



# Making Slovakia a Better Business Place

## SME SURVEY

## CONFERENCE

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## EXECUTIVE SUMMARY

### INTRODUCTION

One of the major goals of the American Chamber of Commerce in Slovakia (AmCham) is to improve the business environment in Slovakia for everyone – be it local companies, foreign investors and large or small businesses. The most recent report by the Global Economic Forum has revealed that Slovakia's competitiveness is on the decline, despite being considered until very recently as a country attractive for doing business. Today, Slovakia can no longer draw on its reputation as a central European tiger with an ideal geographical position in the heart of Europe, cheap labor and interesting investment incentives. The global economic crisis has substantially increased the demands of entrepreneurs and ordinary citizens. Competition among the respective economies is increasing; this requires much more responsibility

as well as creativity from governments as they can no longer rely merely on natural advantages. In 2009, AmCham conducted an extensive survey among foreign investors which identified the major issues and challenges Slovakia is facing as a competitive economy.

Considering the fact that smaller companies account for the majority of its member base, AmCham Slovakia is currently focusing special attention on the needs of small- and medium-sized enterprises (SMEs). Despite receiving much less media coverage in comparison to major foreign investors or large domestic employers, SMEs are an extremely important component of the whole economy. While SMEs contribute up to 60% of total European GDP, as many as 99% of companies are actually classified in this category within the EU. Their opinion

can therefore, no doubt, be considered as relevant. As a major initiative, AmCham Slovakia conducted a survey of SMEs' needs in Slovakia. The main objective was to specify what the new Slovak government could – and should – provide to smaller companies to make the Slovak business environment more SME-friendly. The survey ran from August through November, 2010, in several stages. The online survey conducted from September 8 to November 5 was supplemented by in-depth interviews and a focus group with chosen representatives of SMEs. Altogether 115 companies took part in the AmCham SME Survey. Their opinions and recommendations are outlined in the following three chapters: 1. Legislation and the Judicial System; 2. Administrative Burden and Corruption; 3. Financial Aspects and Employment.

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## I. LEGISLATION AND THE JUDICIAL SYSTEM

According to the survey findings, the area of legislation and jurisdiction represents the biggest opportunity for improvement in the Slovak business environment. Businesses in general perceive the legislative environment in Slovakia as unstable – with frequent changes and complicated, often unclear, legislation that forces entrepreneurs to seek expert assistance even when dealing with minor issues unless they want to risk breaking the law. Distrust of small- and medium-sized enterprises in the legal system and the independence of the courts is demonstrated by the high rate of dissatisfaction when responding to practically all questions in this section of the survey.

*Over 90% of the respondents believe that Slovak courts do not support the equitable resolution of legal disputes (fig.1). As many as 94.5% consider the length of dispute resolution inadequate, while among business with less than 10 employees, this percentage is over 98% (fig.2). Moreover, almost 90% of all entrepreneurs who participated in the survey think that the authorities and official representatives are often unable to sufficiently clarify the requirements for judicial actions (fig.1).*

## II. ADMINISTRATIVE BURDEN AND CORRUPTION

The administrative burden associated with doing business is one of the key factors influencing growth and development, especially for smaller companies. Taking into account the financial cost and the workload put on the personnel, the excessive and unfounded administrative burden on businesses can result in lack of interest in doing business or attempts to avoid compliance with complicated and unclear regulations. Complicated administration and corruption also poses a problem for larger companies and foreign investors as it makes their business activities more expensive. This can, in the end, influence their decision to move their operations to another country. However, in the case of SMEs, this can be a direct threat to their very existence. When it comes to the administrative burden of establishing and operating companies, entrepreneurs admit that the situation in Slovakia is gradually improving, but they are still very dissatisfied with development – or rather the lack of it - in several particular areas.

*Most respondents consider the process of registering a company in Slovakia to be relatively efficient (over 66%) and the related costs are seen as reasonable by 74%. However, many believe that the costs related to further bureaucratic requirements on companies are an issue. These costs – measured in time and money - represent a considerable hindrance for almost 68% of*

Slovak courts currently do not enjoy much trust from the Slovak business community. If this is to change, the responsibility of both parties (i.e. the plaintiff and the defendant) should be enhanced as well as the responsibility of the court itself in order to eliminate the possibilities for obstructions. The entrepreneurs believe that the system enables -- and the courts tolerate -- various obstructions of the defending party as well as artificially drawn-out processes by means of repeated excuses due to health reasons or changes of attorneys. Even law firms themselves say that, to a large extent, the resolution and the length of legal processes in Slovakia cannot be foreseen. Therefore, out-of-court settlement is preferred at any cost.

**“The courts are not perceived as a partner in dispute resolutions, but instead, rather as a scarecrow and an untrustworthy institution.”**

*Comment from respondent*

Many entrepreneurs also point out the low level of enforceability of receivables; they specified that there is no functioning system

*polled entrepreneurs (fig.3). For example, acquiring a building permit is perceived as a lengthy and complicated process by almost 79% of all respondents (fig.4). For small companies, this can be an even more serious issue (fig.5). Among businesses with annual turnover under €1m or firms with less than 10 employees, 93% are dissatisfied with the process of acquiring a building permit. Another barrier is corruption. According to our survey, this affects more than 60% of SMEs (fig.3).*

**“If the conditions are clearly stated, simple, quantified, easy to meet and valid for everybody, we will avoid wasting time, unnecessary costs and the attempts of some individuals to make the rules ambiguous for their own benefit.”**

*Comment from respondent*

Based on the findings of the AmCham 2010 survey, the situation with excessive administrative burden is therefore not critical, but there are a number of areas where Slovakia must improve its performance in order to compare with more experienced EU countries or even some of the more enterprising eastern economies. The actual duration of the registration process and the related fees are apparently acceptable, even when compared to other countries. However, an overwhelming majority of entrepreneurs are convinced the main problems are the attitude, coordination and flexibility of

to do so, which is further complicated by an extremely lengthy process. Here, it is clearly necessary to adjust the legal relationship to the goods from unpaid invoices - the law should stipulate that the goods become the property of the new owner upon settling the invoice, not after issuing it.

### Recommendations of survey respondents:

- Shortening lawsuits and non-acceptance of obstructions (e.g. when “no shows” for health-related reasons occur repeatedly in courts, applying the three strikes rule or perhaps asking for a special form, or the possibility to check the case by an independent healthcare commission; and similar rule should be applied in the case of repeated changes of attorneys)
- Adhere to and consistently check random lawsuit allocation to judges without any possibility of circumventing the system
- Apply more efficient and transparent control of the activities of judges (for example, create an archive of the trial records to enable additional checks, publish court decisions on the web)
- Increase speed and improve the enforceability of receivables

certain state authorities, unclear legislative framework and too complex administration that requires companies to meet additional costs and, very often, seek professional assistance.

Companies believe that the support from state authorities is poor – the respective authorities or magistrates are not interconnected, applicants don't have complex information available to them at a single contact point and, for foreign entrepreneurs, a significant barrier is that almost all information is only available in Slovak. Firms are often burdened with administration that is perceived as useless, e.g. repeated requirements for submitting statements from the Trade Register or the need to submit official documents verified by a notary that could be easily accessible to all state authorities and magistrates in a single electronic system. In a number of cases, the problems are caused by the human factor – be it incompetence, unwillingness or simply making excuses. Although entrepreneurs admit that the attitude to clients in state offices has recently improved, the feeling prevails that instead of providing quality information and support, the authorities still focus mainly on control and penalization. Foreign entrepreneurs have the experience that in other EU countries, state employees, clerks or magistrates welcome them with complete and accurate data and documents while being competent, willing and actually able to provide binding statements on particular matters. SME representatives believe that the current

situation in Slovakia is directly linked to the issue of corruption. Corruption can only appear in the system in places where opportunity arises. Therefore entrepreneurs would appreciate greater transparency when disposing of public resources and property, better coordination in state administration and higher quality information on procedures and exact regulations. This could simultaneously eliminate the excessive administration burden, additional costs as well as corruptive practices.

Today, many of the polled entrepreneurs perceive corruption as a part of the Slovak mentality and a widely accepted fact. Efficient, high-quality informatization of the state administration would go a long way in eliminating bribery and thus increasing the trustworthiness and competitiveness of Slovakia. Public information must be easily and generally accessible. When dealing with small businesses, state authorities should walk the extra mile and treat them as important customers. In order to achieve this, the perception of the business environment should also be improved. Entrepreneurs themselves admit that society in general

does not see their community in a very positive light. The proposed steps to make state administration more efficient include better motivation of state officers and employees – not only financial remuneration but also a higher degree of responsibility. Since self-employed/sole traders account for a relatively large portion of the sample, one cannot omit the repeatedly-mentioned problems connected to specifying the subject of business in accordance with the current version of the List of Trades. Entrepreneurs believe that this is, in some cases, misleading and limiting while it fails to correspond to reality.

#### Recommendations of survey respondents:

- Introduce an efficient system of e-government (electronic state administration) that will eliminate duplicate activities and will reduce the excessive administrative burden put on businesses
- Introduce complex centers (one-stop-shops) providing support to firms, enabling firms to handle the agenda at a single location - at once, without complications, based on comprehensive

information available not only in Slovak language

- Re-evaluate the use of revenue stamps and introduce other forms of payment (e.g. by debit card)
- Substitute the obligation to use an electronic signature with a simpler security code (e.g. a login and a password as introduced into practice in a number of developed economies)
- Terminate the obligation to define each subject of business unless special conditions apply (i.e. introduce unspecified general trade/business license with necessary exemptions)
- Introduce efficient control and punishment of corruption in the state administration
- Equalize positions of authorities and entrepreneurs so that authorities also bear their share of responsibility (e.g. provision of binding statements/opinions or waiver of penalty in case incorrect information was provided)
- Conduct formal assessment of current building-permit processes with the goal to improve efficiency and eliminate corruption.

### III. FINANANCIAL ASPECTS AND EMPLOYMENT

The tax levels, contributions and other costs related to employment are equally important for foreign investors as for local businesses. These factors are often vital for small firms with limited resources.

*In our survey, we first polled respondents on the tax burden in Slovakia, which 68% consider to be adequate (fig.6). The percentage is even higher (76%) among more experienced businessmen – firms operating for at least five years (fig.7). However, the number of satisfied taxpayers declines with the number of employees – from 61% among companies with annual turnover under €1m, to as few as 45% among the self-employed (fig.7). Apart from taxation levels, most firms are dissatisfied with the social contributions burden – as many as 83% consider social contributions to be very high. Additionally, 68% of all SMEs indicated they would appreciate greater flexibility in the Labor Code (fig.8). When it comes to additional financing and stimuli for SMEs in Slovakia, the situation is even worse. Seventy-four percent of respondents specified that bank loans are complicated, even inaccessible (among small firms, the figure is as high as 84% - fig.7). Those who applied for some kind of incentives in the past failed to succeed in 74% of all cases (fig.10). However, the figure goes down to 43% among the self-employed (fig.11), which could perhaps suggest that this group has greater possibilities and information support available. In addition, over 92% of those polled claim that small- and medium-*

*sized enterprises have practically no access to other forms of financing such as venture capital, guarantees, etc.(fig.7)*

**” People should be given a chance when starting something new. Therefore it is necessary to provide incentives to the start-ups, increase state and local support and, above all, show them trust. Small firms can create a great number of jobs in their local communities.**

*Comment from respondent*

Most businesses don't see any major problems when it comes to taxation – although with regard to changes implemented by some other countries, the 19-percent flat tax rate is no longer such a clear-cut advantage for Slovakia. However, some companies point out frequent changes to VAT rates and complicated procedures when filing VAT tax returns. Survey respondents also objected to the slow and cumbersome approaches of tax authorities – particularly when informing the taxpayers or fulfilling their own obligations - while they often take a no-compromise attitude when it comes to deadlines and compliance from businesses. Similar to the survey of foreign investors, complications related to employment are seen as an issue by SMEs as well. This is mainly in connection with the level of social costs/contributions, complicated administration as well as the insufficient flexibility of the Labor Code (LC). Entrepreneurs all agree that there is no shortage of relatively skilled and motivated labor in Slovakia, but employment is still difficult. They also criticized insufficient links between education

and practice combined with continued low workforce mobility. Financing possibilities are seen as very limited in Slovakia. Entrepreneurs are often not even aware of them and feel an acute lack of reliable information about EU funds or public procurement. They also feel that the state should provide more support to other forms of financing - such as bank loans and incentives - especially for smaller businesses and in the first years of their operations. Most entrepreneurs consider the process of structural funds distribution and public procurement as too complicated and non-transparent, creating space for corruption and negative development of the business environment. Late payments from clients, insufficient protection of creditors and various bank fees all cause serious trouble to a number of small firms.

#### Recommendations of survey respondents:

- Simplify the taxation system and introduce a unified/single payment of taxes and contributions to social and health insurers
- Decrease the social cost/contribution burden by 10-15 percent
- Simplify hiring based on work agreements (including students) and part time employment; make the Labor Code more flexible overall
- Support SME financing through banks or other institutions
- Consider a tax holiday for small start-up entrepreneurs
- Increase the support of businesses at a local level in an effort to strengthen their links with the local community and create jobs in less developed regions



## CONCLUSION

As we see from the AmCham survey findings, there are significant opportunities to improve the competitiveness of the SME business environment in Slovakia. According to the majority of respondents, the strengths include flat tax and a relatively simple process of registering a new company as well as customs regulations that do not excessively complicate cross-border trading. For the growth of companies, it is an advantage that there is still an unsaturated market in some areas of Slovakia which enables businesses to apply good ideas that were successful abroad.

Key opportunities for improvements include addressing what SMEs perceive as a dysfunctional justice system, bureaucracy and red tape, the administrative burden

of a number of legally required processes, uncoordinated state administration, high contributions/social costs, low level of transparency, corruption and nepotism as well as poor state support for businesses are the main weaknesses. A number of questions showed that the larger and more experienced businesses (especially if enjoying support from a foreign parent company) are less likely to perceive many of the above-mentioned barriers as impassable. However, during extensive discussions with entrepreneurs within the AmCham workgroups, it turned out that this is the result of accepting the status quo (and/or having more resources) rather than appreciating the current situation in Slovakia.

Based on the survey of small- and medium-sized enterprises, the priority for the

Slovak government should be to unify and simplify the state administration at all levels. Entrepreneurs indicated that this would very much unburden not just state administration itself but also companies, while the resources saved could be used to provide further support for the development of the economy. In general, it is necessary to improve the support, not only financial but also administrative and moral support, to SMEs as they represent the backbone of the economy and are an assurance of regional development. In relation to this, a number of respondents in the survey pointed out the need for positively influencing the attitudes of state officers and the general public so that the word 'entrepreneur' in Slovakia was not associated only with the idea of self-interested, unscrupulous speculators.



We would like to thank the following companies and people for their help with the SME survey:

Pavol Kopečný, Ecenter; Steven Kelly, KNO; Ján Bunčák, Associate Professor, and the 4<sup>th</sup> year students of sociology at the Comenius University; Poradenské rozvojové centrum (PRC) at the Faculty of Management CU; Peter Kolenič and Ivan Miniarik, SAP Slovakia; Andrej Viceník, VÚB; Juraj Bizoň, Bizoň & Partners; Roman Javorček, Volksbank; Gerard Koolen, Lugera; Milan Poliak, Elwa; Miro Koleník, CLASS Language school; Martin Sloboda, MS Agency; Maroš Kamenský; Iveta Griačová, Airport Bratislava; Beata Hlavčáková, Pontis Foundation; and David Ondrejko. And of course to all companies who shared their views and suggestions for the improving business environment in Slovakia.



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