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### Final Status for Kosovo and Economic Sustainability

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# ECONOMIC SUSTAINABILITY AND FINAL STATUS FOR KOSOVO

HENRY H. PERRITT, JR.\*

## 1. INTRODUCTION

Nation-building cannot succeed unless political trustees<sup>1</sup> give greater priority to economic development. In the political trusteeships of the late twentieth and early twenty-first centuries, private sector economic development has taken a backseat to humanitarian relief, human rights work, and the establishment of political institutions. Part of the problem may be the immaturity of

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<sup>1</sup> The term "political trusteeship" refers to the administration of a territory by one or more foreign states for the benefit of the population of the territory, aimed at eventual autonomy, self-government, and economic sufficiency. Recent examples are the U.N.-approved trusteeships in Bosnia, Kosovo, East Timor, Afghanistan, and Iraq. See Henry H. Perritt, Jr., *Structures of Political Trusteeship*, 8 UCLA J. INT'L L. & FOREIGN AFF. (forthcoming 2004) [hereinafter Perritt, *Structures of Political Trusteeship*] (describing the history of political trusteeship, arguing that political trustees cannot be successful unless they enjoy international and internal legitimacy, and offering prescriptions for success).

development theory. Some scholars emphasize capital formation as the crucial component needed to accelerate development through universal stages; others emphasize human capital formation; structuralists emphasize country-specific analysis of institutional impediments to development;<sup>2</sup> and neoclassicists emphasize the need for the government to stay out of the way.<sup>3</sup>

But political trusteeships are not academic exercises, and development theory actually has played only a dim background role in recent initiatives. More often, inattention to economic development has resulted from the reality that human rights violations or international security threats usually justify the intervention, and that senior personnel recruited to run political trusteeships are more oriented by background and expertise to human rights or diplomacy than to private sector entrepreneurship and capital formation. Administrators of political trusteeships do not have textbooks on development by Walt Rostow or Gale Johnson behind their desks; instead they have copies of the International Covenant on Civil and Political Rights, the Geneva Conventions, the European Convention on Human Rights, and the Helsinki Accords.

The political trusteeship in Kosovo provides an interesting case study from which lessons can be learned about how to place private sector economic development higher on the list of trustee priorities. The mandate of the political trustee in Kosovo was especially robust, including virtually every aspect of sovereignty. The local culture and experience, while problematic, was hospitable to market-oriented economic interaction. Accordingly, a close examination of the missteps in Kosovo can inform future political trusteeships so that the international community does a more effective job in promoting economic opportunities for trust beneficiaries.

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<sup>2</sup> See Dani Rodrik, *Institutions for High-Quality Growth: What They Are and How to Acquire Them*, 35 *STUD. IN COMP. INT'L DEV.* 3, 27-28 (2000) [hereinafter Rodrik, *Institutions for High-Quality Growth*] (discussing the types of institutions that permit markets to perform effectively and the importance of experimenting and considering each country's experience); see also DANIEL KAUFMANN ET AL., *GOVERNANCE MATTERS* (1999) (discussing the impact of good governance on development outcomes), available at <http://www.worldbank.org/wbi/governance/pdf/govmatrs.pdf> (last visited Feb. 25, 2004).

<sup>3</sup> See The History of Economic Thought Website, *Economic Development* (commenting on the evolution of the theory of economic development), at <http://cepa.newschool.edu/het/schools/develop.htm> (last visited Feb. 25, 2004).

For administrators who are interested in promoting economic development, the immediate practical challenges are not ones of selecting the right theory of economic development. Rather, they involve construing the trustee's mandate broadly enough to make the legal and institutional changes necessary for enterprise formation and capital investment; designing and erecting a hospitable legal infrastructure for private enterprise; establishing necessary financial service intermediaries; and assisting local entrepreneurs to promote products, services, and investment opportunities. Successfully meeting these challenges requires pragmatic legal and business acumen rather than theoretical creativity.

Familiarity with competing models for company law, payment systems, commercial dispute resolution, and property law transformation is more important to the operational decisionmaking of political trustees than is deep knowledge of theories of constitutionalism. Knowing how microcredit and investment promotion for small and medium enterprises ("SMEs") has worked in other countries in transition is more important than understanding the latest data on total factor productivity in the developing world.

Five years of political trusteeship by the international community in Kosovo has produced insufficient economic progress. The unemployment rate remains close to 60%; no overall vision for economic self-sufficiency exists; privatization has barely begun; and few steps have been taken to exploit the potential of entrepreneurial energy to start new SMEs.

Uncertainty about the final status of Kosovo is partly responsible for the slow start. U.N. lawyers questioned the legal authority to restructure inefficient enterprises, and Kosovo's lack of independent identity discourages outside investors. The U.N. Mission in Kosovo ("UNMIK") arbitrarily denies contact between Kosovar governmental representatives and the rest of the world. The European Union ("EU") Stability Pact mostly leaves Kosovo out of regional economic development activities. Kosovar political leaders are distracted from the important job of developing concrete programs for developing the private economy.<sup>4</sup> In other

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<sup>4</sup> A January 2003 survey by the United Nations Development Programme ("U.N.D.P.") of 6,000 Kosovars showed widely varying satisfaction and confidence in municipal government, ranging from positive views in Suharekë and Gjiilan, to negative views in Zveqan and Malishevë. The U.N. Development

respects, uncertainty about final status is merely an excuse for public entities to not do their jobs. Among other problems, there is a lack of transparency. Neither UNMIK nor the Provisional Institutions of Self Government ("PISG") promptly and reliably publishes their legislative acts.

The United States should begin the process of convening an international conference to decide the final status of Kosovo. UNMIK and provisional governmental institutions must meet their responsibilities to reform law and public administration to create a better investment climate. UNMIK must also establish important financial services intermediation to make it easier for entrepreneurs and investors to get together and make deals.

Successfully finishing the job in Kosovo is an important step in the achievement of the goals of political trusteeships elsewhere, such as in Afghanistan and Iraq. Withdrawing from Kosovo or perpetuating an increasingly illegitimate U.N. trusteeship there would likely lead to chaos, the collapse of physical security, renewed inter-ethnic conflict, and threats to security elsewhere in the western Balkans. Such a failure in a major international commitment would encourage those who believe that the campaign against terrorism cannot be won because the West lacks the discipline to persevere and to define achievable goals.

Kosovo's population is overwhelmingly Muslim and overwhelmingly loves America. Abandoning the prospects for a stable, democratic, prosperous secular state in Kosovo would raise doubts about the U.S. capacity to interact successfully with less hospitable Muslim populations elsewhere in the world.

On the other hand, staying the course in Kosovo, refocusing attention on economic development, providing leadership to other elements of the international mission there, and eventually achieving an independent state with appropriate political, economic, and security ties to the rest of the region will yield valuable lessons that can inform other nation-building efforts.

Ambiguity in the mandate for the political trusteeship in Kosovo led to roadblocks to early initiatives for economic restructuring. The elements of a sustainable private economy that still need attention in Kosovo are the same in any nation-building enterprise. Preoccupation with privatization, at the expense of attention to agricultural reform and to SME formation, is a mistake

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Programme, *The Kosovo Mosaic: Perceptions of Local Government and Public Services in Kosovo*, at 10 fig. 1 (2003), at <http://undg.ks.undp.org/mosaic.htm>.

that can be avoided elsewhere. Shortfalls in private sector-oriented economic expertise and tools hamstrung the early Kosovo trusteeship; it should not impede similar efforts in the future.

## 2. BACKGROUND

The political trusteeship<sup>5</sup> in Kosovo exists under the mandate of U.N. Security Council Resolution 1244, which followed military intervention in Kosovo by the North Atlantic Treaty Organization ("NATO") in 1999. Tensions between Albanians, the majority ethnic group, and Serbs, the minority ethnic group, in the territory of Kosovo predated the dissolution of the Ottoman Empire. As the Ottoman Empire eroded in the late nineteenth century, emergent Serbia, initially as an autonomous principality within the Ottoman Empire, and then as an independent state, began to press Albanians to leave the territory of modern-day Kosovo.<sup>6</sup> In 1878, Albanian nationalists assembled at the League of Prizren to develop a strategy to defend Muslim and Albanian traditions against encroachment. The League took over the administration of Kosovo for about a year, but in 1881 the Albanian "insurrection" was crushed by Turkish troops.<sup>7</sup>

By the time of the first Balkan war in 1912, Serbia was an independent state and sent its troops into Kosovo, consolidating Serbian rule and thereby preventing the unification of the Albanian population in Kosovo with the new state of Albania, recognized in 1913.<sup>8</sup>

In 1915, the Austro-Hungarians, Germans, and Bulgarians expelled the Serbs from Kosovo and occupied Serbia. But in 1918, Serbs reoccupied Kosovo and on December 1, 1918, a new Yugoslav state called the "Kingdom of Serbs, Croats and

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<sup>5</sup> "Political trustee" refers to situations in which one or more states, acting on their own, or under approval by the U.N. Security Council, administer the territory of another state. Political trusteeship is distinguished from conquest, in which successful military intervention is usually followed by the annexation of conquered territory into the conquering state. In contrast, political trusteeship legitimizes intervention and foreign administration only for the benefit of the peoples of the territory administered. Political trusteeships are inevitably followed by a return to local political control. See Perritt, *Structures of Political Trusteeship*, *supra* note 1.

<sup>6</sup> See TIM JUDAH, *KOSOVO: WAR AND REVENGE* 11-12 (2000) (discussing the background to the war in Kosovo).

<sup>7</sup> *Id.* at 12.

<sup>8</sup> *Id.* at 18.

Slovenes," was established.

Kosovar Albanians resisted incorporation of Kosovo into the emerging Yugoslavia. "It was, after all, a state of the south Slavs, as it[s] name suggested, and the Albanians are not Slavs."<sup>9</sup> Briefly, during the post-World War I Paris peace conference, Kosovar Albanians were encouraged to believe that a unified Albanian state would emerge from the wreckage of the now defunct Ottoman Empire.<sup>10</sup> Eventually, however, not only was Kosovo made part of what became Yugoslavia, but only with President Woodrow Wilson's intervention did Albania avoid its own breakup and partition.

Albanian resistance to the Serb government continued at various levels of intensity during the interwar period. When World War II broke out, Italy occupied Albania and eventually extended its military control throughout Kosovo and Albanian areas of Macedonia. Tito, the new ruler of Yugoslavia, sought to attract Albanian support for his "partisan" movement by promising autonomy to Kosovar Albanians. However, after the end of World War II, attracting Serbian support was more important to Tito and Albanian national aspirations had to be deferred once again. Only in 1974, with the adoption of a new constitution for Yugoslavia, were Kosovar Albanians granted formal autonomy as an "autonomous province" within Serbia. The legal status of autonomous province was equivalent to the "republic" status given Slovenes, Croats, Montenegrins, and Macedonians except that an autonomous province had no power to secede from Yugoslavia. Under the 1974 constitution, Kosovar Albanian aspirations intensified as Albanians were allowed to set up Albanian-language institutions, such as the University of Prishtina.

Historically, investment in Yugoslavia was politically motivated. Kosovo was a grim place in the 1960s; the only way to survive was agriculture. Consequently, anyone who could emigrate did so, and the Serbs were concerned that this would deplete the Serb population.

Later, 80% of all Yugoslav investment in underdeveloped parts of Yugoslavia was in Kosovo. Most of it went to the Trepca mines.

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<sup>9</sup> *Id.* at 21.

<sup>10</sup> See MARGARET MACMILLAN, PARIS 1919: SIX MONTHS THAT CHANGED THE WORLD 358-63 (2001) (describing the power struggle over Albania following the Great War).

Kosovo was a supplier to socially owned enterprises ("SOEs")<sup>11</sup> elsewhere in Yugoslavia with an emphasis on colored metals. Money flowed, as the Yugoslav government thought it necessary to prevent unrest. This process started in 1974. Infrastructure was only built to support SOEs. A good example is Rahovec, where an SOE with supporting infrastructure was built to prevent a Serb exodus.

Susan Woodward has developed a persuasive case that the collapse of Yugoslavia was occasioned as much by an economic implosion as by a leadership succession crisis after Tito's death, and far more by economic hardship and immature political institutions than by "ancient ethnic hatreds."<sup>12</sup> As the Cold War ended, international institutions such as the World Bank and the International Monetary Fund ("IMF") lost interest in Yugoslavia. Unemployment in all of Yugoslavia grew from just under 14% in 1979 to nearly 17% in 1988, and from just under 40% in Kosovo to nearly 60% during the same period. Gross domestic product ("GDP") growth declined from a positive 5% in 1979 to a negative 10% in 1990.<sup>13</sup>

The University of Prishtina, established in 1974, was meant to reduce Albanian unrest, but it made problems worse. It led to the creation of an Albanian bourgeoisie, which strengthened Albanian nationalism. As Yugoslavia began to fall apart after the death of Tito and the end of the Cold War, Serb Communist leader Slobodan Milosevic discovered that he could accelerate his political rise by currying favor with minority Serbs within Kosovo.<sup>14</sup> Milosevic changed the Yugoslav Constitution to revoke Albanian autonomy.<sup>15</sup> This decision was followed by an "Albanian declaration of independence" in September 1991 and the erection of a parallel political, legal, and economic structure, beginning in

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<sup>11</sup> A socially owned enterprise ("SOE") is a unique type of economic organization implemented by Tito in Yugoslavia. It shifts ownership of productive assets from the state to groups of employees making up an individual enterprise and to the municipalities where they live. Sorting out property interests associated with the SOE concept is daunting. See generally Abdulla Aliu, *The Law on Ownership Rights in Kosova*, 1 EURO-ATLANTIC REV. 49 (2002).

<sup>12</sup> SUSAN L. WOODWARD, *BALKAN TRAGEDY: CHAOS AND DISSOLUTION AFTER THE COLD WAR* 15-17 (1995) (discussing the history of the conflict in the Balkans).

<sup>13</sup> *Id.* at 52-55.

<sup>14</sup> See LOUIS SELL, *SLOBODAN MILOSEVIC AND THE DESTRUCTION OF YUGOSLAVIA* 39-64 (2002) (describing Milosevic's rise to power).

<sup>15</sup> See *id.* at 93 (detailing how the Serb Assembly dissolved its Kosovo counterpart and declared all of its laws invalid).



1992.<sup>16</sup>

By the mid-1990s, when the Dayton Accords ended the Bosnian War, it was clear that the campaign of passive resistance organized by Ibrahim Rugova, the leader of the Democratic League of Kosovo ("LDK"), was not working—or in any event that it would not attract sufficient international intervention to make an independent Kosovo a reality. Gradually, armed resistance to Serb control developed among Kosovar Albanians, crystallizing into the Kosovo Liberation Army ("KLA") in early 1998. After 1989, the Kosovar Albanians were removed from management positions in the SOEs, but they became middlemen in a hyperinflationary Yugoslavia. The fact that the Albanians became rich made them a target of the Financial Police in 1998 and 1999. As Albanian unrest increased, so did Serb repression, which had the effect of improving KLA recruitment.<sup>17</sup>

By mid-1998, NATO began to threaten military intervention unless Milosevic ceased his efforts to drive Kosovar Albanians from their homes into refugee camps in Albania and Macedonia. After a brief agreement in October 1998, brokered by Ambassador Richard Holbrooke, violence flared up again in early 1999. In January, a peace conference was convened in Rambouillet, France. After much maneuvering and pressure, the KLA signed the agreement, but the Serbs did not. Kosovar agreement was induced in part by a letter dated February 22, 1999, from Secretary of State Madeleine Albright promising a "referendum on the final status of Kosovo after three years."<sup>18</sup> After a round of ultimately futile last minute meetings with Milosevic, the NATO bombing campaign began on March 24, 1999.<sup>19</sup>

On June 10, 1999, NATO "suspended its bombing and the U.N. Security Council passed Resolution 1244."<sup>20</sup> U.N. Security Council Resolution 1244 ("Resolution 1244") envisions the possibility of independence.<sup>21</sup> But the Resolution is ambiguous in that it

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<sup>16</sup> *Id.*

<sup>17</sup> See JUDAH, *supra* note 6, at 117-43 (detailing the strengthening of the Kosovo Liberation Army ("KLA")).

<sup>18</sup> *Id.* at 215.

<sup>19</sup> *Id.* at 237.

<sup>20</sup> *Id.* at 285.

<sup>21</sup> See S. Res. 1244, U.N. SCOR, 4011th meeting, U.N. Doc. S/Res/1244 (1999) [hereinafter Resolution 1244] (embracing the Rambouillet Accords as a touchstone), available at <http://ods-dds-ny.un.org/doc/UNDOC/GEN/N99/172/89/PDF/N9917289.pdf> (last visited Mar. 2, 2004). Paragraph 8.3 of the

recognizes Yugoslav sovereignty during the period of U.N. civil administration. The ambiguity has permitted some lawyers and policymakers to obstruct political and economic development in Kosovo.

Resolution 1244 put the United Nations in the position, for the first time, of exercising sovereignty and running a country.<sup>22</sup> Resolution 1244 and subsequent implementing documents issued by the Secretary General of the United Nations established UNMIK<sup>23</sup> as a political trustee,<sup>24</sup> exercising sovereignty on behalf of the people of Kosovo. Under this arrangement, UNMIK exercises legislative, executive, and judicial functions without differentiating them very clearly.<sup>25</sup> These governmental powers continued even after elections were held and local judges, legislators, and ministers took office under the "constitutional framework."<sup>26</sup>

Resolution 1244, while recognizing Yugoslav sovereignty,<sup>27</sup> vests UNMIK with "basic civilian administrative functions where and as long as required."<sup>28</sup> This authority is to be transferred to "local provisional institutions,"<sup>29</sup> and eventually from them to

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Rambouillet Accords provided for an international conference three years after signing, at which the "will of the people" would substantially affect a determination as to final status.

<sup>22</sup> *Id.* art. 10 (authorizing the Secretary General to establish civil administration for Kosovo).

<sup>23</sup> *Id.* art. 6 (authorizing the appointment of a Special Representative of the Secretary General to head civil administration).

<sup>24</sup> This Article uses the terms "trust" and "political trustee" in the sense of an entity that exercises sovereignty on behalf of another, rather than in the formal sense that the term "trust territory" is used in Chapter 12 of the U.N. Charter. See generally Perritt, *Structures of Political Trusteeship*, *supra* note 1; Henry H. Perritt, Jr., *Stabilizing Kosovo: Enterprise Formation and Financial Markets*, 2 J. GLOBAL FIN. MARKETS 28 (2001) [hereinafter Perritt, *Stabilizing Kosovo*] (explaining the "trustee-occupant" concept as defining the role of the U.N. Mission in Kosovo ("UNMIK")).

<sup>25</sup> Resolution 1244, *supra* note 21, art. 11 (delineating the powers and responsibilities of civil administration).

<sup>26</sup> UNMIK Regulation 2001/9 (May 15, 2001) (formalizing a constitutional framework for provisional self-government in Kosovo), available at <http://www.unmikonline.org/regulations/2001/reg09-01.htm>.

<sup>27</sup> Resolution 1244, *supra* note 21, pmbl. (reaffirming territorial integrity of the Federal Republic of Yugoslavia ("FRY")).

<sup>28</sup> *Id.* art. 11(b).

<sup>29</sup> *Id.* art. 11(d).

<sup>30</sup> *Id.* art. 11(f).

institutions emerging from the final political agreement, under UNMIK oversight.<sup>30</sup> UNMIK is expressly directed to support "the reconstruction of key infrastructure and other economic reconstruction."<sup>31</sup> Section 6 of UNMIK Regulation Number 1 expressly provides for UNMIK's administration of movable and immovable property registered in the name of the Federal Republic of Yugoslavia ("FRY").<sup>32</sup> UNMIK thus possesses the necessary legal authority to adopt legislation and to take executive steps to create and to transfer property rights necessary to economic development and the attraction of foreign capital.

The sovereignty provisions of the preamble to Resolution 1244 were carefully worked out, and the Resolution in its entirety represents a thoughtfully negotiated ambiguity with respect to the question of whether Kosovo should be an independent sovereign state or only "autonomous" within the Yugoslav federation.

UNMIK comprises four "pillars": Police and Justice (Pillar I), Civil Administration (Pillar II), Institution Building (Pillar III), and Economic Reconstruction (Pillar IV). Each pillar is headed by a Deputy Special Representative. UNMIK itself is responsible for Pillars I and II. The Organization for Security and Cooperation in Europe ("OSCE") is responsible for Pillar III, and the EU is responsible for Pillar IV.

While substantial international resources have been made available to Kosovo, economic development beyond physical infrastructure reconstruction and macroeconomic frameworks

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<sup>31</sup> *Id.* art. 11(g).

<sup>32</sup> UNMIK began to use this authority in October 1999. See UNMIK Regulation 1999/10 (Oct. 13, 1999) (abolishing discriminatory laws relating to housing and property ownership, after determining they violated the human rights of people of the territory), available at <http://www.unmikonline.org/regulations/1999/reg10-99.htm>. The regulation repealed two specific laws, one on real estate transactions, and another on granting farm land to citizens. See also UNMIK Regulation 1999/11 (Oct. 13, 1999) (authorizing UNMIK to use Kosovo's Public Payment Service, headquartered in the capital, Prishtina, to collect and disburse public funds), available at <http://www.unmikonline.org/regulations/1999/reg11-99.htm> (last visited February 25, 2004); UNMIK Regulation 1999/12 (Oct. 14, 1999) (authorizing the Post and Telecommunication Enterprise of Kosovo ("PTK") to provide mail and phone services to Kosovo, under the overall supervision of UNMIK), available at <http://www.unmikonline.org/regulations/1999/reg12-99.htm>. By the new regulation, PTK was given use of all public postal and telecommunication assets in the territory, including any future expansions. UNMIK also nullified post-1989 Yugoslavia law through its regulations. UNMIK Regulation 1999/24 (Dec. 12, 1999), available at <http://www.unmikonline.org/regulations/1999/reg24-99.htm>.

seems to be almost an afterthought in UNMIK policy. For example, the June 2003 report by the Secretary General to the Security Council on the U.N. Mission in Kosovo<sup>33</sup> does not mention economic development until the forty-second paragraph and then contains seven relatively general paragraphs focused primarily on public finance and privatization.<sup>34</sup>

By early 2003, criticism of and frustration with UNMIK was growing, fueled by impatience with the slow pace of transferring final decisionmaking authority from UNMIK to local institutions. Frustration with UNMIK is also fueled by a growing belief that UNMIK institutions are not transparent, are frequently corrupt, and in any event have no political accountability in the democratic sense.

The most important barriers to private sector economic development are unreliable electricity, high wages, high tariffs, small markets, and a heavy flow of imports.

Kosovo's comparative advantages include: large numbers of young people with skills and languages, and linkages with those in the Albanian diaspora around the world which can be turned into stronger and more traditional business linkages.

There are significant lignite reserves in Kosovo. It has the best in the region, and the costs of extraction are only one-third those of runner-up Bulgaria. So exporting energy in the form of lignite itself or in the form of electricity is an interesting possibility. It is true that Kosovo used to export electricity to Montenegro and Croatia, but via a transmission system through Serbia. The Kosovo Energy Corporation ("KEC" or "KEK") plan is completely outsized unless it was built to produce power for export.

### 3. THE RECORD SO FAR

Five years of political trusteeship by the international community over Kosovo have produced an end to ethnic cleansing, increased law and order, improved standards of living for the majority Albanian population, produced three sets of peaceful and fair elections—albeit with declining turnout—and

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<sup>33</sup> *Report of the Secretary-General on the United Nations Interim Administration Mission in Kosovo*, U.N. SCOR, U.N. Doc. S/2003/675 (2003), available at <http://www.un.dk/doc/s2003675.pdf> (last visited Feb. 25, 2004).

<sup>34</sup> *See id.* paras. 42-49 (noting generally that there have been Economic and Fiscal Council meetings, some voluntary compliance with tax laws, and high numbers of illegal or unregistered public utility customers).

overseen the functioning of local government institutions in the executive, legislative, and judicial spheres. The political trustee, UNMIK, has made far less progress, however, on the economic front. After the war, the KLA took over vacant SOEs by posting "property of the Kosovo state" posters. It is not altogether clear that this was illegitimate because the Democratic Party of Kosovo ("PDK") led the interim government. But many people perceived it as illegitimate. The prewar Kosovar Albanian businessmen were the elites of the private sector, but after the postwar construction boom, which now has tailed off, they are not sure of the "next big thing." They have no skills in the modern sense, only instincts, courage, and money. The unemployment rate remains at about 60%. Most of the good jobs are with international organizations, all of which plan to cut back on their levels of activity and employment in Kosovo. Only twelve of several hundred SOEs were commercialized,<sup>35</sup> and only eighteen have taken the first steps toward being privatized, before a new EU administrator of Pillar IV "froze" privatization in October, 2003. According to most estimates, only about sixty of these SOEs will develop into viable businesses in a market economy. U.N. lawyers opposed to fundamental reform of real property law and questioning the U.N. mandate to restructure certain enterprises delayed repeatedly – for two years and then again in late 2003 – operation of a Kosovo Trust Agency ("KTA"),<sup>36</sup> originally established in 2001.

Publicly owned enterprises such as the telephone company ("PTK"), KEC, the Trepca mines, the airport authority, and the railways have not been privatized, lack clear direction, and are inefficient. Electric power interruptions continue to be common; telephone service, while reasonably reliable in major cities, is absent in the countryside, and the plant is obsolete.

In some ways, however, the private sector is flourishing. Almost immediately after the war, restaurants and filling stations

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<sup>35</sup> According to the "Lessons Learned and Analysis" unit of the EU Pillar of UNMIK, Pillar IV, five of the twelve commercialization ventures were successful, three were clearly failures, and two were too recent to assess. European Stability Initiative, *The Ottoman Dilemma: Power and Property Relations Under the United Nations Mission in Kosovo: Lessons Learned and Analysis Unit of the EU Pillar of UNMIK in Kosovo* (Aug. 8, 2002) [hereinafter *The Ottoman Dilemma*], at [http://www.esiweb.org/pdf/esi\\_document\\_id\\_35.pdf](http://www.esiweb.org/pdf/esi_document_id_35.pdf).

<sup>36</sup> See Kosovo Trust Agency, *Socially Owned Enterprises/Publicly Owned Enterprises* (2002) (describing the objectives of the Kosovo Trust Agency ("KTA")), at <http://www.kta-kosovo.org/soediv.htm> (last visited Feb. 25, 2004).

sprang up everywhere. Private entrepreneurial energy created an internet backbone whose revenues are growing at rates of 250% per year, and which operates one of the most advanced wireless backbones in the world. Local places providing lodging and recreation such as swimming pools and hotels catering to internationals are numerous and profitable. But most entrepreneurs channel their energy into trade rather than manufacturing or service undertakings attracting foreign exchange. Individual Kosovars wanting to start a business do not know how to do so and do not have a place to go to get basic advice. Only sporadic organized efforts inform outside investors about investment opportunities in Kosovo.<sup>37</sup>

Neither the international community nor local economic and political leaders have articulated an overall vision for self-sufficiency in Kosovo.

Part of the problem is that the international community, especially UNMIK and the World Bank, wasted too much time wringing their hands over whether UNMIK's mandate under Resolution 1244 and the World Bank's Charter permitted either of them to take action necessary to stimulate local economic development. The answer is clearly "yes" with respect to Resolution 1244 under the Political Trustee concept.<sup>38</sup> Now, the World Bank has figured out a way to channel assistance through UNMIK.<sup>39</sup>

Serious progress on the economic front in Kosovo requires a rapid and successful privatization of SOEs and implementation of a more robust plan for publicly owned enterprises. But more importantly, it requires an initiative for development of SMEs that

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<sup>37</sup> The KTA has presented several "Invest in Kosovo" conferences in Frankfurt, London, and New York. Regrettably, the expanded role for the Kosovo Chamber of Commerce that the Author advocated in his 2001 article has not occurred in any meaningful way. See Perritt, *Stabilizing Kosovo*, *supra* note 24, at 37-38.

<sup>38</sup> See Perritt, *Structures of Political Trusteeship*, *supra* note 1.

<sup>39</sup> A 2002 report explains how the World Bank can provide financial and technical support by channeling it through UNMIK, even though its charter would not permit direct grants to the government of Kosovo. World Bank, *Kosovo, Federal Republic of Yugoslavia: Transitional Support Strategy*, Report No. 24275-KOS, para. 26 (July 2, 2002) [hereinafter *Transitional Support Strategy*] (discussing the International Development Association ("IDA") grants to UNMIK, a subsidiary of a public international organization, permitted by article V(2)(c) of IDA's Articles of Agreement), available at [http://www.seerecon.org/kosovo/documents/wbtss\\_kosovo.pdf](http://www.seerecon.org/kosovo/documents/wbtss_kosovo.pdf).

can provide jobs, achieve import substitution, and, eventually, earn foreign exchange. Success with privatization and SME development requires a clearer macroeconomic vision, a stronger sense of where comparative advantage lies for Kosovar industry, and the development of a richer array of financial intermediaries, including small business assistance entities, more transactional lawyers, professional education tracks, targeted investment funds, and possibly stock market and futures exchanges. It also requires progress on final status.

#### 4. SECURITY COUNCIL RESOLUTION 1244 AS A ROADBLOCK

Creating acceptable conditions for private investment was an essential part of nation-building in Kosovo from the outset. UNMIK was slow to accept this responsibility for two reasons. First, many observers of Kosovo thought that investment and private sector engagement had to wait for a comprehensive rule of law and market-oriented political institutions to be established. That was a mistake; nothing will ever be fixed if the private sector or policymakers wait for these changes before beginning economic development efforts. Instead, economic development must be integrated with building a rule of law, and both must proceed in tandem. That should have been the case in Kosovo from the end of the war, but, regrettably, economic development has always had a lower priority than UNMIK consolidation, war crimes investigations, organizing elections, and facilitating interethnic cooperation.

Second, UNMIK's lawyers misinterpreted Resolution 1244 so as to limit UNMIK's power over the factors of production in Kosovo. They interpreted the explicit reference in the preamble of Resolution 1244 to the continued sovereignty of the FRY over Kosovo as a limitation on any change in property interests. That refusal to allow UNMIK to alter property interests and the resulting uncertainty created negative consequences for investors.

The acknowledgement of sovereignty in the preamble was not a legal barrier to thoroughgoing U.N. efforts to rationalize the Kosovar property regime. While Resolution 1244 acknowledges FRY sovereignty, it also grants plenary powers of "civil administration" to the U.N. In addition, it explicitly authorizes the U.N. to transfer these powers to local provisional authorities and ultimately to institutions created or provided for in the eventual political settlement.

#### 4.1. UNMIK, as a Trustee, Has Broad Powers

UNMIK should be understood as a political trustee<sup>40</sup> for Kosovo, exercising most of the important attributes of sovereignty on behalf of the people of Kosovo. UNMIK has the same power over property as a common law trustee,<sup>41</sup> and also has authority to transfer these powers to interim governmental entities, private investors, and institutions defined by the ultimate political settlement. The FRY has, at most, a defeasable reversionary interest,<sup>42</sup> which an ultimate political settlement might alter.<sup>43</sup>

Although there is no provision of Resolution 1244 that explicitly provides for termination of the U.N. trusteeship and the ultimate disposition of Kosovo, there is a pledge to respect the territorial integrity of the FRY for the duration of the trust.<sup>44</sup> There

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<sup>40</sup> In 1973, Allan Gerson developed the idea of trustee-occupant to explain the status of the West Bank. See Allan Gerson, *Trustee-Occupant: The Legal Status of Israel's Presence in the West Bank*, 14 HARV. INT'L L.J. 1 (1973) (submitting the concept of "trustee-occupancy" as a standard move reflective of the rights of Jordan and of the West Bank inhabitants, and descriptive of Israel's powers and responsibilities in administering that area). The concept of the "political trustee" used in this Article is an adaptation of the trustee-occupant concept, developed more fully in Perritt, *Structures of Political Trusteeship*, *supra* note 1.

<sup>41</sup> The analysis of common law trusts is adapted from material written by John M. Scheib, member of the Virginia and District of Columbia bars, for an earlier paper on U.N. administration of Kosovo. A trustee has the power to transfer trust property, even when a transfer cuts off reversionary interests, as long as the trustee exercises the power consistently with the terms of the trust and its purpose.

<sup>42</sup> Actually, it is not necessary to know the owner of the reversionary interest in order to understand the powers and duties of the trustee. As a trustee, the U.N. has similar powers to change laws and institutions as appropriate to pursue the goal of self-determination and economic growth. Such exercise of powers in pursuit of that goal will benefit the Kosovars, the beneficiaries of the trust.

<sup>43</sup> Resolution 1244, *supra* note 21, art. 11(e). Even if the identity of the beneficiaries of the trust is ambiguous, this does not invalidate the trust. Under the law of trusts, it is not necessary that the beneficiary be known at the creation of the trust. RESTATEMENT (SECOND) OF TRUSTS § 112 (1959). The beneficiary must be ascertainable when the trust is created, but that includes a beneficiary who is not yet ascertained or in existence at the time the trust is created. *Id.* cmt. c. Thus, the Kosovo beneficiary could be an existing state, such as Yugoslavia, or it could be a state that subsequently comes into existence, such as an independent Kosovo. Alternatively, one can conclude that the people of Kosovo are the beneficiaries of the trust, as suggested in the text, and that it is the reversioner and the transferee of legal title who is to be ascertained later. Under this interpretation, there is no difficulty with the identity of the beneficiary, and the above analysis, applying section 112 of the RESTATEMENT (SECOND) OF TRUSTS, is unnecessary.

<sup>44</sup> Resolution 1244, *supra* note 21, pmbl. ("Reaffirming the commitment of all Member States to the sovereignty and territorial integrity of the Federal Republic



is a further obligation, in Article 11(e) of the Resolution, for the trustee to facilitate a political process designed to determine Kosovo's future status, taking into account the Rambouillet accords.<sup>45</sup> Thus, the identity of the reversioner is an open question accompanied by a duty in the trustee to resolve that question, much like when a court holds property in trust until it can determine the rightful owner of the property, or when a common law trustee enjoys a power of appointment.<sup>46</sup>

In the meantime, as a trustee, UNMIK cannot waste the trust assets, must invest the asset prudently, and use reasonable care and skill to make the trust property productive.<sup>47</sup> Resolution 1244 includes authority for economic reconstruction and development;<sup>48</sup> UNMIK must work prudently to reconstruct and develop Kosovo's assets, including its real property. Like any trustee, UNMIK may sell trust property for the benefit of the trust and its beneficiary;<sup>49</sup> it can privatize industries and otherwise make transfers of property to facilitate economic development.

These trust concepts are not unique to the Anglo-American legal tradition. Indeed, many scholars assert that Roman, German, and Islamic legal traditions embodied trust concepts even before they arose in England.<sup>50</sup>

#### 4.2. *Displacing Discriminatory Property Law*

Resolution 1244 empowers UNMIK to displace discriminatory laws and those inconsistent with international human rights principles. A series of discriminatory laws enacted by the FRY after 1989, including the alteration of traditional "social ownership" of many enterprises, cloud property ownership in Kosovo.<sup>51</sup> Beginning in 1989, Slobodan Milosevic accelerated his

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of Yugoslavia and the other States of the region, as set out in the Helsinki Final Act and annex 2 . . .").

<sup>45</sup> *Id.* art. 11(e).

<sup>46</sup> RESTATEMENT (SECOND) OF TRUSTS § 21 (1959).

<sup>47</sup> *Id.* § 181.

<sup>48</sup> Resolution 1244, *supra* note 21, art. 11(g).

<sup>49</sup> RESTATEMENT (SECOND) OF TRUSTS § 190(b) (1959).

<sup>50</sup> See Avisheh Avini, *The Origins of the Modern English Trust Revisited*, 70 TUL. L. REV. 1139 (1995) (discussing several theories concerning the origins of trusts); Thomas B. Lemann, *Trust: A Common-Law Institution in a Civilian Context*, 8 TUL. EUR. & CIV. L.F. 53 (1993).

<sup>51</sup> See generally DEP'T OF HUMAN RIGHTS AND RULE OF L., ORG. FOR SECURITY AND CO-OPERATION IN EUROPE, PROPERTY RIGHTS IN KOSOVO 3 (2002-2003)

efforts to displace Kosovar Albanian control over state and social property (two distinct categories) in Kosovo, shifting control to Serbian and foreign ownership, often through integration of Kosovar and Serbian enterprises. The result was Serb, French, and Italian ownership of many facilities and buildings that were needed to establish public functions and major enterprises. The U.N., by initially recognizing Yugoslav law as of March 1999, appeared to recognize these ownership interests.<sup>52</sup> In early December 1999, however, UNMIK promulgated Regulation Number 1999/24, repealing its initial determination to apply Yugoslav law that was in effect in June of 1999, substituting instead UNMIK regulations as primary law, with Yugoslav law that was in effect as of 1989 as a fallback.<sup>53</sup> The applicable-law regulation permits judges and other persons responsible for interpreting law to apply post-1989 law when it is not covered by UNMIK regulations or pre-1989 law and is "not discriminatory."<sup>54</sup> In the case of privatization, the proviso permitting application of post-1989 law is inoperative, because UNMIK's privatization regulations<sup>55</sup> occupy the field. There is, therefore, coverage by UNMIK regulations, and the predicate "not covered by UNMIK regulations" is not satisfied.

Invalidating the discriminatory property laws is an example of the kinds of powers that should have been exercised aggressively by the political trustee, recognizing such powers as entirely faithful to the duties imposed by Resolution 1244.

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(describing the peculiarities of the property rights regime in Kosovo, including emphasis on "use" rather than full ownership; lack of clarity in social ownership concepts; unrecorded informal transfers by Albanians during periods of discrimination; and complex conflicts between UNMIK regulations and pre-1989 Yugoslav law), at [http://www.osce.org/kosovo/documents/reports/property/property\\_report\\_eng\\_20030619.pdf](http://www.osce.org/kosovo/documents/reports/property/property_report_eng_20030619.pdf) (last visited Feb. 25, 2004).

<sup>52</sup> UNMIK Regulation 1999/1 § 3 (July 25, 1999), available at <http://www.unmikonline.org/regulations/1999/reg01-99.htm>, repealed by UNMIK Regulation 1999/24, *supra* note 32, § 1.1.

<sup>53</sup> UNMIK Regulation 1999/24, *supra* note 32, § 1.1.

<sup>54</sup> *Id.* § 1.2.

<sup>55</sup> UNMIK Regulation 2002/12 (June 13, 2002) available at [http://www.unmikonline.org/regulations/2002/Re2002\\_12.pdf](http://www.unmikonline.org/regulations/2002/Re2002_12.pdf); UNMIK Regulation 2002/13 (June 13, 2002), available at [http://www.unmikonline.org/regulations/2002/RE2002\\_13.pdf](http://www.unmikonline.org/regulations/2002/RE2002_13.pdf).

## 5. THE MACROECONOMY

Two unusual features support Kosovo's economy: 1) expenditures by the international community and 2) remittances by Kosovars working in other countries. In 2003, Kosovo's GDP was \$2.16 billion, or \$1,122 per capita. The real GDP growth rate was 7.4% in 2002 and projected to be 4-5% in 2003.<sup>56</sup> Consumption was 126% of GDP and investment was 38% of GDP, down from 45% of GDP in 2002. Exports and imports of goods and services were 12.3% and 88.7% of GDP, respectively. Net transfers from abroad were 22.3% of GDP from private sources and 41.7% of GDP from public sources. The 22.3% was almost entirely remittances from Kosovars living outside Kosovo.<sup>57</sup>

The World Bank and the IMF observe that the Kosovo economy must be prepared to absorb the impact of declining outside investment and declining expatriate expenditures in Kosovo.<sup>58</sup> The IMF projects that foreign transfers will fall from 67% of GDP in 2001 to 15-20% of GDP in 2004.<sup>59</sup> The difference must be made up by increased domestic production.

International institutions hire Kosovars and pay them higher salaries than they can earn in domestic activities. The vast majority of young professionals work for international institutions, as opposed to working for the local governmental institutions or striking out on their own in private business or professional services.<sup>60</sup> In addition, international institutions are paying for

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<sup>56</sup> 3 U.N. Development Programme & U.S. Agency for International Development, *Kosovo Early Warning Report*, at 3 (Jan.-Apr. 2003) [hereinafter *Early Warning Report*], available at [http://www.kosovo.undp.org/Projects/EWS/ewrn3\\_eng.pdf](http://www.kosovo.undp.org/Projects/EWS/ewrn3_eng.pdf).

<sup>57</sup> *Transitional Support Strategy*, *supra* note 39, Annex I. The remittances represent part of the flow from the Kosovar Diaspora that provides special opportunities for financial intermediaries to steer savings into productive investment opportunities.

<sup>58</sup> Present levels of 10,000 UNMIK staff, 5,000-10,000 expatriates working for other inter-governmental organizations ("IGOs") and non-governmental organizations ("NGOs"), and 40,000 NATO-led Kosovo Forces ("KFOR") troops will decline, as will foreign transfers. DIMITRI G. DEMEKAS ET AL., *KOSOVO: INSTITUTIONS AND POLICIES FOR RECONSTRUCTION AND GROWTH* 7, 14 (2002). 50,000 expatriates presently in Kosovo and donor support of \$500 million—half of gross domestic product ("GDP")—in 2001 will decline to half that level in 2003, when expatriate presence also is reduced. *Transitional Support Strategy*, *supra* note 39, at 3, 5.

<sup>59</sup> DEMEKAS, *supra* note 58, at 14.

<sup>60</sup> A December 2002 labor market survey showed, however, that only 67% of those employed were working in the private sector and agriculture, while 29%

much of the infrastructure investment. Road signs are all over Kosovo identifying the donor who paid for a particular road improvement. Any plan for the Kosovo economy must specify how these sources of national income will be replaced as the international community withdraws and reduces its financial commitment, as is already beginning to occur. Continuing to work as a lawyer or an economist for a nongovernmental organization ("NGO"), intergovernmental organization ("IGO"), or the offices of foreign state is not likely to prove a very good career plan for many Kosovars. What else will they do?

Stimulating SME development and accelerating privatization are important for the creation of jobs. But enterprise formation and restructuring require capital, which requires savings, which requires income.

That means, in the short run, that the economic development plan for Kosovo must encourage those working for international institutions to save significant parts of their salaries. It also means that other streams of income from abroad must be identified and examined to exploit potential for savings.

The other source of international income, which may or may not be temporary, comprises remittances—money sent home by Kosovars working in other countries. Remittances usually are paid to family members and are extremely difficult to value because of the absence of a banking system in Kosovo until recently and the tendency for remittances to be paid in cash or in kind.

A rough estimate is useful. There are about 600,000 Kosovars living abroad. If one assumes that half of these earn compensation at an average of \$25,000 per year and send 25% of that home, that amounts to \$1.8 billion per year in remittances. The population in Kosovo is about 1.8 million, so the figure translates into \$1,000 per capita in additional national income.<sup>61</sup>

### 5.1. Labor Markets

Even if Kosovo does not establish a strong enough economy to make up for the departure of the internationals, supply and demand in international labor markets will produce an equilibrium. Those Kosovars who are younger, better trained, and

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were working for SOEs, public enterprises, and the government. *Early Warning Report*, *supra* note 56, para. 8.

<sup>61</sup> World Bank and IMF figures estimate remittances to be about 20% of this amount. *Transitional Support Strategy*, *supra* note 39, Annex I.

capable of speaking English, German, or French will take jobs outside the country and will bid down their wage demands until they get jobs. That will tend to increase per capita income for those remaining in Kosovo in two ways: 1) by reducing the population remaining in Kosovo and 2) by increasing the flow of remittances.

But depopulation, especially in the form of a "brain drain," is not an attractive scenario. Moreover, the possibility of more Kosovars going to other countries to work depends on the willingness of other countries to accept them. Throughout the 1990s, the Milosevic apartheid created conditions that qualified many, if not most, Kosovars seeking work elsewhere for asylum. Now, and in the future, asylum abroad will be much harder to get, and there is no guarantee that countries with good jobs will throw open their doors to immigration by Kosovars seeking those jobs.

### 5.2. *Savings and Investments*

The second set of macroeconomic questions has to do with the level and nature of savings and investment. Anecdotal evidence suggests that the savings rate for Kosovar Albanians is relatively high.<sup>62</sup> The level of savings available for domestic investment, however, is another question. Much of the domestic savings may go to other countries for safekeeping against possible future economic or political upheavals or be held in the form of cash. Neither cash nor foreign bank accounts are available for domestic investment.<sup>63</sup> On the other hand, the experiences of ProCredit Bank (formerly Micro Enterprise Bank or "MEB")<sup>64</sup> and Reifessen Bank (formerly the American Bank in Kosovo or "ABK") suggest that when trustworthy savings institutions are established and promoted effectively, Kosovars are willing to put their money in such domestic institutions, which then channel it into productive investment.

Questions also exist as to how much of the actual domestic

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<sup>62</sup> The formal World Bank and IMF figures are not very helpful in quantifying savings because consumption exceeds GDP. See generally *Transitional Support Strategy*, *supra* note 39.

<sup>63</sup> Cash, of course, may be invested in family enterprises.

<sup>64</sup> As of December 2002, the Micro Enterprise Bank ("MEB") claimed to have banking relationships with 50% of Kosovar households. MICRO ENTERPRISE BANK, MEB/PROCREDIT MANAGEMENT REPORT 4 (2002) [hereinafter MEB/PROCREDIT MANAGEMENT REPORT], at [http://www.procreditbank-kos.com/pdf/MEB\\_Management\\_Report2002.pdf](http://www.procreditbank-kos.com/pdf/MEB_Management_Report2002.pdf) (last visited Feb. 25, 2004).

investment is productive in terms of the capacity to produce future income. Capital market institutions and other business formation services are almost entirely lacking, and that makes it less likely that the available savings will be channeled into productive investment. Anyone who has driven around Kosovo realizes that an enormous fraction of total investment is going into the construction of large, detached houses. Based on anecdotal evidence, including personal conversations by the Author, many of the builders of these houses have vague notions that some sort of business will occupy the first floor.

Any modern economy relies on its pension system as an important source of savings. UNMIK has established the basic structure for a pension system in Kosovo.<sup>65</sup> The investment policy expressed in the UNMIK regulation allows pension trust funds to be invested domestically only in registered securities.<sup>66</sup> Pension payroll taxes will begin to produce efficient savings that can be channeled into productive domestic investment as Kosovo capital markets mature, depending on the investment policies of the pension fund managers. The content of these pension administration policies has enormous implications for economic development in Kosovo.

Much controversy surrounds the decision of the pension program administrators to invest pension plan assets outside of Kosovo. The decision was engendered by the absence of any financial markets institution within Kosovo that would permit investment in Kosovar enterprises while maintaining prudent diversification. The existence of some kind of investment fund, or at least a stock market, offering shares or holding interest in private Kosovar enterprises would facilitate keeping some pension plan assets inside the country, adding to the savings available for productive investment.

Similarly, ProCredit Bank has been criticized for obtaining far more in deposits from Kosovars than it loans to Kosovar

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<sup>65</sup> See UNMIK Regulation 2001/35 (Dec. 22, 2001) (establishing the pension system in Kosovo), available at <http://www.unmikonline.org/regulations/2001/REpercent202001-35.pdf>.

<sup>66</sup> See *id.* § 10.4 (listing allowable pension asset investments). The regulation explicitly prohibits investment of pension fund assets in: 1) securities that are either unlisted or not publicly traded, 2) assets not capable of alienation, 3) derivatives, and 4) real estate or physical assets not listed on organized markets and for which valuation is uncertain. *Id.* § 10.8.

enterprises, investing the rest outside the country.<sup>67</sup> ProCredit Bank itself, however, reports rapidly increasing domestic loan volumes and describes major success stories of Kosovar businesses in which it has invested.<sup>68</sup>

The ABK (now "Reiffeisenbank") told the Author in 2003 that its loan-to-deposit ratios are close to 100%, but ABK sources report that the money available for investment exceeds the number of good business plans that are presented to lending institutions.

Many Kosovar business professionals identify the tariff structure as a significant impediment to developing viable business models. Raw materials and machinery are taxed at 25-26% (10% tariff plus 16% value added tax ["VAT"]). Finished goods come in through Serbia and Montenegro with no tax at all because these are not designated "borders." This squeezes margins for Kosovar manufacturers to the vanishing point. Fixing the situation does not require policymakers to embrace a protective tariff policy; it simply requires reducing import barriers for raw materials and machinery. There was a proposal before the Economic and Fiscal Council<sup>69</sup> to reduce the tariff for machinery to zero, but the World Bank vociferously opposed this and, in the end, prevailed. Economists argue that both the import duties and the VAT provide a level playing field for domestic Kosovar producers. A producer must pay a VAT on raw materials and capital goods, but receives credit for this VAT when remitting a VAT charge to its customers.<sup>70</sup>

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<sup>67</sup> The audited financial statements for the bank for 2002 show a loan to deposit ratio of less than 10%. See MICRO ENTERPRISE BANK, MEB/PROCREDIT ANNUAL REPORT, 22 (2002), at [http://www.procreditbankkos.com/pdf/MEB\\_Audit\\_Report2002.pdf](http://www.procreditbankkos.com/pdf/MEB_Audit_Report2002.pdf) (last visited Mar. 2, 2004). Thirty-one percent of the loans were to the service sector, 53% to the trading sector, 11% to manufacturing, less than 0.5% to agriculture, and 5% to private individuals. *Id.* at 33.

<sup>68</sup> MEB/PROCREDIT MANAGEMENT REPORT, *supra* note 64, at 4.

<sup>69</sup> UNMIK Regulation 2002/10 (May 6, 2002) (establishing the Economic and Fiscal Council ("EFC") as an advisory body to the Special Representative of the Secretary General ("SRSG")), available at [http://www.unmikonline.org/regulations/2002/RE2002\\_10.pdf](http://www.unmikonline.org/regulations/2002/RE2002_10.pdf). The following comprise the membership of the EFC: the Special Representative of the Secretary-General (Chairman), the Principal Deputy Special Representative of the Secretary-General, the Deputy Special Representative of the Secretary-General for Civil Administration, the Deputy Special Representative of the Secretary-General for Economic Reconstruction, the Prime Minister, the President of the Assembly of Kosovo, the Minister of Finance and Economy, the Minister representing the Kosovo Serb community, and another Minister nominated by the Prime Minister and confirmed by the SRSG. *Id.* Annex.

<sup>70</sup> For example, suppose a trading company pays 100 euros for raw materials

Import duties provide a level playing field because everyone is taxed at the same rate. A Croatian milk producer pays 10% import duty on the total price of its milk, which includes capital costs. A Kosovar milk producer pays 10% on its capital goods, placing them in the same position. However, Kosovars argue that they are still at a disadvantage because of the long period of neglect of capital assets, combined with wartime destruction, meaning that they must rebuild their capital base and thus end up paying more in duty. Perceived inequities also may result from producers who buy in the formal sector, and thus pay tax, but sell in the informal sector. These producers do not collect tax, or their operations in the informal sector deprive them of the necessary documentation to receive credit for VAT paid. Kosovar producers also receive a rebate on import duties when they export. Proposals to reduce the import duty substantially, across the board, are under consideration.

Momentum is building to develop a "Balkans without borders" through a set of bilateral agreements that would eliminate tariffs for trade within the Balkans. A free trade zone would permit trade and investment patterns to be developed according to the wishes of entrepreneurs and natural relationships. This, more than any likely formal economic or political structures, would permit Albanians in various political territories to forge close relationships with each other. It is important to understand, however, that negotiation of a free trade area agreement for the Western Balkans may be a mixed blessing. While it will open up markets for finished goods to large Albanian populations in Albania, Macedonia, Serbia, and Montenegro, other results may make matters worse. Finished goods are more likely to come from within the region covered by a free trade agreement, while raw materials such as petroleum and machinery are more likely to come from outside the region and, therefore, from outside any free trade area.

## 6. MICROECONOMICS

In the absence of a macroeconomic vision, it is difficult to be specific about what forms of enterprise creation are most likely to produce a sustainable economy. It is clear that Kosovo's economy

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and sells the materials for 200 euros. It pays 16% value added tax ("VAT") on the raw materials, or 16 euros. It collects 16% VAT on the products it sells, or 32 euros. It remits only the difference—16 euros—to the taxing authority.



will flourish in the aggregate only if it produces a substantial and reliable stream of foreign exchange. In other words, Kosovo must be in a position to export goods and services.<sup>71</sup> This is only possible in those sectors where it has a comparative advantage.

This is only one aspect of an essential tailoring of economic development policy to the unique circumstances and experiences of the target territory and population:

[T]here is growing evidence that desirable institutional arrangements have a large element of context specificity, arising from differences in historical trajectories, geography, political economy, or other initial conditions. . . . In the words of Douglass North: "economies that adopt the formal rules of another economy will have very different performance characteristics than the first economy because of different informal norms and enforcement."<sup>72</sup>

#### *6.1. Which Sectors Are Most Likely To Be Viable?*

One can begin an analysis of viable sectors by stepping through the obvious possibilities. The mining sector is one candidate, although it would require large-scale foreign investment. Kosovo historically was a source of raw materials for the rest of Yugoslavia, but its proven reserves for many minerals such as nickel have been nearly exhausted. On the other hand, Kosovo has substantial lignite reserves, with extraction costs estimated to be less than one-third of the level in Bulgaria, the next most attractive source. Its mining facilities, however, are obsolete and inefficient, and some of the largest mines—for metals, not lignite—are the subject of potentially violent conflicts between Serbs and

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<sup>71</sup> In the near term, Kosovo's economic situation can be improved by developing productive enterprises that provide import substitution, especially in food and building materials.

<sup>72</sup> DANI RODRIK ET AL., INSTITUTIONS RULE: THE PRIMACY OF INSTITUTIONS OVER GEOGRAPHY AND INTEGRATION IN ECONOMIC DEVELOPMENT 22 (Int'l Monetary Fund, Working Paper No. WP/02/189, 2002) [hereinafter RODRIK, INSTITUTIONS RULE] (quoting Douglass C. North, *Economic Performance Through Time*, 84 AM. ECON. REV. 359, 366 (1994)).

Albanians.

Even though Kosovo once exported electricity, the current poor state of its electricity-generating and distribution systems dims hopes that this is a sector for the future. Some analysts and policymakers favor the idea of a seven- to ten-year concession for an outside investor who could rehabilitate lignite mining facilities, build new high-efficiency generating plants, rehabilitate electric distribution lines running to Montenegro, Serbia, and Macedonia, and earn a good rate of return by exporting electricity. The political risk of this plan would be greatly reduced by the realization of a plan to build a spur from a new 400 kilovolt-amps ("KVA," equivalent to kilowatts) distribution line from Tirana to Podgorica, the capital of Montenegro, that would tie Kosovo's electric grid into the larger European grid through Albania. This would permit it to import and export electricity according to seasonal variations in supply and demand, without being at the mercy of political vicissitudes in Serbia, Montenegro, or Macedonia. The mining, generating-plant, and distribution-line rehabilitation costs could amount to \$1 billion.

This approach is superior to mining the lignite and simply shipping it out of the country because the rights of way and some of the physical structures for electric distribution already exist and merely need to be upgraded. In contrast, it would be necessary to build a new railroad or road almost from scratch to transport the lignite itself. Unfortunately, the European Union has blocked a USAID initiative to finance a management contract for KEK that would permit implementation of this approach.

In telecommunications, Kosovo has no more strategic advantage than any one of a number of places. Kosovo does not have an attractive telecommunications infrastructure, except for the broadband wireless network built by Internet Project Kosovo ("IPKO"). The IPKO network is oriented toward domestic telecommunications and is not designed as a transit network for international communications.

Food, lodging, and entertainment certainly are possibilities. Kosovars have proven their capacity to establish restaurants. The food and service are much better than elsewhere in central, eastern, and southeastern Europe, but this sector does not generate any foreign exchange in the absence of tourism to make up for a declining international presence. The attention drawn to Kosovo in recent years, as well as its beauty as a former outpost of the Ottoman Empire and its mountains, could attract some foreign

tourists, but only if investment is attracted for that purpose. Additionally, these tourist attractions must be marketed effectively in order to be successful.

Agriculture will require much work to become competitive because of the primitive character of most of the farms, which are very small and located in villages with very poor infrastructure. However, many observers think that white wines<sup>73</sup> and potato products hold promise for exports.

Manufacturing is a possibility for any economy, as long as telecommunications and transportation infrastructures are sufficient to support it, and as long as an appropriately skilled workforce with a good work ethic is available. Because Kosovo has at least two of these prerequisites (skilled workforce and telecommunications), wood processing, lumber construction materials,<sup>74</sup> metalworking, and textiles and garment making<sup>75</sup> can eventually penetrate export markets. Its internet protocol ("IP") telecommunications infrastructure, based on the IPKO wireless data network, is world-class. Its workforce is energetic, self-reliant, and may have the skills for many manufacturing jobs. The transportation infrastructure, on the other hand, is terrible. The country has only one airport, near Prishtina, its rail system has barely begun to operate again along a few routes, and its roads are in marginal condition, although much improved since the war. One of the most useful transportation infrastructure projects, a good highway between Prishtina and Dures, Albania (a seaport), has not begun, due to a combination of passivity by local political leaders and concerns of the international community that this would tie Kosovo too closely to Albania. Building this highway should receive much greater priority.

Some entrepreneurs envision Kosovo building professional service firms that would deliver their services over the internet. Kosovo's comparative advantage is significant because of its high literacy rates. Also important is the number of its young people that have studied outside the country, learned major foreign languages, and picked up competitive professional skills in law,

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<sup>73</sup> There is a modern winery near Gjakova. As well, dairy products, egg production, and animal feed for dairy and egg production could provide significant import substitution.

<sup>74</sup> Some people think that timber production would take a long time to begin because most of the timber is on state-owned land.

<sup>75</sup> This sector can be efficient only if successful privatization occurs.

economics, architecture, and technology. It is possible that high-tech incubators could accelerate the formation of such professional service firms.

### 6.2. *The Role of SMEs*

In the first conversation the Author had with senior officials of the Interim Government of Kosovo in 1999, he urged emphasis on small and medium enterprise development as the only practicable way to create jobs.

The Bologna Charter 2000 on SME Policies, adopted by representatives from forty-seven countries meeting under sponsorship of the Organisation for Economic Co-operation and Development ("OECD"),<sup>76</sup> recognized that "entrepreneurship and a dynamic SME sector are important for restructuring economies and for combating poverty."<sup>77</sup> It recognizes that SME competitiveness would benefit from a regulatory environment that does not impose undue burdens on SMEs, education that fosters an innovative and entrepreneurial culture, and effective access to financial services, "particularly to seed, working (sic) and development capital."<sup>78</sup> In particular, it recommended that "financial barriers to innovation in SMEs be reduced by: i) facilitating the development of market mechanisms for equity financing, and related services, especially for innovative start-ups . . . ."<sup>79</sup> It further suggested that partnerships involving private actors, NGOs, and different levels and sectors of public administration could be helpful, and that self-help organizations such as business associations and technical assistance centers can foster international cooperation and partnership among SMEs and can improve access to information, financial and technological resources, and new markets.

Western Balkan countries, including Albania, Bosnia and Herzegovina, Croatia, the former Yugoslav Republic of Macedonia, Serbia, and Montenegro, adopted the European Charter for Small

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<sup>76</sup> Including the United States, the United Kingdom, France, Germany, Italy, Spain, the Netherlands, Slovenia, and Canada.

<sup>77</sup> ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT ("OECD"), Bologna Charter 2000: The Bologna Charter on SME Policies (June 15, 2000), available at [http://www.oecd.org/document/56/0,2340,en\\_2649\\_201185\\_1866232\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/56/0,2340,en_2649_201185_1866232_1_1_1_1,00.html).

<sup>78</sup> *Id.*

<sup>79</sup> *Id.*

Enterprises<sup>80</sup> at the Thessalonica Summit, in June 2003. Kosovo was not empowered to adopt the charter because Kosovo is not yet a state.

## 7. DEVELOPMENT THEORY

The economics profession has recognized that institutions matter in achieving a prosperous private sector.<sup>81</sup> Private initiative and incentives are important to economic growth in countries in transition.<sup>82</sup> Private entrepreneurial energy is unlikely in the absence of institutional underpinnings of market economies, including a clearly defined system of property rights, a regulatory means for curbing fraud and anticompetitive behavior, social and political institutions that limit risk and manage social conflicts, rule of law, and clean government.<sup>83</sup> Effective strategies "of institution-building must not overemphasize best-practice 'blueprints' at the expense of local experimentation."<sup>84</sup> Laws not only must be written, they must be "backed up by the use of sanctioned force."<sup>85</sup> In property reform, the key characteristic is "'control' rather than ownership . . . . Formal property rights do not count for much if they do not confer control rights."<sup>86</sup> Moreover,

[T]he quality of institutions trumps everything else. Once institutions are controlled for, integration has no direct effect on incomes, while geography has at best weak direct effects. Trade often enters the income regression with the "wrong" (i.e., negative) sign, as do many of the

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<sup>80</sup> THE EUROPEAN COMMISSION, EUROPEAN CHARTER FOR SMALL ENTERPRISES (June 19-20, 2000), available at [http://europa.eu.int/comm/enterprise/enterprise\\_policy/charter/charter\\_en.pdf](http://europa.eu.int/comm/enterprise/enterprise_policy/charter/charter_en.pdf). The charter commits signatories to ten principles: education and training for entrepreneurship, cheaper and faster start-up, better legislation and regulation, availability of skills, improving online access, getting more out of the Single Market, taxation and financial matters, strengthening the technological capacity of small enterprises, making use of successful e-business models and developing top-class small business support, and developing stronger, more effective representation of small enterprises' interests at the Union and national level.

<sup>81</sup> See Rodrik, *Institutions for High-Quality Growth*, *supra* note 2, at 4-5.

<sup>82</sup> *Id.* at 1.

<sup>83</sup> *Id.* at 2.

<sup>84</sup> *Id.* at 3.

<sup>85</sup> *Id.* at 4.

<sup>86</sup> *Id.* at 5.

geographical indicators. By contrast, our measure of property rights and the rule of law always enters with the correct sign, and is statistically significant, often with t-statistics that are very large.<sup>87</sup>

Deep cleavages along ethnic or income lines can impede political decisionmaking and implementation of formal political decisions to the detriment of economic development. The risk is "coordination failure in which social factions fail to coordinate on outcomes which would be of mutual benefit."<sup>88</sup> As Dani Rodrik writes, "healthy societies have a range of institutions that make such colossal coordination failures less likely. The rule of law, a high-quality judiciary, representative political institutions, free elections, independent trade unions, social partnerships, institutionalized representation of minority groups, and social insurance are examples of such institutions."<sup>89</sup> In other words, strategies for economic development focused on institution-building converge with strategies for developing liberal democracy.<sup>90</sup>

Moreover, institutionalist strategies connect nicely with the goal of building "rule of law," as long as "rule of law" is understood to encompass private law as well as public law—a framework for entrepreneurship as well as a framework for human rights.

## 8. PRIVATIZATION

Privatization is at the top of the list of most neo-liberal economic reformers. It took a long time to rise to the top of UNMIK's list, however. After much wrangling and delay, the frequently obstructionist legal advisors to the Special Representative of the Secretary General ("SRSG")<sup>91</sup> were finally

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<sup>87</sup> RODRIK, INSTITUTIONS RULE, *supra* note 72, at 4.

<sup>88</sup> Rodrik, *Institutions for High-Quality Growth*, *supra* note 2, at 10.

<sup>89</sup> *Id.*

<sup>90</sup> See FAREED ZAKARIA, THE FUTURE OF FREEDOM: ILLIBERAL DEMOCRACY AT HOME AND ABROAD 252 (2003); Perritt, *Structures of Political Trusteeship*, *supra* note 1.

<sup>91</sup> The SRSG is the head of UNMIK. Every well-informed observer of developments in Kosovo says that the local legal advisor to the SRSG is unaccountably obstructionist, making bizarre interpretations of Resolution 1244 and strained interpretations of the constitutional framework, in virtually every case taking positions that delay decisions, and impede economic development of,

persuaded, in 2002, to allow the establishment of a structure for privatization. This is reflected in UNMIK Regulation 2002/12, which transfers complete control over all of the assets of publicly owned and socially owned property to a new KTA, an agency independent of both UNMIK and local government institutions.<sup>92</sup>

The board of the KTA approved its operational plan on February 25, 2003, and identified six SOEs for tender, beginning the privatization process.<sup>93</sup> A four-month delay ensued, however, because UNMIK lawyers had further objections to necessary property rights transfers.<sup>94</sup> Privatization finally began, with bids received on an initial six SOEs by July 14, 2003. One hundred three bids were received, and another nineteen were due by August 2003, and bids were due on a third group by November 2003.

More than 130 million euros were bid in the second round of privatization, with approximately 23.6 million euros in commitments accepted.

Despite this promising start, a new Deputy SRSG from the EU, Nickolas Lambsdorff, upon arriving in Kosovo in October 2003, "froze" privatization because of concerns and confusion about legal immunity and claims by Serb interests that certain enterprises being considered for tender were not within the jurisdiction of the KTA because they had legally been transformed after 1989. It is unfortunate that this interruption occurred because it creates uncertainty likely to discourage investors. Mr. Lambsdorff appointed a new Managing Director of KTA, Marie Fucci, who insisted on uprooting the conceptually sound operational policies of KTA, and substituting policies that would discourage investment by saddling investors with the uncertain liabilities of SOEs. Local Kosovar governmental institutions opposed the Lambsdorff/Fucci blockages to privatization, pointing out that their positions conformed substantially with those of Serbia, which opposes privatization altogether.

The concept of Regulation 2002/12 is sound: it strips liabilities

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and transfer of further power to, local institutions.

<sup>92</sup> See UNMIK Regulation 2002/12, *supra* note 55 (describing the board of directors and its authority).

<sup>93</sup> Press Release, Kosovo Trust Agency ("KTA"), Approval of KTA Operational Policies Green Light for Privatisation to Begin (Feb. 25, 2003), at <http://www.kta-kosovo.org/ktapress/pr0022.pdf>.

<sup>94</sup> Of the first two groups of twenty-five SOEs, construction is the dominant sector (14 million euros in revenue), followed by consumer goods (5 million euros), tourism, and pharmaceuticals (1.5 million euros each).

from the assets of publicly owned and socially owned enterprises, thus allowing the assets to attract private investment capital, while the claims against those assets must be asserted before the KTA. Private investors acquire the assets of these enterprises by bidding in an open-tender process. The amount of the successful bid is paid to the KTA, which then holds those payments in trust for claimants. Conceptually, the KTA approach builds a wall between the assets and the investor, on the one hand, and the liabilities on the other. This is necessary in order to attract private investment to any of these enterprises because of the complexity of the claims.

The model resembles that used by the U.S. Congress to save the Northeast and Midwest railroads after bankruptcy proceedings proved inadequate. Under the Regional Rail Reorganization Act of 1973,<sup>95</sup> the United States Railway Association, roughly analogous to the KTA, decided which properties should be preserved for rail transportation and which need not be. The rail properties were conveyed to a new federally chartered private corporation, Consolidated Rail Corporation ("Conrail").<sup>96</sup> The other properties remained in the estates of the bankrupt railroads. The estates received stock in Conrail plus \$500 million in government-guaranteed bonds.<sup>97</sup> In subsequent litigation, the Supreme Court of the United States determined that no unconstitutional taking of property without just compensation had occurred because the estates were entitled to litigate the fairness of what they received for their property in the United States Claims Court. If that court determined the amount to be inadequate, it could award a deficiency judgment against the U.S. government under the Tucker Act.<sup>98</sup>

The Kosovo privatization process differs in two respects from the Regional Rail Reorganization process in the United States. First, the Rail Act covered only one industry; the Kosovo privatization process covers all SOEs. Second, the Tucker Act remedy against the U.S. government provided far more reliable compensation for any deficiency in value of properties than is present in the Kosovo privatization scheme. The U.N. has asserted

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<sup>95</sup> 45 U.S.C. §§ 701 *et seq.* (1973).

<sup>96</sup> The Author was a senior lawyer of Conrail from 1976-1981.

<sup>97</sup> See *Blanchette v. Connecticut Gen. Ins. Corp.*, 419 U.S. 102, 111 (1974) (describing the structure of the Rail Act).

<sup>98</sup> 28 U.S.C. § 1491 (1996). See generally *Blanchette v. Connecticut Gen. Ins. Corp.*, 419 U.S. 102 (1974).



immunity from any recovery. The local Kosovar government has uncertain creditworthiness. The uncertain nature of judicial remedies for inadequate compensation or other violations of rights associated with the privatization process is a further distinction.<sup>99</sup> Still, disputes are inevitable in any privatization or other corporate reorganization process. The designers of the privatization process for Kosovo recognized this reality and established the Special Chamber of the Supreme Court of Kosovo with exclusive jurisdiction to resolve these disputes. To avoid local bias, international judges decide cases filed in the Special Chamber.

The privatization process will unravel if lawsuits can be heard in national courts around the world. In September 2003, a breach of contract lawsuit arising out of privatization of an SOE was filed in a New York state court. It was subsequently removed to federal court, and the Author prepared an amicus brief on behalf of the Government of Kosovo, arguing that the United States District Court should dismiss the case on immunity or *forum non conveniens* grounds, since governmental immunity of UNMIK and KTA had been waived only to the extent of cases filed in the Special Court, which in any event is an adequate and exclusive forum.

Sorting out claims to state-owned enterprises in any socialist economy desiring to make a transition to a private market economy is complex, but complexity is greater in Kosovo than in states outside Yugoslavia. The socially owned property concept in Kosovo (as in other states of the former Yugoslavia) introduces uncertainties. Also, many property transfers occurred after 1989 under a series of discriminatory laws passed under the Milosevic regime, intended to dispossess Kosovar Albanians of property. Kosovars aggressively challenge the validity of these transfers. Other transfers after 1989 occurred "off the books," because Albanians were not permitted to be transferees under formal law. Sorting all this out could take years, if not decades, and will involve diplomacy and international politics as much as straightforward application of legal rules to properly recorded property claims.<sup>100</sup>

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<sup>99</sup> UNMIK Regulation 2003/13 (May 9, 2003), *available at* [http://www.unmikonline.org/regulations/2003/RE2003\\_13.pdf](http://www.unmikonline.org/regulations/2003/RE2003_13.pdf).

<sup>100</sup> Another difficulty is that Kosovar Albanians usually did not formally record property transfers during the period of Milosevic apartheid, so proving property ownership as between Albanian claimants is difficult.

The KTA concept appropriately separates the complexity of property claim resolution from privatization, but the soundness of the concept behind KTA is not enough. Many Kosovars—both ordinary people and political leaders—mistrust KTA. Some fear corruption. Some resent the fact that KTA's broad assertion of control over all property, including municipally owned property not directly associated with SOEs,<sup>101</sup> impedes SME development because it interferes with property transfers from municipalities, a power critics of KTA claim to be well within the powers of local government under the constitutional framework. There may be merit to the idea that municipalities should be allowed greater control over property they own, but it is difficult to separate SOE property from purely municipal property. Some central mechanism for sorting out the complexity was probably inevitable to push privatization along, especially since many municipal governments were slow to begin functioning at all.

Still others believe that KTA should obtain formal appraisals of the value of each enterprise before soliciting bids. This idea lacks merit because an appraised value is essentially worthless if no one will bid that much in an open-tender process. Moreover, under Yugoslav accounting practices, assets are not depreciated. Therefore, the book value of every SOE is vastly inflated.

Others want to make sure that employees of the SOE control the privatization process.<sup>102</sup> That idea is also a bad one because the employees naturally will prefer to maintain the maximum number of jobs and require potential investors to work with an unpredictable employee board that will discourage bids.<sup>103</sup> On the other hand, many managers and employees of SOEs have worked hard to develop commercialization and privatization plans on their own, often working for nothing. To remove them from the process now will engender considerable resentment. Their lack of

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<sup>101</sup> See UNMIK Regulation 2002/12, *supra* note 55, § 5.5 (“[T]he administrative authority of the Agency shall include . . . all Enterprises and assets within the scope of: . . . (b) UNMIK Regulation No. 2000/45 of 11 August 2000 on Self-Government of Municipalities in Kosovo . . .”).

<sup>102</sup> UNMIK Regulation 2003/13, *supra* note 99, entitles employees of an SOE to a priority 20% of the proceeds from the sale of shares in privatization of an enterprise. *Id.* § 10.

<sup>103</sup> The Pillar IV Analysis unit concluded, with respect to commercialization, that “wherever an elected workers’ council was in place, negotiations to lease the company were protracted and ultimately unsuccessful, with the workers predictably reluctant to relinquish control over the company to an external investor.” *The Ottoman Dilemma*, *supra* note 35, at 22.

cooperation informally may jeopardize successful privatization.

Still others want to begin the privatization process with the worst SOEs instead of the most promising ones. That would also be a bad idea. It is important to get the privatization process started as quickly as possible, and the best way to do that is to begin with the most promising enterprises. By any analysis, only the very best SOEs stand any chance of successful privatization.

Controversy also exists over how real property associated with the SOEs should be handled. Some legitimate fear exists that the KTA will allow ownership in real property to be transferred to investors who bid a low amount for an SOE, intending to shut it down and simply to trade the real estate.<sup>104</sup> Traditionally, in Yugoslavia, the state retained ownership of virtually all real property in urban and other industrialized areas. SOEs and others have a use right upon the real property for as long as they engage in productive economic activity. Many people think that merging the use right into fee simple ownership and transferring that to an investor gives the investor a windfall.

The most serious obstacle to privatization, however, is the illogical insistence by the head of the EU Pillar IV, Nickolas Lambsdorff, and his hand-picked Managing Director of KTA, Marie Fucci, on uprooting the conceptually sound operational policies of KTA and substituting a new scheme that would saddle investors with liabilities of SOEs.

Nevertheless, the importance of KTA may lie not so much in privatization of SOEs as in its power to clear clouds and conflicting claims to property that can be made available for new enterprise formation.

Recent reports by the analysis unit of the EU Pillar IV, responsible for economic development in Kosovo, say that the main impediment for new enterprise development is shortage of land near decent infrastructure. Such land is locked up in the SOEs. Privatization is necessary to unlock the land even if few SOEs are privatized as going concerns. According to this perspective, one of the purposes of privatization is to permit bidders to exploit the real property regardless of what they do with the other assets.

Privatization is necessary to remove obstacles to successful development of new private sector institutions. In the words of the

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<sup>104</sup> Most SOEs do not have value as going concerns; instead, they have value because they control real estate. *Id.*

EU Pillar IV's Economic Analysis Unit, "[i]f economic prosperity and job creation are critical to Kosovo's future, then the priority for the international mission is to break up these quasi-feudal estates [SOEs] and replace them with a fair and effective system of property rights."<sup>105</sup> The problem with the status quo is that defunct SOEs are informally controlling property and leasing it to those having political or personal ties with the SOE, while not accounting for the lease revenue or paying taxes on it. This behavior blocks access to real assets needed by investors, undermines certainty needed to attract investment, and erodes the tax base.

Economists and potential investors were concerned that KTA might react to concerns over SOE real property assets by giving investors only relatively short-term leases to the property on which machinery, equipment, and the building stand. Commercialization rules of KTA's predecessor, the Department of Trade and Industry, for example, allowed leases of only five or ten years in connection with investment incident to commercialization. A leasehold of ninety-nine years would be more appropriate and should satisfy the needs of legitimate new investors.<sup>106</sup> On May 9, 2003, UNMIK promulgated Regulation 2003/13, which provides that a transfer of an SOE-use right in the privatization process results in a ninety-nine-year lease, thus resolving this question, at least for the time being.<sup>107</sup>

Available data suggests that Kosovo has been substantially "deindustrialized" as industry built within the geographic framework of the former Yugoslavia has collapsed. Few SOEs have any promise of successful operation in a market economy.<sup>108</sup>

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<sup>105</sup> *Id.* at 6.

<sup>106</sup> For example, ninety-nine-year leases were common in the development of the railroad industry in the United States.

<sup>107</sup> See generally UNMIK Regulation 2003/13, *supra* note 99.

<sup>108</sup> European Stability Initiative, *Lessons Learned and Analysis Unit of the EU Pillar of UNMIK: De-industrialisation and Its Consequences: A Kosovo Story* (Mar. 2002), available at [www.esiweb.org/pdf/esi\\_document\\_ID\\_33.pdf](http://www.esiweb.org/pdf/esi_document_ID_33.pdf). No more than a few dozen of these enterprises—the vast majority in the manufacturing sector—can make anything the rest of the world wants at prices that will cover their costs and provide a return to investors. This ability is not an indictment of the skills or commitment of management and workers in these enterprises. The Author of this Article had the privilege of visiting six SOEs in late 2001 and was impressed with the cleanliness of the facilities, the willingness of the employees to work without pay to keep the machinery in good order, and the commitment of the managers to develop business plans and do whatever else was necessary to interest foreign investors. No doubt, some of these enterprises can be successfully privatized. But

Privatization has a larger role to play in shifting the focus to entirely new businesses to create new jobs and wealth.

#### 9. PRIVATIZATION IS NOT ENOUGH

Only the most optimistic projections would conclude that privatization of existing SOEs will generate enough jobs and production to assure a bright economic future for Kosovo.

What will take up the slack? Part of the problem, and part of the indictment of UNMIK's and the EU's stewardship on the economic front, is that no one knows. No good assessment has been made of the areas where Kosovars may have a comparative advantage in regional and world trade. No assessment of workforce skills and deficiencies has been done. Neither the international community nor local political institutions have produced an economic vision for the future.

The point is not to develop a central "plan" which then can be executed by the state; the point is to have a concrete scenario or scenarios that inform policymakers, entrepreneurs, and investors as to where they should place their bets. It is perfectly acceptable to have competing economic visions. It is a disappointment that the Kosovar political process has not produced that yet. Most Kosovar political reformers venture little beyond commitment to independence for Kosovo.

The engine of economic growth must be the private sector, acting through entrepreneurial energy, and investment targeted towards new enterprises.

#### 10. IMPROVING PUBLIC ADMINISTRATION

Many people identify indifference by the staff of public administration as an important barrier to enterprise formation and investment.<sup>109</sup> These are offices where business operators must get

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in many cases, probably the majority, enterprises were established to serve functions within intra-Yugoslavia trade patterns and had grossly inflated workforces as part of the socialist tradition. Others were established simply to artificially create jobs to quell social unrest or to discourage migration patterns not desired by policymakers.

<sup>109</sup> According to surveys of private business conducted by Riinvest in 2001 and December 2002, those doing business in Kosovo ranked the barriers as including, in descending order of importance: unfair competition, lack of laws, high taxes, access to finance, and administrative burdens. *Early Warning Report*, *supra* note 56, para. 14. Of those surveyed, 28% considered administrative burdens to be a "very large barrier" and a "large barrier," and 31.3% considered

export licenses, pay taxes, and register their businesses. Some Kosovars familiar with the business climate have said the most important thing that could be done is to conduct effective training in public relations and public service for the staff in public offices in municipal and national governmental agencies. Many senior governmental officials agree with this assessment, also noting that low salaries impair public employee morale. On the other hand, the Author and one of his students visited the business registration office in July of 2003, stating that they wanted to register a business. The Author noted they were treated courteously and efficiently, as well as in any major American city and better than many.

In addition to improving the attitudes of those who serve the public and the business community, comprehensive attention should be given to the regulatory environment for private business and to the urgent need for greater governmental transparency at all levels of government, especially at the UNMIK level.

#### *10.1. Regulatory Review*

Kosovo now has much of the traditional regulatory apparatus for financial institutions or capital markets. It has a board that can set accounting standards, which can be reinforced by legal obligations to report fully and accurately when one issues securities. It has the beginnings of a regulatory regime to regulate financial intermediaries and capital markets through its banking regulation and Banking and Payments Authority. The banking regulations channel the activities of key financial institutions: banks. Kosovo has addressed the operation of foreign entities in domestic markets through the foreign investment regulation, assuring them of non-discrimination. It has also provided for a central monetary authority. Kosovo has a real property registry, and "lenders are successfully pursuing claims in court that are secured by real property."<sup>110</sup>

Now, the tariff law needs to be re-evaluated and mechanisms for capital aggregation and other financial intermediation outside the banking and public sectors should be established. The KTA privatization fund should be invested, at least to some extent, in local SMEs. An investment fund may help make that possible by

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them to be a "medium intensity barrier." *Id.* para. 15.

<sup>110</sup> *Id.* para. 15(iv).

diversifying risk for KTA, and consideration should be given to amendments to the banking regulation that would keep more depositor capital inside Kosovo. Attention should be given to imperfections in the process of executing judgments of the Commercial Court—imperfections which impair the value of collateral for lenders.

Finally, a regulation should be drafted and promulgated to accommodate small investment funds resembling venture capital funds in the United States.

### *10.2. Government Transparency*

Greater transparency of regulation and government administration is an important priority. Lack of governmental transparency makes it easier for governmental officials to act arbitrarily and encourages corruption in the form of bribes for favorable treatment.

An essential attribute of the rule of law is being able to find out what the law is. When the law is secret, known only to a privileged few, entrepreneurs cannot conform their plans to legal requirements and, therefore, must give up their plans for running a business or take their chances on violating the law. Such a situation breeds economic passivity and indifference to the law.

Part of any system of rule of law should include a freedom of information act requiring every governmental authority to publish documents that express rules imposing duties on the populace and orders representing decisions in contested cases. In addition, such an act should entitle any person to make copies of other records, subject only to specific and narrow exemptions. These obligations should be enforceable in a court or other independent tribunal and should be supported by penalties against the agency and particular personnel, including penalties imposed through the personnel system of the agency.

The publication requirement should allow its duties to be satisfied either by ink-on-paper or electronic publishing. Ink-on-paper is often thought to be preferable to electronic publishing in a country in transition such as Kosovo, but, in fact, that usually is not the case. Ink-on-paper publishing involves delays associated with preparing camera-ready copy and the printing, binding, and distribution stages. Unless the society has a well-developed and reliable postal system, ink-on-paper publishing is unlikely to communicate broadly the existence or contents of a new legislative

or agency act.

Electronic publishing through the internet, on the other hand, happens immediately, as soon as the decision is made and a word processing document containing the legal text can be posted on a website. Space on a server to maintain the website need not cost more than a few hundred euros per year for the entire Kosovar government and UNMIK.

Internet penetration into homes and offices in Kosovo is low, but increasing. For those people who do not have their own points of access at home or in their offices, there is ready access to hundreds of internet cafés scattered all over Kosovo. It is as easy in an internet café to download and print new items of interest from an official electronic gazette as it is to go to a ministry and look at an official bulletin board.

Kosovo has a long way to go to establish real transparency, but not because the process is costly. For the first three years of its existence, UNMIK regularly and promptly published new regulations on its website in full text.<sup>111</sup> From January 2003 to June 1, 2003, however, UNMIK published nothing on the regulation section of its website, notwithstanding the fact that a very significant property regulation was issued in late April. There is no excuse for this. UNMIK should be an exemplar of the rule of law; while this may be difficult with respect to certain controversial issues relating to competence or tax policy, it is not difficult with respect to publishing its regulations. UNMIK should keep the regulations section of its website up-to-date.

Almost none of the provisional government institutions have websites. This glaring impediment should be corrected forthwith. It is important to understand that the internet permits decentralized publishing, agency by agency. It is better to have some governmental transparency than none at all, while an elaborate, centralized, official electronic gazette operation is put in place. For example, KTA finally has put together a reasonably good, basic website. It may be years before certain other ministries and UNMIK entities organize themselves for publication of their rules and orders on the internet. The pace of rule of law development should not be set by the slowest.

It also is imperative to avoid the usual temptation of setting up a state-granted monopoly for the dissemination of government

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<sup>111</sup> No electronic publishing aimed at improving governmental transparency is worthwhile unless it publishes the full text.



information, whether the monopolist is governmental or private. Indeed, an appropriate freedom of information act entitles alternative publishers of governmental information to obtain the information so that they can compete with any de facto monopolist.

Governmental transparency is necessary not only at the level of the central government, but also at the level of municipal government. This requires technical assistance, but the cost of the effort is modest.

The Freedom of Information Law adopted by the Assembly in the spring and summer of 2003 is well-drafted, and appropriately addresses the benefits of electronic access. It should be approved promptly by the SRSG, extended to UNMIK, interpreted broadly, and enforced vigorously.

### *10.3. Business Advocacy*

Legislative advocacy is an important feature of any liberal democracy. As political institutions develop in Kosovo, ensuring that narrow ethnic and extreme nationalist voices are not the only voices heard is important.

Given the slow pace of private sector economic development in Kosovo and the lack of governmental transparency and public services necessary to support it, organizing effective business advocacy is essential both to development of the private sector and to the development of the right kind of democracy.

Trade associations, such as a chamber of commerce, a small business association, and an association aimed at attracting foreign investment, should develop data showing why existing policy approaches are harmful and new proposals including the text of regulations and statutes. These associations then should develop relationships with politically influential persons in the parties, in the government, and in the assembly, as well as in UNMIK, and persuade political actors to embrace their proposals. The Kosovo Chamber of Commerce could take on such an advocacy role, but so far it has not done so with any vigor.

An effective business advocacy organization would consult regularly with business constituents, listening carefully to understand the problems they face. Such an organization would fight for easy access to business laws and other legal systems through some form of electronic database. It would have the capacity to do legal analysis aimed at explaining how best the

practices from other legal systems can be adapted to the needs of Kosovo businesses. Its staff would possess exemplary communication skills so they could develop materials persuading people of the merits of the association's position. Effective business advocacy for Kosovo must reach not only UNMIK, other international organizations playing a governmental role, and the indigenous institutions of provisional government; it must also include foreign governments and NGOs capable of applying pressure to domestic decisionmakers. Certain business advocacy associations also may wish to become involved in channeling campaign contributions to responsive political parties and candidates.

### 11. THE WEAK "MIDDLE"

Impediments to enterprise formation in the private sector include not only failures of vision and planning, governmental barriers, and obstacles to property reform, but also include a failure to take some fairly obvious and inexpensive steps to put entrepreneurs together with business opportunities, and investors together with entrepreneurs. The problem is in the "middle": Kosovo needs more financial intermediaries.

A 2002 World Bank report<sup>112</sup> noted positive developments in the creation of the Central Fiscal Authority, the Banking and Payments Authority, and functioning tax and customs administrations. Such institutions are necessary for economic recovery.<sup>113</sup> Next, the report said, Kosovo needs to establish an adequate business climate, concentrating on completion of a legal and institutional framework for commerce; development of an independent, professional, impartial, and multiethnic judiciary; provision of significant flows of financial intermediation for viable productive activity; and establishment of adequate systems of business support and information.<sup>114</sup> "Kosovo's financial sector is stunted by lack of confidence in banks; lack of trained, experienced managers and supervisors; and a weak legal framework for private business."<sup>115</sup> Financial intermediaries must be able to evaluate and price risk, allocate savings, finance investment, and enforce good

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<sup>112</sup> *Transitional Support Strategy*, *supra* note 39, at 3.

<sup>113</sup> *Id.*

<sup>114</sup> *Id.* at 5 (noting additionally that Kosovo should accelerate privatization).

<sup>115</sup> DEMEKAS, *supra* note 58, at 17.

accounting and management practices.<sup>116</sup>

The institutionalists in the economic profession<sup>117</sup> give insufficient attention to financial services intermediation. Not only are securities-market regulators such as the Securities and Exchange Commission ("SEC") necessary, so are institutions such as stock exchanges that permit entrepreneurs and investors to find each other and that provide a secondary market for securities. In addition, institutional arrangements that Americans often take for granted as naturally occurring in the private sector may be essential to realize the potential for private enterprise development and growth. A clear example is the debit and credit card system. The inability of consumers to use, and merchants to accept, credit and debit cards in Kosovo is a significant obstacle to growth in the retail and service sectors. For credit card use to become pervasive, institutions that market cards to consumers and to merchants must first exist. Often, these are different institutions. In addition, inter-bank clearing networks are necessary. Credit bureaus must also exist to maintain easily accessible databases on the creditworthiness of potential cardholders and card-accepting merchants.

It is not likely that political trustees or local governmental institutions should themselves establish these intermediaries as governmental enterprises. Instead, they should understand that a goal of economic development is the creation and management of such institutions; in addition, political trustees must pursue legal and macroeconomic policies to remove disincentives to establishment of such institutions by private entrepreneurs.

Considerable progress has occurred in the banking sector.<sup>118</sup> On January 12, 2000, MEB (now "ProCredit Bank")<sup>119</sup> became the first bank licensed by the Banking and Payments Authority of Kosovo ("BPK") in post-conflict Kosovo.<sup>120</sup> ProCredit Bank now

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<sup>116</sup> *Id.*

<sup>117</sup> See *supra* Section 7 (discussing development theory).

<sup>118</sup> But see *Early Warning Report*, *supra* note 56, para. 15(iv) (noting that short-term bank loans from Kosovo banks are "usable only for cash flow and not for manufacturing businesses and investments").

<sup>119</sup> See ProCredit Bank website (describing the most successful bank in Kosovo in 2001, 2002, and 2003), at <http://www.procreditbank-kos.com/dev.php?qjuha=english> (last visited Feb. 25, 2004).

<sup>120</sup> See Internationale Micro Investitionen Aktiengesellschaft website (describing the history of MEB in Kosovo), at <http://www.imiag.de/projects/countries/KOSOVO/main.htm> (last visited Feb. 25, 2004).

has branches all over the country offering current account services, check cashing, interest-earning saving accounts, time deposits, debit cards, access to ATM machines, and domestic and international money transfers. BPK also introduced credit cards in February 2004.

ProCredit Bank offers easily accessible loans to small and micro enterprises at all its branches, initially making loans in amounts of a few hundred dollars, and now making loans of much larger amounts up to several hundred thousand dollars. Applicants' businesses must be within the bank's operational area, have existed for at least one year, and generate a regular cash flow.<sup>121</sup> The bank also issues letters of credit and bank guarantees.

In May 2001, the U.S. Agency for International Development ("USAID") established the Kosovo Business and Finance Fund (the "Fund") to aid SMEs in the manufacturing sector and to establish a bank. As a result, the Fund established the American Bank in Kosovo ("ABK"). In late 2001 or early 2002, the BPK stopped commercial banking and sold its branches to ABK. In December 2002, the Austrian bank, Raiffeisenbank bought a 76% ownership stake in ABK and rebranded it in May 2003.

The lending policies of ABK are typical of European banks, making loans from 5,000 euros to 500,000 euros, with larger amounts available on an exception basis. Loans of up to thirty-six months at interest rates of 14-15% are available, but shorter terms of twelve to eighteen months are more typical. Startups cannot get financing, but if an entrepreneur can find sufficient capital to operate for six months, his business becomes eligible for debt financing. The bank requires security of 150-200% of the loan value.

The bank sees two kinds of inadequate applications: Kosovars who have grandiose plans but do not understand the limitations of their hopes, and Kosovars returning from abroad expecting a U.S., German, or Swiss-level infrastructure and seeking to apply their business experience from more developed countries.

While the banking and legal systems have progressed, there is still a crippling shortage of intermediaries who can provide business formation assistance, legal assistance, and accounting services. There also is little in the way of startup capital

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<sup>121</sup> See Business Loans, Micro Enterprise Bank website (detailing the business loan practices of MEB), at <http://www.mebkosovo.com/services/loans.html> (last visited Feb. 25, 2004).

intermediation.

### 11.1. *Getting Started*

Many Kosovars have the desire and the financial wherewithal to start a small business, but do not know where to begin. There are few places they can go for advice on how to select the type of business or how to start it. A grant from CARE Nederland and Hivos started the Kosovo SME Support Center (the "Center") in Gjakova,<sup>122</sup> but it now struggles to continue operations based on fees. The Center services walk-up clients, but does not provide assistance to the agricultural sector, the service sector, or to startups because it does not believe they can obtain financing. The Kosovo Business Support ("KBS")<sup>123</sup> is a contract operation in Prishtina, funded by USAID. KBS has an even more limited role, excluding privatization, startups, services, and anything outside the manufacturing and production sector.

The Kosovo Chamber of Commerce could perform this function, however, its organizational efforts have been slow. Kosovo needs the equivalent of the American Small Business Administration, with local offices, including internet and paper publications with such titles as, "How to Start your Own Business."<sup>124</sup>

### 11.2. *Finding a Lawyer*

Kosovo needs more transactional lawyers who can help small businessmen get off to a good start. Apparently, only one or two legal practitioners in all of Kosovo have sufficient knowledge of both the 1989 Yugoslav law<sup>125</sup> and of UNMIK regulations, and the ability to speak English or another major foreign language.

Too much emphasis on reform of legal education and the legal profession is focused on human rights and criminal proceedings.

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<sup>122</sup> See CARE Nederland website (detailing the activities of CARE Nederland in Kosovo), at <http://www.carenederland.org/projecten/kos006.htm> (last visited Feb. 25, 2004).

<sup>123</sup> See Kosovo Business Support website, (listing the mission, history, and contact information of the Kosovo Business Support ["KBS"]), at <http://www.usaidkbs.com/default.htm> (last visited Feb. 25, 2004).

<sup>124</sup> See, e.g., United States Small Business Administration website, at [http://www.sba.gov/starting\\_business](http://www.sba.gov/starting_business) (last visited Feb. 25, 2004).

<sup>125</sup> This law applies in all cases except when it conflicts with international human rights law, or when it is preempted by UNMIK regulations.

Greater emphasis needs to be placed on commercial and business law and lawyering. The international community funds the Criminal Defense Resource Center to train and otherwise support criminal defense attorneys, but there is no equivalent support for developing transactional lawyer capability.<sup>126</sup>

One useful addition to the "middle" would be a small business assistance clinic operated jointly by certain local consulting firms, drawing on support from the law and economics faculties of the University of Prishtina, the Kosovo Chamber of Commerce, and the Ministry of Trade and Industry. Such a clinic would permit law and economics students, under appropriate supervision by professors and experienced practitioners, to assist would-be proprietors of SMEs in refining their business models, executing marketing research, developing business plans, determining the most important legal forum for their business, registering the business, and writing contracts for employees, customers, and suppliers. The clinic also would maintain close contacts with diaspora groups and with assistance obtaining capital for startups.

### *11.3. Promotion and Advertising*

Trade and investment promotion is anemic or altogether lacking. The initiatives undertaken by the Kosovo Chamber of Commerce in 1999—or at least envisioned by the Chamber in 1999—have not gone anywhere due to a lack of resources and leadership. There are outside investors who would invest in Kosovo if they knew about the opportunities. Kosovo businessmen and women, and the local institutions of provisional government, must promote investment opportunities in Kosovo to the rest of the world. They also need to make it easy for investors to follow up; this implies the need for someone to facilitate foreign trade missions to Kosovo to inspect facilities and sites, explore the capacity of the professional services sector for potential foreign investors, conduct market research for Kosovars, and pay for legal services.

A good example of part of what needs to be done is the work by KTA, and by the U.S. Department of Commerce Central and Eastern Europe Business Information Center ("CEEBC"). KTA has held a number of investment conferences in international financial

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<sup>126</sup> Icon-Institute, funded by the German government, is a modest exception. It is funded for one year to support the development of lawyers and judges in the Commercial Court. This effort, however, is still litigation-oriented.

centers such as Frankfurt and New York. The October 2003 conference attracted more than one hundred interested parties. The presentations were professional, complete, and persuasive. The attendees expressed concern, however, about the freeze on the third round of privatization, which had been announced by the Deputy SRSG just days before the conference. To say the least, the timing of the freeze was poor.

CEEbic has a website that offers basic information on privatization in Kosovo.<sup>127</sup> It has a basic explanation of how privatization works and provides basic information about eight SOEs including a winery in Prizren, a radiator and air-conditioning equipment manufacturer in Gjlane, a printing enterprise in Mitrovica, a paint factory in Vushtrri, a shock absorber factory near Prishtina, a health spa and water bottling plant in Gjlane, Hotel Theranda in Prizren, and a fish farm and motel in Peja. Comparing the CEEbic website with the EU's Pillar IV website<sup>128</sup> exposes the shortcomings of the EU's effort to assist economic development in the SME sector. To its credit, Pillar IV has contracted with the European Stability Initiative<sup>129</sup> to operate the "Lessons Learned and Analysis Unit of the EU Pillar of UNMIK" ("LLA"). LLA has prepared and published a number of excellent reports on the challenges involved in developing a viable market economy in Kosovo.

As late as February 2003, the KTA did not have its own website. Now it does.<sup>130</sup> The website explains methods for privatization of SOEs contemplated by KTA, and has basic information about the five sectors: agribusiness, construction, hotels and tourism, mining and metals, and other industries. Links are provided to Adobe Acrobat fact sheets about major SOEs. This website is a step forward.

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<sup>127</sup> Central and Eastern Europe Business Information Center, *Privatization Programs in Kosovo*, at <http://www.mec.doc.gov/ceebic/tlkosovo.htm> (last visited Feb. 25, 2004).

<sup>128</sup> European Union Commitment to Kosovo website, at <http://www.euinkosovo.org> (last visited Mar. 2, 2004). As late as June 1, 2003, the EU website was "under construction" and had nothing whatsoever about privatization or small business investment opportunities—not even a link to the KTA website.

<sup>129</sup> See generally European Stability Initiative website, at <http://www.esiweb.org> (last visited Feb. 25, 2004).

<sup>130</sup> See generally Kosovo Trust Agency website, at <http://www.kta-kosovo.org> (last visited Feb. 25, 2004).

Overlapping with investment promotion, public and private institutions must promote the products of new enterprises in foreign markets. This also could be the job of the Kosovar Chamber of Commerce, if it will step up to it. If it will not step up to it, then others in the private sector in Kosovo, in the local government institutions, and in the diaspora need to do this.

#### 11.4. *Investment Fund*

It is time to consider starting one or more investment funds to aggregate capital and permit risk management, thereby enhancing capital available to SMEs. Already, some observers believe that Kosovo pension assets would be more available to Kosovar businesses if such a fund existed. Presently, prudent pension fund management cannot invest in new SMEs or in privatized SOEs because the risk is too great. An investment fund, on the other hand, would manage risk through diversification and the pension fund managers might be able to invest in the investment fund.

An investment fund would perform three important economic functions:<sup>131</sup> providing maturity intermediation; reducing risk through diversification; and reducing the costs of searching, contracting, and information processing associated with finding attractive investments, negotiating appropriate relationships, and monitoring management.<sup>132</sup>

Historically, U.S. investors were little interested in equity investments in foreign enterprises, but this has changed as these investors seek higher rates of return and risk-reducing diversification.<sup>133</sup> The foreign investment originally focused on shares of companies in developed countries, but has begun to shift to include developing country markets.<sup>134</sup> The biggest deterrents for investment in developing country markets are insufficient

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<sup>131</sup> The fourth economic function traditionally associated with financial intermediation, providing a payments mechanism, is more appropriately associated with banks than investment funds.

<sup>132</sup> See generally FRANK J. FABOZZI ET AL., FOUNDATIONS OF FINANCIAL MARKETS AND INSTITUTIONS 21 (1994) (enumerating the functions of financial intermediaries, including investment funds).

<sup>133</sup> See Christopher J. Mailander, *Searching for Liquidity: United States Exit Strategies for International Private Equity Investment*, 13 AM. U. INT'L L. REV. 71, 73-74 (1997) (discussing the recent trend of U.S. investors who have seen growth in mutual funds and pension plans).

<sup>134</sup> See *id.* at 74-75 (arguing that U.S. investors are increasing investment interest in emerging markets).



liquidity, currency risk, lack of managerial expertise and culture, and lack of a viable exit strategy.<sup>135</sup>

Even if investors and managers for such a fund cannot be lined up in the short-term, serious practical steps should be taken to determine what additional legislation may be needed in the United States, Kosovo, and possibly Switzerland and Germany to permit such a fund to be set up. It also may now be possible to take the initial administrative and legal steps to establish the fund, such as filing a charter and drafting bylaws.

Such a fund would also permit Kosovars to pool money they already have available in amounts of, for example, 50,000 euros so that groups of Kosovars might be able to afford to participate in tenders for SOEs as part of the privatization process. Providing some kind of financial intermediation for this would reduce the political fallout of all the SOEs being brought up by foreign investors.

#### 11.5. *Stock and Futures Exchanges*

Consideration also should be given to the establishment of a Kosovar or Balkans stock market. Stock markets already exist in Ljubljana, Zagreb, Skopje, and Belgrade. Kosovo would be better served by making arrangements with these regional markets instead of developing a stock market of its own, considering the amount of literature on the difficulties of effective functioning of a small stock market. Kosovo's characteristics make it a relatively poor candidate for establishing its own stock market. Linking Kosovo's capital formation initiatives with stock markets in other Balkan countries, especially those of Slovenia and Croatia, however, can be an initial step toward regional integration of capital markets that will benefit Kosovo in the long run.

There are 150 securities exchanges in the world.<sup>136</sup> Several

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<sup>135</sup> See *id.* at 77-78 (analyzing the difficulties of investing abroad). Exit strategies include taking the company public, making the company available for acquisition by another company, repurchasing of shares, and secondary purchasing of shares by a third party. *Id.* Offering shares in the United States is one possible way for a foreign company to promise an exit strategy to its early investors, but this involves compliance with stringent U.S. corporate laws. *Id.* at 81-82.

<sup>136</sup> See John C. Coffee, Jr., *Racing Towards the Top?: The Impact of Cross-Listings and Stock Market Competition on International Corporate Governance*, 102 COLUM. L. REV. 1757, 1759 (2002) (discussing the likelihood that the number of stock exchanges will shrink in the future).

countries in transition<sup>137</sup> have started stock exchanges in order to facilitate the flow of private equity capital into local enterprises including: Albania,<sup>138</sup> Brazil,<sup>139</sup> Cambodia,<sup>140</sup> Hungary,<sup>141</sup> Poland,<sup>142</sup> Mexico,<sup>143</sup> the Czech Republic,<sup>144</sup> Slovakia,<sup>145</sup> Mozambique,<sup>146</sup> China,<sup>147</sup> and Thailand.<sup>148</sup> All of the countries of the former Yugoslavia – Bosnia,<sup>149</sup> Croatia,<sup>150</sup> Macedonia,<sup>151</sup> Montenegro,<sup>152</sup> Serbia,<sup>153</sup> and Slovenia<sup>154</sup> – have stock exchanges of some form.

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<sup>137</sup> Coffee estimates that twenty of the twenty-six countries in transition have created stock markets. *Id.* at 1801.

<sup>138</sup> See generally Tirana Stock Exchange website, at <http://www.asc.gov.al/tiranastock.html> (last visited Jan. 17, 2004).

<sup>139</sup> See Coffee, *supra* note 136, at 1808 (reviewing Brazil's experience with listing on the New York Stock Exchange).

<sup>140</sup> See generally Jason Gottlieb, *Launching the Phnom Penh Stock Exchange: Toward a Legal Framework for Launching a Stock Exchange in an Underdeveloped Country*, 14 COLUM. J. ASIAN L. 235 (2000) (examining the possibilities and difficulties of launching a stock exchange in a developing country).

<sup>141</sup> See William C. Philbrick, *The Paving of Wall Street in Eastern Europe: Establishing the Legal Infrastructure for Stock Markets in the Formerly Centrally Planned Economies*, 25 LAW & POL'Y INT'L BUS. 565, 572-73 (1994) (discussing the Budapest stock exchange).

<sup>142</sup> See *id.* at 574 (noting the Warsaw stock exchange).

<sup>143</sup> See Coffee, *supra* note 136, at 1810 (noting the Mexico stock exchange).

<sup>144</sup> See Philbrick, *supra* note 141, at 574 (noting the Prague stock exchange).

<sup>145</sup> See *id.* (noting the Bratislava stock exchange).

<sup>146</sup> See Gottlieb, *supra* note 140, at 249 (discussing Mozambique's experience).

<sup>147</sup> See *id.* at 246 (discussing China's experience).

<sup>148</sup> See *id.* at 247 (discussing Thailand's experience).

<sup>149</sup> The Ljubljana Stock Exchange ("LJSE") provided technical assistance in setting up stock exchanges in Banja Luka and Sarajevo, Bosnia. See The Ljubljana Stock Exchange Website, at [http://www.ljse.si/news/e\\_msg012001.htm](http://www.ljse.si/news/e_msg012001.htm) (last visited Feb. 25, 2004); see also Beth Kampshror, *Sarajevo Stock Exchange Opens*, S.E. EUR. TIMES (Apr. 15, 2002) (providing a new report on the opening of an all-electronic Sarajevo stock exchange), available at <http://www.balkantimes.com/html2/english/020415-BETH-001.htm>.

<sup>150</sup> See About the Zagreb Stock Exchange (providing general information about the Croatian stock exchange), at <http://www.zse.hr/aboutzse.html> (last visited Feb. 25, 2004). In December, 2002, fifty-three issues were traded with a market capitalization of HRKs 28 million (the Croatian currency unit).

<sup>151</sup> See generally Macedonian Stock Exchange website, at <http://www.mse.org.mk> (last visited Feb. 25, 2004). Twenty-two companies were listed on the Macedonia stock exchange as of February 9, 2003.

<sup>152</sup> See generally the Montenegro Stock Exchange website, at <http://www.montenet.org/econ/mberza.htm> (last visited Feb. 25, 2004).

<sup>153</sup> See Beogradska Berza, Belgrade Stock Exchange website, at <http://www.belex.co.yu/> (last visited Feb. 25, 2004).

Successful stock exchanges exist in countries with three characteristics: (1) backing from a strong government (either the local government or another involved in local government affairs), (2) an existing industrial base eager for capital, and (3) capital to invest.<sup>155</sup> It also helps to have large domestic markets, extensive supplies of natural resources, and skilled labor forces.<sup>156</sup> An econometric study of primary securities markets in thirty-two emerging economies from 1980-1995 showed that stock market capitalization<sup>157</sup> and accounting standards were the most important determinants of success.<sup>158</sup> Another study showed that a sustained commitment to privatization was essential to stock market success.<sup>159</sup> Most of the transitional stock exchanges have

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<sup>154</sup> See Ljubljanska Borza, Ljubljanska Stock Exchange, Inc. website, at <http://www.ljse.si> (last visited Feb. 25, 2004). On February 9, 2003, the LJSE listed thirty-three equity issues on the "official market," and 100 equity issues on the "free market." Only Slovenian legal entities may become members of the LJSE and thus become enabled to trade with securities via the LJSE order-driven electronic trading system. In addition, the members of the LJSE may also be the Republic of Slovenia and the Bank of Slovenia. Trading on the LJSE is performed completely electronically via an LJSE electronic trading system, called BTS. Stock Exchange transactions may only be conducted by the LJSE members. Stock Exchange members may enter into BTS a market order or limit orders. Trading is based on the automated processing of orders entered into the system. All securities are included in the daily continuous trading at varying prices—if the price of different orders equals, trade is automatically concluded. Part of an electronic trading system is an automated monitoring system for unusual price and volume movements that also enables an audit trail of all member trading actions. The highest daily price movement allowed is 10%. Short selling is not allowed but can be committed within settlement period (two days). Ljubljanska Borza, Ljubljanska Stock Exchange, Inc., Trading Rules, (stating the block trading rules) at <http://www.ljse.si/StrAng/Trading/TradRule/TradRule.htm> (last visited Feb. 25, 2004). In December 2002, the market had capitalization of 6.7 billion euros in the official market and 2.7 billion euros in the free market. Fifty issues listed 109 securities on the official market, and 148 issues listed 156 securities on the free market. Four closed-end investment funds were listed. See Ljubljanska Borza, Ljubljanska Stock Exchange, Inc., Daily Price List, (listing securities on the LJSE) at [http://www.ljse.si/StrAng/Trading/Menu/tr\\_dpl.htm](http://www.ljse.si/StrAng/Trading/Menu/tr_dpl.htm) (last visited Feb. 25, 2004).

<sup>155</sup> Gottlieb, *supra* note 140, at 237 (enumerating criteria).

<sup>156</sup> Philbrick, *supra* note 141, at 577 (noting the characteristics of Eastern European countries launching successful stock markets).

<sup>157</sup> Measured as the ratio of market capitalization to GDP.

<sup>158</sup> See ANTHONY AYLWARD & JACK GLEN, PRIMARY SECURITIES MARKETS: CROSS COUNTRY FINDINGS (The World Bank, Int'l Fin. Corp. Discussion Paper No. 39) (examining aggregate primary capital market activity in a cross-section of emerging market and developed countries).

<sup>159</sup> Enrico C. Perotti & Luc Laeven, *Confidence Building in Emerging Stock Markets* (Mar. 2002), available at <http://www.worldbank.org/research/>

not been successful, in part because they undermined their credibility by beginning with mass listings of privatized companies, shares of which proved illiquid.<sup>160</sup>

A 2000 study commissioned by the World Bank found that low inflation, good shareholder protection by the legal system, and size of institutional investor assets are important factors in determining the success of stock exchanges in transitional economies.<sup>161</sup> Institutional investors comprise investment and mutual funds, pension funds, and insurance companies.<sup>162</sup>

In countries like Kosovo, there can be problems with both the supply of, and demand for, capital. Supply of capital is limited by mistrust of stock markets by domestic savers, poor protection for shareholders, and uncertain political risk. The pension system is just being established,<sup>163</sup> and the insurance system got off to a false start.<sup>164</sup> There are no investment or mutual funds yet. The demand for equity capital also may be limited. Another problem, similar to one encountered in Cambodia, is that "most enterprises are largely family businesses, [which] are often reluctant to hire outside professionals and resistant to non-family equity ownership."<sup>165</sup>

Futures exchanges also may have a role to play in reducing the risk to agricultural producers, as the agricultural sector is restructured and privatized. Additional information is needed on agricultural futures in other Balkan countries.

### 11.6. *Inattention by All Levels of Government*

The most important shortcoming in the economic sphere is the

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conferences/financial\_globalization/confidence.pdf.

<sup>160</sup> See Coffee, *supra* note 135, at 1801 (noting that the Prague Stock Exchange still has not experienced a single initial public offering).

<sup>161</sup> See STIJN CLAESSENS ET AL., CORPORATE RISK AROUND THE WORLD 11 (2000) (studying the risk characteristics of corporate sectors in the world), available at <http://econ.worldbank.org/docs/1024.pdf> (last visited Feb. 25, 2004).

<sup>162</sup> See *id.* at 10 (exploring the differences in risk-sharing mechanisms). The recent development of funded pension systems makes this type of institutional investor relatively unimportant. The same is true of insurance enterprises. The most important type of institutional investor is the investment and mutual fund categories, usually related to privatization. *Id.*

<sup>163</sup> DEMEKAS, *supra* note 58, at 17-18 (discussing the possible supervision of the pension system by the Banking and Payments Authority ("BPK")).

<sup>164</sup> *Id.* at 12, 18 (describing developments in the insurance sector which began with some DM 67 million in premium income accompanied by suspected corruption).

<sup>165</sup> Gottlieb, *supra* note 140, at 259 (describing Cambodia).

lack of attention given to economic development by international organizations and the provisional institutions of government. Not much can be done about the fact that Pillar IV operated for months with only one economist assigned to it. Something can be done, however, about the roadblocks thrown in the road of privatization, following a very promising start by new EU personnel—beginning with a freeze in October 2003 and followed by an effort to substitute illogical operational policies that would not allow investors to obtain clear title to assets.

Moreover, the provisional government—the parliament, the ministries, and the Kosovar political parties—can be more active in articulating a concrete, specific economic program. It is encouraging that they have taken a strong stand in opposition to the obstructionist policies of the new Pillar IV administrator and the new managing director of KTA.

Such a program would not only give entrepreneurs and investors a road map, it also would be good politics. It would be good politics domestically because it would show ordinary Kosovars that their local political and governmental institutions place a high priority on programs that will make a difference in their lives.<sup>166</sup> Furthermore, it would be good politics in the struggle for more authority for local institutions. Advocates for a more rapid transfer of power from UNMIK can point to specific aspects of the economic program that cannot be moved forward in the absence of further transfer of power. In addition, it would be good politics with respect to final status because it similarly would permit advocates of independence for Kosovo to point to specific aspects of the economic program that cannot be implemented or that are difficult to realize because of Kosovo's lack of sovereignty and status as an independent state.

The international community must push for more energetic development of the private sector, but economic development in the private sector cannot happen if the locals sit back and wait for the international community to do it. Individual Kosovars must take the initiative to start businesses, including those professional

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<sup>166</sup> Opinion surveys show that "dissatisfaction with current political trends is closely correlated with the dissatisfaction... with the current economic situation." *Early Warning Report*, *supra* note 55, at 11-13. A March 2003 survey showed that unemployment and economic development were the top priority issues for the Kosovar population. Yet Kosovar political leaders and political organizations "concentrate their strategy almost exclusively on the issue of the final status of Kosovo." *Id.* at 13.

services that will help other Kosovars understand how to start their own businesses. Existing governmental and quasi-governmental institutions, such as the Chamber, must meet their responsibilities to provide leadership and action in the economic sector instead of putting their energy into lobbying for a quicker transfer of more authority and into debates about eventual independence.

Part of the problem is that the opportunity cost is too great for the best and brightest professionals to do these things. They respond to the lure of good jobs with international organizations and foreign missions. A significant part of the remaining money available from the international community should be allocated to transitioning these young professionals into self-sustaining activities in the private sector.

The SRSG should place greater emphasis on developing the private sector as a prerequisite for achievement of final status. Both inter-ethnic tolerance and a legal system that respects human rights are important, but neither will ever exist without a sustainable economy. Economics is important, and the trustees of Kosovo's future should recognize that concept more than they have so far.

## 12. EFFECT OF FINAL STATUS NEGOTIATIONS

The management of Kosovo's first bank assesses the relationship between final status and economic development in the following manner:

The unresolved status of Kosovo and the lack of a foreign trade regime prevent companies operating in Kosovo from exporting goods to neighboring countries, and in general prevent the region from developing export oriented economic activities. At the same time, foreign investors remain reluctant to place their funds in Kosovo and to acquire stakes in local companies.<sup>167</sup>

Deferring final status negotiations impedes economic development in Kosovo, although it is possible that in some forms final status actually could discourage foreign investment more

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<sup>167</sup> MEB/PROCREDIT MANAGEMENT REPORT, *supra* note 64, at 13.

than would maintaining the status quo. Deferring final status negotiations encourages Kosovar political leaders to focus their energies and rhetoric on statehood for Kosovo rather than on the abundance of difficult public policy issues that need attention from local government. The absence of final status excites not only the attention of the general public in Kosovo more than other issues, but also allows political candidates and elected officials to use the absence of final status as an excuse for failing to make tough choices with respect to matters already within the competence of local government institutions.

The absence of a final status determination discourages threshold inquiries by potential investors. For example, the Author of this article approached McDonald's headquarters near Chicago on behalf of some Kosovar would-be entrepreneurs to find out how to apply for a franchise in Kosovo. McDonald's was not interested because Kosovo does not show up as a country on its lists. The relevant regional franchising authority in Vienna expects to begin processing applications for Kosovo franchises no sooner than 2006.

In June 2003, the Author searched for the website of Raiffeisenbank Kosovo; however, the link was obscured because its parent's website does not list Kosovo in its country list.

The absence of final status forecloses effective participation by Kosovo in the EU's "Stabilization and Association process,"<sup>168</sup> intended to stabilize the western Balkans and to open the possibility of eventual membership in the EU.<sup>169</sup> For example, Kosovo was not included in the western Balkans countries signing the small business charter, because it was not eligible to do so.<sup>170</sup> Its need for the Prishtina-Durres highway was largely ignored because it was not formally a part of the strategic transportation planning process.

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<sup>168</sup> See generally The Western Balkans and European Integration, Communication from the Commission to the Council and the European Parliament, COM(O3)285 final, available at [http://europa.eu.int/comm/external\\_relations/see/2003.pdf](http://europa.eu.int/comm/external_relations/see/2003.pdf) (last visited Feb. 25, 2004).

<sup>169</sup> See INT'L CRISIS GROUP, THESSALONIKI AND AFTER III: THE EU AND SERBIA, MONTENEGRO AND KOSOVO (June 20, 2003) ("So long as Kosovo's status remains unresolved, it cannot be covered by an SAA though the EC itself describes such an agreement as the cornerstone of the Sap."), available at [http://www.crisisweb.org/library/documents/report\\_archive/A401012\\_20062003.pdf](http://www.crisisweb.org/library/documents/report_archive/A401012_20062003.pdf).

<sup>170</sup> See *supra* note 80 for a discussion of the European Charter for Small Enterprises.

Moreover, lawyers unfamiliar with the details of Kosovo's evolution, but called upon by clients for advice on whether they should invest in Kosovo, despair of figuring out applicable law in Kosovo because of the difficulty of synthesizing pre-1989 Yugoslav law and UNMIK regulations.

Part of the problem is lack of transparency, considered in Section 10.2. Uncertainty regarding final status is also a major consideration. Lawyers therefore advise their clients that the law is too unsettled to provide for adequate investor security.

The absence of a well-developed and well-known transactional bar in Kosovo makes this problem worse, because it is extremely difficult for a foreign investor or their foreign lawyer to obtain reliable information about the functions of the court system and the ability of the legal system in Kosovo to resolve disputes between investors and management. While resolving final status will not necessarily improve the availability or visibility of good Kosovar transactional lawyers or make the courts more protective of investor security, the absence of final status encourages foreigners to conclude that Kosovo is a lawless place that investors should avoid.

One further advantage of final status—though not necessarily of incomplete final status *negotiations*—is that it would remove the temptation for UNMIK to interrupt dialogue between Kosovars and those necessary to assure economic development in the international community. For example, in April 2003, UNMIK “punished” the Kosovar provisional government for the Kosovar Assembly’s defying UNMIK on education law. The punishment took the form of, among other things, canceling Kosovar attendance at meetings of the Stability Pact.

Agreement is growing in the United States and the NGO community that final status negotiations must begin without further delay,<sup>171</sup> and that they should result in independence for

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<sup>171</sup> See Hearing on The Successor States to pre-1991 Yugoslavia: Progress and Challenges, Testimony by Daniel Serwer, Director, Balkans Initiative and Peace Operations, United States Institute of Peace, before the Subcommittee on European Affairs, Senate Foreign Relations Committee (June 25, 2003) (stating that the United States needs to get ready to make a decision on final status and should nominate an American to head UNMIK, since Europe cannot proceed alone), available at <http://foreign.senate.gov/testimony/2003/SerwerTestimony030625.pdf>; INT’L CRISIS GROUP, *supra* note 169, at 6 (stating the European Union must address final status without delay, to reach a common understanding among its member states, and that the United States must be involved in determining final status).



Kosovo.<sup>172</sup> Indeed, many observers understood, after the bombing campaign and Milosevic's expulsion of almost the entire Albanian population of Kosovo, that independence was the only long-term option—or, at least, that Kosovo could never become part of Serbia again, no matter how great its “autonomy.”<sup>173</sup>

How can one imagine that a population, half of whom were driven out of their country in spring 1999 by the Yugoslav authorities (and whose identity cards were destroyed precisely to make sure that all links with the country were thereafter severed), could one day consider themselves ‘citizens’ (sic) of that country and ask it for a new passport?<sup>174</sup>

Indeed, just before the bombing campaign started, U.S. Secretary of State Madeleine K. Albright, presented the Yugoslav leadership with a choice, in the metaphor of a fork in the road: “One road led to chaos and killing and definitely, the *further disintegration of the former Republic of Yugoslavia*; [t]he other road had possibilities . . . ultimately lead[ing] to some kind of reintegration . . .”<sup>175</sup>

Having elected to travel Secretary Albright's first road, Serbia is in a poor position to protest the further disintegration of FRY, in the form of independence for Kosovo. In fact, the FRY no longer

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<sup>172</sup> See JANUSZ BUGAJSKI ET AL., *ACHIEVING A FINAL STATUS SETTLEMENT FOR KOSOVO* 4 (2003) (noting that the only viable option now on the table is statehood for Kosovo), available at [http://www.csis.org/ee/kosovo\\_final\\_status.pdf](http://www.csis.org/ee/kosovo_final_status.pdf) (last visited Feb. 25, 2004). But see INT'L CRISIS GROUP, *A KOSOVO ROADMAP* (I): ADDRESSING FINAL STATUS 2, n.4 (Mar. 1, 2002) [hereinafter ADDRESSING FINAL STATUS] (quoting Belgian Foreign Minister Louis Michel after the 2001 Kosovo elections, for the presidency of the European Union, opposing independence for Kosovo).

<sup>173</sup> See Chris Hedges, *Kosovo's Next Masters?*, 78 FOREIGN AFF. 24, 25 (May/June 1999) (stating ethnic Albanians cannot remain in Serbia after the “horrific recent bloodshed”).

<sup>174</sup> Jacques Rupnik, *The Postwar Balkans and the Kosovo Question*, in CHAILLOT PAPER 50: WHAT STATUS FOR KOSOVO? 69, 82 (Institute for Security Studies, Western European Union ed., 2001) [hereinafter WHAT STATUS FOR KOSOVO?] (contending that conditional sovereignty is the best solution, because it would renounce border changes, maintain a measure of international control, and allow Kosovars to participate in working out a viable regional solution).

<sup>175</sup> Secretary of State Madeleine K. Albright, Press Briefing Following Meeting with Contact Group on Kosovo, Paris, France (Feb. 14, 1999), at <http://secretary.state.gov/www/statements/1999/990214a.html>.

exists as a formal state, after reconfiguration of the Serbian-Montenegrin relationship in 2002.

But others conclude: "As long as Kosovo's record on the treatment of minorities remains so poor, as long as internal and external security remain so problematic, there is no prospect of the international community accepting full independence as an option."<sup>176</sup> The International Crisis Group proposed "conditional independence" as a way of bridging the gap.<sup>177</sup> European and American analysts ended up with roughly the same conclusion with earlier analysis.<sup>178</sup>

A number of legal arguments support the view that reincorporation into Serbia is not mandated by Resolution 1244. First, the Resolution "reaffirms" the commitment of member states to the sovereignty of the FRY, but it does not refer to the sovereignty or territorial integrity of the FRY in its provisions relating to negotiation of final status. FRY sovereignty is omitted in its enumeration of principles to guide final status negotiations.

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<sup>176</sup> ADDRESSING FINAL STATUS, *supra* note 172, at 11.

<sup>177</sup> *Id.* at 12-14 (describing and advocating conditional independence).

<sup>178</sup> See Dana H. Allin, *Unintended Consequences – Managing Kosovo Independence*, in WHAT STATUS FOR KOSOVO?, *supra* note 174, at 7 (describing how the North Atlantic Treaty Organization ("NATO") going to war and Serb expulsion of nearly one million Albanians made independence for Kosovo inevitable, and discussing that since de jure independence may have to be delayed, conditional independence is the best immediate alternative); Franz-Lothar Altmann, *The Status of Kosovo*, in WHAT STATUS FOR KOSOVO?, *supra* note 174, at 19 (noting that Resolution 1244's reservation of sovereignty refers to Yugoslavia, not Serbia, and acknowledging the argument that reference to sovereignty in Yugoslavia is limited to the duration of international trusteeship; thus reintegration into Serbia is impossible, but status as a republic within rump Yugoslavia, akin to Montenegro, is a possible approach); Marta Dassu, *Statehood and Sovereignty – Regional and Internal Dynamics in Kosovo's Future*, in WHAT STATUS FOR KOSOVO?, *supra* note 174, at 35 (arguing that "constructive ambiguity" as to sovereignty may have to be maintained for the time being, while rejecting a return to the 1999 status quo of Kosovo as part of Serbia, and that there is a need to speed up the process of building self-rule in Kosovo); Tim Judah, *Kosovo and its Status*, in WHAT STATUS FOR KOSOVO?, *supra* note 174, at 55 (discussing that Serbs do not want to keep Kosovo, but have no idea how to give it up, while Kosovar Albanians have no institutional capacity to be independent); Dimitrios Triantaphyllou, *Kosovo Independence and Regional Stability Are Not Incompatible*, in WHAT STATUS FOR KOSOVO?, *supra* note 174, at 99 (arguing independence should be "on the table" in direct negotiations between Prishtina and Belgrade); Thanos Veremis, *The Ever-Changing Contours of the Kosovo Issue*, in WHAT STATUS FOR KOSOVO?, *supra* note 174, at 85 (noting there are proposals for new international "trusteeship" under Article 76(b) of the U.N. Charter, and that continued UNMIK administration has had a corrosive effect on the capacity of Kosovar political institutions).

The most reasonable inference is that the political trusteeship of the U.N. was obligated to respect the sovereignty of FRY, but that final status is to be unconstrained by that consideration.

Second, the FRY no longer exists, by virtue of the renegotiated confederation of Serbia and Montenegro. This was agreed to on March 14, 2002, which contemplates the possible dissolution of the new "union."<sup>179</sup> The agreement, however, purports to transfer any rights under Resolution 1244 to Serbia.<sup>180</sup>

Third, even if Kosovo exists under the law of Yugoslavia, Kosovo as an autonomous province enjoyed the same power to secede as the Yugoslav republics enjoyed. This distinguished it from Republika Srpska in Bosnia and the Albanian areas of Macedonia. The institutions of Kosovo exercised this right in 1991.

Several things are clear about final status negotiations:

1. Kosovar Albanians will not accept being folded back into Serbia; the Serbs refused to accept the Rambouillet document, and a war intervened. Approaches to autonomy involving continued Serbian sovereignty, although within the scope of Rambouillet, are not useful as templates.
2. Kosovo cannot become a state without international recognition, and that is unlikely to occur without a U.N. Security Council Resolution approving the outcome of final status negotiations; Russia and France can veto such a resolution, which means that both of those states must first accept the outcome of the negotiations.
3. Serbia must be part of the negotiations, or Russia will not accept the outcome.
4. Kosovars will not trust UNMIK as a convener or

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<sup>179</sup> "After a period of three years, the member-states have the right to initiate a procedure to change the statehood status or to leave the union of states." Text of Serbia-Montenegro agreement, Re-examination provision (Mar. 14, 2002), *available at* <http://news.bbc.co.uk/2/hi/europe/1874523.stm>.

<sup>180</sup> "In the event that Montenegro leaves the union of states, the international documents relating to the FRY, especially U.N. Security Council Resolution 1244, would relate in their entirety to Serbia as successor." *Id.*

mediator, and may not trust the European Union in either role. The Serbs will not trust the United States.

The best approach is for the United States, Russia, and the European Union, with Security Council approval, to convene an international conference to determine final status for Kosovo. The Kosovars should be represented directly through the Prime Minister and leaders of the three major political parties. The SRSG should be a full participant, but should not have veto power over the outcome, nor be able to control the timing.

Among other alternatives, the conference should focus on the International Crisis Group proposal for conditional independence.<sup>181</sup> The conditional independence status is flexible enough to devolve substantially greater power to the assembly of Kosovo. It can allow Kosovo to have the status of a state in the international community, permitting full participation in the EU Stability Pact, and allowing it to make trade agreements and to attract foreign investment.

Another possibility is for the UN Security Council to disband UNMIK, and authorize the European Union to replace it with a "European Union Trusteeship in Kosovo" ("EUTRIK"). In the same resolution establishing EUTRIK, the Security Council would devolve further power to local institutions, reserving, however, to EUTRIK a final veto power and continued responsibilities in the foreign relations and security sphere. EUTRIK would be expected to have a very long life, gradually devolving power to Kosovar institutions until it remained a mere figurehead, much as the Queen of England is to Canada—possessed of considerable formal power but not expected to exercise it. Over this period of time, EUTRIK would represent a pathway for gradual Kosovo integration into the European Union. It would be a backdoor into the EU for Kosovo, an alternative to the usual accession route.

The advantages are the pathway to EU integration, and the avoidance of ever having to say formally, "Kosovo is independent of Serbia."

### 13. CONCLUSION—IN THE MEANTIME

Successful nation-building requires political trustees to

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<sup>181</sup> See generally WHAT STATUS FOR KOSOVO?, *supra* note 174 (discussing various possible forms of status for Kosovo).

emphasize economic development. In Kosovo, as in Bosnia, private sector economic development took a backseat to humanitarian relief, human rights, and the establishment of political institutions.

Kosovo continues to provide an interesting test to see if political trustees can get it right, thus providing a model for other political trusteeships.

Despite the desirability of commencing final status negotiations forthwith,<sup>182</sup> it is also essential to recognize that beginning negotiations over final status is not the same thing as having final status decided. Indeed, the existence of negotiations over final status may produce more uncertainty, represent more of a political distraction, and discourage foreign investment to a greater degree than the status quo. Also, most Kosovars assume that final status will be independence, but that is not entirely assured. It is conceivable that the realities of negotiations, and the interacting interests of Europeans, Russians, and the United States, distracted by other priorities, would result in a final status other than independence. Such an unanticipated final status would have unpredictable effects on economic development. Moreover, even independence will not assure sound economic policy, attract outside investment, or ensure the kind of legal and political stability that investors seek.

There are, however, things UNMIK could do now that would help bridge the gap. It must place private sector economic development at the top of its list of priorities, not at the bottom. It must act promptly to approve economic measures passed by the Kosovo Assembly, or give specific reasons why it withholds its approval. It must reverse the decisions by Pillar IV administrator Lambsdorff and KTA Managing Director Fucci to derail privatization, and replace them, if necessary, to put privatization back on track. It must embrace governmental transparency by promptly publishing its own regulations and administrative orders on its website, and by encouraging the provisional institutions of government to establish their own websites on which they publish the full text of enactments and major legislative and regulatory proposals. It also must allow representatives of the provisional institutions to participate directly in international conferences.

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<sup>182</sup> See BUGAJSKI ET AL., *supra* note 172, at 4 (explaining why independence for Kosovo is inevitable and arguing that final status negotiations should not be delayed).

Likewise, the provisional institutions can do much to bridge the gap and to increase their capacity for independent responsibility. They must place private sector economic development at the top of their lists of priorities. The major political parties must articulate concrete economic programs. The Assembly must adopt, and implement an agenda for enacting economic legislation. All levels of government must embrace an aggressive personnel development program and commitment to transparency, thereby reducing barriers to business formation.

Both UNMIK and the provisional institutions, aided by the NGO community, must provide support for business support services—services that provide assistance not only for businesses assured of success, but also for entrepreneurial proposals with higher levels of risk.

Everyone must recognize that refugees will not return without economic hope; that human rights are respected most when people have economic opportunity; that liberal democracies do not exist in societies without well-functioning economies; and that independence will mean little unless Kosovar institutions can give people what they want: not only independence, but also jobs, a way to support their families, and human dignity.

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