. From 2013 to 2015 the EBRD worked closely with the Chamber of Commerce and Industry of Serbia to develop the framework for consensual restructuring cases administered by the Chamber pursuant to the Law on Consensual Financial Restructuring of Companies.[4] This was followed, from 2017 to 2018, with a project that analysed impediments to the resolution of high levels of non-performing loans in Serbia, including some issues in the insolvency framework.

DIGITAL INITIATIVES – RISK-BASED SUPERVISION AND DATA GOVERNANCE

In 2021 there was an opportunity for the EBRD to reengage at another critical stage in the development of the BSA as a regulator. EBRD staff began working with a team led by Dragisa Petrovic, Director of the BSA, and including Jelena Todic, Director of the Supervision and Profession Development Unit, Dejan Milovanovic, Head of Department for coordination and control of internal organisational units, Milan Opacic, Assistant Director for information technology (IT) and communications, and Sladjana Guzijan, Profession Development Adviser.

2 See Bankruptcy Law, Official Gazette of the Republic of Serbia Nos. 104/2009, 99/2011, 71/2012, 83/2014, 113/2017, 44/2018 and 95/2018.

3 In 2014, the EBRD completed a detailed assessment of the insolvency office holder profession that evaluates the profession's state of development and performance in 27 EBRD economies including Serbia. See EBRD (n.d.).

4 See Official Gazette of the Republic of Serbia, No. 36/ 2011 (as amended in 2015, 2018 and 2021).

The occasion for reengagement with the BSA was an initiative by the Serbian Ministry of Economy to create more efficient insolvency procedures, with shorter deadlines and lower costs. The ministry had prepared a set of amendments to the Bankruptcy Law (drafted in 2018) that envisaged greater responsibilities for the BSA in collecting insolvency-related data from relevant court decisions, notices and other legal acts and in preparing official insolvency statistics. With support from Luxembourg, the Bank agreed to work with the BSA to assess its existing IT and regulatory infrastructure, and prepare a methodology, IT concept and roadmap for the development of the BSA's new responsibilities concerning data collection, analysis and the production of statistics.

As a regulator, the BSA uses two digital systems for statistical monitoring and data processing: the Electronic Reporting System (ERS) and the Risk Based Management System (RBMS). The ERS is an electronic reporting system administered by the BSA and officially used since 21 September 2009 by insolvency practitioners for reporting on activities performed in insolvency (bankruptcy) proceedings. The RBMS is a platform used by BSA supervisors to monitor insolvency practitioners. The RBMS uses data from the ERS to review the data of the reports submitted by practitioners in the ERS and identify areas of risk, facilitating the BSA's supervisory functions. Part of the project that the EBRD launched in 2022 therefore analysed the need for a new system to replace the ERS as well as a new software system to replace the RBMS. Furthermore, the EBRD considered the need for new statistical software to extract data from the new ERS, RBMS, E-Sales platform and the BSA's information system, ensuring the interoperability of the platforms.

> "The Bank's engagement was aimed at strengthening the Bankruptcy Supervision Agency's regulatory capacity and contributing to a better investment climate in Serbia, by increasing both the confidence of the investment community in insolvency procedures and the insolvency practitioner profession."

> This regional project is aimed at developing and delivering more scalable and comprehensive official training programmes for insolvency officeholders and judges, grounded in domestic law and practice.

Due to the specific multidisciplinary nature of the project, the Bank retained a team of data governance, policy, IT and legal experts. The team worked with the BSA to develop a methodology for the collection, processing and publication of statistical data and a roadmap for implementation, including the training of BSA employees on using the new software and the production of statistics and reports. One of the innovative features of the project was the development of an IT concept based on low-code/no-code technology that would enable the BSA to tailor its new system in-house to its processes, and so avoid the unnecessary expense and inflexibility of an off-the-shelf IT solution. EBRD staff further recognised, through consultations with the BSA and other stakeholders, the need to develop data-governance skills in parallel with any IT system, so they engaged experts from the National Statistical Office to guide the BSA on how it could produce insolvency statistics.

EBRD legal consultants Moravčević Vojnović i Partneri, in cooperation with Schoenherr, have prepared a draft regulation governing the BSA's role relating to insolvency statistics and reporting to be adopted following amendments to the Bankruptcy Law. Both the BSA and the EBRD are now looking for funding to implement the roadmap and the next phases of the project once those amendments are enacted. The amendments will also support the BSA's new responsibility as operator of a soon-to-be-introduced centralised platform for electronic sales in insolvency proceedings, a concept on which it partnered with the International Finance Corporation. Implementation of the roadmap and the improvements to the BSA's IT and data governance toolkit are expected to strengthen the BSA's regulatory function and will help the Serbian authorities align with their counterparts in the European Union. Undoubtedly, the publication of more data and statistics on the management and outcome of insolvency cases will bring greater transparency to creditors and other insolvency stakeholders.

The Bank recently worked closely with the BSA again by including Serbia in a regional insolvency training pilot. This means the EBRD has been able to support the BSA's training for insolvency practitioners and the roll-out of the official 2024 BSA training curriculum, working with a national team composed of lawyers Luka Andric and Branka Vesovic from Andric Law Office, insolvency practitioner Djordje Jokic and Judge Ninoslav Volarevic, as well as international experts Dr Paul Omar and former UK insolvency practitioner Kerry Trigg (see Table 1). Professional training, as well as "on the job" experience, are essential for the proper implementation of any insolvency law. However, often what is missing – especially for insolvency practitioners – is training infrastructure and a responsible counterpart with the capacity to deliver training for the profession on a regular, continuing basis. This regional project is aimed at developing and delivering more scalable and comprehensive official training programmes for insolvency officeholders and judges, grounded in domestic law and practice. The objective of the project is to develop a full curriculum, training methodology and set of materials (workbooks and training slides) that can be used as a starting point and reference for any country project involving the training of insolvency practitioners.

The pilot in Serbia has adopted a mix of in-person training and remote (webinar-based) training, which became common during the Covid-19 pandemic. EBRD staff have worked with the BSA to deliver a proper needs assessment and identify key areas of training. One challenge under the project has been the fact that the insolvency practitioner profession is not homogeneous. Unlike in some countries, such as Greece, where insolvency practitioners are lawyers, in Serbia the profession today is made up of mostly sole practitioners from a range of backgrounds including law, business, accounting and engineering. Most practitioners, however, come from an accountancy background. This has been relevant when designing materials and agreeing on the focus of the training.

Table 1. Official training programme for bankruptcy administrators

	Topic	Date	Format (seminar/webinar)
1.	Comparative presentation of the position, qualifications and training, supervision and regulation of bankruptcy administrators in different jurisdictions (Workbook 1)	February 2024	Webinar
2.	Ethics and professional standards in bankruptcy proceedings Case management and reporting (Workbooks 2 and 3)	March 2024	Two half-day seminars
3.	Financial mismanagement, asset tracing and recovery (Workbook 4)	April 2024	Webinar
4.	Types and plans of reorganisation in bankruptcy (Workbook 5)	May 2024	Full-day seminar
5.	Forensic accounting	June 2024	Webinar
6.	International bankruptcy and practice (Workbook 6)	September 2024	Webinar
7.	Asset realisation proceedings (Workbook 7)	October 2024	Full-day seminar
8.	Financial skills in the context of bankruptcy proceedings (Workbook 8)	December 2024	Recording

Another challenge has been the need to deliver any in-person training simultaneously in the three locations of Belgrade, Niš and Novi Sad. However, participants in these locations have welcomed the opportunity to connect in person. The BSA has been involved in all the training, including securing the facilities of its partner the Chamber of Commerce on a voluntary basis and organising internally the translation of international presentations and materials for the in-person training. Key topics of training conducted to date include the role of the insolvency practitioner internationally (a webinar) and case management, professional standards and ethics, and restructuring plans (all in-person events).

EBRD staff have learned a great deal from their activities with the BSA since the Bank began working with it in 2004. The vision, determination and sustained effort by the Serbian authorities to invest in their insolvency framework has brought demonstrable results. Serbia has performed highly in EBRD insolvency assessments and the features of its insolvency framework – an active regulator, a developed regulatory framework and disciplinary function, and a developed profession of insolvency practitioners – have laid a solid foundation for future development and growth, in line with its European Union peers.

The Bankruptcy Supervision Agency's role will soon expand to cover the regulation of entrepreneur insolvency and/or consumer insolvency.

A highlight for the BSA and a measure of how far it has come since its creation was its presidency in 2023 of the International Association of Insolvency Regulators. EBRD colleagues were able to attend the association's annual conference, held in Belgrade in September 2023, and to present on their fruitful collaboration with the BSA to a wide audience of regulators from more than 20 economies including Australia, Canada, Hong Kong, India, Singapore, the United Kingdom and the United States of America, as well as other EBRD economies, including Albania, Estonia and Latvia, and fellow international financial institutions, such as the World Bank and the International Monetary Fund.

The BSA's role will soon expand to cover the regulation of entrepreneur insolvency and/or consumer insolvency. These are not yet part of the Serbian insolvency framework, but are part of many national insolvency systems. The EBRD looks forward to continuing its work with the BSA and to implementing similar projects with other national regulators in the EBRD regions, using lessons learned from its partnership in Serbia.

Interview with **Dragisa Petrovic, Director of the BSA**

Dragisa Petrovic joined the Bankruptcy Supervision Agency as a Director in December 2017. Through cooperation with international organisations and looking ahead to the future needs of bankruptcy administrators, he has contributed significantly to the BSA's recognition as a leading regulator in the region and a model for neighbouring countries. Previously, Mr Petrovic spent four years as General Manager of PKB Corporation, the largest agribusiness firm in the former Yugoslavia. Prior to entering the agribusiness sector, he was in banking for more than a decade and gained deep insight into the insolvency field by managing the bankruptcy of AGROBANKA.

The BSA is a leading regulator for insolvency in the Western Balkans. What elements do regulators like the BSA need to be effective in achieving their mandate?

First and foremost, experience, a good team and continuous improvement are must-haves. Since its establishment in 2005, the BSA has gained substantial experience in bankruptcy. It has further strengthened this expertise through direct management of bankruptcy proceedings as the bankruptcy administrator for social and state-owned enterprises. The team is high performing and we strive to maintain this quality by educating and motivating younger colleagues to benefit from the experience of their senior peers. We also encourage creativity, keeping abreast of developments in the sector and incorporating innovations in the bankruptcy field. Lastly, it is essential to leverage the positive effects of digitalisation in daily work, as the BSA recognised 15 years ago.

The BSA assumed the prestigious presidency of the International Association of Insolvency Regulators from September 2022 to September 2023. What did you and your colleagues learn from this experience and from fellow regulators?

We have learned that collaboration can definitely contribute to achieving more. This probably holds true for many spheres of life but, for our profession, it is absolutely true. We have realised that governments and regulators face similar challenges, but there is also a range of good solutions to certain problems that have been implemented in some countries. These solutions, with minor modifications, can be successfully applied in another system. We are glad that the BSA has been recognised as an example of good practice, so we have been very active lately in presenting that practice to our international friends.

How is digitalisation affecting you as a regulator?

As I mentioned earlier, the BSA recognised even 15 years ago that digitalisation was a significant factor for both regulatory tasks and for the implementation of procedures. The use of digitalisation ranges from enabling a significantly larger amount of data analysis and facilitating supervision processes to administering bankruptcy proceedings. We immediately embraced some digital solutions and, in my opinion, it was a good decision. Aware of the speed at which digitalisation is advancing, we initiated a project with the EBRD that demonstrates our intention to progress further and modernise digital systems while devising new solutions. I am pleased that the EBRD shares the same vision and that we are partners in achieving this goal.

What are the priorities for the BSA in the insolvency sphere in the coming years?

The BSA's priorities are to modernise its digital solutions and successfully accomplish the new tasks ahead. These tasks include compiling official bankruptcy statistics for Serbia and implementing electronic sales in bankruptcy proceedings. In addition, we expect to be the main partner to the relevant Ministry of Economy, with which we have excellent cooperation, in designing a personal bankruptcy system and aligning it with EU regulations.

What achievement are you most proud of since you became BSA director?

When I think along those lines, as an economist, I always think in numbers. So I cannot help but feel satisfied that, since 2018, 1,251 sales have been conducted in bankruptcies for which the BSA has been a bankruptcy administrator, generating revenue of RSD 44.7 billion (€382 million). In addition, there have been 746 supervisions of the work of bankruptcy administrators. These are significant figures. But beyond these quantifiable achievements, I am most proud of the fact that the BSA is a relevant and respected institution in Serbia, and I see that its quality is being recognised beyond the borders of our country.

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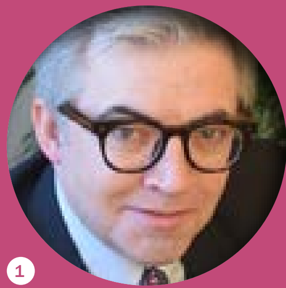
BAKU TO THE FUTURE: HOW THE EBRD IS HELPING TO DIGITALISE AZERBAIJAN'S ECONOMY

“The government of Azerbaijan has embarked on an ambitious programme of digitalisation of the country's economy, with the objective of connecting the whole country to high-speed internet by 2025.”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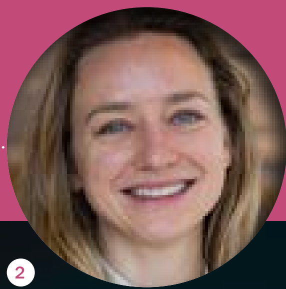
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Hollywood's *Back to the Future* showcases the idea of altering the past to change the future. But Azerbaijan's focus is on using the internet to shape the present and future by deepening and broadening commerce, entertainment, learning, public services, civic participation, social inclusion and more, albeit with fibre optics and radio waves rather than with time-travelling DeLoreans.

INTRODUCTION

In line with all modern economies, Azerbaijan sees affordable access to quality digital services as a critical enabler for both economic and social development. Such access can boost a country's competitiveness on a global level and has become an essential tool in modern society.

Indeed, studies on the economic impact of broadband penetration suggest that a 10 per cent increase in connectivity can significantly boost gross domestic product. According to the World Bank, such an increase can lead to economic growth of about 1.4 per cent in developing countries.[1]

With this in mind, the government of Azerbaijan has embarked on an ambitious programme of digitalisation of the country's economy, with the objective of connecting the whole country with high-speed internet by 2025. Part of this programme commits the government to reform telecoms sector governance and regulation as a means of enabling greater liberalisation, with the aim of driving needed investment into telecoms infrastructure. Admittedly, Azerbaijan has its work cut out for it, having (at the time of writing) one of the slowest internet speeds globally, ranking 117 among 180 countries for fixed broadband internet speed, with an average download speed of 38 Mbps.

To help boost both investment into and reform of the telecoms sector, the EBRD and the Azerbaijani government began a programme of cooperation in 2020. This programme has two main pillars: (1) potential lending by the Bank to help upgrade and extend the country's telecoms infrastructure and (2) an EBRD-led technical cooperation programme to help the government implement sector reform.

This article looks at the telecoms market in Azerbaijan, highlighting the reform measures promised by the government and examining some of the challenges encountered in trying to deliver digital connectivity goals. It also highlights the EBRD's role in the development and reform of Azerbaijan's telecoms sector, in the context of long-standing EBRD/government cooperation on telecoms sector development.

To help boost both investment into and reform of the telecoms sector, the EBRD and the Azerbaijani government began a programme of cooperation in 2020.

TRENDS IN TELECOMS

Telecoms infrastructure is the critical enabler of the digital economy, enabling digital connectivity through its "interconnected networks" – that is, the internet. Essential to delivering such connectivity is investment to upgrade and expand the speed, capacity and resilience of that infrastructure.

While the state historically will have been the main investor in the telecoms sector given its formerly state-owned, vertically integrated and monopolistic characteristics, technology, economics and state budget constraints have long since conspired to

1 See Minges (2015).

make the provision of telecoms infrastructure and digital services a largely private sector-led and profitable enterprise.

However, like broader reform in transition economies, the telecoms market requires structural change if it is to attract the types and volume of investment necessary to achieve digital connectivity targets. The structural change that has proven key to the attraction of investment into telecoms is liberalisation that actively promotes private sector-led competition in the provision of services to end-users.

Over the last three decades, policymakers and regulatory bodies have liberalised telecoms markets by using three key enablers: the removal of historic monopoly rights; adoption of clear, fair and competitive market entry and operation rules; and the privatisation of state-held telecoms assets, separating policymaking and operational control.

These measures have produced very positive outcomes, greatly deepening and broadening digital connectivity around the globe – in terms of network reach, capacity, cost to consumers, choice and quality.[2] Though this approach remains the trend, some countries have been slower than others to adopt liberalisation, particularly in fixed broadband markets where the legacy control of last-mile copper networks by state-owned enterprises persists, leading to monopolistic structures in many non-European Union (EU) economies in the EBRD regions.

Mobile markets, on the other hand, tend to be largely competitive. Recognising their profound economic and social impact, governments have been more proactive in liberalising these markets. Mobile networks, which generally require lower initial investment, offer rapid deployment and the ability to service remote areas effectively. Allocating and managing the radio spectrum (over which much of mobile service is delivered) has also proven comparatively simpler than regulating the extensive infrastructure networks underpinning fixed broadband services.

2 Studies such as Ros (1999), Wallsten (2000a,b), Boylaud and Nicoletti (2000) and Ezzat (2015) demonstrate that the combination of privatisation and liberalisation is associated with significant sector improvements in terms of teledensity and service levels (although the impact of privatisation itself is ambiguous in terms of impact on sector performance).

AZERBAIJAN'S TELECOMS MARKET

Although liberalised and competitive in several respects, Azerbaijan's telecoms market can still be characterised as being at an earlier stage of development than others. This characterisation is largely borne out by the concentration of market power of its fixed incumbent operators, the presence of the state as a shareholder in several sector operators and the absence of an effective wholesale market for telecoms infrastructure.

Against this background, the government committed to major reform of the sector and has begun taking concrete steps to deliver on its commitments. These commitments have come in the form of the government's 2016 ICT Sector Strategic Roadmap.[3] This roadmap, implemented under the supervision of the Ministry of Digital Development and Transport, committed the government to revising the telecoms law as a means of adopting and implementing EU reflective regulatory governance and competition safeguards to anchor liberalisation in Azerbaijan.

The government has followed through in its commitment by establishing a sector-specific regulatory authority for telecoms, in the form of the Information Communications Technology Authority (ICTA), preparing a more modern telecoms law (expected to be approved in 2025) and by beginning to adopt and implement market mechanisms through which a liberalised telecoms market can properly function.

The EBRD has followed through on its cooperation commitments, with a key part coming in the form of technical cooperation support for ICTA, Azerbaijan's new sector-specific telecoms regulatory agency. This support will help ICTA to implement some of the key parts of the new regulatory architecture for the sector.

EBRD/ICTA TECHNICAL COOPERATION

The Bank launched its Regulatory Governance and Competition Safeguards technical cooperation programme with ICTA in September 2023. This programme has two main objectives: (1) help strengthen capacity within ICTA and the Ministry for Digital Development and Transport to implement the new regulatory and governance structures for which the government's sector strategy and the forthcoming telecoms law provide and (2) aid ICTA in designing a methodology for analysing and determining the level of competition in key parts of the telecoms market, as well as helping to undertake the analysis itself.

1 See Government of Azerbaijan (2016).

> The Bank's technical cooperation programme is helping the Information Communications Technology Authority to prepare the methodology and conduct analyses of the fixed broadband and mobile markets in Azerbaijan.

Building ICTA's capacity has taken the form of a custom-built training programme that focuses on its specific priorities, covering both the conceptual basis for modern regulation across key regulatory topic areas (for instance, licensing, network access, spectrum management and market analysis) and the practical measures necessary to implement those concepts. The training programme has been implemented in eight week-long components.

Support for the market-analysis activities has included assisting ICTA in the preparation of a methodology and enabling regulations for data gathering, analysis and determination, drawn from the EU telecoms framework. The EBRD programme is also tasked with helping to conduct the market analysis and consult on its methodology and outcome.

The market analysis exercise is, perhaps, one of the most fundamental and seminal activities necessary before effective competition can emerge in any telecoms environment. This market analysis is a legally mandated activity that provides the evidential basis on which to determine the market power of market participants and, with that, legitimacy to impose remedial measures that can be applied to address the misuse of any such power.

The Bank's technical cooperation programme is helping ICTA to prepare the methodology and conduct analyses of the fixed broadband and the mobile markets in Azerbaijan. Any finding of dominance in a relevant market will give ICTA the basis and the means to apply a range of competitive safeguards to make sure competition can emerge or be sustained. Applying these safeguards will be critical to ensuring the emergence of an effective wholesale market for broadband in Azerbaijan.

CHALLENGES IN AZERBAIJAN

Continued state-ownership
Telecoms privatisation has yet to advance meaningfully in Azerbaijan, with the state retaining stakes in a number of operators. The triple role of the government – which sets policies, regulates and participates in the market – may lead to potential conflicts of interest and distort incentives for investments, product innovation and pricing.

However, Azerbaijan's strategy to establish regulator frameworks and enforcement mechanisms prior to privatisation aligns with global evidence. Indeed, the EBRD's own research suggests that privatising after establishing an independent regulator improves sector performance in terms of fixed and mobile penetration and investment, relative to the alternative scenario where privatisation comes first. When governments privatise before they liberalise, full liberalisation tends not to follow until much later.

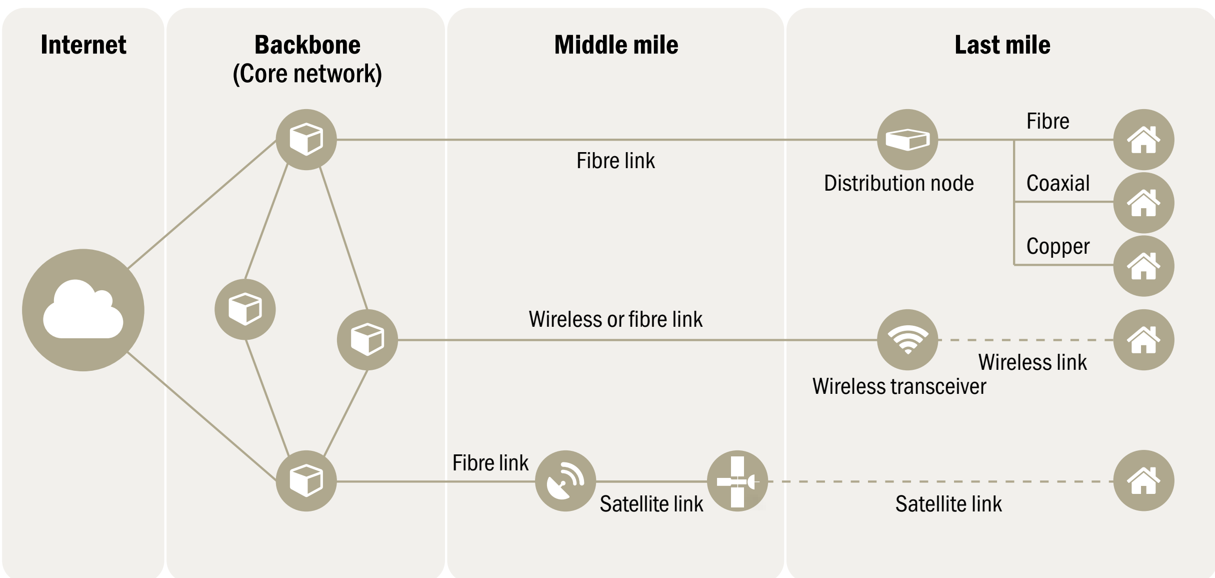
Telecoms regulatory authority
While the government has established ICTA as a sector-specific regulatory authority, the commitment to establish it as an independent authority has yet to be fulfilled. As it currently stands, ICTA remains within the Ministry for Digital Development and

> "Historical evidence consistently demonstrates that liberalised markets deliver superior outcomes for households and businesses in terms of service quality, reach and pricing – thereby amplifying the economic and social benefits of digital connectivity."

Transport structure, reporting to its minister. That said, while not nominally independent, what matters most in this respect is that ICTA operate with independent character, for example, making evidence-based, fully reasoned and published decisions on a transparent basis and with adequate and ongoing consultation with affected parties. Such an approach will, in time, build the confidence of industry participants and consumers alike.

Wholesale market development
Effective wholesale markets allow ease of market entry and are therefore attractive to investors given the prohibitive cost and high risk associated with

Figure 1. The segments of a broadband network



Source: European Court of Auditors (2018).

duplicating incumbent infrastructure – especially ducts, other civil engineering works and last-mile connections. The most important wholesale element of the telecoms market involves an incumbent network operator granting another operator or service provider access to its network, especially to the critical and costly last-mile segment. This access enables other operators – particularly new entrants – to use existing infrastructure to offer services to end-users without the substantial initial investment required to build equivalent infrastructure. Over time, new players can generate enough revenue and experience to start investing in their own competing infrastructure and thus engage in infrastructure competition rather than merely reselling the services of the incumbent operators.

This "ladder of investment" view of market development has inspired regulatory bodies globally to mandate that incumbent telecoms operators provide access to their networks on a cost-based basis. Experience in liberalisation over the last three decades has shown regulators worldwide the importance of ensuring effective wholesale markets, given the potential for existing infrastructure owners (especially those that hold a strong market position) to obstruct the development of competition by refusing competing operators access to that infrastructure, or by offering access on terms and conditions (especially price) that undermine the viability of competing operators or hinder their progression up the investment ladder.

Under best-practice regulation, competitive markets have developed efficiently, with regulators often focusing entirely on wholesale markets, leaving retail markets unregulated. This balance has proved attractive to market players because it allows them to compete freely at the retail level, while having favourable (regulated) conditions to make economic decisions about whether, when and how to invest in infrastructure as a means of growing their business.

Azerbaijan's telecoms market is now at the point where the most effective way to attract investment into the expansion of the sector and advance its technological growth is to ensure the creation and smooth operation of an effective wholesale market. While new players are starting to deploy networks to compete with the incumbents' these remain limited to the country's most profitable, urban areas.

The EBRD's support for ICTA is laying important foundations for an effective wholesale market in Azerbaijan. Determining the level of competition in specific telecoms markets, through formal market analysis activities, will provide the basis for imposing regulatory measures that will help establish a functioning wholesale market. Specifically, where infrastructure owners are found to have a level of market power which allows them to prevent competing operators from accessing their infrastructure on a wholesale basis as a means of delivering services to their retain customers, ICTA can impose tried and tested competition safeguards to mandate such access. Among the measures that can be applied in such situations are transparency, accounting separation and cost-justified wholesale charges.

CONCLUSIONS

Azerbaijan exemplifies the complexity of transitioning to a liberalised telecoms market. In many EBRD countries, governments may be seen to be slow to introduce substantial competition when they own the primary operators, influenced by factors such as national sovereignty, scepticism towards private-sector management of crucial infrastructure and the direct revenues and benefits derived from state-owned enterprises. State-owned incumbents may also be ill-prepared for competition due to operational deficiencies, aging infrastructure and disproportionate public-service obligations. However, historical evidence consistently demonstrates that liberalised markets deliver superior outcomes for households and businesses in terms of service quality, reach and pricing – thereby amplifying the economic and social benefits of digital connectivity.

The EBRD's dual approach of financial investment and technical cooperation is unique in endeavouring to address these challenges simultaneously. By financing state-owned operators, the Bank supports essential infrastructure upgrades and competitiveness improvements that prepare incumbents to withstand competition and lays the groundwork for broader market reforms. By sharing experience and global best practices with governments, the EBRD can illustrate the benefits of liberalisation for propelling national digitalisation goals. In the race to the future, who needs a DeLorean when you can have light-speed, fibre optic-delivered broadband?

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ACCELERATING CLIMATE ACTION IN THE BOARDROOM

> “As directors are accountable to shareholders for their organisation’s performance, they are increasingly being expected to address climate change and sustainability issues with the same level of scrutiny as any other issue posing a financial risk to the business.”

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Boards, independent directors and senior management play a critical role in the climate transition as they steer and oversee their organisation's climate strategy, governance, risk management and transition planning. Climate governance has been a key pillar of the EBRD's green strategy and is central to client engagement. As part of these efforts, the EBRD has been working with the Climate Governance Initiative since 2022 to improve the climate governance of companies and boost boards' capacity to move towards a net-zero economy in the EBRD regions.

INTRODUCTION

Climate change is a major disruptor of global business. Climate change-related risks, impacts and opportunities are unique, owing to distinct characteristics such as the need for long-term business planning, the high levels of uncertainty involved, the scarcity of historical data (inhibiting analysis of future trends) and the unprecedented impact on value chains. With growing pressure from regulators, financial institutions, consumers and other stakeholders to enhance climate action, boards and non-executive directors have broadened their focus beyond traditional corporate governance to include climate-related governance issues, climate risk and opportunity management, and the incorporation of climate considerations in their business model and strategy.

Various market developments and trends have accelerated this shift.

a) Focus on climate and sustainability-related disclosures

First, there is widespread consensus that climate and sustainability-related data are essential in order to monitor progress towards achievement of the goals of the Paris Agreement, the stated climate ambitions of countries under nationally determined contributions (NDCs) and climate commitments at corporate level. This, coupled with concerns about the impact that unmanaged climate-related risks could have on markets' financial stability, has triggered a wave of mandatory regulatory requirements and voluntary market-driven standards that require entities to identify, assess, manage and report on climate and sustainability-related matters. Clear and robust governance mechanisms, future-proof strategies, science-based targets and risk management mechanisms are at the core of those emerging standards.

For example, the Task Force on Climate-related Financial Disclosures (TCFD) emphasised governance as a building block of effective climate risk and opportunity management.[1] Governance is one of the four foundational pillars of the TCFD's recommendations. Subsequent sustainability disclosure standards have also followed this approach. The standards issued by the International Financial Reporting Standards Foundation's International Sustainability Standards Board (ISSB) – which the G20 recognises as a global baseline for sustainability-related disclosures – explicitly set requirements for a reporting entity's governance. Similarly, governance is one of the fundamental pillars of the European Sustainability Reporting Standards (ESRS), which are applicable to companies that fall within the scope of the EU's Corporate Sustainability Reporting Directive.

From a governance perspective, the TCFD recommendations, the ISSB standards and the ESRS all require disclosures relating to a board's oversight of climate-related risks and opportunities, as well as skills and competencies in respect of climate and sustainability-related decision-making. The ISSB standards and the ESRS, in particular, require the disclosure of an entity's climate transition plan, which is the action plan adopted by an entity to address climate-related risks, impacts and opportunities. The ESRS go a step further and require a reporting entity to disclose whether the transition plan has been approved by its management and supervisory bodies.

1 See World Economic Forum (2019).

Therefore, the prevailing disclosure regulations and standards implicitly place a responsibility on the management and supervisory bodies of an entity to effectively oversee, identify and manage climate related matters by requiring the disclosure of such internal governance arrangements. This, in turn, requires that boards have the knowledge, skills and experience needed to effectively discuss and decide on climate-related risks, impacts and opportunities and develop climate-conscious strategies.

b) Greater interest in sustainable investment

Second, market appetite for sustainable investment has risen sharply in recent years alongside investor and lender demand for increased climate and sustainability-related disclosure. The term “sustainable investment” refers to investments that consider the impact of climate change and other environmental, social and governance-related (ESG) issues. The 2024 Morgan Stanley Sustainable Signals survey[2] finds that more than half of individual investors (54 per cent) plan to increase their sustainable investment in the coming year, and more than three-quarters of individuals (77 per cent) are interested in sustainable investing. Robust climate governance arrangements and high-quality disclosure of such arrangements can help companies to signal their climate resilience to investors, which will lead to enhanced access to finance through new instruments such as green bonds and sustainability-linked loans.

c) Risk of climate litigation directed at corporate officers

Third, litigation against company directors and senior management for their actions or perceived inaction on climate-related issues is growing. Such litigation is usually related to senior officers’ duties to oversee, identify and consider material climate-related matters in the entity’s day-to-day operations. These cases involve interpreting legal obligations under corporate and financial law to protect shareholders and investors. The objective of bringing such litigation is to disincentivise companies from continuing with high-emission activities or, in the case of the financial sector, to disincentivise investment in high-emission assets. Increasingly, courts are having to adjudicate on matters relating to private and public entities’ handling of climate-related impacts and risks, so directors and senior officers will increasingly be expected to assume responsibility for their company’s actions or inaction in relation to climate change.

2 See Morgan Stanley Institute for Sustainable Investing and Morgan Stanley Wealth Management (2024).

As directors are accountable to shareholders for their organisation's performance, they are increasingly being expected to address climate change and sustainability issues with the same level of scrutiny as any other issue posing a financial risk to the business. However, overseeing climate and sustainability-related matters presents new challenges for boards because of the significant uncertainty involved, the lack of historical data (which makes it difficult to accurately assess impacts, risks and opportunities) and the need to carry out forecasting in the absence of such data. Non-executive directors – sometimes also called independent directors – have a special role to play in holding management to account and asking difficult questions, and this now extends to matters pertaining to climate and sustainability risks, impacts and opportunities. In this context, it is interesting to note that in the 2024 EY Europe Long-term Value and Corporate Governance Survey,[3] fewer than 10 per cent of non-executive directors and chairs reported complete satisfaction with their companies' business rationale for sustainability.

3 See Teigland and Hobbs (2024).

4 See EBRD (2022).

THE EBRD'S ROLE IN PROMOTING CLIMATE AWARENESS IN THE BOARDROOM

Environmentally sound and sustainable development is central to the EBRD's mandate and is promoted through every project and policy initiative. The Bank has committed to becoming a majority green bank by 2025 and has met this commitment over the last two financial years. Since 1 January 2023, the Bank has fully aligned its activities with the mitigation and adaptation goals of the Paris Agreement.[4] Through policy reform and investment, the Bank also helps its clients and countries of operation to align their business models and economies with the goals of the Paris Agreement.

To enhance climate governance among senior managers of companies and financial institutions in its regions, the EBRD has established a dedicated Corporate Climate Governance (CCG) Facility. CCG refers to the set of rules, practices and processes that an entity puts in place to identify and manage the effects of climate change and improve decision-making and disclosure in relation to those impacts. The CCG Facility consolidates the policy reform and business advisory support that is provided by the

EBRD in order to help private-sector and state-owned entities to develop and strengthen their climate-related governance, strategy, risk management, target-setting and disclosure practices.

A key form of business advisory support offered to clients under the CCG Facility is support with developing and implementing corporate climate governance action plans (CCGAPs). Notably, the CCG Facility provides: (i) support with entity-level assessment of governance gaps in respect of climate issues; and (ii) capacity-building support to improve the entity's climate governance and disclosures, in accordance with international best practices and standards.

The Bank has developed policy products and partnerships for the benefit of corporate clients, financial institutions and other stakeholders, with donor support provided through the CCG Facility. For example, the Bank has a long-standing external nominee programme, through which it engages with a network of more than 100 non-executive directors on the boards of its investment companies. Under the CCG Facility, the EBRD has developed a climate toolkit in order to: (i) help its nominee non-executive directors to gain a robust understanding of the governance of climate-related risks, impacts and opportunities; and (ii) equip them with the tools and information they need to become strong drivers of climate action and sustainability in their respective companies. This toolkit helps non-executive directors to assess their company's climate governance maturity and outline the steps needed to strengthen the company's climate agenda.

Other directors and senior managers also have a critical role to play in the climate transition. Their engagement is vital for strategic guidance and oversight on climate action, as well as for the credibility of transition plans and organisational disclosures. However, effective fulfilment of this new role requires both organisational mandates and capacities that are often lacking, especially in emerging markets. In the 2022 Boston Consulting Group-INSEAD Board ESG Pulse Check,[5] around 70 per cent of directors reported that they were only moderately effective or not at all effective at integrating sustainability into company strategy and governance. Among companies with a net-zero commitment, only 55 per cent of directors reported that their organisation had prepared and published a plan for meeting that target.

The actions of private and public-sector entities in the EBRD regions are crucial not only for addressing the climate crisis but also for building strong and resilient economies.

Looking specifically at the EBRD regions, several economies are particularly vulnerable to climate and sustainability risks. This stems from a combination of factors, including geographical characteristics and historical under-investment, which has resulted in infrastructure that is significantly exposed to the physical impacts of climate change. At the same time, there is a significant lack of awareness in these markets and a lack of readiness to effectively identify, consider and mitigate climate-related risks or leverage climate-related opportunities. Many companies in these economies still do not adequately consider the risks associated with the physical impacts of climate change and the transition to low-carbon economies when making business and investment decisions.

The actions of private and public-sector entities in the EBRD regions are crucial not only for addressing the climate crisis but also for building strong and resilient economies. Supporting directors and senior management on their climate journey can help to reduce the climate risk exposure of the EBRD's investments. This support is also vital to achieve the Bank's objective of greening its economies. To increase its impact beyond its projects and clients, the Bank has been working with the Climate Governance Initiative (CGI) on the Chapter Zero initiative since 2022, supported by the CCG Facility.

5 See Boston Consulting Group and INSEAD (2022).

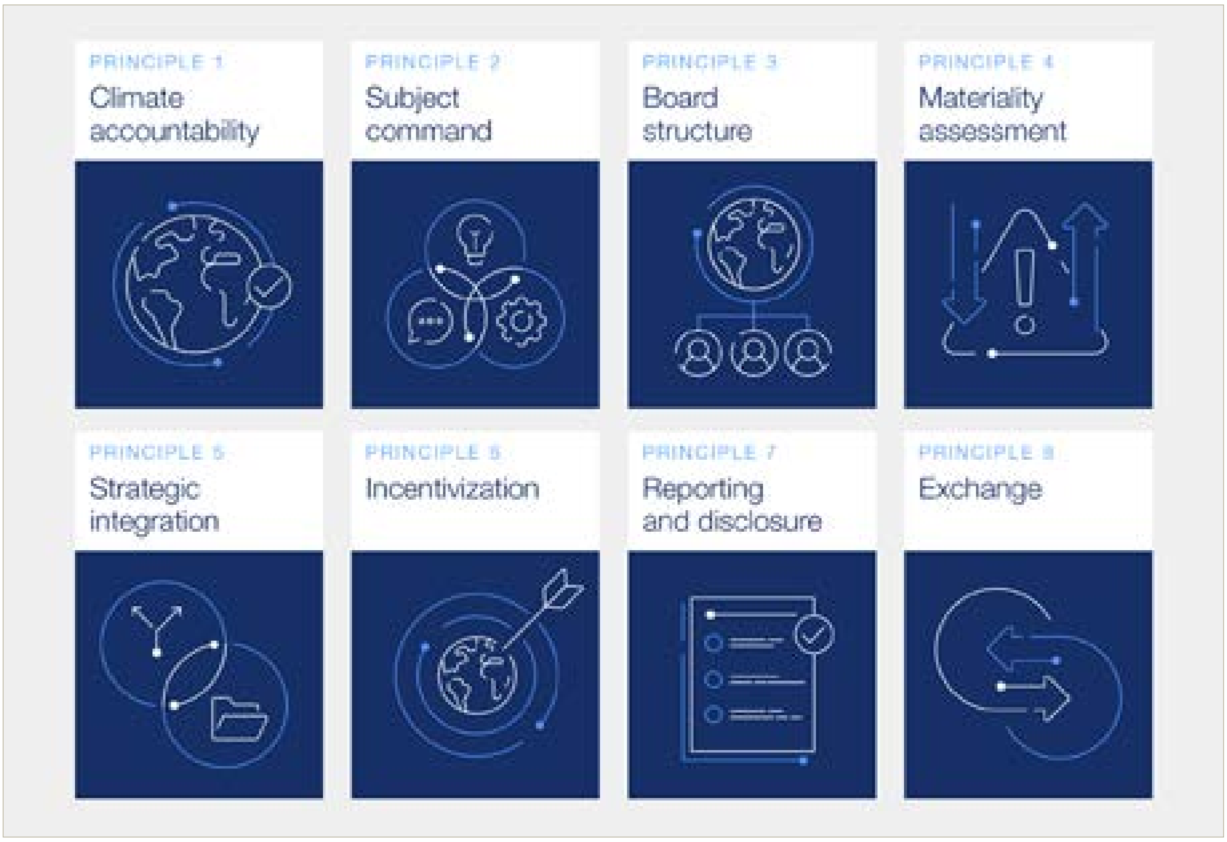
> “ The EBRD’s partnership with the Climate Governance Initiative aims to help senior management of companies and financial institutions in the EBRD regions to improve their capacity to identify and address climate risks, impacts and opportunities, carry out transition planning and prepare climate disclosures. ”

THE EBRD’S PARTNERSHIP WITH THE CGI

The EBRD’s partnership with the CGI aims to help senior management of companies and financial institutions in the EBRD regions to improve their capacity to identify and address climate risks, impacts and opportunities, carry out transition planning and prepare climate disclosures. The CGI was conceived in 2019 as a result of work by the World Economic Forum (WEF) focusing on climate action in the corporate world. It helps companies to set a climate target and develop a plan to meet it.

The foundation of the CGI’s work is the WEF’s eight Principles for Effective Climate Governance (see Figure 1),[6] which range from board accountability (to ensure long-term resilience to climate risk) to knowledge exchange (keeping informed through dialogue with investors, policymakers and others). These principles build on existing corporate governance frameworks such as the International Corporate Governance Network’s Global Governance Principles, as well as other climate risk and resilience guidelines, including the recommendations of the TCFD.

Figure 1. The World Economic Forum’s eight Principles for Effective Climate Governance



Source: World Economic Forum (2019).

6 See Climate Governance Initiative (2019).

The CGI launched Chapter Zero in 2019 in order to mobilise and educate directors and equip them with the skills and knowledge needed to address climate change at board level by applying the WEF's Principles for Effective Climate Governance.

CHAPTER ZERO IN THE EBRD REGIONS

The EBRD has worked closely with the CGI and local host organisations to launch five Chapter Zero organisations – referred to as "chapters" – in Egypt, Kazakhstan, Türkiye, Ukraine and the Caucasus, and Uzbekistan.

Each chapter is set up as a network of boards, non-executive directors and senior managers who are working towards integrating climate risks and governance into the overall business strategy of their entity. It is designed as a platform enabling chapter members to exchange their organisation's practical experience of managing climate-related governance risks, and strategies. Members of those chapters can learn from experts and peer companies that are advanced in the area of climate action in their respective countries by participating in knowledge-sharing events. Chapter members also have access to expert knowledge on climate-related risks, impacts, opportunities and strategies acquired by more advanced chapters, as well as access to leading consultants through webinars, training sessions and workshops organised with the support of the EBRD and the CGI.

Box 1. **Chapter Zero Egypt**

"Chapter Zero Egypt exemplifies the power of collaboration and proactive engagement in addressing climate challenges.

As the first initiative of its kind in Africa and the Middle East, it sets a commendable precedent for fostering climate-resilient business practices. This pioneering initiative marks a significant milestone in climate governance in the region.

As we emphasise the important role of the private sector in climate action, this platform provides invaluable resources and collaboration opportunities for business leaders, allowing them to navigate towards sustainable and low-carbon models. The EBRD is proud to support Chapter Zero Egypt and looks forward to it playing a pivotal role in promoting climate-conscious decision-making among business leaders in Egypt."

Khalid Hamza, Former Head of Egypt, EBRD

Members of those chapters can learn from experts and peer companies that are advanced in the area of climate action in their respective countries by participating in knowledge-sharing events.

For example, Chapter Zero Egypt,[7] which was officially announced at the United Nations Conference of the Parties (COP27) in Egypt, has organised awareness-raising webinars for members on a wide range of topics – including carbon credits, sustainability disclosures, ESG reporting guidelines and the development of sustainability strategies. Chapter Zero Egypt is thereby supporting the green transition of the private sector in the region (see Box 1). Similarly, Chapter Zero Türkiye has organised, in collaboration with the Turkish Industry and Business Association (TÜSİAD), panel discussions and round tables with C-suite executives on the topic of industrial decarbonisation and navigation of the climate challenge at company level.

In some emerging-market economies, an additional challenge may lie in the corporate governance practices of the market, which need to be taken into account when framing the support offered by the chapter. In Uzbekistan, for example, the EBRD's *Corporate Governance in Transition Economies* report[8] revealed a significant lack of corporate governance awareness across the business community, identifying weaknesses in areas such as transparency, disclosure, and the structure and functioning of the board. Clear governance structures and independent boards with strong mandates are important in order for directors and senior management to address climate and sustainability matters effectively.

3 See www.dailynewsegypt.com/2023/10/03/chapter-zero-launched-activities-in-egypt-in-september-2023

4 See EBRD (2020).

Box 2. **Chapter Zero Uzbekistan**

"Collaboration with Chapter Zero in EBRD countries of operation is an opportunity to engage with highly professional, motivated, proactive and self-driven country leaders who are at the forefront of sustainability and business development action in their communities. It is they who drive local change, paving the way to a better and more sustainable future. Supported by international experience and leveraging their own multifaceted complementary expertise and extensive local networks, chapter members are uniquely placed to make meaningful improvements in their countries.

One example of such cooperation was the development by Chapter Zero Uzbekistan of the Corporate Governance Handbook. This idea came from local chapter members, who accurately identified the market gap. Indeed, before introducing corporate climate governance to local firms and building their capacity to respond to climate risks and opportunities, it is necessary to enhance corporate governance in general. To this end, chapter members with extensive experience in this area have been resolute in driving the development of the Corporate Governance Handbook for Uzbekistan.

The EBRD has accumulated a wealth of experience in this area through many projects reforming the governance of state-owned enterprises and enhancing governance structures. With input from representatives of four EBRD departments, the chapter delivered a comprehensive guide tailored to the local context. The chapter's host institution, Westminster University in Tashkent, skillfully managed and supervised the material and its delivery to ensure that the final product was coherent, satisfied market needs and met businesses where they are.

This was a very rewarding experience, and we look forward to carrying out more meaningful action in local markets together with Chapter Zero members."

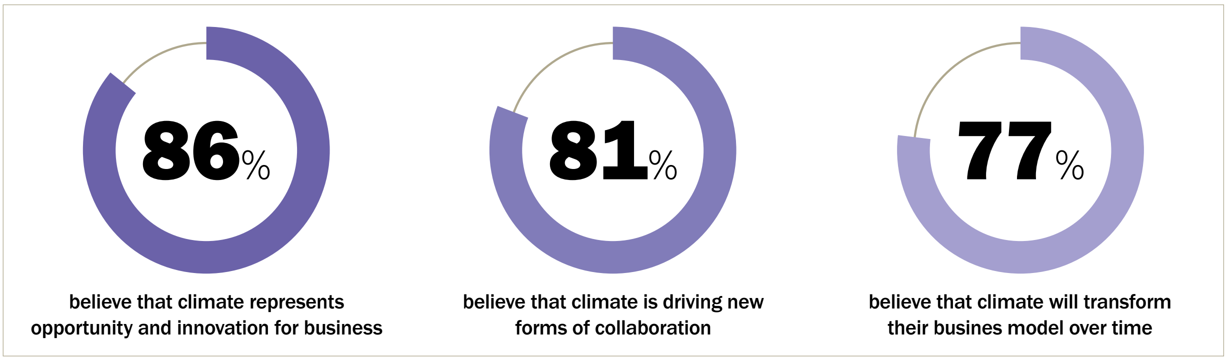
Solomiia Petryna, Principal, Green Financial Systems team, EBRD

As these economies shape their governance landscapes, there is an opportunity to integrate climate governance principles while advancing corporate governance practices, adopting a forward-looking approach that prioritises climate considerations within corporate governance. The EBRD, with its considerable expertise in corporate governance and climate-related practices, is well placed to support its clients on this, as it has in the case of Chapter Zero Uzbekistan (see Box 2).

Last year, the CGI partnered with Kantar to conduct a Global Impact Study covering all Chapter Zero initiatives,[9] which concluded that the more a board director engages with their local CGI chapter, the more likely they are to take positive action in climate discussions in the boardroom. The report also revealed a clear need for Chapter Zero support: nine out of ten respondents said that the climate challenge required new forms of leadership from boardrooms.

9 See www.chapterzeroslovenia.si/en/knowledge-hub_1/global-impact-study-findings-2024-how-can-we--advance-climate--action-on-boards/

Figure 2. Encouraging findings from the Global Impact Study conducted by the CGI and Kantar



Source: Climate Governance Initiative and Kantar (2024).

CONCLUSION

Advancing climate governance and climate action within the boardroom is a strategic imperative for modern businesses. As companies begin their climate journey, it is crucial to build awareness of climate and sustainability-related risks, impacts and opportunities, while understanding the evolving market and regulatory expectations. For those that are more advanced in terms of sustainability efforts, systematically integrating climate considerations into core business processes is essential.

Support provided through the EBRD's CCG Facility – including the Chapter Zero initiatives – seeks to ensure that all companies, regardless of their maturity, size and sophistication, are aligned with the goals of the Paris Agreement and adhere to internationally recognised standards or local regulations. By integrating sustainability considerations into decision-making, boards can drive a systematic greening of their companies, suppliers and economies. Ultimately, robust climate governance and proactive climate action will pave the way for sustainable growth and resilience, positioning companies as leaders in a rapidly changing global landscape.

Advancing climate governance and climate action within the boardroom is a strategic imperative for modern businesses. As companies begin their climate journey, it is crucial to build awareness of climate and sustainability-related risks, impacts and opportunities, while understanding the evolving market and regulatory expectations.

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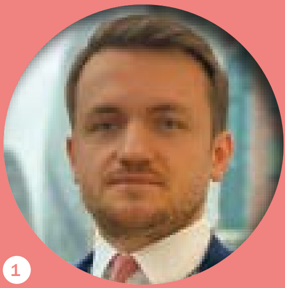
FACTORING SURVEY: TRANSFORMING ACCESS TO FINANCE ACROSS THE EBRD REGIONS

> "The fourth edition of the EBRD Factoring Survey (2023) gives an overview of the current legal and regulatory landscape for factoring and a snapshot of market practices in 10 selected EBRD jurisdictions."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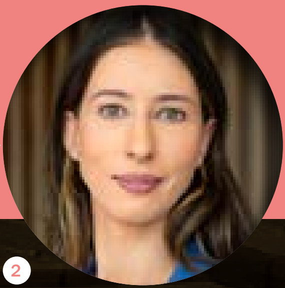
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NEAL HARM
SECRETARY GENERAL, FACTORS CHAIN INTERNATIONAL

For over a decade, the EBRD has helped develop the legal and regulatory frameworks that enable factoring and supply-chain finance. With transaction volumes of these products at an all-time high,[1] now is a good time to look at recent legal and market developments in the EBRD regions to ensure they can support the resilience and sustainability of the sector.

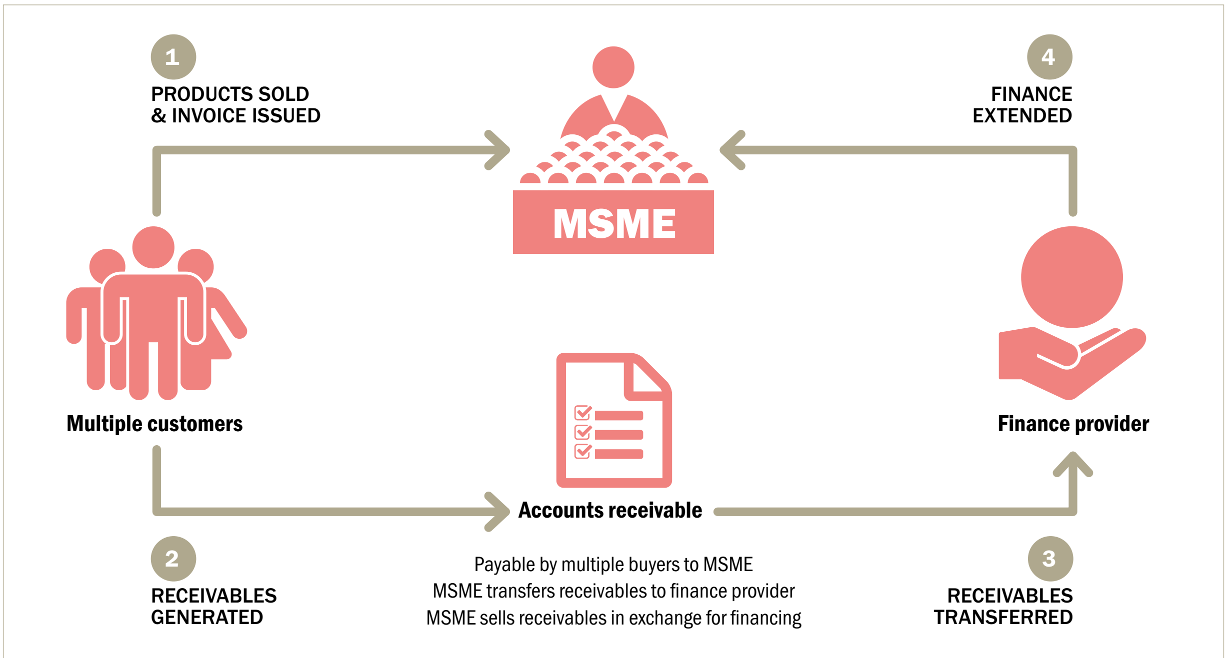
FACTORING AS A FINANCING ALTERNATIVE

Most companies in the EBRD regions typically possess limited immovable assets that traditionally serve as a collateral for banking loans, which remain a predominant form of financing. At the same time, businesses of any size often own receivables that are eligible to be factored. Factoring is a financial service based on the sale of accounts receivables (short-term assets) that unlocks access to working capital.

Given the inclusivity and flexibility of the service, the factoring and receivables finance industry has been growing exponentially. However, legislative, institutional, capacity, market and technological bottlenecks often limit its growth.

The EBRD Legal Transition Programme has been monitoring the evolution of factoring frameworks since 2015. The fourth edition of the EBRD Factoring Survey (2023)[2] gives an overview of the current legal and regulatory landscape for factoring and

Figure 1. Factoring structure



Source: EBRD (2023b).

Note: The company (supplier) sells products to its customers (buyers or creditors) and issues invoices (Step 1). These transactions generate receivables payable 60-90 days after delivery of goods (Step 2). The finance provider (a bank or a non-banking factoring company) purchases receivables (Step 3) and provides the company with immediate payment at a discounted rate, typically 80 per cent of the face value of the invoice (Step 4). The finance provider may choose to notify the company's customers and instruct them to pay into a designated bank account under the control of the finance provider.

1. The 2023 FCI Annual Review indicates that the factoring and receivables finance industry volume witnessed a significant increase of 18.3 per cent in 2022 after a double digit increase of 12.3 per cent in 2021. Compared with the previous year's €3.07 billion, the 2022 estimated volume of €3.66 billion represents back-to-back double-digit increases.
2. See EBRD (2023a).

a snapshot of market practices in 10 selected EBRD jurisdictions (Armenia, Egypt, Georgia, Greece, Kyrgyz Republic, Morocco, Romania, Türkiye, Ukraine and Uzbekistan). It captures changes that have taken place in national laws or practices since the 2018 edition of the Factoring Survey and seeks to assess whether these create an enabling environment for market participants to reap the benefits of factoring.

In comparison with earlier editions of the survey, the fourth edition recognises important trends in digitalisation of the sector and buyer-led, supply-chain financing, places greater emphasis on data protection and examines them in detail. The main findings of the survey are summarised below and can be useful both for policymakers looking for a roadmap to enhance companies' access to finance in their jurisdictions and market players that are considering establishing a presence in a new market.

Stringent regulations tend to concentrate services in the banking sector, limiting smaller market players. The complete lack of regulation, on the other hand, fails to provide the necessary market credibility for the product.

REGULATORY ASPECTS OF ENTITIES OFFERING FACTORING SERVICES

Table 1. **Regulation of factoring services**

Jurisdiction	Licence needed to operate	No capital adequacy requirements	Factoring companies supervised
Armenia	Yes	No	Yes
Egypt	Yes	No	Yes
Georgia	No	Yes	No
Greece	Yes	Yes	Yes
Kyrgyz Republic	Yes	No	Yes
Morocco	Yes	No	Yes
Romania	Yes	Yes	Yes
Türkiye	Yes	Yes	Yes
Ukraine	Yes	Yes	Yes
Uzbekistan	Yes	No	Yes

Source: EBRD Factoring Survey (2024).

Key: Yes No

The first aspect reviewed in the survey relates to the level of regulation applicable to the factoring industry. Stringent regulations tend to concentrate services in the banking sector, limiting smaller market players. The complete lack of regulation, on the other hand, fails to provide the necessary market credibility for the product. Among the surveyed jurisdictions, most lean towards regulating factoring, with Georgia being the exception due to the absence of dedicated regulations.

Seven jurisdictions (Armenia, Egypt, Greece, Kyrgyz Republic, Morocco, Türkiye and Ukraine) require a specific licence for non-banking financial institutions (NBFIs) to start providing factoring services. NBFIs in Romania must register with the National Bank and those in Uzbekistan need authorisation from the regulator. At the other end of the spectrum, Georgian NBFIs are not required to obtain any licences, certifications or authorisations.

PRIVATE AND COMMERCIAL LAW ASPECTS OF FACTORING TRANSACTIONS

Table 2. **Private and commercial law aspects**

Jurisdiction	Specific legal provisions	Eligible receivables	Possibility to assign future receivables	Anti-assignment clause invalid	Electronic execution of agreements	Registration of assignments
Armenia	Yes	Yes	Yes	Yes with limitations	Yes	Yes with limitations
Egypt	Yes	Yes	Yes	No	No	Yes with limitations
Georgia	No	No	Yes	No	Yes	Yes with limitations
Greece	Yes	Yes	Yes	Yes	Yes	Yes with limitations
Kyrgyz Republic	No	Yes	Yes	Yes	Yes	Yes with limitations
Morocco	Yes	Yes	Yes	No	Yes	Yes with limitations
Romania	No	No	Yes	Yes with limitations	Yes	Yes
Türkiye	Yes	Yes	Yes	No	Yes	Yes with limitations
Ukraine	Yes	No	Yes	Yes with limitations	Yes	Yes with limitations
Uzbekistan	No	Yes	Yes	Yes	Yes	Yes with limitations

Source: EBRD Factoring Survey (2024).

Key: Yes No Yes with limitations

The second section of the survey examines private and commercial law considerations that pertain to factoring transactions. While many of the EBRD's jurisdictions have started working on, or already introduced, **specialised laws on factoring**, there are still jurisdictions that have no special provisions on factoring contracts or established and published court practice that would compensate for this lack of clarity. It appears that Egypt, Greece and Türkiye have adopted a specific law on factoring. Other jurisdictions covered by the survey either have specific provisions on factoring in their civil codes (Armenia and Ukraine) or rely on the general provisions for assignment of claims in their legal frameworks (Georgia, Romania, Kyrgyz Republic and Uzbekistan).

The **definition of receivables** that are eligible for factoring should be commensurate with the level of understanding and development of factoring in that market. Markets where factoring is still a nascent product are better off with a narrower definition of receivables (for example, receivables arising from the sale of goods or services with a predefined maturity). This ensures that the market is given a chance to develop a basic understanding of the product before deploying more complex structures. In seven jurisdictions surveyed, factoring is confined to receivables arising from the sale of goods or services, in line with international standards. However, in three jurisdictions (Georgia, Romania and Ukraine), eligibility extends beyond trade receivables.

The **ability to assign future accounts** receivable within factoring relationships is important for establishing a priority over future accounts receivable for factors. The assignment of future receivables (of certain receivables, a group of receivables or all of them) is generally allowed in every surveyed jurisdiction.

Anti-assignment clauses prevent suppliers from assigning their claims to third parties (without the consent of the buyer). In four surveyed jurisdictions (Egypt, Georgia, Morocco and Türkiye) the anti-assignment clauses in commercial agreements are effective against suppliers. The other six jurisdictions (Armenia, Greece, Kyrgyz Republic, Romania, Ukraine and Uzbekistan) render "anti-assignment clauses" as ineffective, but they fail to provide a complete override of such clauses. As such, the buyers/debtors may still claim for damages for breach of contract. International standards, including the UNIDROIT Model Law on Factoring, promote the inclusion of legal provisions that completely override and invalidate any anti-assignment clauses for the purposes of factoring transactions.

The survey also investigates whether surveyed jurisdictions allow for **electronic execution** of factoring contracts, which have a lower overall transaction cost and are more accessible and time-efficient. Egypt is the only jurisdiction where a factoring contract must be executed with a wet-ink signature. In all other nine jurisdictions, electronic execution is possible.

Registration of assignments is desirable for providing notice against third parties and determining priority among competing assignments. It also helps prevent fraud stemming from double factoring. In the surveyed jurisdictions, registries tend to be available only where receivables subject to factoring are not sold outright, but rather assigned by way of security. By contrast, where receivables subject to factoring are fully sold, there is typically not a registry that supports their registration, and they are often left unregistered.

Among the surveyed jurisdictions, only Romania mandates registration for both security and outright transfers to be effective against third parties and establish priority ranking. In Türkiye, there is a registry of factoring transactions where all the receivables used for factoring need to be registered. While such registry creates transparency over the receivables and prevents double-financing of invoices, it is not used to ascertain creditor priority. International standards, including the UNIDROIT Model Law on Factoring, promote the establishment of registries that cover all assignments of receivables, including assignments by way of security as well as outright assignments (sales of receivables).

> “The definition of receivables that are eligible for factoring should be commensurate with the level of understanding and development of factoring in that market.”

OTHER LEGAL CONSIDERATIONS AFFECTING THE UPTAKE OF FACTORING

Table 3. **Miscellaneous issues affecting factoring**

Jurisdiction	Non-restrictive forex regulations	Same tax treatment for bank/ non-bank factoring	Late payment penalties	Data-sharing provisions	E-invoicing infrastructure
Armenia	Yes	Yes	Yes	Yes	Yes
Egypt	Yes	Yes	Yes	No	Yes
Georgia	Yes	Yes	Yes	Yes	Yes with limitations
Greece	Yes	No	Yes	Yes	No
Kyrgyz Republic	Yes	Yes	Yes	Yes	Yes
Morocco	No	Yes	Yes	No	No
Romania	Yes	Yes	Yes	Yes	Yes with limitations
Türkiye	No	Yes	Yes	Yes	Yes
Ukraine	No	Yes	Yes	Yes	Yes with limitations
Uzbekistan	No	Yes	Yes	Yes	Yes with limitations

Source: EBRD Factoring Survey (2024).

Key: Yes No Yes with limitations

Foreign exchange plays an essential role in the development of the factoring industry. To mitigate foreign-exchange risks in international factoring, factors should be permitted to purchase cross-border receivables from domestic clients in the (usually foreign) currency of the receivable. Our survey found that four jurisdictions (Morocco, Türkiye for non-recourse factoring, Ukraine and Uzbekistan) have varying forex restrictions, often limiting acceptance of payments in foreign currency.

Financial institutions require robust information technology (IT) infrastructure to manage factoring operations efficiently. Subscribing to cloud-based IT solutions tailored to factoring often entails transferring data to the provider's jurisdiction, although in-country storage options are available at a premium. National frameworks should facilitate **cross-border data transfers** to other jurisdictions, provided they ensure adequate protection thereof. The survey reveals that 8 of the 10 jurisdictions permit such transfers to "safe" jurisdictions or with data subject consent. In Egypt and Morocco, while this is still technically possible, additional approvals must be obtained from the authorities.

> "Electronic invoicing (e-invoicing) infrastructure is vital for the growth of factoring."

Electronic invoicing (e-invoicing) infrastructure is vital for the growth of factoring. In jurisdictions where such infrastructure exists, electronic invoicing is mandated for all or most business-to-business (B2B) and/or business-to-government (B2G) commercial relationships. This prompts all suppliers to issue invoices in a defined technical standard through the e-invoicing infrastructure. Armenia, Egypt, Kyrgyz Republic and Türkiye have centralised e-invoicing frameworks mandatory for both B2G and B2B transactions, while Romania mandates it for B2G only. Georgia, Ukraine and Uzbekistan have less developed, decentralised systems, whereas Greece and Morocco lack e-invoicing infrastructure entirely.

COMBINING LEGAL REFORM WITH INVESTMENT AND PARTNERSHIP TO STRENGTHEN IMPACT

Over the last decade, the EBRD Legal Transition Programme has supported several jurisdictions in improving their legal and regulatory environments for factoring, namely: Croatia, Georgia, Jordan, Kosovo, Montenegro, North Macedonia, Serbia, Ukraine, Uzbekistan and the West Bank and Gaza.

The Bank's legal reform efforts were traditionally doubled down by investment facilities to support cross-border trade (through cash advances and guarantees). Recently, however, the EBRD launched the Supply Chain Finance Framework, which is essentially a reverse factoring facility that aims to give suppliers in the EBRD economies access to affordable working capital finance. In addition to working capital finance for SME suppliers, such financing structures incentivise the adoption of environmentally friendly operations and practices within supply chains.

The National Bank of Ukraine requested expert support from the EBRD, which has a proven track record in supporting factoring frameworks in the EBRD regions, to align the legislative framework pertaining to factoring with international standards and best practices, including the new UNIDROIT Model Law on Factoring.

Box 1. **Using the legal framework to level up the factoring market in Ukraine**

In Ukraine, the legislative hurdles and court practice that have developed as a result of the existing legislation are seen as the main challenges to the healthy development of the factoring market. For instance, there is a widespread issue of a lack of a clear differentiation between trade factoring and purchase of consumer non-performing loans under the factoring licence due to the loose definition of factoring, and there is no uniform method of achieving third-party effectiveness/perfection (by registration). The secured transactions framework only provides for priority rules that apply to assignees with security rights in receivables registered in accordance with the Movable Pledge Law, not those purchased outright.

The National Bank of Ukraine requested expert support from the EBRD, which has a proven track record in supporting factoring frameworks in the EBRD regions, to align the legislative framework pertaining to factoring with international standards and best practices, including the new UNIDROIT Model Law on Factoring.

We are now finalising the draft law on factoring with international experts and the EBRD team. I am sure that factoring can be one of the main tools to support the development of small and medium-sized enterprises (SMEs), which, following the example of developed countries, should become a cornerstone of the economy and will contribute greatly to post-war recovery.

Serhiy Savchuk,
Director of the Department of Methodology for Regulating the Activities of Non-bank Financial Institutions, National Bank of Ukraine

The EBRD also leverages external partnerships to amplify the messages and lessons learned from experience. One such example is the Bank's long-standing partnership with Factors Chain International (FCI), the largest factoring association in the world.

Box 2. **Greening the supply chains through reverse factoring**

The EBRD launched a €150 million Supply Chain Finance Framework in 2022. Under this framework, the Bank participates in buyer-led supply-chain financing (SCF) programmes in its economies. The framework's primary aim is to allow suppliers in these economies to access affordable working capital.

The EBRD is partnering with reputable international banks that have an established supply-chain financing business. It participates in such international banks' SCF programmes either by funding the purchase of receivables or by providing a guarantee covering the payment obligations of the receivables' debtors.

But the Bank is also working with local banks that have experience with the SCF product to scale up their offering. Ultimately, the EBRD wishes to bring local banks into the SCF market. As highlighted above, this may require the legal framework to be improved in some countries.

The EBRD is engaging with large corporate buyers with a strong credit profile and which have an extensive supplier base. Such buyers value the SCF product, as it strengthens the resilience of their supply chains.

Furthermore, the Bank can help buyers enhance their procurement policies and tools, especially with respect to environmental, social and governance (ESG). Indeed, given regulatory pressure in this area, it has become crucial for buyers to assess and monitor ESG and human rights risks in their supply chains. Buyers also need to be able to understand and measure Scope 3 greenhouse gas emissions in their downstream activities to meet their own greenhouse gas reduction targets. Inclusion and diversity within the supply chain are also a focus of the EBRD's engagement.

In addition to providing suppliers with working capital on better terms, the EBRD can mobilise donor funds that can be used to assist suppliers in tackling ESG gaps in their business. The Bank can offer financial incentives for reaching certain pre-agreed ESG targets or can fund advisory services.

In many EBRD economies, receivable financing levels are well below those in developed countries. The development of the SCF product combined with a sustainability aspect is a good tool to help those countries achieve growth and transition to a green economy.

Markus Renfert, Senior Counsel, EBRD

Box 3. **Partnering for larger impact: the EBRD Legal Transition Programme and Factors Chain International**

Over its 56 years, FCI has been a leader in the establishment, development and growth of factoring in markets around the world. During those six decades, FCI's membership has grown from just three countries to more than 90.

FCI always partners with institutions to boost its voice and impact on a given market. The successful collaboration between FCI and the EBRD is significant in supporting the factoring industry within the EBRD regions, strengthening the factoring and SCF sector and fostering economic development and financial inclusion.

A robust legal and regulatory framework is the bedrock of factoring, providing the necessary structure and guidelines for the sector's operation. This framework is a shield that safeguards the rights and interests of all stakeholders, including factoring companies, clients and debtors. Establishing clear rules and standards enhances transparency, promotes trust and mitigates risk in factoring transactions. This underscores the importance of the partnership's focus on legal transition and regulatory compliance.

Through workshops, training programmes and knowledge-sharing initiatives, FCI and the EBRD facilitate the exchange of expertise between legal professionals and practitioners in the factoring sector. By combining the EBRD's expertise in legal transition with FCI's practical knowledge of the required legal and regulatory framework, the partnership provides regulators, central banks and financial institutions with the tools required to turn the framework into a cohesive financial infrastructure. FCI and the EBRD provide access to vital financial resources and opportunities, especially for SMEs. Thus, their joint efforts strengthen the factoring sector and play a crucial role in advancing broader worldwide goals for socioeconomic development.

Neal Harm, Secretary General, FCI

CONCLUSIONS

The EBRD uses the information in its factoring survey primarily to understand the depth of reform required in each surveyed jurisdiction. As such, the surveys have traditionally formed a good basis for dialogue with regulatory authorities about the need for reform. As one of the only publicly available tools of this kind, the factoring survey has been used as a point of reference by other actors operating in this field.

Within the EBRD, the factoring survey is used to understand potential pitfalls in the legal frameworks as the Bank delivers on its promise to expand financing facilities in as many of the EBRD regions as possible. The survey draws heavily on the provisions and principles introduced in the main international standard for factoring legislation, particularly the UNIDROIT Model Law on Factoring, adopted in 2023.[3] As an institutional observer in the Working Group that led the drafting of the UNIDROIT Model Law on Factoring, the EBRD uses the Model Law as a benchmark in its legal reform work. The survey is a fluid document, which the Bank aims to update and revise as the jurisdictions covered therein introduce any relevant changes. Additional jurisdictions may also be added in the future.

As one of the only publicly available tools of this kind, the factoring survey has been used as a point of reference by other actors operating in this field.

3 See UNIDROIT (2023).

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GLOSSARY

AI	artificial intelligence
ADR	alternative dispute resolution
CGI	Climate Governance Initiative
CCG	corporate climate governance
CCGAP	corporate climate governance action plans
EBRD	European Bank for Reconstruction and Development
ESG	environmental, social and governance
EU	European Union
GHG	greenhouse gas
IPCC	Intergovernmental Panel on Climate Change
ISSB	International Sustainability Standards Board
IT	information technology
IMF	International Monetary Fund
LTP	Legal Transition Programme
MDB	multilateral development bank
NDC	nationally determined contribution
OECD	Organisation for Economic Co-operation and Development
OLL	outcome-linked loan
SDG	Sustainable Development Goal
SME	small and medium-sized enterprise
SOE	state-owned enterprise
TCFD	Task Force on Climate-Related Financial Disclosures
UNCITRAL	United Nations Commission on International Trade Law
UNFCCC	United Nations Framework Convention on Climate Change
UNECE	United Nations Economic Commission for Europe
UNIDROIT	International Institute for the Unification of Private Law

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