

2007 2012 2011  
 2005 2009 2004  
 2008 2006 2010 2013

## Colombia: sustaining reforms over time

- Colombia's experience shows the importance of sustaining reform efforts over time and adjusting them to the changing needs of the economy, whether at the national or local level.
- Colombia is a regional leader in narrowing the gap with the world's most efficient regulatory practice.
- Over time, the focus of Colombia's reform efforts has shifted from reducing the cost and complexity of business regulation to strengthening legal institutions.
- Colombia's most notable regulatory improvements have been in the areas of starting a business, paying taxes, protecting investors and resolving insolvency.
- While development hurdles remain, Colombia's regulatory reforms have increased its competitiveness and have had local and regional "spillover" effects.

Over the past several decades Colombia has pursued a broad range of structural and institutional reforms. The emphasis has shifted over the years, reflecting the priorities of different administrations and the perceived needs of the economy. In the 1980s and early 1990s much of the focus was on macroeconomic management.<sup>1</sup> As progress was made in laying a firm foundation of macroeconomic stability, the focus shifted to other areas. The government gave particular emphasis to policies and institutions seen as central to enhancing productivity and growth and boosting the country's competitiveness. As part of this, it set in motion reforms aimed at improving the regulatory framework and the rules underpinning private sector activity. The Ministry of Commerce, Industry and Tourism led a coordinated reform effort bringing together government agencies, the Congress and the judiciary as well as the private sector.

In 2007 Colombia's government further institutionalized its commitment to regulatory reform by establishing the Private Council for Competitiveness. A public-private partnership, the council is made up of business associations and private sector players working closely with the government to promote sound, business-friendly regulatory practices.<sup>2</sup>

Recent administrations have continued to use national development plans to establish a clear economic agenda. In 2009 President Alvaro Uribe highlighted Colombia's progress and his government's plans for new regulatory reforms aimed at further gains in competitiveness.<sup>3</sup> And since the change of legislature

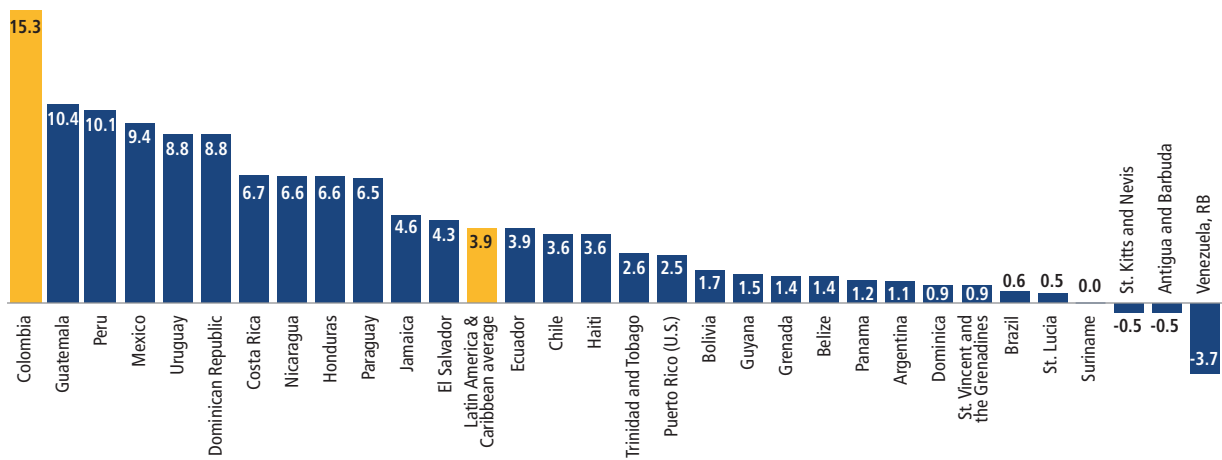
in August 2010, the new government, led by President Juan Manuel Santos, has been pushing forward an economic reform agenda through the "Prosperity for All" national development plan for 2010-14. The plan's overall goals are to reduce poverty, increase income, generate employment, improve security, ensure the sustainable use of natural resources and improve the quality of the business environment.<sup>4</sup>

### SUSTAINED EFFORT AT THE NATIONAL LEVEL

As Colombia has improved its business regulatory environment, results have shown in *Doing Business* indicators—including those on starting a business, paying taxes, protecting investors and resolving insolvency. Indeed, thanks to its sustained efforts, Colombia has made greater progress toward the frontier in regulatory practice since 2005 than any other Latin American economy (figure 3.1).

Other indicators also reflect the improvements. The total number of newly registered businesses in the country rose from 33,752 in 2006 to 57,768 in 2011.<sup>5</sup> Colombia's performance on several relevant measures compiled by the Worldwide Governance Indicators project improved between 2002 and 2010—including the Rule of Law Index (reflecting perceptions of the extent to which firms have confidence in and abide by the rules of society) and the Regulatory Quality Index (capturing perceptions of the government's ability to formulate and implement sound policies and regulations that permit and promote private sector development).<sup>6</sup>

**FIGURE 3.1** Colombia has outpaced the region in advancing toward the frontier in regulatory practice  
Progress in narrowing distance to frontier since 2005 (percentage points)



Note: The distance to frontier measure shows how far on average an economy is from the best performance achieved by any economy on each *Doing Business* indicator since 2005. The measure is normalized to range between 0 and 100, with 100 representing the best performance (the frontier). The figure shows the absolute difference for each economy between its distance to frontier in 2005 and that in 2012. No data are shown for The Bahamas and Barbados, which were added to the *Doing Business* sample after 2005.  
Source: *Doing Business* database.

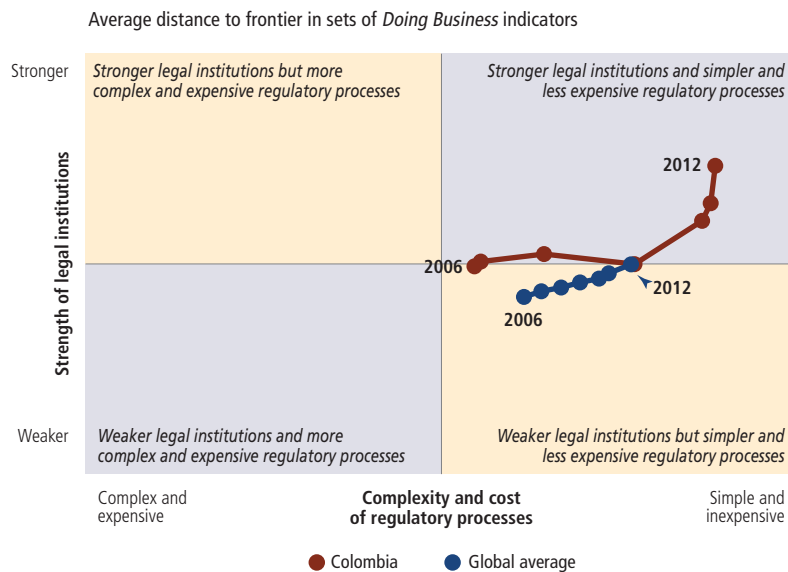
And Colombia's ranking on the ease of doing business rose from 79 among the 175 economies included in 2006 to 45 among the 185 included in 2012.

### Choosing a reform path

While Colombia simultaneously pursued very different types of regulatory

reforms, it first completed those aimed at streamlining business regulation and reducing its cost to companies. Until 2008 the focus was largely on reducing transactions costs, such as by simplifying business start-up procedures or tax administration. These types of reforms have continued since 2008, but the focus has shifted toward strengthening legal institutions such as bankruptcy systems and investor protections (figure 3.2).

**FIGURE 3.2** A trend toward stronger legal institutions and less expensive regulatory processes in Colombia



Note: *Strength of legal institutions* refers to the average distance to frontier in getting credit, protecting investors, enforcing contracts and resolving insolvency. *Complexity and cost of regulatory processes* refers to the average distance to frontier in starting a business, dealing with construction permits, registering property, paying taxes and trading across borders. The distance to frontier measure shows how far on average an economy is from the best performance achieved by any economy on each *Doing Business* indicator since 2005.  
Source: *Doing Business* database.

This sequencing of reforms is not unusual. Many economies have focused first on simplifying regulatory transactions for businesses, then moved on to more complex and time-consuming reforms aimed at improving legal institutions such as court systems. Such reforms require more sustained efforts, often over a period of several years.

### Encouraging business start-ups

Regulatory reforms implemented by Colombia in recent years have made a clear difference in the ease of starting a business as measured by *Doing Business*. They have reduced the time required to start a business from 60 days to 14, the cost from 28% of income per capita to

8% and the number of procedures from 19 to 9 in 2011 (figure 3.3).

The introduction and subsequent upgrades of one-stop shops for business registration at chambers of commerce account for much of the change. The first one-stop shops started to operate in May 2003. As the changes in the start-up process yielded positive results, the government continued to improve it. In 2005, for example, Law 962—the “*antitrámites*” (“antipaperwork”) law—eliminated around 80 bureaucratic processes required to start a business and introduced a provision preventing government agencies from creating new procedures. It also simplified the procedures required by allowing electronic submission of documents and eliminating the need to have signatures notarized.

More improvements came in 2010. A new public-private health provider, Nueva EPS, replaced the previous provider administered by the Social Security Institute. The new system enables employers and employees to register for health services in just 1 week. In addition, Colombia introduced online preenrollment for new companies, making registration faster and simpler.

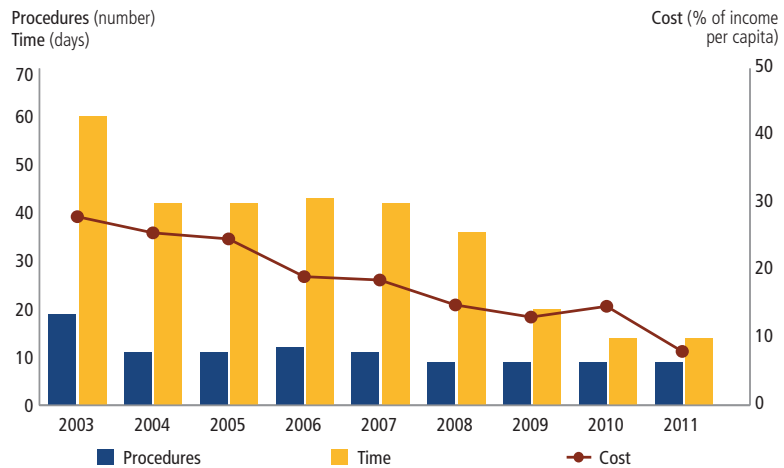
New regulations recently introduced a progressive fee schedule for new companies.<sup>7</sup> The fee schedule exempts new firms from up-front payment of regulatory fees during their first few years of operation. And the start-up fee associated with the commercial license is no longer required.

### Simplifying tax compliance

Over the years Colombia has greatly improved its tax and social security compliance processes. In 2002, as the government realized that about a third of its potential revenue from corporate income, personal income and value added taxes went uncollected, it decided to introduce an electronic payment system in an attempt to lower tax evasion.<sup>8</sup>

In 2009 the government lowered corporate income tax rates and introduced an online form for social contribution

FIGURE 3.3 Starting a business is now faster and less costly in Colombia



Source: Doing Business database.

payments. This form simplified tax compliance for Colombian businesses by combining into a single online payment all contributions for social security, the welfare security system and labor risk insurance.

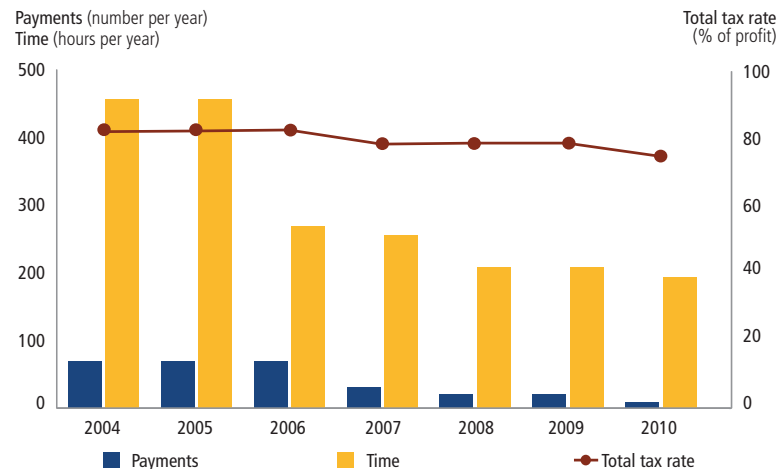
To further improve and simplify tax compliance, in 2010 the government made electronic filing of corporate income tax and value added tax mandatory for firms with annual sales exceeding 500 million Colombian pesos (about \$280,000) in or after 2008.

Thanks to these continued efforts, paying taxes as measured by *Doing Business* became considerably easier between 2004 and 2010. The number of payments fell from 69 a year to 9, and the time needed to prepare and file taxes from 456 hours a year to 193. And the total tax rate declined from 82.1% of profit to 74.8% in this period (figure 3.4).

### Enhancing investor protections

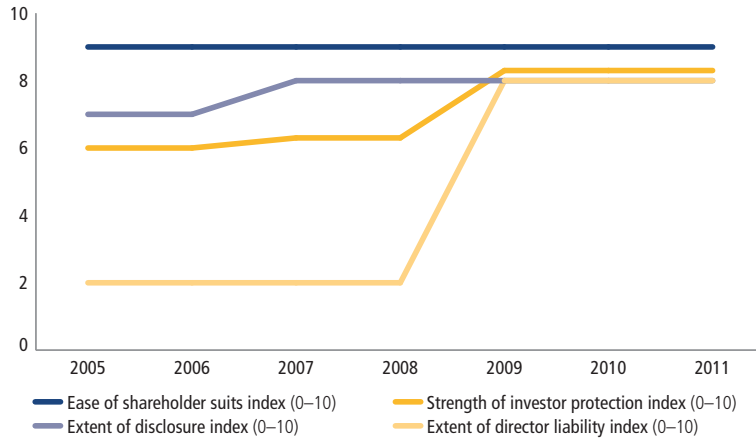
Starting in 2005, Colombia implemented 3 major legal reforms aimed at strengthening investor protections. In 2005 Colombia enacted Law 964, providing

FIGURE 3.4 Colombia has made tax compliance simpler for businesses



Source: Doing Business database.

FIGURE 3.5 Legal and regulatory changes have strengthened investor protections in Colombia



Source: Doing Business database.

a modern framework for capital market activity. The law encourages better corporate governance practices by requiring greater transparency and disclosure, equitable treatment of minority shareholders and more effective boards of directors.

In 2007 the government amended Colombia's securities regulation. Decree 3139 requires listed companies to report more information to investors. Before, listed companies had to report any "relevant" or "extraordinary" event—a subjective standard open to abuse. Although the decree still includes the broad "relevant" requirement, it lists specific events that must be disclosed to the financial authorities. It also requires companies to report extensive information before going public.

In 2010 the government made further progress by amending the company law. The amendments clarified the liability regime for company directors involved in related-party transactions that harm the company. Now directors can be forced to pay damages and disgorge profits made from such transactions.

As a result of these changes, Colombia's scores have improved on both the extent of director liability index (which measures the liability of company executives for abusive related-party transactions) and the extent of disclosure index (which

measures the approval and disclosure regime for related-party transactions; figure 3.5).

### Making insolvency proceedings more efficient

Colombia's insolvency reforms began almost 2 decades ago. In 1995 the enactment of Law 222, allowing debtors and creditors to resolve disputes before the Superintendence of Companies, helped ease the burden on the judiciary. In 1999 changes to the reorganization law improved the existing corporate reorganization proceedings and introduced new time limits for negotiations. These changes increased the efficiency of the bankruptcy system and improved its capacity to distinguish between viable and nonviable businesses.<sup>9</sup>

Another series of insolvency reforms took place in the past 6 years. Thanks to these reforms, creditors' recovery rate rose from 56 cents on the dollar to 76 and the time to complete a liquidation proceeding fell from 3 years to 1.3.

The reforms began with a comprehensive revision of the insolvency proceedings available. In 2007 authorities introduced 2 new proceedings: a reorganization procedure to restructure insolvent companies and a mandatory liquidation procedure. And a new insolvency law

imposed more stringent time limits for negotiating reorganization agreements.

In 2009 the government issued several decrees as part of continued efforts to better regulate the profession of insolvency administrators. In addition, it introduced an electronic filing system to make insolvency proceedings faster and more efficient. And it eliminated the requirement to submit financial statements to request reorganization in cases where these statements had previously been submitted to the Superintendence of Companies.

### Improving other areas of regulation

Colombia has also made improvements in other areas of regulation. In 1995 the country undertook a complete overhaul of its construction approvals. It moved the administration of building permits out of the state-run planning office into the private domain, becoming the first economy in Latin America to privatize the review process. This move carried risks, but public and private stakeholders in the country were calling for comprehensive change.

Bogotá's mayor first appointed 5 ad hoc "urban curators," all architects or engineers with construction experience, to review building permit applications. Soon after, a more transparent, merit-based hiring system was established that is still in place. Potential curators now undergo a selection process that includes exams and interviews with public and private sector experts. Privatizing the issuance of building permits improved timeliness and freed up the planning office's resources.

In other regulatory areas, introducing electronic systems made processes easier. When registering property, a business can now obtain online certification of valuation, ownership and good standing for property taxes. And for properties with no liens, it can submit online certificates directly to the land registry. Certificates have no cost if requested online.

An electronic data interchange system was introduced for exports, making it possible to centralize electronic data. The new system also allows traders to pay duties electronically, eliminating the need to go to a bank to submit payments. And it allows shippers to share information with customs electronically, so that customs declarations can be processed before the vessel even arrives at the port. Most importantly, since 2008 Colombia has implemented improvements to the Single Window for Foreign Trade (VUCE) system. The system now connects over a dozen government agencies that are involved in import and export procedures.

### **SPILLOVER TO THE LOCAL LEVEL**

Colombia has been actively reforming its regulatory environment at the local as well as the national level. Local efforts have been inspired in part by a subnational study. Carried out through the National Department of Planning, the 2008 study was designed to analyze the regulatory environment in different regions with the aim of improving regional competitiveness across the country. The study was also intended to enable Colombian cities to learn from one another and adopt good practices from elsewhere in the country.

The subnational *Doing Business* report resulting from the study was soon followed by another, and work on a third began in 2012.<sup>10</sup> The second report showed that all 12 cities included in the first one had improved on at least one *Doing Business* indicator.

Among these 12 cities, Neiva made the most progress in improving the ease of doing business. Local authorities took several measures to increase the city's competitiveness, including creating an anti-red-tape committee to reduce the regulatory burden on the private sector. The committee encompassed wide representation, with participants from the municipality, the chamber of commerce, business associations and national agencies such as police and tax authorities.

Neiva's local government also set up one-stop shops for registering new companies. This eliminated 11 procedures and reduced the time required to register a business from 32 days to 8. The success of the one-stop shops has been due largely to cooperation between municipal and national government departments.

Medellín is another city that substantially improved its business regulatory environment. The city government cut 3 procedures required to start a business by improving one-stop shops and eliminating the requirement for a land use certificate. And it made registering property easier by merging 2 certificates and eliminating a stamp previously required as proof of registration tax compliance.

### **CONCLUSION**

Colombia's commitment to regulatory reform has led to substantial improvements in the quality of the business environment and a more solid foundation for private sector development. Its experience shows the importance of sustaining reform efforts over time and adjusting them to the changing needs of the economy. Initially, most of the regulatory reforms took place at the national level. But as the business environment continued to improve, the reforms spilled over to the local level.

Colombia's experience is having "spillover" effects in the region as well. Bolivia has shown an interest in learning more about Colombia's experience with business entry. Paraguay has sought to learn from Colombia's innovations in construction permitting. And both Costa Rica and El Salvador intend to learn from Colombia's trade logistics reforms.

Colombia's experience also shows the importance of setting out economic policy objectives. The government's commitment to well-defined, long-term economic goals has helped drive implementation of the reforms. Having made major strides in safeguarding macroeconomic stability, the government widened the focus of its policies to include a range of institutional and economic reforms aimed

at boosting productivity. The steady pace of change led to the development of the broader competitiveness agenda and the creation of a public-private partnership aimed at promoting business-friendly regulatory practices.

Yet despite the government's sustained efforts, and its success in improving the business climate and implementing an ambitious competitiveness agenda, a number of challenges remain. Addressing income inequality remains a key priority, in part because it would strengthen support in the business community and in civil society for the government's overall development strategies.

While the country has more development hurdles to overcome, the measures taken over the past years have greatly improved its competitiveness. The regulatory reforms may take more time to show full results in all areas of doing business, but they have already led to substantial immediate benefits. Colombia's reform agenda is expected to continue to expand—and to inspire further improvements in the region.

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### **NOTES**

This case study was written by Valentina Saltane and Hayane Chang Dahmen.

1. According to the International Monetary Fund, average annual inflation in Colombia fell from 23% in the 1980s to 6% by the 2000s. Management of public finances also improved, with public deficits in recent years lower as a percentage of GDP. Colombia's general government public debt was 35.9% of GDP in 2009, low by international standards ("IMF Data Mapper," <http://www.imf.org/>).
2. Consejo Privado de Competitividad, <http://www.compite.com.co/site/sistema-nacional-de-competitividad/>.
3. Remarks delivered before the Americas Society/Council of the Americas, September 24, 2009. Available at <http://www.as-coa.org/article.php?id=1908>.
4. International Fund for Agricultural Development, "Rural Poverty Portal," <http://www.ruralpovertyportal.org/>.
5. *Doing Business* database; World Bank

Group Entrepreneurship Snapshots database.

6. World Bank, Worldwide Governance Indicators, "2011 Update," <http://www.govindicators.org>. The Rule of Law Index and the Regulatory Quality Index both range from -2.5 (weak) to 2.5 (strong). On the Rule of Law Index Colombia's score rose from -0.84 in 2002 to -0.33 in 2010. On the Regulatory Quality Index its score rose from 0.05 in 2002 to 0.31 in 2010.
7. Law 1429 of 2010 and Decree 545 of 2011.
8. Sohn 2008.
9. Giné and Love 2010.
10. Subnational *Doing Business* reports are available at <http://www.doingbusiness.org/reports/subnational-reports>.