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### RESEARCH ARTICLE

#### BUSINESS INSPECTION REFORMS IN UZBEKISTAN.

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#### Abstract

This paper describes recent legislative reforms of business inspection in Uzbekistan. Taking into consideration international organization recommendations, it will be evaluated these recommendations in order to make inspection system simple and effective.

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Since gaining of independence Uzbekistan has introduced prudent political, economic and social reforms. In this term there was taken a number of steps in order to reform and modernize its national economy. As a mean to transition from a centrally planned economy to the market economy, it carries out slowly and gradually as it was emphasized by the President of the Republic "Do not destroy old homes before you have built new ones".

In this transition term, government inspection plays an important role to maintain business entity. It is possible that business inspection are found in almost all countries. It can be used for a variety of forms (including similar words like "audit", "checks", "visit"). Inspection is usually used for state regulatory system as a key enforcement mechanism. Demand for inspection reforms has triggered a few factors. The aspect of business inspection, the negative impact of extreme or arbitrary inspection leads to rising costs, demoralizing new business entity and investment, diminishing competitiveness.

Inspector performance has come under increasing scrutiny as the high costs of poor inspection practices for economic performance. To reach this aim it is important to establish a good inspection system. The good inspection system should include:

- *The Maximizing of compliance with clear and legitimate government regulations by detecting and deterring non-compliance consistently and fairly;*
- *The Minimizing uncertainty and regulatory risks for businesses by operating transparently and under the rule of law;*
- *The Fights of corruption by reducing the opportunity for abuse of discretionary powers*
- *The Minimizing of costs to businesses and optimizes costs to governments by using resources efficiently to target the highest risks.*

The establishing of good inspection needs the strengthening of the rule of law at the national governing structure. "The rule of law" reforms should include a number of elements, it specifically creates a reliable legal system. The establishing of effective institution under legal system provides fair market competition, regard property rights,

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equal rights for market entrants. At the same time these elements of a legal system, neutral, transparent, efficient and accountable.

Excessive frequent inspections charges direct costs on the private sectors as well as they can have negative impact on competition climate for investors. Nowadays, most countries suffer from a lack of clear inspection regulation which sets rules for selection of certain business to be focused on inspection. Under this circumstances, business entities often complain about facultative or abuse power of inspection.

Corruption and the lack of transparency are also another problem for inspection system. Corruption has been defined in a variety of ways. According to the World Bank definition, *corruption is the abuse of public power for private benefit*. International experience shows that it is impossible to prevent or control corruption by a single institution. Taken as an example, law or police alone is unable to combat with the whole economic crimes. Furthermore, the existence of limited resources in developing economies makes it impossible to cope corruption. Therefore, the best way to tackle corruption is through a sector by sector control and analyses<sup>1</sup>. Corruption sabotages the reputation of inspections among the business community and society. In this circumstances, inspectors can be seen as enemy to hide real situation instead of proving public safety.

Most countries have adopted many laws related to inspection without taking consideration the existence of laws. The main reason for this is that most adopted new laws already had covered part of the same issue or provision. This is nearly the same pattern in every country except for countries where have “*better regulation*” framework. These countries review the existence legislation before adopting new laws otherwise the power of executive body is restricted.

### Steps taken by Uzbekistan to this effect:-

Today's one of the most important problems in the implementation of free market is to modernize the economy, liberalization of entrepreneurship activity and measures to improve the welfare of society through methods of social protection to increase the incomes of population. This will serve the realization of rights as it is mentioned in the Constitution of Uzbekistan “*Man, his life, freedom, honor, dignity and other inalienable rights are the highest value*”. At the speech at the joint session of the Senate and the Legislative Chamber of the Oliy Majlis, the President of the Republic of Uzbekistan Islam Karimov emphasized “*it shows that there is serious necessity for economic liberation to improve the objective analysis, the logical consistency and to assess their compliance with the norms of the modern market economy, strengthening the management of the system. First and foremost, to strengthen the protection of private property rights, there must be created a system of reliable guarantees for lawfully private property owners whether acquired or created*”.

In order to establish a good inspection system, Uzbekistan makes a great effort to improve business framework. In this term the following measures have been taken:

- Inspectors' power is restricted and their ability to illicitly interference in the operation of business has been significantly decreased.
- The number of inspections has been reduced, oversight duplication has been removed. The forms and methods of inspections have been improved
- Criteria based on risk analyses has been introduced into the process of selecting business for inspections
- Uzbek law defines the scope of inspection as specifically as possible. According to the definition of inspection is *one time control carried out by controlling bodies over the economic entities' compliance with the laws and other legislative acts regulating their activity*. Generally, inspection enforce by controlling bodies. Controlling body should be the ministries and departments authorized by the legislation to carry out state control over the activity of business entities (for example, tax authorities).

Establishing legal framework related to inspection is a key tool to protect business entity's right. Without effective framework, violation of business entity's rights is easily possible. Generally, most businesses don't dare to ask grounds of inspection as they have vague who is responsible for inspection, what are the right of their business in the process and what documents they are entitled to demand<sup>2</sup>. In this case, one of the most important strategies for the

<sup>1</sup>Salifu, A. (2008). Can Corruption and Economic Crime be Controlled in Developing Economies – and if so is the cost worth it?. *Journal of Money Laundering Control*, 11(3), pp.274-276.

<sup>2</sup>Blanc, F, pp.21.

protection of the business entity's rights is to prevent illegal activities from interfere in the investigation, to protect the rights of minority business enterprises and to provide financial support for their effective function. As noted above the main purpose of adopted laws throughout the last twenty years, Presidential resolution and decrees, Resolution of Cabinet of Ministers, support the business activities and create favorable conditions for them.

If abuse of business rights exists, it will turned to privileges and then it is possible to deny without any reason to obtain bribes or to suspend certain group of business<sup>3</sup>. Uzbek's law is banned to investigate different activities or unjustified interference in business entities. Particularly, the investigation bodies are prohibited by the regulation to assign arbitrary inspections or to take the initiative without sufficient reasons. In accordance with applicable regulation, only state tax authorities can investigate the activity of business entity. But they have to carry out investigations on the basis of the decision of the regional department of the Coordination Council.

Since July 1, 2015 it has been introduced legal measures, termination of activities of business entities, suspension of activities, suspension of operations with bank account, the application of financial sanctions, subjects of violations of the state's income, dealing with certain types of business activity licenses (permits) for a period of more than ten working days to cancel the suspension or termination, extra taxes and fees for lately payments only through a court order<sup>4</sup>.

Pursuant to the Presidential Decree of Uzbekistan "*On Measures of Further Improvement of the System of Legal Protection of Business Entities*", activities of business entities are only checked by state tax authorities<sup>5</sup>, if they detect an indication of tax and currency crime cases it would be carried out by the Department for Combat against Tax and Currency-related Crimes (the General Prosecutor's Office of the Republic of Uzbekistan). Officials and heads of regulatory bodies are responsible for their unlawful inspection and even they would be chargeable with crime. In this regard, it is only allowed to investigate the relationship of other business entities with the decision of a criminal investigation or the decision of special authorized body. It is prohibited to demand unrelated financial, accounting and other documents from business entity during the inspection.

This regulation also established that damage of business entity from unlawful decisions of the state bodies or these officials' illegal actions (inaction) is fully covered by these government agencies on the basis of the decision of the court. First and foremost, it should not be compensated from the budget funds.

According to the Presidential Resolution of the Republic of Uzbekistan "*About enhancement of reporting system represented by subjects of entrepreneurship, and strengthening of responsibility for its illegal claim*"<sup>6</sup>, state bodies, local authorities and other organizations are strongly cautioned to be charged for the violation of this paragraph of the resolution that demands any information, additional financial and statistical reports ( the state statistics bodies and agencies of the State Tax Service), other information and documents (the manner prescribed by law, except for the requirements during the investigation), getting any information with unlawful way by other state bodies, local authorities and other organizations including established procedure with unacceptable way of demanding report, data and information.

The Presidential Decree of the Republic of Uzbekistan, "*Private property, small business and private entrepreneurship, provide reliable protection measures to remove barriers to the rapid development*"<sup>7</sup> in accordance with the activities of economic entities in connection with criminal cases involving law enforcement agencies is

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<sup>3</sup>Channel, W.(2012). Business Environment Reforms in Conflict –affected Contexts, Strengthening The Economic Dimensions of Peacebuilding, International Alert, pp.3. Web: [http://www.enterprise-development.org/wp-content/uploads/IntlAlert\\_PracticeNote\\_BER\\_March2010.pdf](http://www.enterprise-development.org/wp-content/uploads/IntlAlert_PracticeNote_BER_March2010.pdf), (accessed 02.06.2016)

<sup>4</sup>The Presidential Decree of the Republic of Uzbekistan No.UP-3619 "On Measures of Further Improvement of the System of Legal Protection of Business Entities" dated 14 June 2005.

<sup>5</sup>See Uzbek Tax Reforms, Tadjibaeva, D, Komilova, I.(2009). The Influence of Tax Reforms on the Prosperity of Micro-Firms and Small Businesses in Uzbekistan, Asia-Pacific Development Journal, 16(2).

<sup>6</sup>The Resolution of the President of the Republic of Uzbekistan from June 15\ 2005. No. PP-100 "About enhancement of reporting system represented by subjects of entrepreneurship, and strengthening of responsibility for its illegal claim".

<sup>7</sup>The Decree of the President of the Republic of Uzbekistan dated 15 May, 2015 "Private property, small business and private entrepreneurship, provide reliable protection measures to remove barriers to the rapid development".

carried out in the participation of lawyers (with the exception of the provisions of this law may be rejected by the economic entities).

The frequency of inspection in countries may lead to a widespread of corruption and harassment. In this case, it can be beneficial to limit the frequency of inspection by law. A good way of restricting this is to design an overall limit of each type of inspection for a given business. But it could be acceptable to permit frequent inspection for high risk business<sup>8</sup>.

Uzbekistan has taken important steps to restrict the frequency of inspection. It is divided into three groups by law<sup>9</sup>. In according with Article 39, first group, scheduled inspections of business entities can be performed by controlling bodies not more than once a year by the decision of a specially authorized body on coordination with the activity of controlling bodies. The second group, inspection of business entities and private enterprises not more than once in two years. The third group, scheduled inspections of financial-economic activity of micro-firms, small enterprises and farm enterprises shall be performed not more than once in four years, for other business entities - not more than once in three years. The fourth group, financial-economic activity of newly established micro firms, small enterprises and farm enterprises is immune from scheduled inspections during the first two years from the moment of their state registration.

There is only one exception to restrict the frequency of inspection if the prosecutor's office, police and the National Security Service open criminal case. The reason for an opened criminal case should be performance of inspection of business entities and this criminal case merely covers the business entity's relevant to the inspection.

The duration of inspection is also crucial to be defined in laws. The reason for this provision prevents from illegal visit of inspectors who are looking for "*illicit income maximization*". For instance, inspectors visit as many business as possible in looking for unofficial payments<sup>10</sup>. Inspection of reform laws in different countries has adopted several provisions. For example, in Poland, SMEs (small and medium enterprises) can be inspected up to four weeks in a year, except in criminal cases. In Ukraine, planned inspection can be a maximum of 15 working days for large business and two working days for SMEs<sup>11</sup>. In Uzbekistan, duration of inspection may not exceed 30 calendar days. In the exceptional circumstances it can be extended by the decision of the specially authorized body. Compared to other countries, provision of inspection period in Uzbek's law can be criticized. But there is no universal rule concerned to the duration of inspection. This limit is connected with the level of development of country. Generally, in developed countries, larger and more complex firms are subject to be inspected<sup>12</sup>.

Launching of complaint mechanism plays an important role to protect business entity' rights. National phone line should take complain from citizens or businesses. Complainant identity should be anonymous<sup>13</sup>. In Uzbekistan, such kind of communication is established under the minister of justice special telephone which called "trust line". This is good way to protect business entity from illegal inspection and interference of controlling body.

### **Comparing recommendation with Results:-**

As it is mentioned above there is a number of new laws and legislative changes to foster favorable condition for business entities. In this sense, it is really appreciated the decrease and the simplification of diverse bureaucratic and administrative procedure for business entities. Furthermore, these changes make business inspection system more simple and transparent than before.

In spite of improvement of inspection system in business field, there are still gaps in the business legislation to protect business entity adequately. At this point it is crucial to take consider and evaluate international organization recommendations and reports to fill these gaps.

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<sup>8</sup>ICAS, pp.37.

<sup>9</sup>Article39 of the Law of the Republic of Uzbekistan "On guarantees of freedom of entrepreneurial activity.

<sup>10</sup>Blanc, F, pp.37, IFC, pp.38.

<sup>11</sup>IFC, pp.38.

<sup>12</sup>IFC.(2008). pp.41

<sup>13</sup>Good Practices for Business Inspection: Guidelines and Reforms. World Bank Group, Small and Medium Enterprise Department, pp.16.

International organization recommendations and reports are based on evaluation of developing countries' practices. In this case, their guidance sheds on future inspection reforms. As an example, the primary field for future reforms decreases the power of the inspector setting financial penalty by establishing checks and stabilizing higher up in the hierarchy.

Today's business should be protected from unrelated records to a given inspection. Currently, it is hard to define provided what kind of documents should be involved in the case of inspection or not. Under this circumstance, inspectors often require documents against the intention of investigation. If it is taken account of the specific sides of each inspection, it is difficult to define along lists of documents. For that reason it is still waiting to solve problems in legislation.

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