Doing Business in Bhutan

Reform Memorandum

January 2020
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Introduction

The overall business environment in an economy depends on many factors, ranging from market size, macroeconomic conditions, and business regulations. A regulatory environment that can help the private sector thrive matters for poverty reduction. According to a World Bank Group survey of the poor, getting a job or starting a business is the most effective way out of poverty.\(^1\) Empirical literature confirms it. Regardless of the methodology employed, literature points to the fact that more and better paid jobs have been critical in lifting people out of poverty.\(^2\) Governments can play a key role by creating a regulatory environment with rules that establish and clarify property rights, minimize the cost of resolving disputes, increase the predictability of economic interactions and provide contractual partners with core protections against abuse. Simple and inexpensive business registration processes, for instance, can facilitate formal entrepreneurship, enhance job creation and economic growth\(^3\), and lower levels of corruption and informality.\(^4\)

A number of international benchmarks and surveys identify key constraints to a country’s competitiveness and private sector development.\(^5\) While such benchmarks only give an indication of the overall enabling environment for firms, they can help identify specific areas of business regulation in need for reform to create a more business-friendly environment for firms supporting private sector productivity and growth.

The World Economic Forum’s Global Competitiveness Index 2017-18 ranks Bhutan 82\(^{\text{th}}\) out of 137 economies, with a Global Competitiveness Index of 4.1. Bhutan’s best performance is reported in its Health and Primary Education pillar (5.4 out of 7), followed by Institutions (4.8 out of 7). Bhutan scores lowest in Market size (1.9 out of 7), and Innovation Technological readiness (both at 3.2 out of 7). In comparison with South Asian economies, Bhutan performs better in almost all pillars. (Figure 1).

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5 Among others, these international benchmarks and surveys include the Enterprise Survey and the annual Doing Business Report by the World Bank Group, the annual Executive Opinion Survey by the World Economic Forum, World Governance Indicators and the Corruption Perception Index by the Transparency International.
Figure I. Bhutan’s performance across the 12 pillars measured by the Global Competitiveness Report 2017-18, compared with South Asia region.

![Diagram of Bhutan's performance across the 12 pillars compared to South Asia.](image)

Source: Global Competitiveness Report 2017-2018

Firms interviewed for the Global Competitiveness report, identified five key obstacles to business operations in Bhutan: 16.4 percent of firms found access to financing as most burdensome, followed by restrictive labor regulations (14.1 percent), inadequate supply of infrastructure (10.8 percent), poor work ethic in national labor force (10.5 percent) and foreign currency regulations (8.2 percent) (Figure II).

Figure II. Top obstacles identified by formal firms in Bhutan

Source: Global Competitiveness Report 2017-2018

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6 Note: From the list of factors, respondents to the World Economic Forum’s Executive Opinion Survey were asked to select the five most problematic factors for doing business in their country and to rank them between 1 (most problematic) and 5. The score corresponds to the responses weighted according to their rankings.
According to the World Governance Indicators\(^7\), Bhutan’s score varies widely across each of the six categories (the estimate gives the country's score in units of a standard normal distribution, i.e. ranging from approximately -2.5 to +2.5), with control of corruption and political stability and absence of violence/terrorism scoring strongly at 1.65 and 1.10, respectively, but regulatory quality earning a negative score (Table I).

**Table I. Governance and quality of regulatory implementation**

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Country</th>
<th>Year</th>
<th>Governance (-2.5 to +2.5)</th>
<th>Percentile Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Voice and Accountability</td>
<td>Bhutan</td>
<td>2018</td>
<td>0.06</td>
<td>49.75</td>
</tr>
<tr>
<td>Political Stability and Absence of Violence/Terrorism</td>
<td>Bhutan</td>
<td>2018</td>
<td>1.10</td>
<td>88.57</td>
</tr>
<tr>
<td>Government Effectiveness</td>
<td>Bhutan</td>
<td>2018</td>
<td>0.36</td>
<td>67.31</td>
</tr>
<tr>
<td>Regulatory Quality</td>
<td>Bhutan</td>
<td>2018</td>
<td>-0.33</td>
<td>39.42</td>
</tr>
<tr>
<td>Rule of Law</td>
<td>Bhutan</td>
<td>2018</td>
<td>0.55</td>
<td>71.63</td>
</tr>
<tr>
<td>Control of Corruption</td>
<td>Bhutan</td>
<td>2018</td>
<td>1.65</td>
<td>91.83</td>
</tr>
</tbody>
</table>

Source: Worldwide Governance Indicators 2018

The objective of this Reform Memorandum is to provide analysis and advice to the Royal Government of Bhutan by identifying and prioritizing reforms in the regulatory areas covered by the World Bank Group’s Doing Business Report. The Doing Business project provides a measure of the “ease of doing business” in 190 countries through a set of objective indicators that focus on the impact of laws, regulations and their enforcement on the ease of Doing Business for domestic firms in 10 areas from starting a business, operations to resolving insolvency.\(^8\)

The Doing Business 2021 report will include a new indicator set in the calculation of the ease of doing business ranking named “Contracting with the government”. The Contracting with the government indicator set measures the procedures and time to win a public procurement contract according to a standardized case study focused on the infrastructure sector. It also assesses the compliance of regulation with internationally recognized good practice.

**Regulations that are efficiently implemented, transparent, accessible, and strengthen property rights are important for poverty reduction through growth and job creation.**\(^9\) The Doing Business indicators cover an important, albeit not comprehensive, set of such regulations. Since the publication of the first Doing Business report in 2004, governments around the world have implemented over 3,000 reforms striving to align domestic business regulation with the good practices advocated by Doing Business. Many governments use Doing Business indicator sets to formulate and monitor their reform efforts. Regulatory reforms inspired by Doing Business have

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\(^7\) The Worldwide Governance Indicators (WGI) project reports aggregate and individual governance indicators for 215 economies over the period 1996-2016, for six dimensions of governance: Voice and Accountability, Political Stability and Absence of Violence/Terrorism, Government Effectiveness, Regulatory Quality, Rule of Law, and Control of Corruption.

\(^8\) www.doingbusiness.org

been implemented by economies in all regions. Economies as diverse as Brazil, Colombia, the Russian Federation, Rwanda, and Mauritius among many others have utilized Doing Business as a catalyst for their business reform agenda.

Bhutan’s overall rank in *Doing Business 2020* was 89<sup>st</sup> out of 190 countries, and 2<sup>nd</sup> out of 8 economies in the South Asia region. In terms of the Ease of Doing Business Score, Bhutan scores above the regional average of 58.2 percentage points with 66.0 percentage points toward the global best performance (where 0 is the lowest and 100 is the best performance). However, Bhutan’s performance varies significantly across the ten indicators, suggesting room for improvement in a range of areas – especially in protecting minority investors (46.0 percentage points), getting credit (55.0 percentage points), dealing with construction permits (68.9 percentage points) and resolving insolvency (0.0 percentage points). The country performs best in Trading across Borders (94.2 percentage points) and Paying Taxes (89.2 percentage points) (Table II).

### Table II. Bhutan’s performance across *Doing Business 2020* topics in order of best to worst

<table>
<thead>
<tr>
<th>Area of Business Regulation</th>
<th>Doing Business 2020 ranking (out of 190 economies)</th>
<th>Score (0-100)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trading across Borders</td>
<td>30</td>
<td>94.2</td>
</tr>
<tr>
<td>Paying Taxes</td>
<td>15</td>
<td>89.2</td>
</tr>
<tr>
<td>Starting a Business</td>
<td>103</td>
<td>86.4</td>
</tr>
<tr>
<td>Getting electricity</td>
<td>78</td>
<td>77.5</td>
</tr>
<tr>
<td>Registering Property</td>
<td>53</td>
<td>72.6</td>
</tr>
<tr>
<td>Enforcing Contracts</td>
<td>29</td>
<td>70.0</td>
</tr>
<tr>
<td>Dealing with Construction Permits</td>
<td>91</td>
<td>68.9</td>
</tr>
<tr>
<td>Getting Credit</td>
<td>94</td>
<td>55.0</td>
</tr>
<tr>
<td>Protecting Minority Investors</td>
<td>111</td>
<td>46.0</td>
</tr>
<tr>
<td>Resolving Insolvency</td>
<td>168</td>
<td>0.0</td>
</tr>
<tr>
<td><strong>Overall (Ease of Doing Business)</strong></td>
<td><strong>89</strong></td>
<td><strong>66.0</strong></td>
</tr>
</tbody>
</table>

Source: Doing Business 2020 database

Bhutan’s efforts to improve the business environment have been recognized by the Doing Business report in the last decade. Since 2008, Bhutan has implemented 13 reforms as recognized by *Doing Business*. Over the last two years, Bhutan made paying taxes easier by introducing an online platform for filing corporate income tax and personal income tax returns. Bhutan has undertaken the highest number of reforms aimed at simplifying starting a business (4) and getting credit (3). In comparison, Doing Business has not recorded any major reform in Bhutan on Dealing with Construction Permits; Trading across Borders and Resolving Insolvency. (Figure III).
Figure III. Doing Business reform count by indicator from 2008 to 2020.

Scope of the Memorandum

Doing Business offers policy makers a benchmarking tool useful in stimulating policy debate, both by exposing potential challenges and by identifying good practices and lessons learned. Over the past decade, it has been used by policy makers in an increasing number of economies to advance their business environment and competitiveness reform agendas. More than 40 economies globally have established units dedicated to specific reform action plans leveraging international benchmarks such as Doing Business to inform and monitor regulatory reform programs. Economies as diverse as Malaysia and the Russian Federation have created regulatory reform committees using Doing Business as an input to inform their programs for improving the business environment. (Box I outline key features of successful reformers and examples from different countries).

Box I: Common Features of Successful Reformers

Reformer economies may vary widely in their political systems, the quality of their institutions, income level and administrative structure, yet they all share some common elements which have contributed to initiating and sustaining their reform process.

**High-level leadership and ownership of the reform agenda.** Countries that took reform efforts seriously and succeeded at achieving significant results are often those that commit to these issues at the highest political level. Oftentimes a clear champion can be identified—e.g. the President, Prime Minister, or a powerful Minister—with strong ownership of the reform agenda. These champions often personally and publicly commit to achieving specific goals and are able to mobilize support from stakeholders inside and outside government to ensure the reform effort move forward. Countries like Rwanda, Russian Federation, and Kazakhstan have strong Presidents who have championed the business environment reform efforts. Other mechanisms may be necessary to mobilize stakeholders in the reform effort. For example, in Peru, despite changes in Government, significant progress has been achieved since 2009 due to the existence of a National Competitiveness agenda. An inter-ministerial institution with private sector representation, the National Competitiveness Council regularly consults and reports to the private sector and general public on implementation progress.

**A long-term vision with clear objectives.** Reform programs need to define clear objectives that are related to the long-term strategic vision of the country. Malaysia and Mauritius set goals in their national development plans to become among the world’s most competitive economies and achieve the status of a high-income economy by 2020. Colombia wants to become one of the three most competitive countries in Latin America. Successful governments
follow a longer-term agenda that aims at increasing the competitiveness of the economy. Adopting a more comprehensive approach increases the chances of success and impact, given that reforms in different areas tend to be complimentary. Many countries like Mauritius, the Russian Federation, Kazakhstan and Peru have targeted specific improvements in the Doing Business ranking. Improvements in the ranking can be difficult to predict but having a specific goal can generate momentum and focus efforts around achieving that objective.

**Inclusive reform with an appropriate institutional mechanism.** Regulatory reforms often span a wide range of areas and require the involvement of multiple agencies. Successful reformers establish reform processes that are inclusive—including all relevant public agencies and private sector representatives—and create clear mechanisms to ensure coordination and information flows across all parties involved. Many establish high level oversight committees that work to prioritize the reform agenda and maintain reform momentum. Technical working groups then lead implementation at the agency level. The most successful technical committees have representatives from all key agencies involved in a particular area, as well as knowledgeable members of the private sector. A Ministry or dedicated team is designated to take responsibility and lead the coordination of the overall reform efforts. Many of the governments that succeeded in ambitious reform programs had dedicated reform teams connected to the top of government and in charge of formulating the reform strategy and coordinating its implementation. A study of five countries that have achieved sustained economic progress over the last 30 years also concluded that relying on a small, dedicated team with direct access to the top government was a common feature of their reform strategies. The advantage of these structures is that they are embedded in the policy process, yet at the same time are relieved of daily administrative matters. Therefore, they are in an ideal position to suggest actions to the national leadership and monitor their progress.

The approach to create institutional coordination mechanisms varies by country. Countries like Malaysia and the Russian Federation, created new autonomous entities, separated from the government structure. In Latin America, countries like Colombia, Costa Rica and Peru have relied on national competitiveness councils, with public and private participation, to drive the investment climate reform agenda. Other countries, like Burundi, Côte d’Ivoire, and Rwanda created dedicated inter-ministerial committees including relevant ministers, as well as representatives of other government entities focused specifically on the investment climate reform agenda. All the countries above created specific technical working groups, often organized around the areas of business regulation measured by Doing Business, but also going beyond those to include topics such as gender issues, human capital development, agribusiness, among others. Oftentimes, the agency in charge of coordinating the reform effort has a mandate to promote investment, support SMEs or improve the business environment. In order to give the needed mandate to the institutional mechanism, governments often pass decrees, circulars or other instruments establishing these mechanisms and giving these structures an official mandate. Terms of Reference (ToR) describing the role and functions of these mechanisms are frequently approved to ensure accountability and commitment to implementation from all involved stakeholders.

**Monitoring of Goals and clear accountability.** Having a reform structure in place does not guarantee success. Effective reformers are able to identify priority areas, set specific measurable goals and actions to achieve them, along with clearly defined deadlines and responsibilities. Many countries, such as Cote d’Ivoire, Colombia, Mauritius, Rwanda and Peru have developed specific action plans, which are monitored and updated regularly. Progress is monitored during implementation to identify areas of success as well as areas where further effort is needed. Clear accountability mechanisms and oversight at the highest levels of government are common features in countries with successful reform track records. Reform steering committees, like the ones set up in Burundi and Rwanda meet regularly to discuss progress. In other countries, like Korea and Peru, reporting progress to the public provides another dimension of accountability. Ensuring the flow of information across the different levels of the reform structure is critical to ensuring progress is monitored and bottlenecks are addressed. In countries as diverse as Albania, Macedonia, FYR, Rwanda, and the Russian Federation, the Minister or agency in charge of coordinating the reform effort reports regularly to the President or Prime Minister.

**Private sector participation and effective communication.** Consultation and collaboration with the private sector is another key aspect in the reform process. Without understanding private sector’s concerns and the barriers that prevent them from starting, operating and growing their businesses, no government can claim to set up a comprehensive reform agenda. Successful governments have established an effective platform that allows regular consultations between the public and private sectors, making the latter an important part of the reform process. In most, if not all, the countries considered for this note, the private sector has participated in the reform process to some
Indicators and benchmarks give an indication of factors that contribute to the creation of an overall enabling environment for business and can help governments identify areas of business regulation that could benefit from further improvement to support private sector growth and investment. This reform memorandum provides recommendations in areas where the government can have a direct impact on business conditions and discusses how some of these shortcomings can be addressed through legal and regulatory reforms.

The recommendations are based on Bhutan’s results in the *Doing Business 2020* report, global regulatory trends and practices, as well as relevant and extensive analytical work. They focus on regulatory and administrative reform options in the areas of business regulation measured by the *Doing Business* project. Each chapter presents features of effective regulatory systems in the respective area, examples from across the world, and specific recommendations for the Royal Government of Bhutan. The recommendations do not address all aspects of the investment climate in Bhutan, but focus on how to:

- Ease business entry and operations with a focus primarily on small and medium domestic firms by reducing complexity and cost of regulatory processes and increasing transparency (e.g. by streamlining registration and licensing procedures)

- Strengthen the regulatory and institutional framework aimed at securing property rights and increasing access to credit (e.g. through strong secured transactions and insolvency frameworks, credit information sharing systems and effective contractual enforcement mechanisms)

The recommendations take into account ongoing reform initiatives and policy discussions, some of which can positively impact the business environment as well as the areas included in the *Doing Business* report. Some of the recommendations provided can be addressed in the short to medium term, while other recommendations are only implementable over a longer period. The indicated timeframes are preliminary and based on the experience of other countries. All actions will require consultations and coordination with different stakeholders. Interagency coordination and a strong focus on implementation will be crucial to the success of any reform efforts in Bhutan.

Predicting whether the improvements in investment climate topics highlighted in this memorandum will impact the *Doing Business* rankings for Bhutan is difficult as this also depends on the relative performance of other countries. For reforms to be captured by the *Doing Business* report, it will be essential that they are fully implemented and enforced by the public sector and adopted by the private sector and the practitioners. The *Doing Business* project records reforms that are not only enacted into law and regulation but that are fully implemented (in other words, all reforms need to be known and used by the majority of the private sector and the legal reforms have to be properly entered into force) (Box II). Rather than aiming at specific
advancements in the rankings, emphasis should be placed in implementing key reforms to improve the investment climate. A rigorous reform effort will likely be reflected in those areas and—more importantly—provide a better business environment that is more conducive to private sector development and economic growth.

Consultation with the private sector is a crucial aspect of the reform process. Without understanding the private sector’s concerns and the barriers that prevent them from starting, operating and growing their businesses, no government can claim to set up a comprehensive reform agenda that will bring a real difference to its businesses.

Finally, strong reformers measure and communicate their success. Monitoring the implementation and impact of reforms highlights areas of success as well as areas where further effort is needed. Communicating reforms effectively to implementing agencies, the business and legal communities, and the general public ensures that changes are accepted and put in practice consistently. Enhancing the regulatory environment to facilitate the creation and growth of enterprises is a major undertaking, and the path is different in each country. There is no “one size fits all” for regulatory reform. Improvement to the business climate can, however, help set a foundation for the private sector’s sustainable development and the creation of a competitive and diversified economy.

Table III. Provides a summary of the rest of the short and medium-term reform recommendations, which are described in more detail in this memorandum.
### Table III. Bhutan’s performance on the *Doing Business* indicators and suggested short and medium to long-term reform recommendations

<table>
<thead>
<tr>
<th>Topics</th>
<th>Indicators (Doing Business 2020 report)</th>
<th>Short-term reform recommendations</th>
<th>Medium- to long-term reform recommendations</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Starting a Business</strong></td>
<td>Procedures (number): 8&lt;br&gt;Time (days): 12&lt;br&gt;Cost (% of income per capita): 3.7%&lt;br&gt;Paid-in min capital (% of income per capita): 0%&lt;br&gt;Global rank: 103</td>
<td>1. Replace the requirement for police clearance by allowing a declaration, or having the registry conduct the check internally.&lt;br&gt;2. Introduce a risk-based approach for operating licenses.&lt;br&gt;3. Merge the name search and clearance process with registration.</td>
<td>4. Consider alternatives to the practice of using company seals.&lt;br&gt;5. Introduce a single business identifier and develop interoperable ICT systems and a common database to transmit and share business information among all government agencies.&lt;br&gt;6. Introduce an electronic single window for business registration.</td>
</tr>
<tr>
<td><strong>Dealing with Construction Permits</strong></td>
<td>Procedures (number): 21&lt;br&gt;Time (days): 150&lt;br&gt;Cost (percent of warehouse value): 0.9%&lt;br&gt;Building quality control index: 12/15&lt;br&gt;Global rank: 91</td>
<td>1. Consider issuing the occupancy certificate on the spot for low-risk projects in full compliance, at the time of final inspection.</td>
<td>2. Review the risk-based classification of buildings based on their intrinsic features and intended use.&lt;br&gt;3. Establish clear standards to determine liability for problems occurring after the completion of the construction and consider a mandatory insurance requirement to cover structural defects.&lt;br&gt;4. Introduce a single online window for online application and approval of construction permits.</td>
</tr>
<tr>
<td><strong>Getting Electricity</strong></td>
<td>Procedures (number): 4&lt;br&gt;Time (days): 61&lt;br&gt;Cost (percent of income per capita): 381.6%&lt;br&gt;Reliability of supply and transparency of tariffs index: 4/8&lt;br&gt;Global rank: 78</td>
<td>1. Review and streamline the procedure for electricity connections.&lt;br&gt;2. Assess the feasibility of simplifying and reducing the cost of obtaining electricity connections for new customers.</td>
<td>3. Introduce Geographic Information System (GIS) for the electricity distribution network to further streamline the procedure to obtain electricity connection by eliminating site visits to approve a request.</td>
</tr>
</tbody>
</table>

10 A detailed description of each reform recommendation can be found in the chapters.
<table>
<thead>
<tr>
<th>Topics</th>
<th>Indicators (Doing Business 2020 report)</th>
<th>Short-term reform recommendations</th>
<th>Medium- to long-term reform recommendations</th>
</tr>
</thead>
</table>
| Registering Property | Procedures (number): 3  
Days: 77  
Cost (percent of property value): 5.0%  
Quality of land administration index: 23/30  
Global rank: 53 | 1. Disseminate and encourage the use of the online platform.  
2. Implement a specific and separate mechanism for filing complaints related to Thimphu Thromde.  
3. Increase transparency of the land administration by publishing the fee schedule to access maps of land plots. | 4. Implement an automated system to monitor outages and restore service.  
4. Improve transparency at the Thimphu Thromde by expanding the access to information on land ownership, maps and boundaries which are now only limited to interested parties.  
5. Implement an electronic database covering all interests in land, including financial encumbrances.  
6. Establish a specific compensation mechanism to cover for losses incurred by parties who engaged in good faith in a property transaction based on erroneous information certified by the immovable property registry.  
7. Conduct a study to assess whether a reduction in property transfer duty is warranted. |
| Getting Credit | Strength of legal rights index: 4/12  
Depth of credit information index: 7/8  
Credit registry coverage (% of adults): 0%  
Credit bureau coverage (% of adults): 42.5%  
Global rank: 94 | Credit information:  
1. Develop a credit scoring system complementing credit reports as an additional valued-added service.  
Legal Rights of Creditors and Borrowers in Secured Transactions:  
1. Ensure the new Secured Transactions framework will address the gaps identified in the current legislation.  
   A. Ensure an integrated legal framework for secured transactions that extends to the creation, publicity and enforcement |
## Protecting Minority Investors

<table>
<thead>
<tr>
<th>Topics</th>
<th>Indicators (Doing Business 2020 report)</th>
<th>Short-term reform recommendations</th>
<th>Medium- to long-term reform recommendations</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Extent of disclosure index (0-10): 4.0</td>
<td>B. Explicitly provide that all types of obligations and debts can be secured.</td>
<td>of functional equivalents to security interests in movable assets exist in the country.</td>
</tr>
<tr>
<td></td>
<td>Extent of director liability (0-10): 4.0</td>
<td>C. Balance secured creditor and borrower rights by mandating an automatic stay on enforcement with effective limits.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Ease of shareholder governance index (0-10): 6.0</td>
<td>D. Ensure that a secured creditor’s priority is respected based on the principle of “first-in-time, first-in-right,” while respecting other critical national policy objectives.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Extent of shareholder rights index (0-6): 3.0</td>
<td></td>
<td>2. Ensure that the Central Registry system for secured transactions is up and running fully under modern principles.</td>
</tr>
<tr>
<td></td>
<td>Extent of ownership and control index (0-7): 3.0</td>
<td>3. Implement awareness raising campaign and capacity building activities on the new tools introduced by the reforms.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Extent of corporate transparency index (0-7): 3.0</td>
<td></td>
<td>1. Revise the Companies Act of Bhutan 2016 as to include the following best practices in corporate governance.</td>
</tr>
<tr>
<td></td>
<td>Strength of minority investor protection index (0-50): 23</td>
<td></td>
<td>The amendments to the Companies Act law should introduce the following:</td>
</tr>
<tr>
<td></td>
<td>Global rank: 111</td>
<td></td>
<td>1.1. Require an independent review of related-party transactions prior to their approval.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1.2. Require the interested director to fully disclose all materials facts of a conflict of interest to the board of directors.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1.3. Require a detailed disclosure of the conflict of interest in the annual report.</td>
</tr>
<tr>
<td>Topics</td>
<td>Indicators (Doing Business 2020 report)</td>
<td>Short-term reform recommendations</td>
<td>Medium- to long-term reform recommendations</td>
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<tr>
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<tr>
<td></td>
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<td></td>
<td>1.4. Provide shareholders with the possibility of holding company directors liable for damages caused by unfair or prejudicial related-party transactions.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1.5. Introduce remedies for prejudicial related-party transactions.</td>
</tr>
<tr>
<td></td>
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<td></td>
<td>1.6. Allow the court to void related-party transactions that are unfair or entails a conflict of interest.</td>
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<tr>
<td></td>
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<td></td>
<td>1.7. Require the consent of the majority of shareholders when disposing large assets of the company.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1.8. Ensure that all shareholders can exercise preemptive rights on new shares that cannot be waived by a simple majority vote.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1.9. Require majority approval of holders of a class of shares for any changes affecting such class of shares.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1.10. Require the board of directors to have a separate audit committee.</td>
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<td></td>
<td>1.11. Introduce legal provisions to ensure that all shareholders are offered an exit option in case of major takeover of the company.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1.12. Prevent subsidiaries from being able to acquire shares issued by their own parent company.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1.13. Require disclosure of direct and indirect beneficial ownerships representing 5% or more of the share capital of a Joint Stock Company.</td>
</tr>
</tbody>
</table>
|        |                                        |                                   | 1.14. Require disclosure of information about the compensation of directors and high-
<table>
<thead>
<tr>
<th>Topics</th>
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<th>Medium- to long-term reform recommendations</th>
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</thead>
</table>
| Paying Taxes | Payments (number per year): 18 Time (hours per year): 52 Total tax and contribution rate (percent of profit): 35.3% | 1. Encourage use of electronic systems through outreach campaign and trainings. | ranking officers of a company, including bonuses and incentive schemes on an individual basis.  
1.15. Require the notice of shareholder meetings to be published and sent to shareholders at least 21 calendar days in advance and contain sufficient information on the matters to be discussed during the meeting.  
1.16. Ensure that shareholders representing 5% of the issued capital can include additional items on the general meeting agenda.  
2.1. Require immediate disclosure of information regarding related party-transactions to the public (or to the market regulator).  
3. Consider amending the Civil and Criminal Procedure Code of Bhutan of 2001 as to:  
3.1. Facilitate access to corporate documents by plaintiffs during trial.  
3.2. Allow plaintiffs to directly question the defendant and witnesses during the trial.  
3.3. Allow shareholders to recover legal expenses regardless of the outcome of their legal action. |

2. Streamline and automate the process of amending tax returns.  
3. Implement a robust risk-management system for corporate income tax audit. |
<table>
<thead>
<tr>
<th>Topics</th>
<th>Indicators (Doing Business 2020 report)</th>
<th>Short-term reform recommendations</th>
<th>Medium- to long-term reform recommendations</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Post-filing index: 95/100</td>
<td></td>
<td>3. Modernize the customs legislation.</td>
</tr>
<tr>
<td></td>
<td>Global rank: 15</td>
<td>1. Identify opportunities to reduce the administrative and procedural costs linked to importing and exporting.</td>
<td>4. Consider establishing a national single window for trade.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2. Improve information availability, particularly on procedures and fees for trading across borders.</td>
<td>5. Consider reduced or joint physical examinations and adopt the use of risk management in all border agencies, including risk-based inspections.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>3. Modernize the customs legislation.</td>
<td>6. Enhance cross-border cooperation with neighboring countries.</td>
</tr>
<tr>
<td><strong>Trading across Borders</strong></td>
<td>Time to export: Border compliance (hours): 5</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Cost to export: Border compliance (USD): 59</td>
<td>1. Identify opportunities to reduce the administrative and procedural costs linked to importing and exporting.</td>
<td>4. Consider establishing a national single window for trade.</td>
</tr>
<tr>
<td></td>
<td>Time to export: Documentary compliance (hours): 9</td>
<td>2. Improve information availability, particularly on procedures and fees for trading across borders.</td>
<td>5. Consider reduced or joint physical examinations and adopt the use of risk management in all border agencies, including risk-based inspections.</td>
</tr>
<tr>
<td></td>
<td>Time to import: Border compliance (hours): 5</td>
<td>4. Consider establishing a national single window for trade.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Cost to import: Border compliance (USD): 110</td>
<td>5. Consider reduced or joint physical examinations and adopt the use of risk management in all border agencies, including risk-based inspections.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Time to import: Documentary compliance (hours): 8</td>
<td>6. Enhance cross-border cooperation with neighboring countries.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Cost to import: Documentary compliance (USD): 50</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Global rank: 30</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Enforcing Contracts</strong></td>
<td>Time (days): 225</td>
<td>1. Make publicly available judgments in commercial cases at all levels.</td>
<td>2. Strengthen limits on adjournments by linking the granting of adjournments to performance management systems and setting and monitoring time limits.</td>
</tr>
<tr>
<td></td>
<td>Cost (% of claim): 23.1</td>
<td>3. Consider creating a small claims court or a fast track procedure for small claims.</td>
<td>3. Consider creating a small claims court or a fast track procedure for small claims.</td>
</tr>
<tr>
<td></td>
<td>Quality of judicial processes index: 8/18</td>
<td>4. Introduce fully-automated random assignment of cases to judges at the Thimphu District Court, Commercial Bench.</td>
<td>4. Introduce fully-automated random assignment of cases to judges at the Thimphu District Court, Commercial Bench.</td>
</tr>
<tr>
<td></td>
<td>Global rank: 29</td>
<td>5. Consider developing an electronic case management system for judges and lawyers in</td>
<td>5. Consider developing an electronic case management system for judges and lawyers in</td>
</tr>
<tr>
<td>Topics</td>
<td>Indicators (Doing Business 2020 report)</td>
<td>Short-term reform recommendations</td>
<td>Medium- to long-term reform recommendations</td>
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</tr>
<tr>
<td>Resolving Insolvency</td>
<td>Time (years): No practice Cost (percent of estate): No practice Recovery rate (cents on the dollar): No practice Outcome (0 as piecemeal sale and 1 as going concern): 0 Strength of insolvency framework index: 0/16 Global rank: 168</td>
<td>1. Encourage the use of insolvency and debt collection proceedings.</td>
<td>the Thimphu District Court, Commercial Bench. 6. Consider introducing court automation features, such as electronic filing of the initial complaint, electronic service of process and electronic payment of court fees. 7. Consider financial incentives for parties to attempt mediation or conciliation (e.g. refund of court filing fees). 2. Ensure that the new Bankruptcy Act Draft and/or amendments to the Companies Act of 2016 address the gaps identified in the current legislation. a. Introduce provisions allowing the continuation of contracts supplying essential goods and services to the debtor (goods and services necessary for the survival of the business) after commencement of insolvency procedures. b. Include explicit and direct provisions authorizing avoidance (invalidation) of undervalued transactions concluded before the commencement of insolvency proceedings. c. Establish the possibility for the insolvency representative to request new financing after commencement of insolvency proceedings and grant creditors who provide post-commencement financing with priority over claims of existing creditors. d. Allow creditors to select or appoint an insolvency representative.</td>
</tr>
<tr>
<td>Topics</td>
<td>Indicators (Doing Business 2020 report)</td>
<td>Short-term reform recommendations</td>
<td>Medium- to long-term reform recommendations</td>
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<td></td>
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<td></td>
<td>e. Require the creditors’ approval for the sale of substantial assets of the debtor.</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td>f. Establish the right of individual creditors to request at any time information from the insolvency representative on the debtor’s business and financial affairs.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>g. Provide for a trained, licensed and regulated cadre of insolvency professionals to advise courts, creditors, and debtors, and in the appropriate case, to oversee the conduct of collective insolvency proceedings.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>h. Introduce effective reorganization provisions in the corporate legal framework of Bhutan.</td>
</tr>
</tbody>
</table>
**1. Starting a Business**

Efficient and effective business regulations support firm creation and productivity. Economies that have efficient business registration processes also tend to have a higher entry rate by new firms and greater business density.\(^\text{11}\) Faster business registration is associated with more businesses registering in industries with the strongest potential for growth, such as those experiencing expansionary global demand or technology shifts.\(^\text{12}\) Empirical evidence also suggests that more efficient business entry regulations improve firm productivity and macroeconomic performance.\(^\text{13}\) Another recent study found that higher entry costs are associated with a larger informal sector and a smaller number of legally registered firms.\(^\text{14}\) Furthermore, higher compliance costs cut into firm profits and discourage entrepreneurs, which in turn reduces job creation in the economy.\(^\text{15}\)

The *Doing Business* “Starting a Business” indicator measures the procedures, cost, time and paid-in minimum capital necessary for a domestic entrepreneur to register and formally operate a new limited liability company. Globally, Bhutan ranks 103\(^\text{rd}\) out of 190 economies globally in *Doing Business 2020* on the ease of starting a business. It scores 86.4 percentage points (out of 100) on the *Doing Business* score. As reported in *Doing Business 2020*, to start a business in Bhutan, an entrepreneur must go through 8 procedures, namely: conduct a company name search at the Company Registry Division, obtain a Security Clearance Certificate (SCC) from the Royal Bhutan Police, submit a project proposal to the Industrial Department Division (IDD), register at the Office of the Registrar, obtain a business license from the Regional Trade and Industry Office, register for taxes, as well as obtain the Business Identifier Code (BIC) Number, obtain a company seal and open a bank account. The cost to complete all these procedures amounts to 3.7 percent of the country’s income per capita. No paid-in minimum capital is required. Overall, the process takes 12 days whereas in economies like Hong Kong, for example, an entrepreneur can start a business in 1.5 days with only 2 procedures. Table 1.1 provides an overview of Bhutan’s performance in this area as compared to the highest ranked countries.

<table>
<thead>
<tr>
<th>Doing Business Indicator</th>
<th>Bhutan</th>
<th>Regional Average(^\text{16})</th>
<th>Global best performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Procedures (number)</td>
<td>8</td>
<td>7.1</td>
<td>1 (2 countries)</td>
</tr>
<tr>
<td>Time (days)</td>
<td>12</td>
<td>14.5</td>
<td>0.5 (New Zealand)</td>
</tr>
<tr>
<td>Cost (percent of income per capita)</td>
<td>3.7</td>
<td>8.3</td>
<td>0 (2 countries)</td>
</tr>
<tr>
<td>Paid-in Min. capital (percent of income per capita)</td>
<td>0</td>
<td>0.2</td>
<td>0 (120 countries)</td>
</tr>
</tbody>
</table>

*Source: Doing Business 2020 database*

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\(^{16}\) Countries in the South Asian region are: Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka.
Short-term Reform Recommendations:

1. Replace the requirement for police clearance by allowing a declaration, or having the registry conduct the check internally.

To register a limited liability company, an entrepreneur must obtain a security clearance certificate from the Royal Bhutan Police. The criminal background check is performed electronically, and it takes one day. It can also be requested online at www.sec.rbp.bt.

If Bhutan intends to align business registration to best practices, the process should become declaratory in nature, rather than requiring the approval of an agency. While the Government has recently reduced the time required to obtain the security clearance certificate and made the process available online, the requirement has been considered obsolete and is present in only three other economies and/or replaced by a simple self-declaration or affidavit. Luxembourg and the Democratic Republic of Congo, where a similar requirement exists, a signed declaration from the directors certifying that they do not have a criminal record suffices.

New Zealand introduced clear restrictions on some categories of applicants, who by law cannot create a company, based on age restrictions or following a Court order. The local Company Registrar uses this list of restrictions without requesting each applicant to get a police clearance.

Alternatively, checking the status could be done by the registry’s office since the SCC clearance is now integrated with the online single window registry system. The Royal Government of Bhutan could consider shifting the responsibility of checking this information to streamline the overall company incorporation process to the company registry.

2. Introduce a risk-based approach for operating licenses.

Before registration, entrepreneurs must obtain clearance from the Industrial Development Division (IDD) of the Department of Industry under the Ministry of Economic Affairs. In the case of small and cottage-scale companies with startup capital of up to BTN 10 million, the Regional Trade & Industry Office of the Department of Cottage and Small Industries reviews the business proposal. The proposal approval is required to verify that the proposed industrial project is in line with industrial development plans, and for issuance of the industrial license. This requirement of compliance with development plans is uncommon in many economies where such decisions are left up to the entrepreneurs themselves as to whether a business is viable given market circumstances.

Best practice economies do not require a license first to register as a legal entity. In these cases, the enterprise is registered, and only after that it needs to get its relevant license(s) to operate. For example, in New Zealand an entrepreneur registers their company in less than a day and is then deemed to be a legal person which can then determine for which activities it will need licenses.

Additionally, in Bhutan after registration with the Registrar of Companies, the entrepreneur needs to obtain an operating license from the Regional Trade and Industry Office of the Ministry of Economic Affairs. This requirement applies to all kinds of businesses. The Royal Government of Bhutan should consider developing a risk-based approach for businesses that perform low risk, general industrial or commercial activities. Globally, the best practice is to take a risk-based approach and require licenses only for activities that pose risk to public health, safety or the environment. Many countries ask the applicant to mention the main type of commercial activity a company intends to engage in. It helps the government

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17 Besides Bhutan only Cambodia, Iran and Oman require a police report or clearance.
to have information on commercial activities in various sectors of the economy. Such information may be updated as part of the annual returns to reflect the main activity a company was involved in during the past year of operations. However, in most countries, no separate operating license is required for general commercial activities as part of the business registration process. In countries such as Colombia, businesses register at the one-stop shop which later notifies the local authority. The local authority then classifies the company according to a risk-based system and decides whether to inspect the business and to require a license. In 2012, Costa Rica introduced a new risk-based system which classifies business activities by potential risk for the provision of sanitary permits from the Ministry of Health. Under this new system, companies which perform activities identified as having a low health risk (Category C) are granted a sanitary permit automatically upon request. Over the past three years, countries as diverse as Peru and Guinea-Bissau have eliminated the requirement of operating licenses for general commercial companies.

3. Merge the name search and clearance process with registration.

In Bhutan, companies’ names must be cleared by the Registrar. According to the Chapter 5 of the Companies Act, 2016 no company shall be incorporated with a name which, in the opinion of the Registrar, is undesirable or is identical with, or too nearly resembles the name by which a company in existence has been previously registered. Entrepreneurs submit a company name search application to verify the uniqueness of the desired company name. Preliminary search of availability of the name can be done online at http://www.cra.gov.bt/searchCompanyName and there is also the option to conduct name search and approval online. However, most entrepreneurs still prefer to do this in person. In the short term, an outreach campaign to communicate the benefits of the online procedures would bring attention and encourage the public to use the online services.

Additionally, the Royal Government of Bhutan could also consider merging the name search with registration. Companies would list their desired names in the registration application in order of priority and the registrar’s office would conduct the search and approval on their behalf. Recently, Pakistan introduced such a reform: after consulting online the available names, the company submits the desired names in the incorporation forms. In 2001, Australia introduced clear rules for ascertaining whether company names are identical, restricted words and phrases, and instances in which consent is required. These rules lead to an automatic name rejection or acceptance at the time of registration, and they have proved successful in increasing both transparency and efficiency in company name search and clearance. Individuals may check online the availability of the name they intend to use and subsequently apply for it. A set of automated tests are then performed to determine if the proposed business name is available. This can result in either an automated acceptance or rejection. In exceptional circumstances, the Australian Securities and Investments Commission, i.e. the authority in charge of reviewing company names, may also perform a manual review and reject the name applied for, if it is an unknown word or if it is deemed to be offensive or potentially misleading for the public.

Medium-term Reform Recommendations:

4. Consider alternatives to the practice of using company seals.

According to Section 225 of the Companies Act, 2016, companies may have a company seal. Obtaining a seal requires one day and the cost varies between BTN 100-1,200. In 2016, pursuant to the Companies Act, the Government made the seal optional. However, the update has not translated into practice yet. In practice, a company must have a seal to conduct its operations and it stands as a requirement to opening a bank account.
The Royal Government of Bhutan should consider carrying out a dissemination campaign and encourage businesses and banks to stop requiring the seal. Other countries that successfully repealed the seal did so through updated legislation, coupled with technological improvements such as the introduction of e-signatures. In the United Kingdom, for example, the Companies Act provides that a document is validly executed by a company if signed on behalf of the company by (i) two ‘authorized signatories’, or (ii) one director, in the presence of a witness who attests the director’s signature. Further, the authentication of the person signing on behalf of the company can easily be verified through the commercial registry.

None of the top-ranking countries on the ease of starting a business in the Doing Business report require new companies to obtain seals to begin operating. The UK, where the common seal originated, made its use optional about 20 years ago. Ghana, Rwanda, Singapore and Tanzania also took the necessary steps to abolish it. In Central Asia, the Kyrgyz Republic made obtaining a company seal optional, while Georgia eliminated it altogether.

5. Introduce a single business identifier and develop interoperable ICT systems and a common database to transmit and share business information among all government agencies.

The Royal Government of Bhutan has introduced measures to increase the automatization of the company registry and other agencies that partake in the incorporation of a company. An important step in integrating company registration services across different entities is the introduction of a single company identification number, which becomes the unique identifier for all interactions between the company and the different government entities. It reduces the risk of errors in identifying the same companies due to the different numbers used by different agencies which may be incompatible. A single ID (or “unique business identifier”) system would reduce the risk of errors in identifying the same companies and support enforcement. It would greatly facilitate information sharing across agencies and remove the need to ask entrepreneurs to provide the same set of information multiple times across the various application forms.

To successfully implement the single ID, a common database and interoperable information and communication technology (ICT) systems of relevant government agencies should be developed to transmit and share business information among all agencies. Such organization would make it easy for businesses to deal with different regulations, and for different government agencies to effectively monitor and regulate business activities. When Norway introduced a single ID, the Ministry of Finance was a powerful supporter of the reform. The Ministry and the tax authorities aimed at a more efficient tax reporting system and saw that they would benefit from the exchange of business information by a common unique identifier. This kind of reform does not necessarily require introducing an entirely new ID. The Government of Belgium, for example, refrained from introducing a new number but rather changed the old Value Added Tax (VAT) ID number into an enterprise number. Two approaches to implementing this reform are most common. In one case, business registration is the initial step and includes the allocation of a unique ID, which is then also used by other authorities, such as the tax authorities or social security agencies. In Australia, for example, business registration is the first step in the process and includes the allocation of the company ID. Norway takes another approach: entrepreneurs are allocated a unique ID before they proceed to register their business. The ID and the identifying information are then made available and re-used by all agencies involved in the registration process.

Introducing a common ID for businesses requires mapping and conversion of existing identifiers. It is a comparatively complex and cost-intensive reform. Nonetheless, a growing number of countries have introduced such common IDs to increase efficiency within the public sector and reduce the administrative burden on businesses. In 2009, Singapore introduced a single identification number (SINGPASS) for all business-to-government transactions. In Estonia and Norway, systems are interoperable and interlinked
with six other agency systems, namely e-procurement system for government agencies, and the land, labor, tax, pledges and citizen’s registries. Similarly, Slovenia’s system is also interoperable with six systems: land, labor, tax, pledges and citizen’s registries and the trade database. Malaysia, Peru, Burkina Faso and Armenia have also unified their tax and business registrations. In Malaysia, after the introduction of the unique company identification number in 2010, companies being registered at the Companies Commission of Malaysia (CCM) complete company incorporation, and at the same time comply with registration with the Tax authorities, Employment Provident Fund, Social Security Organization, and the Inland Revenue Board. In addition, CCM now provides a post-incorporation package for sale, which includes the company seal, statutory books and share certificates. If applications are dropped off in the morning, the incorporation is completed the same day and the incorporation documents can be picked up later that afternoon.

6. Introduce an electronic single window for business registration.

All the agencies with which entrepreneurs should register in Bhutan currently operate in silos, requiring entrepreneurs to move across the different offices and submit the same information to each agency. Throughout all these interactions the entrepreneur appears in person before six different agencies (Company Registry Division - Ministry of Economic Affairs; Royal Bhutan Police; Industrial Department Division (IDD) of the Ministry of Economic Affairs; Regulatory Authority for Companies - Ministry of Economic Affairs; Regional Trade and Industry Office; Department of Revenue and Customs, Ministry of Finance) as part of the process. This is a time consuming and cumbersome process.

After having streamlined and modernized the registration systems with different agencies as recommended above, in the long term, Bhutan could create a single interface for all registration formalities. After streamlining the information required by the agencies, a single electronic registration form could be introduced to capture information required by all involved agencies. This application should include all the information needed by the two agencies in a single document, which should correspond only to one identification number. Other agencies could be given access to the registration database for the type of information they need.

Before establishing a one-stop shop, it is critical to streamline all business registration processes currently in place. Some requirements may be removed or merged with others. Once processes have been streamlined, all relevant administration approvals should be consolidated at one single access point. The objective of a one-stop shop is to reduce the number of interactions between the entrepreneur and any administration agency. After the introduction of a single registration form for all agencies, it is recommended that the systems and databases of multiple agencies be gradually linked to move towards a “single interface” for business registration, which would allow an entrepreneur to complete company creation in one interaction with the administration. Key to the success of the reform is giving officials decision-making power for their respective agencies and ensuring a full interoperability among the databases of the different agencies involved. Without it, delays will continue as the approvals would still be done at each agency’s back-office. Economies that fail to do this see their one-stop shop become “one more stop” in the company registration process.

Today over 115 economies around the world have one-stop shops for business registration, including 41 that established or improved one in the past 6 years. While some one-stop shops are solely for business registration, others carry out many integrated functions, including post-registration formalities with tax agencies or municipalities. Some one-stop shops are virtual; others are physical, with one or more windows. Models vary. For example, in 2016, Niger streamlined the procedures of company registration by allowing applicants file documents with the Commercial Registry at the Greffe du Tribunal (RCCM) at the one stop shop (CFE) while simultaneously registering with the tax administration representatives, the social security and the labor agency. Malta’s Registrar of Companies and the Inland Revenue Department merged their
operations to allow Tax Identification Number to be automatically generated. Some other one-stop shops provide a single electronic interface for entrepreneurs, as in Denmark, New Zealand and Norway.

Nonetheless, in the economies that have one-stop shop offering at least one service besides business registration, the time it takes to register a business is more than twice as fast as in those without such services. A recent study in Portugal shows that introducing a one-stop shop for business registration led to a 17 percent increase in new firm registrations and 7 new jobs per 100,000 inhabitants. In Malaysia, after the introduction of the unique company identification number in 2010, companies that register at the Companies Commission of Malaysia (CCM) complete company incorporation, and at the same time comply with registration to the Tax authorities, Employment Provident Fund, Social Security Organization, and the Inland Revenue Board. In addition, CCM provides now a post-incorporation package for sale, which includes the statutory books and share certificates.

In the medium to long term, and once it has become electronic, the Registrar of the Companies could then link its database with the tax authority database, and the agencies could harmonize workflows through automation to move the single window to a full-fledged electronic one-stop shop for business registration. The one stop shop could initially accept manual applications but eventually it would allow for online business registration. Making registration electronic is the ultimate way to speed up and streamline business start-up.

Seven of the economies with the fastest business start-up offer on-line electronic registration—Portugal, Denmark, Australia, Canada, Estonia, New Zealand and Singapore. More than 20 economies have introduced electronic registration over the past 6 years. In Portugal, the online platform “FastTrack” allows users to select a pre-approved name from the registry’s website and proceed to the one-stop website to register one’s company. The registry then automatically processes the taxation, social security and labor registration, and publishes the incorporation notice.

Mauritius provides another example of a successful reform in this area. Since October 2006, all new businesses, including companies and individuals in Mauritius are registered through a “Companies & Business Registration Integrated System.” The applications for incorporation and registration are done online. The Commercial Registry grants access to information on new company registrations to tax, social security and local authorities through a Central Business Registration Database. At the time of registration, the Companies Registrar electronically informs the tax and local administration of newly registered companies. Tax registration then takes place automatically. Once informed by the registry, local administration will contact the companies and inform them of fees to be paid or any additional requirements based on the activity of the company. After the introduction of the computerized system in Mauritius, the total time of business registration was reduced by 80 percent.

Bhutan has already laid the ground work for online registration with the enactment of Bhutan Information Communications and Media Bill in 2016 which introduced regulatory framework for digital and electronic signatures. Box 1.1 contains some further and important considerations for the administration in Bhutan to keep in mind before implementing an online business registration system.

**Box 1.1: Key Considerations in Implementing Company Registry Software Applications**

1. Complete the legal and business process reforms before automation—to fully realize the potential benefits of technology.

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2. Critically assess the agency’s ICT capacity, both staff and infrastructure—if internal capacity is inadequate, identify hosting alternatives within administration or the private sector.

3. Fully document the business and functionality requirements before procuring a technology solution—this will also inform decisions concerning packaged versus custom-developed software.

4. Identify and build data linkages with other administration agencies - both to simplify the overall business entry process and ensure company data is fully leveraged to improve regulatory oversight.

5. Leverage the technology platform to produce new revenue streams - including information products for financial institutions, credit bureaus, and other firms seeking company data.

6. Address change management and communications in the implementation plan - to ensure all stakeholders are fully invested in the new solution.

Source: *Leveraging Technology to Support Business Registration Reform, World Bank 2011*

Electronic single windows for business start-up not only save time and money, but also can help streamlining all business registration procedures, easing the administrative burden on customers, making procedural requirement more transparent and easier to access and help all agencies involved to improve coordination of their approvals.
2. Dealing with Construction Permits

Reforms that make regulation of constructions more efficient and transparent can help reduce corruption and informality, while encouraging construction companies to go through formal channels and ensuring compliance with important standards, such as those impacting safety or mitigating climate change. Good regulations, combined with sound enforcement mechanisms, ensure safety standards that protect the public while making the permitting process efficient, transparent and affordable for both building authorities and the private professionals who use it. A recent study shows that long delays to obtain permits could lead to higher transaction costs and less transactions. However, the payoff of construction permitting reforms can be significant. In 2005, a PriceWaterhouseCoopers study found that accelerating permit processes in the United States could permanently increase government revenues. Examining the impact of building permit reforms on new income generation, for every 10 jobs directly related to a construction project, another 8 jobs are created locally. These impacts yield not only additional income for the community, but also additional investments and tax revenues. Beyond economic returns and the pay-off in attracting more investment, the most important benefit of building permit reforms is to protect public safety.

Efficient building permitting systems share key features. Clear building codes and regulations written with a consultative process are at the core of well-designed construction permitting systems. Countries like Canada and New Zealand are increasingly steering towards performance-based codes. Germany, Singapore and Mauritius have incorporated risk-management tools to streamline the issuing of permits and optimize the effectiveness of inspections. Up-to-date land use and zoning plans improve transparency and predictability for developers. Establishing sound licensing mechanisms for practitioners, in addition to well-functioning liability regimes and compulsory insurance systems, have become pivotal to introduce more efficient regulatory systems. Many countries are outsourcing building control procedures to the private sector. For example, France and the UK introduced inspections by accredited bodies, which in turn required improvements in their private liability and insurance regimes.

*Doing Business 2020* records the procedures, time and cost required to build a warehouse and connect it to water and sewage services in Bhutan following all the official requirements. Bhutan ranks 91st globally on the ease of dealing with construction permits, with an overall Distance to the Frontier score of 68.9 percentage points. According to the report, dealing with construction permits requires 21 procedures, takes 150 days and costs 0.9 percent of the warehouse value. Since 2016, the *Doing Business* report also benchmarks building quality control. This index looks at the quality of building regulations, the strength

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19 Sonia Hamman, “Housing matters, Volume 1,” World Bank Policy Research Working Paper 6876, 2014. In particular, the paper mentions that “Mayer and Somerville’s (2000) study of U.S. regulations estimates that a metropolitan area with a 4.5-month delay in approval and two different types of growth-control restrictions would have about 45% less construction than a metropolitan area with a 1.5-month delay and no growth management policy.”

20 For a single building project, accelerating permit processes provides a temporary acceleration of property tax collections. For a representative series of projects, the study shows that these revenue increases could reach 16% over a period of 5 years. “Economic Impact of Accelerating Permit Processes on Local Development and Government Revenues” PriceWaterhouseCoopers, December 2005.


22 Performance-based codes provide more flexibility and support innovation by focusing on outcomes to be achieved rather than prescribing how the building must be constructed. The use of performance-based codes, however, requires a higher level of technical competence to enforce than do other approaches.


24 For example in France, the Spinetta Act of 1978, required broad-based insurance and warranty coverage.

25 It accounts for a quarter of the overall ranking for Dealing with Construction Permits indicator.
of quality control and safety mechanisms, liability and insurance regimes, and professional certification requirements. Out of 15 possible points, Bhutan scores 12 in the building quality control index. (Table 2.1.).

Table 2.1 Dealing with Construction Permits ranking and best performers

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Bhutan</th>
<th>Regional average</th>
<th>Global Best Performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Procedures (number)</td>
<td>21</td>
<td>14.6</td>
<td>None in 2018/19</td>
</tr>
<tr>
<td>Duration (days)</td>
<td>150</td>
<td>149.7</td>
<td>None in 2018/19</td>
</tr>
<tr>
<td>Cost (percent of warehouse value)</td>
<td>0.9</td>
<td>12.5</td>
<td>None in 2018/19</td>
</tr>
<tr>
<td>Building quality control index (0-15)</td>
<td>12</td>
<td>9.4</td>
<td>15.0 (6 Economies)</td>
</tr>
</tbody>
</table>

Source: Doing Business 2020 database

Short-term reform recommendations:

1. Consider issuing the occupancy certificate on the spot for low-risk projects in full compliance, at the time of final inspection.

Low-risk buildings require less documentation and fewer inspections than more complex structures and can be approved faster. This saves time for both the entrepreneurs and the authorities and allows them to direct their efforts and resources more efficiently. The Royal Government of Bhutan could review the document requirements, approval, and inspection processes and introduce a simplified process for smaller, low-risk projects. Currently, the occupancy certificate is granted within 14 days of the final inspection by Thimphu Thromde. The completed construction is inspected by a team (architect, engineer, surveyor, the building inspector, and representatives of electrical, plumbing, and sanitation agencies) joined by the National Environment Commission if necessary. In several other countries, the authority issues the certificate of completion on the spot during the final inspection if the project fully complies with the previously-approved building permit, eliminating the need for an additional interaction between the entrepreneur and the authorities.

Canada is one such example: if all required inspections have been carried out and the building or structure is deemed substantially complete and fit for occupancy, the completion certificate is issued—avoiding any additional interactions for the builder. In Vietnam, at the end of construction, the Department of Construction visits the site to confirm that the building was built according to the master plans, rules, and regulations and issues the certificate on the spot. Singapore has an integrated online system through which builders can request the final inspection and the occupancy permit without delay. In Portugal the municipality of Lisbon has developed a tracking system that is automatically updated once the final inspection takes place, so the occupancy permit can be obtained from the municipality on the same day. Following this practice could potentially save time for both entrepreneurs and public officials in Thimphu Thromde. The Republic of Korea introduced risk-based approvals in 2005/06. In May 2006, small construction projects could choose a fast-track option. This allowed regulators to focus their time and resources on more complex projects with potential environmental or public safety risks. The reform was timely because it coincided with higher demand for construction: between 2004 and 2009, the number of applications for commercial building permits in Seoul increased from 1,521 to 3,895. Following this practice could potentially save time for both entrepreneurs and public officials in Thimphu Thromde.

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26 Doing Business Report 2012
Medium to longer-term reform recommendations:

2. Review the risk-based classification of buildings based on their intrinsic features and intended use.

International good practice shows that not all building projects are associated with the same economic or environmental risks and as a result, not all construction plans require the same degree of scrutiny. Efficient governments have implemented rigorous yet differentiated construction permitting processes to treat buildings according to their risk level and location. The short-term recommendation above is to introduce a shorter timeline for issuing occupancy permits for low-risk commercial buildings, but it is important that the risk classification be done in the longer term in a more comprehensive way.

It is recommended to conduct a risk assessment of the stock of buildings in Bhutan, which would serve as basis for a risk-based system for building permits applications and pre/post construction inspections, and a review of existing construction regulations to differentiate areas that warrant more attention and direct controls from the building authorities from those that warrant less. This exercise would allow the competent authority to streamline and prioritize the issuance of building permits in a responsible manner. It would provide the basis for actions that could reduce the procedures and the time to obtain building permits in the future.

Modern best practices have established risk categorizations typically associated with the footprint of the building, the building’s size and height, and its intended purpose. This classification determines the level of checks required for each building type and creates a predictable framework for building authorities and building professionals. Rwanda has recently passed legislation with delineating the inspection type of buildings in relation to their anticipated risks, and clearly outlines the building classifications and provides a risk matrix.

Today, nearly 20 countries have risk-based inspections mandated by law, including Djibouti, India, Peru and Jamaica.\(^\text{27}\) Under the “Smart Regulator” program, Hong Kong reduced the time to deal with construction permits by 36 days and eliminated or merged 8 procedures related to inspections and preapprovals. In the European Union, the European Standard EN 1990 sets three “Consequence Classes” determined by the risks to users as well as social and economic consequences (Figure 2.1). Each category requires a different and proportionate degree of scrutiny from building authorities.\(^\text{28}\)

\(^{27}\) Doing Business database.

Other jurisdictions have combined the use of risk-based approvals with the provision of fast-track options. For example, for small, low risk projects, developers of commercial buildings in Ontario, Canada, can opt for the “Commercial Xpress” permit review process which takes just 10 days. A similar procedure is in place for further construction works in existing residential buildings. Under Article 10 of the new building code, anyone who intends to construct a building may choose to apply for a fast-track procedure. Similar fast track procedures exist in the United States. For example, the New York City Department of Buildings (DOB) offers a fast-track service for simple projects called the Professional Certification Program, as it relies on self-certification mechanisms by certified private practitioners. In these cases, the process of DOB

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30 The following projects qualify for the Commercial Xpress service: interior alterations to assembly, business, industrial, office and retail uses, up to 300m² in area, no change of use, no change in patron area for restaurants, tents, and minor fire damage repair For more information on the project based building permitting procedures in Ontario, please visit: http://www1.toronto.ca/wps/portal/contentonly?vgnextoid=ec14b1c296e0410VgnVCM10000071d60f89RCRD
examination and approval of plans is eliminated, although the application must go through the same pre-filing payment and data entry process as normal applications. In addition, 20 percent of all applications will have an audit within 10 days of the building permit issuance. As a general rule, fast-track options should only be implemented where regulations clearly spell out the requirements and enforcement is strong. This can avoid risks associated with structural flaws, as well as corruption. Additionally, risk-based inspections eliminate the necessity of all building types undergoing the same set of inspections. Usually, risk-based inspections are conducted during construction. If a warehouse is a low-risk building, then the number of inspections done by the public sector is fewer than in the case of building a tall residential building. Usually a risk-based inspections matrix defines the risk category by use purpose, size, and type of the building and mandates a specific number of inspections for each category.

3. Establish clear standards to determine liability for problems occurring after the completion of the construction and consider a mandatory insurance requirement to cover structural defects.

When defects are discovered during construction, they are more likely to be easily remedied. However, defects are often discovered only after the building has been occupied. Remedy defects at that stage can be both costly and time-consuming. It is important that the responsible party be held liable and that the parties involved in the building design, supervision and construction obtain insurance to cover the costs of any structural defects. In Bhutan, the law does not define which parties are responsible once the building is in use nor mandates any party to obtain insurance to cover for structural flaws or problems that occur after the building has been legally occupied.

Establishing clear standards to determine liability for problems occurring after the completion of construction, and insurance to cover any costs arising from structural defects, benefits clients as well as contractors and encourages more construction, particularly for small and medium-size construction companies. While many advanced economies also lack specific legal provisions related to insurance, they typically have standard contractual clauses that set the liability regime and insurance requirements for structural defects. In order to align itself to good international practice, Bhutan should define which parties are held legally liable for structural defects and which are required to obtain insurance policies to cover damages caused by defects. In doing so, Bhutan can follow the example of Denmark or France, both early adopters of mandatory insurance regimes, to introduce a mandatory decennial insurance requirement. In both countries, the term of the insurance is ten years. In Denmark, the mandatory decennial insurance is required for construction of new permanent dwellings. The municipality checks the validity of insurance before the issuance of the building permit and after the completion of construction, when issuing the occupancy permit. In France, the same requirement applies to all new buildings, regardless of the functional purpose, and has two levels – insurance covering defects in the constructed property (dommage ouvrage) taken out by the owners of the building, and decennial insurance taken out by constructors to cover possible structural flaws. As a first step, Bhutan could start by introducing and promoting voluntary mechanisms. A public-private partnership between the Government and the construction association could then identify the most relevant cases for a decennial insurance and develop standard contractual clauses. Alternatively, the mandatory decennial insurance requirement could be introduced only for major projects. For example, Italy has introduced compulsory decennial insurance for public procurement projects exceeding 10 million Euros.

31 http://www1.nyc.gov/site/buildings/industry/professional-certification.page
32 Consortium formed by Centre d’Études d’Assurances (CEA) and Centre Scientifique et Technique du Bâtiment (CSTB) (2010). Liability and insurance regimes in the construction sector: national schemes and guidelines to stimulate innovation and sustainability. Paris: ELIOS
4. Introduce a single online window for online application and approval of construction permits.

Recently, the Municipality of Thimphu implemented an online system for obtaining a building permit. However, it is not widely used. Therefore, every process and transaction in construction permit is still paper based in many cases in Bhutan. The deployment of new technologies can help Bhutan “leapfrog” to a more efficient and transparent building regulatory apparatus. New technologies such as e-applications (e.g. web-based software applications) or web and SMS-based tracking and notification systems can bring automation which can substantially improve efficiency in construction-permitting administration as well as increase formality and compliance with safety requirements. Automation will require transparency with respect to regulatory agency approval processes and documentary requirements. The Municipality of Bhutan should ensure that the new system include:

- Online submission of applications for construction license or notification, renewals, appeal processes, inspections, occupancy certificates;
- Online tracking of applications;
- Comprehensive database pertinent to construction permitting processes that shall include: legacy data of construction permit approval, renewal, rejection, related inspections, related appeals, and occupancy certification; This should also include database of registered vendors/ architects’ information;
- Automated workflow capabilities for construction permit approval, renewal, carrying out inspection activities such as planning, scheduling, risk assessment, documenting visit checklists, reports and actions, communication with business via e-mail or SMS, etc., and occupancy certification;
- Analytical Reporting;
- Document management and archiving capabilities to handle attachment uploaded to the system.

Several countries already have such computerized systems in place. Developers in countries as distinct as Nepal, India, Egypt, Portugal and the United States can complete their building permit applications online. In Singapore, the data management system, established in 2001, enables easy access to information needed for obtaining a building permit, it allows on-line submission of plans, and it facilitate efficient permit processing. Today, builders regularly receive updates on the status of their application either by e-mail or text messaging. As a result, the time for dealing with construction permits has been reduced by two-thirds. This reform saves time for builders and government officials alike. In addition, developers can pay the fees by using an online system called CORENET. In 2009, Egypt introduced a single window for processing construction-related approvals. In Nepal, the Kathmandu Metropolitan City (KMC) has implemented an online system allowing for building permit and all design plans and relevant documents to be submitted online. The applicant has the option of tracking the status of their application online.

In September 2011, Kenya implemented a web-based software application to automate plan review procedures and delivery of construction and occupancy certificates, also complemented by a web and SMS-based tracking and notification system. It used to take 6 months for a building permit approval in Nairobi, before this reform, it now takes 30 days and the use of “expeditors’ by architects has been eliminated (see Box 2.2).
In its ultimate form, automation would allow for the electronic submission and review of building plans. However, automation, unlike the other reforms, would require substantial technical hardware investments. Lastly, it should be noted that to reap the full benefits of automation and new technologies, prior initiatives must be undertaken. Before implementing automated solutions, it is advisable to reengineer the issuance of building permits, modernize the workflow systems and physically reorganize the office floor to mirror the steps of a simplified process.

After the full operationalization of the online application process, the Government could extend the existing single window to the application and approval of connections with utility companies where applicants would be able to apply and pay the respective fees for all clearances simultaneously and all the utility connections by submitting one online form along with the design plans. There should be in-built safeguards to allow for the confidentiality and security of information provided by building professionals. Strict digital signature protocols as well as data encryption functionalities should be incorporated into the system.

Many countries that introduced some form of single window gradually improved it by integrating more services. For example, in Hong Kong the one-stop shop hosts six local departments and two private utility companies under the same roof. Similarly, in Malaysia, developers can now apply for pre-construction authorizations, building permits and utility connections through the new “One Stop Centre” (OSC) at the Kuala Lumpur City Hall. After the single application is submitted, the OSC refers the submissions to all the competent authorities, including the sewerage and water agencies, while it also arranges and coordinates the inspections and final connections with the utility providers.

In Mumbai, a single online application is submitted along with all requisite documents and drawings of the proposed work. The concerned officer at the zonal building proposal office will scrutinize the proposal and essential documents as per procedure. If all documents are in order and the file is complete, the scrutiny fees are paid online via the portal. Communication to obtain approvals from various other agencies (Stormwater and Drain Department, Sewerage Department, Hydraulic Engineer Department, Roads and Traffic Department) are also submitted and obtained through this portal.
3. Getting Electricity

The World Economic Forum (WEF) sees infrastructure, including electricity provision, as one of the four pillars of competitiveness – i.e. the set of institutions and factors that determine a country’s productivity. A reliable electricity supply boosts firms’ output – while also affecting societal welfare in areas like education\(^{33}\) and healthcare.\(^{34}\) Without a stable energy supply, businesses cannot make full use of their capital and risk under production. Where the quality and accessibility of infrastructure services is poor, companies’ productivity is negatively impacted.\(^{35}\) This holds especially true for small and medium enterprises (SMEs), as many cannot turn to captive power options (e.g. generators) due to limited resources.\(^{36}\) Empirical research has shown that investment (domestic and foreign) tends to be attracted to countries that are able to offer a reliable supply of electricity.\(^{37}\) Moreover, the 2018 World Bank Enterprise Surveys data reports that business owners in developing economies perceive electricity (or lack thereof) as the fourth biggest obstacle to their activities behind only access to finance, the informal sector and political instability.\(^{38}\)

Demand-side challenges are arguably the biggest obstacle to greater electrification according to a World Bank study.\(^{39}\) Such challenges mostly come in the form of power reliability and supply adequacy, tariff affordability and the complexity of the connection process. Studies, for example, have shown that cost-effective connections lead to an increase in electrification.\(^{40}\)

Simpler electricity connections - in terms of time, cost and procedures – positively impact firm performance. This is particularly the case in industries with high electricity needs, such as manufacturing.\(^{41}\) Research further finds that removing hurdles related to obtaining an electricity connection is associated with positive sector outcomes, like an increase in electrification rates.\(^{42}\) Finally, studies have shown that businesses that lack access to electricity connections are prevented from moving into higher-value-added activities.\(^{43}\)

Efficient electricity connection processes share key features. Approvals that customers must obtain for the connection should be consolidated. Moreover, in countries with efficient electricity connection processes, the responsibility for the safety compliance of the building’s internal wiring is transferred to private electrical contractors, and customers do not have to go through inspection procedures themselves. Economies in which responsibility for safety compliance is transferred to private electrical contractors usually have a well-regulated industry of electrical engineers with a national accreditation system and professional licensing.

The Doing Business Getting Electricity indicator measures the ease of the connection process, along with the reliability of electricity supply and the transparency of tariffs. The indicator set helps to understand the challenges and potential bottlenecks firms face vis-à-vis the electricity sector. For example,


\(^{35}\) Calderon and Serven (2003), Dollar et al. (2005), Eiffert (2007).

\(^{36}\) Moyo (2013)

\(^{37}\) Audinet and Rodriguez Pardina (2010).


\(^{41}\) Ramalho and Geginat (2015).

\(^{42}\) Ramalho and Geginat (2015).

\(^{43}\) Shaw (2014).
it provides data on the process of obtaining a new electricity connection for local SMEs, detailing the associated procedures along with their time and cost. This benchmark enables utilities and regulators to gauge the connection service and learn from best practices as efficient connection processes share key features.

To measure the reliability of supply and transparency of tariffs, the Getting Electricity indicator presents an index scored from 0 to 8 points. It encompasses quantitative output data on the duration and frequency of power outages, measured through SAIDI and SAIFI\(^44\) for calendar year 2018, as well as qualitative input information, i.e. the role of the energy regulator, the use of automated systems to monitor power outages and restore power supply, whether financial deterrents exist to limit outages, and whether tariffs and tariff changes are communicated efficiently to customers.

As reported in the Doing Business 2020 report, the process to connect to the grid in Bhutan is relatively less time-consuming than the regional average. Entrepreneurs must go through 4 procedures over 61 days and pay the equivalent of 381.6 percent of GNI per capita to comply with all official requirements. Bhutan also scores 4 out of 8 points on the reliability of supply and transparency of tariffs index – in part due to the relative frequency of power outages through 2018 and the lack of mechanisms for monitoring outages and restoring service. Globally, Bhutan ranks 78 out of 190 economies on the ease of getting electricity with a score of 77.5. Table 3.1 provides an overview of the country’s performance in getting electricity.

**Table 3.1. Getting Electricity ranking and best performers**

<table>
<thead>
<tr>
<th>Doing Business indicator</th>
<th>Bhutan</th>
<th>South Asia average</th>
<th>Global Best Performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Procedures (number)</td>
<td>4</td>
<td>5.5</td>
<td>3 (28 Economies)</td>
</tr>
<tr>
<td>Duration (days)</td>
<td>61</td>
<td>86.1</td>
<td>18 (3 Economies)</td>
</tr>
<tr>
<td>Cost (% of GNI per capita)</td>
<td>381.6</td>
<td>952.6</td>
<td>0.0 (3 Economies)</td>
</tr>
<tr>
<td>Reliability of supply and transparency of tariff index (0–8)</td>
<td>4</td>
<td>2.7</td>
<td>8 (26 Economies)</td>
</tr>
</tbody>
</table>

*Source: Doing Business 2020.*

*Doing Business* focuses on a local firm seeking a commercial connection for new a warehouse located in an industrial area of Thimphu.\(^45\) The utility provider is Bhutan Power Corporation and *Doing Business* reports that the connection will take 4 procedures, 61 days and 381.6 percent of GNI per capita (Figure 3.1). These estimates reflect a scenario where there isn’t enough network capacity to accommodate a new 140 kVA connection to the low voltage network, so the customer needs to finance a network extension and build a substation. While this can be avoided if there is, in fact, enough capacity,

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\(^44\) *Doing Business* uses the system average interruption duration index (SAIDI) and the system average interruption frequency index (SAIFI) to measure the duration and frequency of power outages in the largest business city of each economy. SAIDI is the average total duration of outages over the course of a year for each customer served, while SAIFI is the average number of service interruptions experienced by a customer in a year.

\(^45\) The electricity connection is a permanent one. Is a three-phase, four-wire Y connection with a subscribed capacity of 140-kilovolt-ampere (kVA) with a power factor of 1, when 1 kVA = 1 kilowatt (kW). Has a length of 150 meters. The connection is to either the low- or medium- voltage distribution network and is either overhead or underground, whichever is more common in the area where the warehouse is located. It Requires works that involve the crossing of a 10-meter wide road (by excavation, overhead lines) but are all carried out on public land. There is no crossing of other owners’ private property because the warehouse has access to a road. Includes only negligible length in the customer’s private domain. Does not require work to install the internal wiring of the warehouse. This has already been completed up to and including the customer’s service panel or switchboard and the meter base. For Bhutan, the specific area of Thimphu is Babesa.
private contractors report that this is often not the case, resulting in the following connection process. First, a connection request needs to be formally lodged with the Bhutan Power Corporation in person. There is no charge for submitting the application. Then, the client receives a site inspection, so that the utility company can prepare an estimate. Following this step and depending on the customer's preference, the external connection and trench works will be carried out by either Bhutan Power or a private contractor. The cost estimate provided to the customer also includes the cost of the required materials such as a substation, rabbit conductor, cables, poles and line extension. The customer has a choice of getting external connection works done by either the utility or by a private contractor. In general, customers choose to have the external done by the private contractor as it can be done faster. All materials, except the distribution transformer are purchased from the utility as they have materials of the correct specification. The distribution transformer needs to be imported, usually from India. When the external works are completed, the customer receives internal wiring inspection, transformer testing, meter installation and electricity flow.

Figure 3.1. Procedures to get a new electricity connection in Bhutan.

Source: Doing Business 2020

Reliability of supply and transparency of tariff index

The reliability of supply and transparency of tariff index of Doing Business shows that the electricity sector in Bhutan is transparent and regulated, but reliability can still undermine firms. The country's SAIFI index shows that each customer served experiences on average, 2.9 outages per year, whereas the SAIDI index show that on average, each customer experiences 7.1 hours of outage in a year. 46 Bhutan has established

46 An economy is eligible to obtain a score on the reliability of supply and transparency of tariffs index if it satisfies two conditions. First, the utility must collect data on all types of outages (measuring the average total duration of outages per customer and the average number of outages per customer). Second, the SAIDI value must be below a threshold of 100 hours and the SAIFI value must be under 100 outages. An economy is not eligible to obtain a score if outages are too frequent or long-lasting for the electricity supply to be considered reliable- that is, if the SAIDI or the SAIFI values exceed the determined thresholds. An economy is also
an energy regulatory agency to monitor the utility’s performance on reliability of supply; provides financial
deterrents to limit power outages and the utility does not use automated tools to restore service or to monitor
outages. Bhutan publishes electricity tariffs online and communicates tariff changes at least one billing
cycle in advance to customers and publishes the information on line. However, it is missing automated tools
to monitor and restore outages (Table 3.2).

### Table 3.2. Getting Electricity in Bhutan – Measure of Quality

<table>
<thead>
<tr>
<th>Reliability of supply and transparency of tariff index (0-8)</th>
<th>4</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total duration and frequency of outages per customer a year (0-3)</td>
<td>1</td>
</tr>
<tr>
<td>System average interruption duration index (SAIDI)</td>
<td>7.1</td>
</tr>
<tr>
<td>System average interruption frequency index (SAIFI)</td>
<td>2.9</td>
</tr>
<tr>
<td>What is the minimum outage time (in minutes) that the utility considers for the calculation of SAIDI/SAIFI</td>
<td>5.0</td>
</tr>
<tr>
<td><strong>Mechanisms for monitoring outages (0-1)</strong></td>
<td>0</td>
</tr>
<tr>
<td>Does the distribution utility use automated tools to monitor outages?</td>
<td>No</td>
</tr>
<tr>
<td><strong>Mechanisms for restoring service (0-1)</strong></td>
<td>0</td>
</tr>
<tr>
<td>Does the distribution utility use automated tools to restore service?</td>
<td>No</td>
</tr>
<tr>
<td><strong>Regulatory monitoring (0-1)</strong></td>
<td>1</td>
</tr>
<tr>
<td>Does a regulator— that is, an entity separate from the utility—monitor the utility’s performance on reliability of supply?</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Financial deterrents aimed at limiting outages (0-1)</strong></td>
<td>1</td>
</tr>
<tr>
<td>Does the utility either pay compensation to customers or face fines by the regulator (or both) if outages exceed a certain cap?</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Communication of tariffs and tariff changes (0-1)</strong></td>
<td>1</td>
</tr>
<tr>
<td>Are effective tariffs available online?</td>
<td>Yes</td>
</tr>
<tr>
<td>Link to the website, if available online</td>
<td><a href="http://www.bpc.bt/?s=tariff">http://www.bpc.bt/?s=tariff</a></td>
</tr>
<tr>
<td>Are customers notified of a change in tariff ahead of the billing cycle?</td>
<td>Yes</td>
</tr>
</tbody>
</table>

*Source: Doing Business 2020*

The recommendations below do not address all issues affecting the energy sector in Bhutan and focus only
on the electricity connection process and power reliability from the perspective of end-users.

**Short-term recommendations:**

1. **Review and streamline the procedure for electricity connections.**

According to *Doing Business*, the process to obtain electricity in Bhutan is relatively faster than in neighboring economies, but room for improvement remains. Entrepreneurs must complete 4 procedures, which require about 61 days, including physical works. All applications for new electricity connections are submitted in person at the Bhutan Power Corporation office along with all the required paperwork, according to the Doing Business 2020 data.

Recently, the Bhutan Power Corporation introduced a new online platform for electricity applications. However, it is not widely used, and the majority of the private sector is still not aware of the existence of this online platform.

not eligible to obtain a score on the index if data on power outages are not collected or collected partially (for example, planned outages or load shedding are not included in the calculation of the SAIDI and SAIFI indices), and if the minimum outage time considered for calculation of the SAIDI and SAIDI indices is over 5 minutes.
Bhutan Power Corporation could achieve marginal improvements in time by automating not only the application process for new electricity connections, but also automating the scheduling of the external and internal inspections. Based on the experience of other countries (box 3.1), an online application system should benefit applicants in Bhutan by lowering the time to issue new grid connections. An online portal typically prompts by default customers to submit a complete application – otherwise submission is not possible. These systems also free up human resources for utilities, which they can then allocate towards other functions. Finally, an online portal also increases transparency; customers can usually track the status of their application while the utility is able to determine in real time what are the pending applications. This initiative is among the most effective ways to reduce connection delays as long as (i) it is accompanied with an awareness campaign for users and (ii) there is a dedicated troubleshooting taskforce to address any outstanding issue and/or technical glitch in real time. To further streamline the process to connect to the electricity grid in Bhutan, an online system should facilitate payment of all submission fees electronically using credit card or wire transfers at the time of applying for a new electricity connection. Finally, Bhutan Power Corporation should encourage the use of the new online platform for electricity applications among the private sector and conduct an extensive outreach campaign.

2. Conduct assessment on the feasibility of reducing the cost of obtaining electricity connections for new customers.

According to Doing Business team, obtaining electricity connection for new businesses is costly in Bhutan. Completing the procedures required to connect to the electrical grid costs 412.3 percent of GNI per capita. The cost burden results mainly from the cost of hiring an electrical engineer to carry out external works and purchase the equipment, including the required materials such as a 250 KVA substation, rabbit conductor, cables, poles and line extension (BTN 801,250.05) and the deposit charge for the meter (BTN 5,000).

As a preliminary step, the Bhutan Power Corporation could carry out a study on the cost of the materials/equipment and on the opportunity to share the upfront cost. With regard to the cost of the connection works and transformer, the Bhutan Power Corporation could carry out a study on what drives the cost of the materials and equipment. They may be expensive either because importing them is very costly due to tariff duties and transportation risks; or because there is a shortage of such materials and equipment. After a careful cost-benefit analysis that considers the impact on the budget, the utility company may consider the possibility to share more of the upfront burden of the costs. Subsequently, the utility company may consider implementing measures in line with its assessment.

Indeed, the low capacity of a network does not necessarily mean higher costs for customers. Where the new connection requires a more complicated installation that means installing a distribution transformer, utilities can still regulate costs. In both Osaka and Tokyo there are no connection fees related to getting electricity. The application process, as well as the external connection works and meter installation are not billed by the utility to the customer. For all overhead connections up to 1,000 meters long, the costs are entirely shouldered by the utility. These costs are, in turn, recuperated in the longer run through end-user tariffs.

The Royal Government of Bhutan could also consider providing the option to pay connection fees in installments. While seeking ways to reduce costs, the utility can provide financing options on the short term. One option worth considering is the payment in installments. A fraction of the bill would need to be paid immediately, but the balance could then be reported back to the first few electricity bills after the connection is finalized. In countries like in Korea and North Macedonia, premises are energized ahead of the last installment payment, which is reported to the first electricity bill. In the Republic of Korea, the distribution utility KEPCO charges a standard construction cost of about USD 10,000 for a 150-meter
service line and 140 kW load for underground power intake. Thirty percent of the cost is paid up front, while the remaining 70 percent is paid in installments over a period of up to two years.

Medium- to long-term reform recommendations:

3. Introduce Geographic Information System (GIS) for the electricity distribution network to further streamline the procedure to obtain electricity connection by eliminating site visits to approve a request.

The electricity distribution companies should consider the use of a GIS system to map their distribution network and connection points throughout Thimphu and Bhutan. Thanks to such a system, the Bhutan Power Corporation would be able to have better control over the new electricity connections and require less inspections. It is recommended that the GIS system includes the distribution network and connection points. In other economies, utilities use GIS to make it obsolete to conduct a site visit. In Mexico, for example, the distribution utility developed a GIS to map the electricity distribution network in 2011/12 and thus no longer carries out a physical inspection before issuing the feasibility study. Likewise, with the widespread use of GIS in Turkey, the utility Boğaziçi Elektrik Dağıtım A.Ş. no longer conducts external inspections for new electricity connections. For all new connections, the utility can now check via GIS whether an additional transformer is needed to provide electricity to the new customer.

4. Implement an automated system to monitor outages and restore service.

To improve the capturing and reporting of system reliability and quality indicators such as SAIDI and SAIFI, automated systems should be put in place in Bhutan. Positive changes to the quality of power supply can only be achieved with substantial investment and a long-term approach targeting transmission losses and inadequate generation capacity. Addressing these issues is often outside of the utility’s control. However, utility companies have practical tools at their disposal to address the some of the sources of power failures, and restore the service when outages occur.

Whether planned or unplanned outages, the speed and efficiency at which power can be restored depends largely on the type of control systems and tools available to the distribution utility. The traditional approach for restoring power that is used by many utilities is through dispatching maintenance crews to the fault location following customer calls. This may take several hours to complete, depending on how quickly customers report the power outage and the maintenance crew locates and solves the problem. Hours without power in turn pose financial risks to businesses in the form of equipment and inventory damages and spoilage. Instead of relying on call centers to keep track of power cuts, utilities may significantly reduce power restoration time and equipment damages through electronic systems such as SCADA (Supervisory Control and Data Acquisition) and IMS (Incidence Management System). A modern SCADA system is one of the most cost-efficient solutions that not only helps utilities increase reliability through automation but also helps to lower costs and enable problem areas to be detected and addressed automatically and remotely.

The Doing Business report finds that in over 130 economies, utilities were able to benefit from these automated systems to monitor power outages and in 136 economies, they used such systems to restore service, which allowed them to provide a more reliable service to their customers.
4. Registering property

Research shows that registered property rights play an important role in supporting investment, productivity and growth. Cadasters or surveys, together with land registries, are institutions with the mandate to secure property and land use rights. These institutions are part of the land information system of a country. With land and buildings accounting for between half and three-quarters of the wealth in most countries, having an up-to-date land information system matter. Research suggests that property owners with registered titles are more likely to invest and that they also have a better chance of getting credit when using their property as collateral. Clear property titles can allow buyers to use the property for expanding their businesses, to pledge it as collateral for new loans or to sell to another business. Governments also benefit from having reliable, up-to-date information in cadasters and land registries as it is essential to correctly assess and collect tax revenue.

The Doing Business ‘Registering Property’ indicator records the full sequence of procedures, time and cost necessary for a business to transfer a property title of a land and a building to another business so that the buyer will be in a position to use the property for expanding its business, as collateral in taking new loans, or to sell to another business. The indicator also includes an index of the quality of the land administration system in each economy which has five dimensions: reliability of infrastructure, transparency of information, geographic coverage, land dispute resolution and equal access to property rights.

According to the Doing Business methodology, it takes 3 procedures, 77 days and costs 5.0 percent of the property’s value to transfer property in Bhutan (table 4.1). In addition, it scores 23.0 points out of 30 on the quality of land administration index. Globally, Bhutan ranks 53rd on the ease of registering property in Doing Business 2020 among 190 economies and has a Doing Business score of 72.6.

<table>
<thead>
<tr>
<th>Doing Business Indicator</th>
<th>Bhutan</th>
<th>Regional Average</th>
<th>Global Best Performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Procedures (number)</td>
<td>3</td>
<td>6.9</td>
<td>1 (5 countries)</td>
</tr>
<tr>
<td>Duration (days)</td>
<td>77</td>
<td>107.8</td>
<td>1 (2 countries)</td>
</tr>
<tr>
<td>Cost (% of property value)</td>
<td>5%</td>
<td>7.0%</td>
<td>0.0 (Saudi Arabia)</td>
</tr>
<tr>
<td>Quality of the land administration index (0-30)</td>
<td>23.0</td>
<td>9.1</td>
<td>None in 2018/19</td>
</tr>
</tbody>
</table>

Source: Doing Business 2020 database

Procedures at the Thimphu Municipality’s Land Records Section take approximately 77 days to complete. The business owner first needs to submit a complete set of Land Transfer Form to the Thimphu Thromde (Thimphu Municipality Office), which issues a PIN (Personal Identification Number). The land registry will then verify whether the property is legally registered, and all tax liabilities are cleared. As per Section 161 of the Land Act 2007, Thimphu Thromde shall post a notice

of the transaction for public viewing for 30 days. If no objection is raised, the Land Section transfers the documents to the Land Commission for approval, and the Commission will issue the Ownership Certificate confirming that the property transfer is completed. Finally, the Municipality informs the buyer to pick up the certificate and pay the transfer tax.

In the last 5 years, Bhutan made transferring property easier by introducing the eSakor, a computerized land information system. As a result, documents and maps for land plots were digitalized and the process became faster. Nevertheless, some room for improvement remains.

**Short-term Reform Recommendations:**

1. **Disseminate and encourage the use of the online platform.**

Since October 2017, the National Land Commission has been working on the development of a new eCitizen Portal (citizen.nlcs.gov.bt) with the aim to deliver convenient and efficient services to the public during the process of land and property transactions. Nevertheless, *Doing Business* continues to report that the majority of citizens prefer to go personally to Thimphu Thromde, and do not significantly use the online portal.

The Royal Government of Bhutan could consider encouraging the use of the online platform by lifting the registration fee (BTN 1,000) when submitting the online transfer Form. Moreover, a dissemination campaign could be conducted making use of brochures, news and social media as well as the online portal so that the general public becomes aware of the advantages of the portal. Once online registration becomes widespread, and widely accessible, the Royal Government of Bhutan could consider making the online platform the only way to conduct the transfer.

2. **Implement a specific and separate mechanism for filing complaints related to Thimphu Thromde.**

Currently, there is no specific and separate mechanism for filing complaints about a problem that occurred at the registry or cadaster. One powerful consequence of transparency is accountability: information gives citizens the power of knowing what to expect and whom to hold accountable in case things go awry. But if the mechanisms through which individuals or agencies are held accountable function poorly, information alone will not be enough. A specific and separate mechanism for filing complaints offers companies and individuals a safe and efficient way to pose complaints. The complaints can be submitted electronically or via competent agencies. For example, in Vanuatu a Land Ombudsman is available. Once a complaint is filled, he has 30 days to conduct and publish a report to the Land Ministry with the results of his follow up. In Thailand and Malaysia, complaints can be submitted electronically with a specific and separate form on the federal Land administration website: http://www.dol.go.th/dol/index.php?option=com_dol_complain in Thailand and in Malaysia; http://www.jkptg.gov.my/ms/content/aduan. Most recently, Rwanda introduced a similar mechanism by putting in place a complaint mechanism at the District Land Registry.

3. **Increase transparency of the land administration by publishing the fee schedule to access maps of land plots.**

A transparent land administration system—one in which all land-related information is publicly available, not only in person, but also online, whereby all procedures and property transactions are clear, and information on fees for public services is easy to access—minimizes the possibilities for informal payments and abuses of the system.
Bhutan has most information available online, except for the fee schedule to consult maps, so this should be added. It publishes the fees schedule and documentary requirements for land transfers as well as service standards for cadastre and land services. Annual statistics on land transfers are also available. Currently, more than 125 economies make this information available to the public and they are mostly online. In the South Asia region, Bangladesh, India, Pakistan and Nepal publish their fee schedules online.\textsuperscript{51}

**Medium-term Reform Recommendations:**

4. **Improve transparency at Thimphu Thromde by expanding the access to information on land ownership, maps and boundaries which are now only limited to interested parties.**

Making land-related information accessible to the public, subject to legal protections, allows third parties to determine property ownership and to obtain data on the operation of the real estate markets such as transaction values and volumes. Land title registers hold public information meant to be accessible and available to the public and are developed to confirm an individual’s claim to ownership of a particular piece of land, and to keep record of any encumbrances placed on a title. Access to land title records provides the public with a means to gain confidence in matters of property ownership, whether there are any limitations, reservations, or claims to ownership on a specific property, and what, if any, registered interests against the title to the land form a charge on the land such as mortgages, caveats, covenants, or any ongoing dispute.

Currently, only intermediaries and interested parties can obtain information on land ownership in Bhutan. Worldwide, approximately 140 economies make information on property ownership publicly available and, in over 130 economies, maps and boundaries are widely available. For example, Indonesia, Malaysia and Singapore make ownership information widely available for anyone. A more recent example is the city of São Paulo, Brazil,\textsuperscript{52} which in 2016 made all its property registry records public in an effort to combat corruption and fiscal evasion. In New Zealand, a detailed cadastre showing plots and the tenure type of each plot has been available since 2011, but access to data that includes ownership information requires users to agree to a separate license for personal data. In the United Kingdom, individual title information can only be accessed for individual plots by purchasing title deeds, but a unified dataset of land held by commercial, corporate, and government owners was made available for free as bulk data in 2017, under restrictive licensing terms that emphasize it should only be used for personal and non-commercial use, effective management of land, and prevention of crime. The land registry in the Netherlands allows any citizen to query for a particular property (after registering and receiving an identity key) but grants bulk access to users that have signed an agreement that ensures that they will not share the data with others or use it for targeted marketing. Through this system, the Land Agency can monitor who uses the data and for what purpose to monitor potential abuses. A hybrid system similar to the Netherlands that opens non-sensitive data in bulk, while monitoring access and use of sensitive data to verify users could provide a balanced approach to open ownership data. Nevertheless, with open data comes the concern of lack of privacy and Bhutan should carefully study the implications keeping in mind its benefits.

5. **Implement an electronic database covering all interests in land, including financial encumbrances.**

\textsuperscript{51} Doing Business 2020 report
\textsuperscript{52} https://www.transparency.org/news/pressrelease/sao_paulo_to_open_up_property_register_to_scrutiny_following_accord_with_t
A reliable land administration system provides clear information on the ownership of property, supports the security of tenure and facilitates the development of a land market. One key to fulfilling these functions is to have in place the infrastructure needed to maintain land information, supported by an appropriate institutional framework and adequate capacity. A common element of reliable systems is the existence of a consolidated database with information on property ownership and encumbrances. An electronic database for encumbrances can quickly show whether there is a mortgage or other liens on property or any other limitations that would impede its sale to a third party. At present, more than 100 economies around the world have an electronic database for rights and encumbrances.

Bhutan has made progress towards a more reliable transfer system with eSakor, a computerized land information system. Documents and maps for land plots were digitalized and the process became faster. However, an electronic encumbrances database has not been implemented, which contributes to adding layers of complexity and time to the due diligence process to ensure the safety of the transfer. Leveraging the benefits from the eSakor, creating an electronic database for encumbrances by linking the property tax database and civil registration database with eSakor would be the natural step following records digitization.

A comprehensive encumbrances database would also help reduce the overall time to transfer a property. Currently, as per Section 161 of the Land Act 2007, Thimphu Thromde shall post a notice of the transaction for public viewing for 30 days as a call to raise any possible objections to the transfer. An encumbrances database would compile all property liens into a single source, and could eventually, replace the 30-day waiting period.

6. Establish a specific compensation mechanism to cover for losses incurred by parties who engaged in good faith in a property transaction based on erroneous information certified by the immovable property registry.

In Bhutan, there are no specific compensation mechanisms to cover for losses by parties engaged in good faith in property transactions based on erroneous information provided by the land registry. The most advanced forms of guarantee indemnify individuals for losses suffered because of deficiencies in information provided by the registry. Without them, the matter is usually settled by the courts, which can be a costly and extensive process. In Chile, for example, the land registry has established an insurance fund that compensates losses due to errors by the registry. In England and Wales indemnity is also payable for losses incurred because of a mistake in an official search or an official copy. In Shanghai, the state provides full compensation for losses due to a technical error by a public officer.

Like the examples highlighted, Bhutan could consider introducing clear compensation mechanisms to align itself to international good practice in property administration. Should such mechanisms be created, they need to be advertised through a nation-wide awareness campaign so that local experts know that there is now a recourse to obtain compensation in case losses are incurred on a property transaction certified by the state.

7. Conduct a study to assess whether a reduction in property transfer duty is warranted.

Although property transfer taxes are an important source of revenue, when too high and prohibitive to a large part of the population, might result in informal transfers resulting in lost revenues and lost opportunity for owners to leverage their assets. Overall, although Bhutan’s cost to register property is below the regional average, it remains higher than global best practices. Studies have shown that high property transaction costs, including government-imposed transfer fees, can be a serious obstacle to market development. Evidence, for example, suggests that high transaction costs limit access to land
and reduce the ability of the less wealthy to participate in overall market activity.\textsuperscript{53} This, in turn, can constrain the development of the private sector as it becomes difficult for financial institutions to provide credit or develop collateral substitutes. A study estimates that in India, such land market distortions reduce the annual rate of gross domestic product growth by about 1.3 percent\textsuperscript{54} There is also evidence that when transfer fees and taxes are too burdensome, already registered properties may become informal again if subsequent transactions are not registered.\textsuperscript{55} This not only weakens the protection of property rights, but it also reduces potential revenue from property taxes.

Over the past 10 years 69 economies lowered transfer taxes and other government fees. Thirty-one of them are in Sub-Saharan Africa, where costs have been the highest. For example, Guinea decreased the transfer tax from 10 percent to 5 percent of the property value. Senegal lowered the transfer tax from 15 percent to 10 percent. The Bahamas reduced the stamp duty from 12 percent of the property value to 10 percent. Chad cut the property transfer tax from 15 percent to 10 percent. Côte d’Ivoire lowered the transfer tax from 10 percent to 4 percent. In 2016, Indonesia lowered the transfer tax to 2.5 percent paid by the seller, plus 5 percent on the excess of IDR 80 million. Before the reform, the transfer tax used to be 5 percent paid by the seller plus 5 percent on the excess of IDR 80 million, paid by the buyer. In 2018, Myanmar also reduced its stamp duty, reducing in an overall cost reduction of 1.5 percent of the property value.

In 2005, the Government of Egypt lowered the cost of registration aiming to provide incentives to bring informal property into the official national framework by formalizing it. The total property registration fees decreased from 5.9 percent of property value to 1 percent. Nevertheless, revenues from title registrations rose 39 percent between the 6 months before the reform and the 6 months after.\textsuperscript{56} More affordability usually means more registrations and less evasion. Property registries then have better information on property values and who owns what. And that supports the collection of capital gains and property taxes.

\textsuperscript{56} Doing Business 2008
5. Getting Credit

Doing Business covers two aspects of the regulatory framework and infrastructure that affect the availability of credit: the depth of credit information and the strength of the legal rights of borrowers and lenders. The first aspect, measured by the Depth of Credit Information Index, includes the coverage, scope and quality of credit information available through credit registries and credit bureaus. The second, measured by the Strength of Legal Rights Index, evaluates the degree to which movable property can be effectively used as collateral and the protection of creditor rights and priorities in bankruptcy.

In Doing Business 2020, Bhutan ranked 94th of 190 economies on the getting credit indicator and 3rd out of 8 economies in the South Asia region. Bhutan scored 55.00 percent points in the Ease of Doing Business score in getting credit. Under the Depth of credit information index, Bhutan receives 7 points out of 8. However, under the Strength of legal rights index, Bhutan receives only 4 points out of 12.

A. Credit Information

A credit reporting system is an integral part of a well-functioning credit market. Credit reporting systems help satisfy lenders’ need for accurate, credible information that reduces the risk of lending and the cost of loan losses by providing a reliable indication of whether an applicant will repay a loan. The lack of credit information makes checking borrowers’ credit history an onerous and uncertain process. This raises transaction costs for banks and, ultimately, increases the cost of credit to borrowers. The lack of credit information could also result in approval of loans based on personal connections, and not necessarily the likelihood of repayment.

Research suggests that bank risk is lower, while profitability is higher, in countries where lenders share borrowers’ information through credit bureaus and registries.57 Well-functioning credit reporting systems can help to reduce adverse selection and moral hazard and contribute to both an expansion of credit and a reduction in lending costs by facilitating the adoption of lending technologies based on credit scoring models. The development of credit information systems is particularly important for smaller firms, given the more severe problems of information opacity and asymmetry in these cases.

The Depth of credit information index measures 8 features of a credit bureau or a credit registry, provided that it covers at least 5 percent of the economy’s adult population. Bhutan scores 7 out of 8 points on the Depth of credit information index. As of January 1, 2019, 42.5 percent of adults were covered by the private credit bureau. (Table 5.1).

Table 5.1 - Credit information ranking and best performers in Doing Business 2020

<table>
<thead>
<tr>
<th>Doing Business Indicator</th>
<th>Bhutan</th>
<th>Regional Average</th>
<th>Regional best performer</th>
<th>Best global performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Depth of credit information index (0-8)</td>
<td>7.0</td>
<td>5.1</td>
<td>7.0 (Bhutan, India, Pakistan)</td>
<td>8 (53 economies)</td>
</tr>
<tr>
<td>Private credit registry coverage (percent of adults)</td>
<td>0.0</td>
<td>5.1</td>
<td>22.4 (Maldives)</td>
<td>100 (2 economies)</td>
</tr>
<tr>
<td>Public credit bureau coverage (percent of adults)</td>
<td>42.5</td>
<td>21.0</td>
<td>63.1 (India)</td>
<td>100 (14 economies)</td>
</tr>
</tbody>
</table>

Source: Doing Business 2020 database

According to the *Doing Business* database, as of January 1, 2019, Bhutan’s credit bureau covered 217,895 individuals and 2,915 firms.

**Table 5.2 - Credit information score in Doing Business 2020**

<table>
<thead>
<tr>
<th>Depth of credit information index (0-8)</th>
<th>Private credit bureau</th>
<th>Public credit registry</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Are data on both firms and individuals distributed?</td>
<td>Yes</td>
<td>No</td>
<td>1</td>
</tr>
<tr>
<td>Are both positive and negative credit data distributed?</td>
<td>Yes</td>
<td>No</td>
<td>1</td>
</tr>
<tr>
<td>Are data from retailers or utility companies - in addition to data from banks and financial institutions - distributed?</td>
<td>Yes</td>
<td>No</td>
<td>1</td>
</tr>
<tr>
<td>Are at least 2 years of historical data distributed? (Credit bureaus and registries that distribute more than 10 years of negative data or erase data on defaults as soon as they are repaid obtain a score of 0 for this component.)</td>
<td>Yes</td>
<td>No</td>
<td>1</td>
</tr>
<tr>
<td>Are data on loan amounts below 1% of income per capita distributed?</td>
<td>Yes</td>
<td>No</td>
<td>1</td>
</tr>
<tr>
<td>By law, do borrowers have the right to access their data in the credit bureau or credit registry?</td>
<td>Yes</td>
<td>No</td>
<td>1</td>
</tr>
<tr>
<td>Can banks and financial institutions access borrowers’ credit information online (for example, through an online platform, a system-to-system connection or both)?</td>
<td>Yes</td>
<td>No</td>
<td>1</td>
</tr>
<tr>
<td>Are bureau or registry credit scores offered as a value-added service to help banks and financial institutions assess the creditworthiness of borrowers?</td>
<td>No</td>
<td>No</td>
<td>0</td>
</tr>
</tbody>
</table>

**Score ("yes" to either public bureau or private registry)**

7

Source: *Doing Business 2020* database

**Bhutan’s performance on the Credit information indicator over time**

The credit information system of Bhutan has progressively evolved over time. Prior to the establishment of the Credit Information Bureau of Bhutan (CIB), all Financial Institutions shared credit information on the client through a Loan Clearance Certificate which had the following drawbacks: a) long duration (the system of sharing credit information amongst the financial institutions through the exchange of Loan Clearance Certificate was time consuming); inappropriate means of communication (the means of communication used in exchange of Loan Clearance Certificate was usually through fax, as a result of which certificates were often misplaced); and incorrect/incomplete data (some of the financial institutions have faced the situations where the data provided on the certificates was not complete or incorrect). In consideration of the above issues, Bhutan decided to replace the procedure of exchanging Loan Clearance Certificates with a more systematic and advanced credit information exchange by setting up the CIB.

In 2004, a task force was established to set up a Private Credit Bureau. A memorandum of agreement was signed by five financial institutions on November 1, 2005. The CIB “went live” partially four years later on December 3, 2009, however at that time, the borrower’s data available was very limited. The private credit bureau was officially launched and operational in 2010. *Doing Business* acknowledged this reform as part of the *Doing Business 2012* report. In 2012/2013, Bhutan improved access to credit information through new regulations governing the licensing and functioning of the credit bureau and guaranteeing borrowers’ right to access their data. In 2016/2017, the CIB started to distribute payment data from two utility companies (Bhutan Power Corporation Limited and Bhutan Telecom Limited). Those developments
were also acknowledged by the *Doing Business* project. Currently, the CIB has thirteen members consisting of five financial institutions, three non-financial institutions, five retailers and utility companies and one private money lender. Since the credit bureau was established the percentage of the adult population in Bhutan that had their credit information covered by the private credit bureau has increased significantly. (Figure 5.1.).

**Figure 5.1. CIB coverage in Bhutan from 2014 to 2018.**

Source: Statista database

**Medium to long-term reform recommendations**

1. **Develop a credit scoring system complementing credit reports as an additional valued-added service.**

Credit scoring helps expand access to finance. It is a statistical method of evaluating the probability that a prospective borrower will fulfill the financial obligations associated with a loan. Well-developed credit scores based on credit bureau data pool information across many creditors as well as some public information sources. They therefore include characteristics otherwise unavailable to any individual creditor, such as total exposure, number of outstanding loans and previous defaults within the system. To sharpen the predictive value of credit scores, credit bureaus and registries are also increasingly collecting data from a wider range of sources (such as bankruptcies and court judgements). As a result, credit scores generally have a higher predictive value than assessments derived from credit histories alone. Bureaus can also offer credit-related services including credit alerts and credit analytics.

The CIB could develop a credit scoring regulatory framework and metrics to be able to offer them as value-added service to help banks and financial institutions assess the creditworthiness of borrowers.

Credit scores may improve market efficiency and provide borrowers with more opportunities to obtain credit. The availability of credit scores allows lenders that could not otherwise analyze the raw credit data to extend credit to underserved markets at lower cost. This value-added product is most widely available in Latin America and the Caribbean and the OECD high-income group, offered in 80 percent of economies with a credit bureau or registry covering at least 5 percent of the adult population- compared with 40 percent in Europe and Central Asia, 38 percent in the Middle East and North Africa, 25 percent in East Asia and the Pacific and 24 percent in Sub-Saharan Africa.
On February 28, 2018, the credit bureau (Biro Kredit) managed by the Autoriti Monetari of Brunei Darussalam (AMBD) began offering credit scores to banks and other financial institutions to better inform their lending decisions. The score is based on the probability of default model, which uses 3 years of historical data. It ranges from 215 to 570, where higher scores indicate a lower probability of default. The credit scores are calculated for both consumer and commercial borrowers.

**B. Legal Rights**

This section focuses on aspects measured by the Legal Rights Index, which covers the secured transactions and creditor’s and debtor’s rights. Access to finance remains a problem for SMEs in many countries around the world including Bhutan. Part of the reason is that financial institutions require SMEs to provide real property as collateral for loans, with a preference for commercial real estate. However, micro, small and medium enterprises seldom have real estate as collateral for a commercial loan. Their concentration of assets is movable property—including inventory, accounts receivables, and equipment. Accordingly, the Legal Rights Index measures the effectiveness with which the current legal and institutional framework facilitates the use of such movable assets as collateral.

Research suggests that in countries where security interests over collateral are enforceable against third-parties in cases of loan default based on a predictable priority system, credit to the private sector represents 60 percent of GDP on average, compared with only 30 percent to 32 percent on average for countries without these creditor protections. In industrial countries, borrowers with collateral receive nine times the level of credit on average as borrowers without collateral, for a given level of cash flow. They also benefit from repayment periods that are up to 11 times longer and pay interest rates that are up to 50 percent lower. In countries with registries for movable collaterals, the number of firms with access to finance increased on average by 8 percent. These countries also showed lower interest rates and extension in loan maturity. The increase was even stronger for small firms, which often find it more difficult than bigger firms to access credit due to lack of fixed assets to be used as collateral.

In the *Doing Business 2020* report, Bhutan scores 4 out of 12 (12 = highest score for strongest protections) on the strength of legal right index. Bhutan’s score is lower than the regional average in South Asia, thus highlighting a need for substantive reforms related to secured transactions to make the existing legal framework compatible with international best practices (Table 5.3). Usually, banks in many countries strongly prefer real estate as collateral, as movable assets are considered too risky. Such practice makes it difficult for MSMEs and sole entrepreneurs to obtain loans.

**Table 5.3 - Legal Rights of Creditors and Borrowers in Secured Transactions ranking and best performers in Doing Business 2020**

<table>
<thead>
<tr>
<th>Doing Business Indicator</th>
<th>Bhutan</th>
<th>Regional Average</th>
<th>Regional best performer</th>
<th>Best global performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strength of Legal Rights Index (0-12)</td>
<td>4</td>
<td>5.5</td>
<td>10 (Afghanistan, Nepal)</td>
<td>12 (5 economies)</td>
</tr>
</tbody>
</table>

*Source: Doing Business 2020 database*

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Legal rights of creditors and borrowers: need for a comprehensive structural reform

Improving the legal framework for secured transactions requires efforts not only to address the existing gaps in the legislation but also to raise awareness on the merits and benefits of such reforms as to make them user-friendly and easily enforceable. The Movable and Immovable Property Act of 1999 relates to loans, mortgages and other security interests in moveable and immovable property. It also regulates the collateral registry. In addition, in 2013, the Royal Monetary Authority (RMA) launched the Central Registry System for Secured Transactions (CRST), a collateral registry for movable and immovable goods created with the assistance from the Asian Development Bank (ADB). The Central Registry was only available to Financial Institutions. Recently, the Regulations for Functioning of the Central Registry of Bhutan of 2013 has been amended and supersede by the Rules and Regulations for Central Registry for Secured Transactions in Bhutan applicable to Financial Institutions, which entered into force on July 1, 2019. The Central Registry System for Secured Transactions is now under the management of the Royal Monetary Authority of Bhutan. The new registry will register all types of security interests on movables as outlined in the Movable and Immovable Property Act (MIPA), with the exception of Companies charges which are still registered at the Companies office, until the MIPA amendments are passed and a repeal of the related provisions within the Companies Act of 2016. Also, machinery is registered in the Central Registry.

Bhutan are currently seeking to amend the Moveable and Immovable Property Act of 1999. Bhutan should ensure that the new framework for secured transactions, include all international best practices in this area (Table 5.4).

Table 5.4 - Legal Rights of Creditors and Borrowers in Secured Transactions score in Doing Business 2020

<table>
<thead>
<tr>
<th>Strength of legal rights index (0-12)</th>
<th>Bhutan’s score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Does an integrated or unified legal framework for secured transactions that extends to the creation, publicity and enforcement of functional equivalents to security interests in movable assets exist in the economy?</td>
<td>No</td>
</tr>
<tr>
<td>Does the law allow businesses to grant a non-possessory security right in a single category of movable assets, without requiring a specific description of collateral?</td>
<td>Yes</td>
</tr>
<tr>
<td>Does the law allow businesses to grant a non-possessory security right in substantially all of its assets, without requiring a specific description of collateral?</td>
<td>Yes</td>
</tr>
<tr>
<td>May a security right extend to future or after-acquired assets, and may it extend automatically to the products, proceeds and replacements of the original assets?</td>
<td>Yes</td>
</tr>
<tr>
<td>Is a general description of debts and obligations permitted in collateral agreements; can all types of debts and obligations be secured between parties; and can the collateral agreement include a maximum amount for which the assets are encumbered?</td>
<td>No</td>
</tr>
<tr>
<td>Is a collateral registry in operation for both incorporated and non-incorporated entities, that is unified geographically and by asset type, with an electronic database indexed by debtor's name?</td>
<td>No</td>
</tr>
<tr>
<td>Does a notice-based collateral registry exist in which all functional equivalents can be registered?</td>
<td>No</td>
</tr>
<tr>
<td>Does a modern collateral registry exist in which registrations, amendments, cancellations and searches can be performed online by any interested third party?</td>
<td>No</td>
</tr>
</tbody>
</table>

60 Rule 1 (b) of the Rules and Regulations for Central Registry for Secured Transactions in Bhutan 2019.
Strength of legal rights index (0-12)

<table>
<thead>
<tr>
<th>Question</th>
<th>Bhutan’s score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Are secured creditors paid first (i.e. before tax claims and employee claims) when a debtor defaults outside an insolvency procedure?</td>
<td>No</td>
</tr>
<tr>
<td>Are secured creditors paid first (i.e. before tax claims and employee claims) when a business is liquidated?</td>
<td>No</td>
</tr>
<tr>
<td>Are secured creditors subject to an automatic stay on enforcement when a debtor enters a court-supervised reorganization procedure? Does the law protect secured creditors’ rights by providing clear grounds for relief from the stay and setting a time limit for it?</td>
<td>No</td>
</tr>
<tr>
<td>Does the law allow parties to agree on out of court enforcement at the time a security interest is created? Does the law allow the secured creditor to sell the collateral through public auction and private tender, as well as, for the secured creditor to keep the asset in satisfaction of the debt?</td>
<td>Yes</td>
</tr>
</tbody>
</table>

Score (number of "yes" responses) 4

Source: Doing Business 2020 database

In order to strengthen the legal framework on secured transactions and to align it to international best practices, authorities should undertake a holistic assessment and reform of the current secured transactions legal framework. Bhutan is currently reviewing the Bankruptcy Act to strengthen legal rights for creditors and borrowers and therefore, Bhutan should ensure the new draft is aligned with international best practices. Such a reform process should take into account the international best practices that have been globally adopted: the UNICITRAL Model Law and/or the World Bank Principles on Effective Creditor/Debtor Regimes. The latter, for example, states that “the legal framework for secured lending should address the fundamental features and elements for the creation, recognition, and enforcement of security interests in all types of assets—movable and immovable, tangible and intangible—including inventories, receivables, proceeds, and future property and, on a global basis, including both possessory and non-possessory interests. The law should encompass any or all of a debtor’s obligations to a creditor, present or future, and debt obligations between all types of persons. In addition, it should allow effective notice and registration rules to be adapted to all types of property and should provide clear rules of priority on competing claims or interests in the same assets. For security rights and notice to third parties to be effective, they must be capable of being publicized at reasonable costs and easily accessible to stakeholders. A reliable, affordable public registry system is therefore essential to promote optimal conditions for asset-based lending. Where several registries exist, the registration system should be integrated to the maximum extent possible so that all notices recorded under the secured transactions legislation can be easily retrieved.”

Medium and long-term reform recommendations:

2. Ensure the new Secured Transactions framework will address the gaps identified in the current legislation.
   A. Ensure an integrated legal framework for secured transactions that extends to the creation, publicity and enforcement of functional equivalents to security interests in movable assets exist in the country. Secured transactions are understood as all transactions that create a right in any type of asset meant to secure the performance of an obligation. A functional approach to secured transactions translates into an integrated or unified legal framework that extends to the creation, publicity and enforcement of four functional equivalents to security interests in movable

assets: fiduciary transfers of title; financial leases; assignments or transfers of receivables; and sales with retention of title. In Bhutan, the Movable and Immovable Property Act (MIPA) of Bhutan addresses the functional approach. However, the MIPA and the Companies Act of 2016 are not coordinated. Companies charges will still need to be registered at the Companies office, until the MIPA amendments are passed and a repeal of the related provisions within the Companies Act of 2016. Also, machinery is still registered in the Central Registry.

Good practice economies follow the unitary approach to secured transactions. This approach allows the registration of not only traditional security interests, but also other transactions secured with movable property (i.e. functional equivalents), meaning rights in movable assets that are created by agreement and secure the payment or other performance of an obligation, regardless of the form of the transaction or the terminology used by the parties. Moreover, all transactions secured with movable property, including functional equivalents, should be covered by the same legislation and registered at the same registry. Adopting a unified legal framework approach to secured transactions eliminates the need to have different laws governing different types of secured transactions, which is cumbersome; instead, economies can adopt a single piece of legislation covering all types. This approach provides transparency and predictability for creditors – because the legal framework covers all rights in movable assets that secure the performance of an obligation, regardless of the type of transaction. What matters is no longer the form that the agreement takes (whether a floating charge or a pledge agreement, for example) but the rights and obligations that it creates. Such legal framework should extend not only to the creation of the security interest, but also to its publicity and enforcement of non-possessory security rights and all transactions secured with movable property. The same legal framework should apply for both incorporated and non-incorporated entities.

B. Explicitly provide that all types of obligations and debts can be secured. The Movable and Immovable Property Act of 1999 permits the general description of debts and obligations in collateral agreements and in registration documents, but it does not allow that all types of conditional monetary and non-monetary debts and obligations be secured.

C. Balance secured creditor and borrower rights by mandating an automatic stay on enforcement with effective limits. Two issues are at stake: 1) Whether secured creditors are subject to an automatic stay on enforcement when a debtor enters a court-supervised reorganization procedure; and, 2) whether secured creditors’ rights are protected thanks to clear grounds for relief from the stay. When debtors initiate court-supervised reorganization procedures, the court should automatically issue a stay order temporarily halting creditors from enforcing their securities. The momentary shelter helps borrower restructure and continue operating as a going concern if the business is viable. An insolvency framework following the international best practices in this area should include an automatic stay – a suspension of enforcement proceedings that is not to be granted upon the judge’s discretion, but operation of law as well as time limits to the stay to protect the rights of secured creditors. The insolvency framework should also provide either or one of these two reliefs (relief

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62 Fiduciary transfer of title means a transfer of ownership for security purposes until the debt is extinguished. The debtor may retain possession of the assets.

Financial lease agreement means an agreement where the lessor receives payments to cover its ownership costs.

Assignment of receivables means the creation of a security right in a receivable that secures the performance of an obligation.

Retention of title sale means the sale of goods where the title to the goods remains vested in the seller until certain obligations (usually payment of the purchase price) are fulfilled by the buyer.

for perishable goods or assets) which are not indispensable for the business under reorganization proceedings. First, where the stay poses a substantial risk to the collateral and, second, where the collateral is not necessary for the reorganization proceedings or the sale as a going concern. Lastly, the types of relief should be clearly stipulated in the insolvency regulation as these should be viewed as an exception to the general rule on the stay of enforcement actions.

D. Ensure that a secured creditor’s priority is respected based on the principle of “first-in-time, first-in-right,” while respecting other critical national policy objectives. Currently, secured creditors do not have an absolute priority over all creditors when the debtor defaults outside court-supervised procedures—for example, general tax claims have priority. It is critical that creditors can lock in their priority by registration, with a high degree of predictability, and that potential subsequent creditors are notified of existing priorities. Given the important role that secured creditors often play in providing credit to businesses, the priority of their claims should be recognized, both within and outside of insolvency, unless other claims were registered before the secured creditor’s claim. Claims that rank higher than the secured creditors may increase the cost or limit the availability of credit.

If secured creditors can predict their ranking vis-à-vis other types of creditors (including statutory creditors) with confidence, they are likely to make credit available more easily and at a lower cost to the borrower. But when other types of creditors, such as the tax authority and labor claims in the case of state income taxes, have priority over secured creditors—especially if they came into existence after the registration of the security interest—secured creditors will be less able to predict their level of risk. Providing secured creditors with the highest level of priority possible based on the “first in time, first in right” principle will encourage more credit to be available to entrepreneurs at a lower rate. There may be broader or more important policy objectives served by ranking certain claims higher than those of secured creditors. If so, both the nature and the scope of these priority claims should be very clearly defined.

2. Ensure that the Central Registry system for secured transactions is up and running fully under modern principles. A modern collateral registry is a key ingredient of a modern economy. In many economies, creditors continue to be hesitant to take moveable assets as collateral without a unified, notice-based, fully electronic registry that would (i) enable creditors to know their priority vis-a-vis others, and (ii) allow the registration, amendment, cancellation and search of all types of security interests and encumbrances over moveable assets in a simple, free and reliable way. Countries that accept a broad variety of movable assets to be registered as collateral, have a unified electronic (web-based) database, do not require submission of underlying documents and have low registration fees. Such countries experience the largest number of registrations, searches, amendments, and terminations of security interests over moveable assets. This translates into a higher lending volume as each registration represents a loan secured with movable property.

According to the new Rules and Regulations for Central Registry for Secured Transactions in Bhutan

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64 Article 112 of the Bankruptcy Act of Bhutan states that in the distribution of the property of the debtor, the debts listed in this section be paid in priority to all other debts in the following order: i) first, in payment of administration expenses and fees assessed against the estate; ii) second, in payment of all salary, wages, commissions, severance and sick leave pay, not exceeding Nu. 25000/earned by any individual in respect of services rendered to the debtor during the 90 days prior to the filing of bankruptcy petition or against the debtor; after the receipt of such amounts such individuals shall rank as ordinary, unsecured creditors for any residue owed by the debtor; iii) third, in payment of all debts due to the Royal Government of Bhutan or to any local authority, except for debts due to the Royal Government or to any local authority when they are acting in a commercial capacity; iv) fourth, in payment of claims for debts to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for or support of such spouse or child, in connection with a separation agreement, divorce decree or other order of a court.

65 Love et al. (2013).

applicable to financial institutions, which entered into force on July 1, 2019 and supersede the Regulations for Functioning of the Central Registry in Bhutan of 2013, the Office of the Central Registry System for Secured Transactions (CRST) shall be under the Royal Monetary Authority of Bhutan (RMA) for effective, efficient and worthy of public trust and confidence. The CRST is open to the public during regular business hours but electronic access to the Registry services is generally available 24 hours a day, 7 days a week, however the Registrar may suspend access to the Registry services in whole or in part for maintenance purposes or when circumstances arise that make it impossible or impractical to provide access.

Bhutan should ensure that the CRST, has the following modern features:

- Single data source (centralized nationally) registry for all security interests (including functional equivalents), for both incorporated and non-incorporated entities (currently in Bhutan, the CRST is only operational for interests registered by financial institutions);
- Web-based electronic system accessible 24/7 (currently in Bhutan, accessibility is granted only to those who have user account for the system. For those who do not have the user account, they have to fill out a form and pay a nominal fee applied to the registry office for the access to the system);67
- Information entered into the registry should be reflected online in real time;
- Notice-based system, meaning that only information on the creditor, the debtor (who can be both a legal or natural person), and the collateral are entered, without the need for any documentation in order to maintain or verify that information (Bhutan should ensure that all functional equivalents could be register at CRST);
- Registrations to be done by creditors or their legal representatives directly into the system (without interference of a clerk, notary or otherwise);
- Information available for free to the general public for searches;
- Search criteria that include, at least, a debtor search criterion or a debtor’s identifier search criterion when available;
- Flat and reasonable fees for registrations;
- Registrar role limited to management, not to verify and modify information in the registry;
- Non-cash payments (debit/credit cards, electronic transfers, or pre-paid accounts);
- Secured and protected registry data, with established disaster recovery sites.

3. Implement awareness raising campaign and capacity building activities on the new tools introduced by the reforms. Once the legal and institutional frameworks are established, it will be important to raise awareness of various public and private sector stakeholders about the new tools. Specifically, the following activities can be considered:

- Supporting the public awareness campaign, targeting stakeholders with information on the new secured transactions law, registry system and their economic benefits;
- Ensuring managers and staff of the credit bureau are well-trained.

68 Article 270 (B) of the Companies Act of 2016 of Bhutan requires the instrument creating the charge, together with a copy thereof be delivered to the Registrar for registration.
6. Protecting Minority Investors

**Corporate governance matters in all types of economies.** Good corporate governance practices have led to significant increases in economic value-added of firms, higher productivity, and lower risk of systemic financial failures for countries. Thus, it is crucial in both established and developing economies. In high income economies, ill-conceived corporate regulations can hamper the growth of the private sector. In developing economies, confidence in the institutions is sorely needed to encourage the creation of a strong flow of flourishing corporations.

**Corporate governance is first and foremost a balancing act.** The immediate interests of four parties are at play here: company directors, managers, shareholders and public authorities. In an ideal setting, the seemingly contrary interests of one party become beneficial in the long run to that of another. For instance, empowering shareholders by granting them more control over sensitive and/or major transactions reduces the risk on their investment and may allow directors and managers to more easily raise the capital needed to grow, innovate, diversify and compete. Similarly, eliminating undue regulatory requirements or clarifying and merging existing ones may seem to be at first a loss of oversight for public authorities yet lead to increased job creation and tax revenues further down the road.

**Minority investor protections can have important implications for firm valuation and firm growth.** Research on 539 large firms in 27 economies shows that firm valuation is higher in economies with good investor protections than in those with poor protections. Other research shows that corporate risk-taking and firm growth rates are positively related to the quality of the system of investor protections. Better systems may lead corporations to undertake riskier but value-enhancing investments. In addition, another study found that in economies with stronger investor protections, investment in firms is less sensitive to financial constraints and leads to greater growth in revenue and profitability.

**Without investor protections, equity markets fail to develop, and banks become the only source of finance.** Economies that have dynamic capital markets tend to effectively protect investors. In these economies’ investors receive financial information they can trust, they participate in major decisions of the company, and directors are accountable for their managerial decisions. If the laws do not provide such protections, investors may be reluctant to invest, unless they become controlling shareholders.

**The benefits extend beyond greater access to finance. Corporate governance also contributes to value maximization throughout the life cycle of a company.** Properly executed, it ensures that directors run the business in the best interest of the company. Executives and managers are given authority to do so efficiently, with sufficient discretion to apply their skills and business acumen. Internal structures and processes are clearly laid out. The risk of mismanagement and abuse is mitigated thanks to increased accountability, predictability and transparency. The aggregate effect of all companies following good practices in corporate governance promises significant positive outcomes for the economy overall. Empirical research shows how corporate governance reform can lead to higher returns on equity and greater efficiency.

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The *Doing Business* indicators on protecting minority investors are a proxy for an economy’s corporate governance standards and ease of access to financing from capital markets. One set of indicators analyzes the regulation of related-party transactions and shareholder access to judicial redress. These indicators shed light on protection of minority shareholders against self-dealing, or the use of corporate assets by company insiders for personal gain. Another set examines the adoption of key corporate governance practices that contribute to better managed companies, beyond self-dealing. These indicators measure the rights and role of shareholders in major corporate decisions, rules governing how companies are owned and controlled, and corporate transparency.

The Protecting Minority Investors indicator measures the minimum legal protections afforded under the law and therefore it only measures mandatory provisions of the law that companies are required to observe. It does not take into account provisions that allow company bylaws, incorporation documents, articles of association or any other internal regulations of the company to mandate otherwise. It also does not take into account code of corporate governance that are applied on a “comply or explain” basis.

According to *Doing Business 2020*, Bhutan ranks 111th out of 190 economies globally on the strength of minority investor protection index, with an ease of doing business score of 46.0. Regionally, WBG ranks Bhutan 6th of 8 economies in the South Asia region. Bhutan has an overall score of 4.6 out of 10 on the strength of minority investor protection (below the regional average of 5.7) The ranking of economies on the strength of minority investor protections is determined by sorting the scores for protecting minority investors. These scores are the sum of the extent of conflict of interest regulation index and the extent of shareholder governance index. Bhutan scores below the regional averages on all sub-indicators. Therefore, there is a considerable room for improvement on minority investors protections across all indicators measured. (Table 6.1).

<table>
<thead>
<tr>
<th>Doing Business Protecting Minority Investors Indicator</th>
<th>Minority Protection score (0-100)</th>
<th>South Asia Regional average</th>
<th>Regional best performer</th>
<th>Global best performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strength of minority investor protection score (0-100)</td>
<td>Bhutan 4.6</td>
<td>5.7</td>
<td>8.0 (India)</td>
<td>9.2 (Kenya)</td>
</tr>
<tr>
<td>Strength of minority investor protection index (0-50)</td>
<td>23</td>
<td>28.5</td>
<td>40 (India)</td>
<td>46 (Kenya)</td>
</tr>
</tbody>
</table>

Table 6.1. Protecting Minority Investors rankings and best performers.

<table>
<thead>
<tr>
<th>Extent of conflict of interest regulation index (0-30)</th>
<th>Minority Disclosure index (0-10)</th>
<th>South Asia Disclosure average</th>
<th>Regional best performer</th>
<th>Global best performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extent of conflict of interest regulation index (0-30)</td>
<td>4.0</td>
<td>5.8</td>
<td>8.0 (India, Afghanistan, Sri Lanka)</td>
<td>10 (13 economies)</td>
</tr>
<tr>
<td>Extent of director liability index (0-10)</td>
<td>4.0</td>
<td>5.0</td>
<td>8.0 (Maldives)</td>
<td>10 (Cambodia; Kenya, United Arab Emirates)</td>
</tr>
<tr>
<td>Ease of shareholder suits index (0-10)</td>
<td>6.0</td>
<td>7.4</td>
<td>9.0 (Afghanistan, Nepal)</td>
<td>10 (Djibouti)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Extent of shareholder governance index (0-20)</th>
<th>Minority Disclosure index (0-10)</th>
<th>South Asia Disclosure average</th>
<th>Regional best performer</th>
<th>Global best performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extent of shareholder governance index (0-20)</td>
<td>6.0</td>
<td>7.4</td>
<td>9.0 (Afghanistan, Nepal)</td>
<td>10 (Djibouti)</td>
</tr>
</tbody>
</table>

73 New Zealand; Singapore; Hong Kong SAR, China; Malaysia; United Kingdom; Thailand; North Macedonia; Azerbaijan; United Arab Emirates; Bulgaria; Indonesia, Kenya and China.
Figure 6.1. Protecting Minority Investors in Bhutan and comparator economies

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Bhutan</th>
<th>Comparator (economies)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extent of shareholder rights index (0-6)</td>
<td>3.0</td>
<td>3.5</td>
</tr>
<tr>
<td>Extent of ownership and control index (0-7)</td>
<td>3.0</td>
<td>3.6</td>
</tr>
<tr>
<td>Extent of corporate transparency index (0-7)</td>
<td>3.0</td>
<td>3.3</td>
</tr>
<tr>
<td></td>
<td></td>
<td>6.0 (India)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>7.0 (Pakistan)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>6.0 (India)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>7.0 (19 economies)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>7.0 (9 economies)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>7.0 (13 economies)</td>
</tr>
</tbody>
</table>

Source: Doing Business 2020 database

Bhutan’s performance on the Protecting Minority Investors indicator over time

Doing Business has recorded only one major reform in Bhutan on this topic during the last ten years. According to DB2018, Bhutan strengthened minority investor protections by clarifying ownership and control structures but weakened minority investor protections by reducing shareholder rights.

In Bhutan, the legal underpinnings for corporate governance for both listed and non-listed companies can be found in the Companies Act of Bhutan 2016, Civil and Criminal Procedure Code of Bhutan 2001 and the Evidence Act of 2005.

Source: Doing Business 2020 database

74 Croatia; Kenya; Kazakhstan; Slovenia; India; Turkey; Egypt, Arab Republic; United Kingdom; Cyprus; Morocco; Spain; Argentina; Malta; Bulgaria; Chile, Zimbabwe; Papua New Guinea; Peru and Panama.
75 Pakistan; Georgia; Austria; Colombia; Uzbekistan; United Arab Emirates; Croatia; Bahrain and Serbia.
76 Norway; Saudi Arabia; Indonesia; Taiwan, China; Lithuania; France; Ukraine; Mongolia; Kuwait; Cyprus; Bulgaria; Italy and Australia.
In *Doing Business 2020*, the Protecting Minority Investors indicator brought back its focus to listed companies. If an economy does not have an active stock exchange with at least 10 listings that are not state-owned, no points are given under the extent of shareholder governance index. Bhutan established the Royal Securities Exchange of Bhutan (RSEB) in August 1993 and officially opened for trading on October 1993. On April 23rd of 2012, RSEB moved its securities to a new and enhanced trading system. The RSEB integrated system was established with grants from the World Bank and developed by the InfoTech Pvt Ltd as per the requirement of the exchange. Currently, the Royal Securities Exchange of Bhutan is the only stock exchange in the country. It has a total of 19 listed firms with equity securities according to its website.

**Medium- to long-term recommendations**

1. **Revise the Companies Act of Bhutan 2016 as to include the following best practices in corporate governance for publicly listed companies.** The amendments to the Companies Act law should introduce the following:

1.1. **Require an independent review of related-party transactions prior to their approval.** An independent and external review of related-party transactions, performed by, for example, an independent auditor, technical expert, financial advisor, stock exchange or regulator, would guarantee an additional layer of protection against self-dealing by ensuring the fairness of the transaction terms. The Companies Act of 2016 should provide for a mandatory third-party review of the terms of significant related-party transactions prior to their approval. As soon as the board of directors is aware of a potential related-party transaction, it should request the appointment of an independent and external expert (usually an external auditor) to review the terms of the transaction and produce an expert and unbiased opinion to help shareholders make an informed decision when called on to vote as outlined in the previous point. The external and independent review should evaluate the main terms of the transaction and present an opinion containing relevant information on the transaction, the conflict of interest, and fairness of the proposed consideration (transaction price) to evaluate potential losses for a company upon its conclusion. Further, the opinion can help evaluating whether the transaction is arm’s length and presents fair market terms.

To increase the effectiveness of such disclosure requirement, the external review should be mandatory. In addition, to balance strengthening protections with compliance costs, the law could also set a threshold and require such review only for related-party transaction representing, at least, 10 percent or more of the company’s assets. Further, the threshold should be defined based on how large the transaction is compared to the company’s assets and should not be required only for transactions that are beyond the company’s ordinary course of business. Indeed, based on company’s size and characteristics, transactions that fall within the company’s ordinary course of business but are large could still present risks and benefit from such independent review. Setting a threshold would avoid a cumbersome and excessively costly requirement for smaller companies and transactions that are not significant ones. In addition, a liability regime should be incorporated in the law in case the independent auditor presents false or misleading information on the transaction.

Top performing economies in this area of business regulation - such as New Zealand, Singapore, Hong Kong SAR, Kenya, China, and the United Kingdom - require a review of the terms of related-party transactions by an independent auditor. Such review is also required in some South Asian economies, for example, in India, Afghanistan and Sri Lanka.

1.2. **Require the interested director to fully disclose all materials facts of a conflict of interest to the board of directors.** Currently, the Companies Act of 2016 does not explicitly require the interested director to provide full disclosure of a conflict of interest to the board of directors. It only requires that every director of a company, who is in any way, directly or indirectly, concerned or interested in a contract or arrangement, shall disclose the nature of his concern or interest at a meeting of the board of directors without any
specifics\textsuperscript{77}. International best practices recommend that company directors provide the board with full disclosure of all material facts concerning conflicts of interests, meaning detailed information on both the nature and extent of the conflict, including the contractual obligation (e.g. assets and services that are going to be purchased or sold; terms of loans to company directors or affiliated companies), a description of the nature and amount of the transaction, a detailed description of the conflict of interest (e.g. position held in the company, share ownership), and potential benefits from the transaction.

For instance, in the United Arab Emirates the Corporate Governance Rules state that if a board member has an interest or benefit, either directly or indirectly, in any transaction made (or to be made) with the company, and such interest or benefit involve (or may involve) a conflict of interest, such board member must disclose to the board stating the nature and extent of the conflict of interest within a period of no more than three business days. Also, the details of such conflict of interest shall be included in the financial report presented by the auditor of the company to the general assembly in the annual meeting.

Another example is Thailand, where the Public Limited Companies Act, Section 88 (1) provides: “Section 88. A director shall notify the company without delay in the following cases:(1) having a direct or indirect interest in any contract which is made by the company during an accounting year, and shall indicate the nature of the contract, names of the contracting party and interest of the director in the contract (if any):(2) holding shares or debentures of the company or an affiliated company, and shall indicate the total number of shares increasing or decreasing during an accounting year (if any)”.

1.3. Require a detailed disclosure of the conflict of interest in the annual report. The Companies Act of 2016 requires disclosure on the terms of a related-party transaction\textsuperscript{78} but does not also require periodic and detailed disclosure on the interested director’s conflict of interest in a company’s annual report. According to international best practice, company managers should periodically provide shareholders and the public with detailed information on both the terms and the conflict of interest concerning concluded related-party transactions. Generally, disclosure on this information is included in the in the company’s annual report. In the South Asia region, Afghanistan, Bangladesh, India, Pakistan, Nepal and Sri Lanka follow this international best practice.

1.4. Provide shareholders with the possibility of holding company directors liable for damages caused by unfair or prejudicial related-party transactions. According to Section 161 of the Companies Act of 2016, every director of a company, in the exercise of his/her powers and discharge of his/her duties under the provisions of this Act or under the Articles, shall act honestly and in good faith in the best interests of the company and shall exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. Therefore, in Bhutan, a director can be held liable for the damage that the transaction causes to the company if a shareholder plaintiff proves that the director breached his/her duties, influenced the approval of a related party-transaction, and/or was negligent.

This means that to prevail, shareholders must prove that directors engaged in a negligent behavior because of an act or failure to act. This section applies in all cases, whereas in the specific case of related-party transactions, existing provisions could be complemented so that shareholders can hold directors liable on the sole basis that said transactions were unfair or prejudicial to the company, including absent any wrong, breach of trust or breach of faith.

However, under this provision, a company director cannot be held liable when related-party transactions are unfair or prejudicial to the company. When the law clearly states that liability arises in case of prejudicial related-party transactions, shareholders can successfully recover damages and bring the interested director

\textsuperscript{77} Section 159 of the Companies Act of 2016.

\textsuperscript{78} Sections 232 and Sections from 265 to 268 of the Companies Act of 2016.
(and the rest of the board) to liability by proving: (i) the damages caused; and (ii) the existence of a conflict of interest. This lowers the burden on shareholders as knowledge or intent to cause damages would be implied because of the conflict of interest, thus increasing the likelihood of recovery of damages and the level of shareholders protection. In light of the above, Bhutan should consider lowering the threshold required to hold directors accountable for their actions. Thus, the Companies Act should be amended so that directors and other disinterested members of the approving body can be held liable when a transaction is unfair or prejudicial to the other shareholders; not only when they are at negligent (as per Section 161 of the Companies Act 2016) or at fault, grossly negligent, commit fraud or act in bad faith. Economies with the strongest protections on corporate self-dealing—such as New Zealand, Botswana and the United Arab Emirates—regulate not only disclosure and approval of related-party transactions but also set out clear rules of accountability for company directors when such transactions are unfair or prejudicial to the company. For example, in Botswana: *The Companies Act. Section 174 states: “Where a shareholder or former shareholder of a company, or any other person entitled, considers that the affairs of the company are being or have been or are likely to be conducted in a manner that is, or any act or acts of the company have been or are likely to be, oppressive, unfairly discriminatory, or prejudicial to that person in that capacity or in any other capacity, he may apply to court for relief. Where the court considers that it is just and equitable to do so, it may make such orders as it thinks appropriate including: i) Requiring the company or any other person to acquire the petitioner’s shares; ii) Requiring the company or any other person to pay compensation to the petitioner; and, iii) Setting aside action taken by the company or the Board in breach of this Act or the constitution of the company”.*

1.5. **Introduce remedies for prejudicial related-party transactions.** The Companies Act of 2016 should be amended to provide that an interested director who proposed a prejudicial related-party transaction should be required to pay damages and repay profits obtained from the related-party transaction in case of a successful claim. Additionally, the law could enable courts to disqualify a director—who is found liable—from representing or holding a managerial position in any company for a one-year period or more, depending on the severity of the self-dealing. International practice has shown that, in case of prejudicial related-party transactions, directors should not only pay the damages caused to the company but should also disgorge the profits made in violation of their duties to the company. To prevent corporate abuses, the interested director should also be removed from his/her position on the board of the company and disqualified from holding any other managerial or director position in any company for a period of one year at least. Generally, official functions include sitting on the board of directors, exercising the role of chief officer and more generally be involved in forming, marketing or running a company. Overall, these safeguards would further inhibit and deter directors from proposing and entering into harmful transactions.

Worldwide, only 9 economies provide for all the above-mentioned remedies for prejudicial related-party transactions. For instance, the Companies Act of Singapore states that the relevant directors may potentially be held liable to pay damages (for breach of common law duties of skill, care and loyalty) or equitable compensation (for breach of equitable fiduciary duties) or be held liable for an account of profits (for breach of equitable fiduciary duties). Specifically, the relevant directors may potentially be held liable if they failed to “act honestly and use reasonable diligence in the discharge of the duties as directors. A director who is found guilty of an offence may be held liable to the company for any profit made by him or for any damage suffered by the company as a result of the breach as well as sentenced to a fine not exceeding $5,000 or to imprisonment for a term not exceeding 12 months.” In addition, a director may also be disqualified from acting as director upon, inter alia, being convicted of any offence under the Companies Act.

1.6. **Allow the court to void related-party transactions that are unfair or entails a conflict of interest.** Currently, in Bhutan, courts have the power to rescind only transactions that prove to be oppressive or

79 Article 157 of the Companies Act of Singapore.
prejudicial to the other shareholders.\textsuperscript{80} In the case of a related-party transaction that is unfair to minority shareholders or entails a conflict of interest (i.e. not only in cases of fraud, bad faith, gross negligence, or when a transaction is oppressive or prejudicial to other shareholders), the Companies Act could offer the possibility of rescission of the transaction. Courts should have the power to void related-party transactions that are harmful to the company on the sole basis of the economic damage caused, as established through a comparison test with the economic situation of the company had the transaction not occurred altogether (rather than had it occurred without the conflict of interest). This will further nullify the effect of prejudicial transactions that jeopardize the economic stability of the company. In several economies – such as Brazil, Rwanda, Mauritius, the United Arab Emirates, and Brunei Darussalam - the courts have the power to rescind not only transactions that are fraudulent or made in bad faith, but also related-party transactions that are harmful or unfair to the company.

1.7. Require the consent of the majority of shareholders when disposing large assets of the company. The Companies Act of Bhutan 2016 does not provide explicitly for shareholders’ approval of the sale of all or major part of the company’s assets\textsuperscript{81}. The Companies Act of 2016 only mentions the disposal of the whole, or substantially the whole of the assets of the company but does not specify whether the sale of 51 percent of assets would fall within the definition of “substantially the whole”. However, no definition is provided. Large transactions of a company’s assets may directly impact the value of the company and change the nature of the business in which shareholders had initially chosen to invest. The specific threshold to determine that a sale of assets is a major one should ensure that sales involving at least 51 percent of the company’s assets fall within this definition. Thus, the specific threshold in the law should be set at any number below 51 percent. When selling a large portion of the company’s assets, the interests of minority shareholders are likely to be negatively affected. Because of this, it is advisable for the law to require that such transactions be concluded only with shareholders’ approval, whether such sale occurred in a single transaction or several transactions taking place within 1 year from the date of the first transaction. Eighty-three economies globally - including India, and Pakistan- have adopted similar provisions.

1.8. Ensure that all shareholders can exercise preemptive rights on new shares that cannot be waived by a simple majority vote.

In Bhutan, the Companies Act of 2016 provides for preemptive rights to shareholders of a company. However, as currently drafted, the Companies Act grants such preemptive rights to shareholders only if these are included in the company’s Articles of association or a shareholders’ resolution.\textsuperscript{82}

Preemption rights are essential to existing shareholders to avoid dilution of their share in the company upon a capital increase by giving them the option to purchase additional shares of a company’s stock or other securities before new investors can buy them. The relevant laws of any given country must require that preemptive rights be automatically given to shareholders of corporations formed in those jurisdictions in order to foster an environment of financial reliability and ownership stability. In other words, the relevant law should include a mandatory provision granting preemptive rights to shareholders. Furthermore, only qualified or reinforced majorities should be allowed to waive preemption rights under a limited set of circumstances, for example waiver of this right approved by at least three-quarters majority of shareholders. Bangladesh, Nepal and Pakistan, for example, grant shareholders’ automatic preemption rights every time a company issues new shares.

\textsuperscript{80} Section 175 of the Companies Act of 2016.

\textsuperscript{81} Section 156 (a) of the Companies Act of 2016: The Board of directors of a public company shall not, except with the consent of such company in general meeting: a) sell, lease or otherwise dispose of the whole, or substantially the whole, of the undertaking of the company.

\textsuperscript{82} Sections 57 to 60 of the Companies Act of 2016.
1.9. **Require majority approval of holders of a class of shares for any changes affecting such class of shares.** The Companies Act of 2016 does not provide that for changes affecting a class of shares, the mandatory approval of holders of such share class must be obtained. According to Section 69 of the Companies Act of 2016, the rights attached to a class of shares may only be varied: a) in accordance with a provision in the company’s articles for the variation of those rights, or b) where the company’s articles contain no such provision, if the holders of shares of that class consent to the variation.

The recommendation is to remove the company’s discretion, so that the law should – at minimum – require the consent of the holders of shares of that class for any variation. Moreover, within any series of a class of shares, all shares should carry the same rights. Additionally, all investors should be able to obtain information about the rights attached to all series and classes of shares before they purchase. Also, any changes in economic or voting rights should be subject to approval by those classes of shares which are negatively affected. Finally, the rights associated with a specific class of shares should only be amended with the approval of the majority of the holders of that specific class of shares. In Bangladesh, India and Sri Lanka, changes to rights associated with a class of shares are only possible if the holders of the affected shares approve those changes. In Sri Lanka, Section 99 (1) of the Companies Act states that a company shall not take any action that would affect the rights attached to shares, unless that action has been approved by a special resolution of each interest group.83

1.10. **Require the board of directors to have a separate audit committee.** Currently in Bhutan, the board of directors may, by a resolution passed at a meeting, delegate its powers to a committee of directors, the Chief Executive Officer or any principal officer of the company. The Companies Act of 2016 should be more specific and mandate for listed companies to establish a separate audit committee within the board of directors, exclusively composed by board members.

Audit committees are charged with the oversight of internal controls functions (audit, risk and compliance), financial reporting and disclosure. Audit committees are usually tasked with the following functions:

- a) overseeing the financial reporting and disclosure process;
- b) monitoring choice of accounting policies and principles;
- c) overseeing hiring, performance and independence of the external auditors;
- d) overseeing regulatory compliance, ethics, and whistleblower hotlines;
- e) monitoring the internal control process;
- f) overseeing the performance of the internal audit function; and,
- g) discussing risk management policies and practices with management.

As such, boards must set up a specialized subcommittee to support the full board in performing its functions and interacting with the external auditor. When committees of the board are established, their mandate, composition and working procedures should be well defined and disclosed by the board. Furthermore, an audit committee should ideally include an independent board member and a member of the board with financial and accounting expertise.

In other South Asian economies – such as Afghanistan, India, Sri Lanka and Pakistan - the board of directors of listed companies must include a separate audit committee exclusively comprising board members.

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83 Section 529 of the Companies Act of Sri Lanka of 2007 interprets “interest group” in relation to any action or proposal affecting the rights attached to shares, to mean a group of shareholders whose affected rights are identical; and whose rights are affected by the action or proposal in the same way.

84 Section 154 of the Companies Act of 2016: a) the power to make calls on shareholders in respect of money unpaid on their shares; b) the power to issue debentures; c) the power to borrow money otherwise than on debentures; d) the power to invest the funds of the company; and, e) the power to make plans.
1.11. **Introduce legal provisions to ensure that all shareholders are offered an exit option in case of major takeover of the company.** In Bhutan, the Companies Act of 2016 does not provide for mechanisms to protect shareholders from a takeover. Similar to shareholder safeguards on disposal of large assets, shareholders could also benefit from a mandatory tender offer, effectively giving shareholders a way out when a new shareholder acquires a major stake in the company. The law should also state that the offer to purchase the remaining shares is triggered by the acquisition of at most 50 percent of shares. The acquirer should not be able to avoid making the offer and the offer price should be equal to the average price paid to reach the triggering threshold. This rule should apply even if such acquisition did not take place in a single transaction. It should also apply to any person who has independently (or through actions in concert with other persons) acquired such interest. The inclusion of such provision is important because it helps prevent an acquirer from exploiting minority members by draining company assets and engaging in self-dealing. Also, a change in the majority ownership might result in a change in the company’s business strategy, and minority members should be protected from having those changes imposed on them with no realistic option to exit. In other South Asian economies like India and Afghanistan, a potential acquirer of a listed company must make a tender offer to all shareholders upon acquiring 50 percent of the company.

1.12. **Prevent subsidiaries from being able to acquire shares issued by their own parent company.** Currently there are no specific provisions in the Companies Act of 2016 concerning the possibility of a company becoming the record owner of shares issued by its parent company. Intra-group ownership increases the relative power of management and makes it more difficult for potential investors to determine who controls the company. Shareholder interests can be better protected in economies where cross-shareholdings are addressed at the regulatory level and limits are imposed on share stakes held by subsidiaries in their parent firms. Restrictions on this type of ownership are particularly important, because they ensure greater clarity in identifying who controls and can influence decisions in a given company. They also mitigate undue board control and entrenchment. Furthermore, they limit attempts to circumvent other limitations and obligations that may be applicable to major shareholders whose participation is at or above a given threshold, by making their direct ownership in a company seem smaller than it actually is. Finally, they prevent the management of the subsidiary—as legal representatives of the subsidiary—from exercising powers as shareholders in the parent company. Ninety-four economies out of the 190 economies measured by Doing Business follow this international good practice. Article 184 of the Companies Law of Saudi Arabia, for instance, states clearly that “an affiliated company shall not own shares or stakes in the holding company, and any act that shall transfer the ownership of the stock or shares of the holding company to the affiliated company shall be null and void.”

1.13. **Require disclosure of direct and indirect beneficial ownerships representing 5 percent or more of the share capital of a Joint Stock Company.**

In Bhutan, neither the Companies Act of 2016 or the Rules governing official listing securities require disclosure of direct and indirect beneficial ownership stakes representing 5 percent or more of the share capital of a joint stock company. One of the basic rights of investors is to be informed about the ownership structure of the enterprise and their rights vis-à-vis the rights of other owners. Such disclosures should make transparent the objectives, nature and structure of a company and disclose who are the ultimate beneficial owners of shares.

Generally, disclosure of ownership data should be provided once certain thresholds of ownership in a company are passed. It is good practice to disclose direct and indirect beneficial ownership stakes representing 5 percent and more. Such disclosure might include data on major shareholders and others that, directly or indirectly, are ultimate beneficial owners of shares. This means disclosure of who can significantly influence or control or may significantly influence or control the company through, for example, special voting rights, shareholder agreements, the ownership of controlling or large blocks of
shares, significant cross shareholding relationships and cross guarantees. It is also good practice to disclose shareholdings of directors, including non-executives.

Studies show that minority shareholders rights are better protected in economies promoting transparency and disclosure of corporate information. Information asymmetry can result in fraud, financial crisis, adverse selection and moral hazard. Investors are entitled to receive accurate, effective and sufficient information which would lead to financial stability, reduction of fraud and manipulation and better company governance in general. For instance, in the South Asia region Pakistan, India and Sri Lanka require listed companies to disclose direct and indirect beneficial ownership stakes representing 5 percent of the share capital.

1.14. Require disclosure of information about the compensation of directors and high-ranking officers of a company, including bonuses and incentive schemes on an individual basis. In Bhutan, the Companies Act of 2016 only mentions annual disclosure of remuneration of the Chief Executive Officers and Directors but does not specify whether these amounts shall be disclosed in an individual or aggregate basis.85 Requiring the disclosure of remuneration of each director and high-ranking officer of a company on an individual basis is considered an international best practice. Such disclosure should also include bonuses, incentive schemes and any other compensation received by board members. All this information should be disclosed in the annual report. For example, India and Nepal follow this international best practice.

In Nepal, Article 109 of the Companies regulates disclosure in the annual reports. Regarding disclosure of compensation, Article 109 (4) letters (s) and (t) of the Companies Act states: “[…] The board of directors of every public company or every private company with the paid–up capital of ten million rupees or more or with an annual turnover of ten million rupees or more shall also prepare a separate report of board of directors during that period stating the following matters, in addition to the annual financial statements required to be prepared pursuant to Sub-section (1): […](s) Amount, if any, outstanding and payable to the company by any director, managing director, chief executive, substantial shareholder or his/her close relative or by any firm company, corporate body in which he/she is involved;(t) Amount of remuneration, allowances and faculties paid to the director, managing director, chief executive and officer; […]”.

1.15. Require the notice of shareholder meetings to be published and sent to shareholders at least 21 calendar days in advance and contain sufficient information on the matters to be discussed during the meeting. In Bhutan, pursuant to Article 185 of the Companies Act of 2016, a twenty-one day’s written notice should be given to shareholders before the general assembly meeting takes place. However, Article 186 of the Companies Act of 2016 established an exception. A general meeting may be called after giving shorter notice than that specified in section 185, if the consent is accorded by at least two third of the shareholders of the company. A good practice followed by many countries is to ensure that there are no exceptions to the twenty-one day’s written notice prior to the general meeting of shareholders and that the notice provides sufficient information regarding the matters to be dealt with during the meeting.86 More specifically, the notice should state clearly the matters to be brought before the meeting for resolution, and include all the following information:

i) reference information required regarding any external acts;
ii) location, day, and time of the meeting;
iii) type of meeting, whether general or extraordinary;
iv) requirements relating to participation and exercise of voting rights;
v) meeting’s agenda; and,

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85 Section 178 (d) of the Companies Act of 2016.
86 63 of the 190 economies benchmarked by Doing Business follow this international best practice by requiring that a detailed notice of general meeting must be sent at least 21 calendar days before the meeting.
vi) description of the way in which remote voting is processed including the address, physical or electronic, safety measures, the deadline for receiving the voting ballots and the date for their count.

1.16. Ensure that shareholders representing 5 percent of the issued capital can include additional items on the general meeting agenda. The Companies Act of 2016 does not provide for a threshold of at least 5 percent of the listed company’s share capital in order to be able to add items to a shareholders’ meeting agenda. Therefore, it is important that the law permits to such members to put items in the agenda of the annual meeting. In addition, in order to encourage shareholder participation in such general meetings, many jurisdictions have improved the ability of shareholders to place items on the agenda through a simple and clear process of filing amendments and resolutions, submit questions in advance of the general meeting, and obtain replies from management and board members.

2. Consider amending the Rules Governing the Official Listing of Securities of the Stock Exchange of Bhutan

2.1. Require immediate disclosure of information regarding related party-transactions to the public (or to the market regulator). In Bhutan, neither the Companies Act of 2016 or the Rules governing official listing of securities require immediate disclosure (within a maximum of 24 or 72 hours of closing of a related-party transaction) to the public or market regulator. The Protecting Minority Investor indicator’s case study concerns a related-party transaction among two listed joint stock companies, Buyer and Seller. In the case at issue, as per methodology’s assumptions, Mr. James is the interested director because he proposes the transaction while he owns 60 percent of Buyer and 90 percent of Seller. International good practice requires immediate disclosure - i.e. within 24 or 72 hours at the latest- of related-party transactions to the public (or to market regulator). In best practice economies, listed companies must disclose explicit information on the terms and conditions of the transaction, as well as the nature of the interest and the extent to which the parties stand to gain personally from the transaction (except for information related to commercial secrets), including the following four specific aspects:

(i) a description of the assets purchased by Buyer;
(ii) the nature and amount of consideration paid by Buyer to Seller;
(iii) the interested director ownership interest and his/her position in Buyer; and
(iv) the ownership interested of the interested director in Seller, meaning, that he/she owns 90 percent of Seller.

To adapt to such international good practice, Bhutan should revise its legislation on listed companies and be more specific as to the timing and level of disclosure required by law. Specifically, the law should list in detail the information to be disclosed to the public and/or market regulator, as noted above, the terms, conditions, nature and the extent of the conflict of interest and all the other relevant information regarding the transaction (except for information related to commercial secrets). It should also specify that disclosure should occur immediately, within 72 hours at the latest. The law should also include a definition of immediateness, so that companies have clear guidance as to the timing of disclosure and would be breaching the law if they do not disclose this information within the specified timeframe. Further, this information should ideally be posted on the website of the company (if one exists) and on the website of the Stock Exchange of Bhutan (https://www.rsebl.org.bt/).

Sri Lanka, Kazakhstan, Singapore and the United Kingdom, are some examples of economies following this international best practice. For instance, in the United Kingdom, under Listing Rule 11.1.7(1) a listed company which enters into a transaction with a related party must make a notification to the stock market via a regulatory information service approved by the FCA, in accordance with Listing Rule 10.4.1, as soon as the terms of the transaction are agreed. The notification must contain the information set out in Listing Rule 10.4.1 and Listing Rule 11.1.7 (details of the transaction and the related party). The company must also send a circular to its shareholders containing the information required by Listing Rules 13.3 and 13.6
before the transaction has been entered into or before it has completed. This circular must contain adequate
details of the transaction and the related party to enable the shareholders to make an informed decision in
an independent shareholder vote. In addition, it should also set out the board’s recommendation as to the
voting decision independent shareholders should take.

3. Consider amending the Civil and Criminal Procedure Code of Bhutan of 2001 as to:

3.1. Facilitate access to corporate documents by plaintiffs during trial. Rights of minority investors
cannot be protected without easy and reasonable access to corporate information. Without access to
documentary evidence, minority investors may find it difficult to prove that directors or the company’s
management have been handling the company’s affairs improperly. Economies can have good laws in
place, but if access to corporate information and evidence is limited or courts are inefficient, investors are
unlikely to resort to judicial options to enforce such laws. For easier access to corporate documentation
during trial, the Civil and Criminal Procedure Code of 2001 should be revised to explicitly allow parties to
request categories of documents without identifying specific ones and allow the plaintiff to obtain any non-
confidential document relevant to the case from the defendant and witnesses at trial. For example, it might
be difficult determining which board meeting minutes contain the relevant discussion if the date of the
record is unknown to the requesting party. Therefore, if the requesting party has the right to ask the court
“all board meeting minutes”, he/she will obtain access to the relevant documents. Further, the scope of
documents that can be requested during trial should be expanded to include information that the defendant
has indicated he intends to rely on for his/her defense. Moreover, this good practice should not be limited
to related-party transactions, but embrace evidence related to all civil lawsuits

Other South Asian economies such as Afghanistan and Nepal, provide more clarity and predictability in
their civil procedure legislation for the parties to a lawsuit and promote easier access to corporate
information during trial, specifically allowing the parties to request certain categories of documents without
identifying specific ones.

3.2. Allow plaintiffs to directly question the defendant and witnesses during the trial. In Bhutan, the
plaintiff can only examine the defendant and witnesses during the trial with prior approval of the questions
by the judge or if the judge can set aside questions for any reason.\(^\text{87}\) In order to promote transparency and
ensure a fair trial, the plaintiff must be able to examine the defendant and witnesses directly without prior
approval of the questions by the judge. In more than 50 percent of the 190 economies analyzed by Doing
Business, the plaintiff (or the plaintiffs’ lawyer) can perform the examination without prior approval by the
court of the questions asked.

3.3. Allow shareholders to recover legal expenses regardless of the outcome of their legal action. In
Bhutan, the decision to allow plaintiffs to recover their legal expenses (e.g., court fees, attorney fees and
related expenses) from the company remains at the discretion of the court.\(^\text{88}\) However, shareholder plaintiffs
should be able to recover legal expenses from the opposing party regardless of the outcome of a lawsuit,
provided that the lawsuit is legitimate, filed in good faith and decided by the court on its merits. In other
words, recovery of legal expenses should be allowed only once the court has accepted jurisdiction, deemed
the claim receivable and reviewed the facts in light of relevant substantive law. Shareholder suits can be an
effective tool for ensuring that the company and its directors comply with their responsibilities and legal

\(^{87}\) Article 67 of the Evidence Act of Bhutan 2005: The Court may question witnesses whether called by itself or by a party. Article 68 of the Evidence Act of Bhutan 2005. The Court shall exercise reasonable control over the mode and order of questioning of witnesses and presenting evidence, so as to: a) Make the questioning and presentation effective for the ascertainment of the truth; b) Avoid needless consumption of time; and, c) Protect a witness from harassment or undue embarrassment. Article 69 of the Evidence Act of Bhutan of 2005: The Court on its own or at the request of a party may call witnesses and all parties are entitled to cross-examine such witnesses.

\(^{88}\) Article 407 of the Companies Act of 2016.
obligations, since shareholders have a strong interest in maximizing their own returns and are therefore highly motivated to seek redress for any actions that would harm those returns. However, the high cost of pursuing a claim is likely to be a prohibitive deterrent for many shareholders.

In light of the above, reimbursement of expenses should not depend on winning the case for shareholder litigation. Shareholders can legitimately suspect wrongdoing and seek to address it, while the court could ultimately not decide in their favor. Rather, it should be conditioned on bringing the case in good faith, for the benefit of the company, that the court has accepted the case as posing an actual question of law or fact, and not be frivolous or abusive. Policymakers can also limit this cost recovery mechanism to shareholders representing a minimum number or percentage of shares, typically 5 percent, again to avoid abusive litigation. The Companies Act could therefore be supplemented to provide such a recovery mechanism in the case of justified derivative suits.

In some countries, such as Afghanistan, Nigeria, and Rwanda, the winning party’s legal expenses are reimbursed by the losing party regardless of the outcome of their legal action. For example: in Afghanistan, the Civil Procedure Code states that any person who is a party to any action or suit, whether civil, criminal, administrative or investigative (other than a Derivative Proceeding), by reason of the fact that the person is, or was a Director, officer, employee, shareholder or agent of the Corporation, shall be indemnified by the Corporation against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement that are actually and reasonably incurred by such person in connection with such action, suit, or proceeding if the person acted in good faith, and in a manner which is in the best interests of the Corporation.
7. Paying Taxes

Efficient tax administration can help encourage businesses to become formally registered and the economy to grow—and thus expand the tax base, decrease evasion and increase tax revenues. There is ample evidence from the data collected in Doing Business that countries that have excessively burdensome tax systems (including in many parts of the world prohibitively high tax rates) end up creating perverse incentives, including widespread tax evasion, informality and, not surprisingly, low levels of revenue collection. Size of the tax cost imposed on businesses has implications for their ability to invest and grow. The efficiency of the tax administration system is also critical for businesses. A low cost of tax compliance and efficient tax-related procedures are advantageous for firms. Tax compliance systems should be designed so as not to discourage businesses from participating in the formal economy.

Until Doing Business 2017, the paying taxes indicator set measured only the cost of complying with tax obligations up until the filing of tax returns and the payment of taxes due. However, filing the tax return with the tax authority does not imply agreement with the final tax liability. Post-filing processes—such as claiming a value added tax (VAT) refund or undergoing a tax audit—can be the most challenging interactions that a business has with a tax authority. In Doing Business 2017, the indicator was expanded to include a new component on the time businesses spend complying with and completing two post-filing processes: obtaining a VAT refund as a result of a large capital purchase and completing a corporate income tax audit triggered by an error in the income tax return and consequently an underpayment of the tax due. The new component is called the ‘post-filing index’.

In Doing Business 2020, Bhutan ranks 15th out of 190 economies on the ease of paying taxes and is 1st out of eight countries in the South Asia region with an overall Ease of Doing Business score of 89.2 percentage points. The standardized case study company would have to make 18 payments, spend 52 hours complying with tax obligations and incur a tax levy of 35.3 percent of commercial profit. Paying taxes is the area where Bhutan’s performance stands out. Nevertheless, Bhutan can become closer to global best practices in the areas of electronical payment and corporate income tax audits (Table 7.1).

### Table 7.1 Paying Taxes ranking and best performers

<table>
<thead>
<tr>
<th>Doing Business indicator</th>
<th>Bhutan</th>
<th>Regional average</th>
<th>Regional best performer</th>
<th>Global best performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payments (number per year)</td>
<td>18</td>
<td>26.7</td>
<td>12 (India)</td>
<td>3 (Hong Kong SAR, China; Saudi Arabia)</td>
</tr>
<tr>
<td>Time (hours per year)</td>
<td>52</td>
<td>273.5</td>
<td>52 (Bhutan)</td>
<td>49 (Singapore)</td>
</tr>
<tr>
<td>Total tax and contribution rate (% of profit)</td>
<td>35.3</td>
<td>43.9</td>
<td>30.2 (Maldives)</td>
<td>26.1 (33 Economies)</td>
</tr>
<tr>
<td>Post-filing Index (0-100)</td>
<td>95.0</td>
<td>41.2</td>
<td>95.0 (Bhutan)</td>
<td>None in 2018/2019</td>
</tr>
</tbody>
</table>

Source: Doing Business 2020

It's important to note here the difference between the statutory tax rates and effective tax rates. Doing Business uses the term Total Tax and Contribution Rate in the data on Paying Taxes to reflect the effective tax rates.

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tax rates as a share of the commercial profits (i.e. what firms actually pay) and not the statutory tax rates. The total tax and contribution rate are designed to provide a comprehensive measure of the cost of all the taxes a business bears. It differs from the statutory tax rate, which merely provides the factor to be applied to the tax base. In computing the total tax and contribution rate, the actual tax or contribution payable is divided by commercial profit. Tax depreciation rules and tax deductions are considered. Only tax exemptions that are related to the size and the age of the company are considered under the Doing Business methodology.

The post-filing index is based on four components—time to comply with VAT refund, time to comply with corporate income tax audit and time to complete a corporate income tax audit. If both VAT and corporate income tax apply, the post-filing index is the simple average of the distance to frontier scores for each of the four components. If only VAT or corporate income tax applies, the post-filing index is the simple average of the scores for only the two components pertaining to the applicable tax. If neither nor corporate income tax applies, the post-filing index is not included in the ranking of the ease of paying taxes. On the post-filing index, Bhutan scores 95.0 points out of 100 (Table 7.2)

<table>
<thead>
<tr>
<th>Post-filing index (0-100)</th>
<th>Answer</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>VAT refunds</td>
<td></td>
<td>95.0</td>
</tr>
<tr>
<td>Does VAT exist?</td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>Does a VAT refund process exist per the case study?</td>
<td>N/A</td>
<td></td>
</tr>
<tr>
<td>Restrictions on VAT refund process</td>
<td>N/A</td>
<td></td>
</tr>
<tr>
<td>Percentage of cases exposed to a VAT audit (%)</td>
<td>N/A</td>
<td></td>
</tr>
<tr>
<td>Is there a mandatory carry forward period?</td>
<td>N/A</td>
<td></td>
</tr>
<tr>
<td>Time to comply with VAT refund (hours)</td>
<td>No VAT</td>
<td>No VAT</td>
</tr>
<tr>
<td>Time to obtain a VAT refund (weeks)</td>
<td>No VAT</td>
<td>No VAT</td>
</tr>
<tr>
<td>Corporate income tax audits</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Does corporate income tax exist?</td>
<td>Yes</td>
<td></td>
</tr>
<tr>
<td>Percentage of cases exposed to a corporate income tax audit (%)</td>
<td>75% - 100%</td>
<td></td>
</tr>
<tr>
<td>Time to comply with a corporate income tax correction (hours)</td>
<td>3.5</td>
<td>96.3</td>
</tr>
<tr>
<td>Time to complete a corporate income tax correction (weeks)</td>
<td>2</td>
<td>93.8</td>
</tr>
</tbody>
</table>

Source: Doing Business 2020

A company in Bhutan like the one measured by the Doing Business methodology in 2017-2018 needed to spend 52 hours (per year) and payed 35.3 percent of its commercial profits on taxes and mandatory contributions (total tax rate). Bhutan has eight different taxes which amount to 18 payments. A widely adopted e-payment system could simplify the process even further. (Table 7.3)
Table 7.3. Tax and mandatory contributions in Bhutan as captured by the Doing Business Paying Taxes’ indicator

<table>
<thead>
<tr>
<th>Tax or mandatory contribution</th>
<th>Payments (number)</th>
<th>Notes on Payments</th>
<th>Time (hours)</th>
<th>Statutory tax rate</th>
<th>Tax base</th>
<th>Total tax and contribution rate (% of profit)</th>
<th>Notes on TTCR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate income tax</td>
<td>2</td>
<td></td>
<td>22</td>
<td>30%</td>
<td>taxable profit</td>
<td>33.86</td>
<td></td>
</tr>
<tr>
<td>Property tax</td>
<td>1</td>
<td>BTN 75</td>
<td></td>
<td></td>
<td>per unit</td>
<td>0.97</td>
<td></td>
</tr>
<tr>
<td>Business license</td>
<td>1</td>
<td></td>
<td></td>
<td>varies from BTN 500 to 25,000</td>
<td>size of building and land</td>
<td>0.28</td>
<td></td>
</tr>
<tr>
<td>Annual vehicle registration</td>
<td>1</td>
<td>BTN 6,000 (Fees and charges) + BTN 7,000 (Motor vehicle tax)</td>
<td>fixed fee</td>
<td></td>
<td></td>
<td>0.18</td>
<td></td>
</tr>
<tr>
<td>Tax on interest</td>
<td>0</td>
<td></td>
<td></td>
<td>5%</td>
<td>interest income</td>
<td>0.12</td>
<td>include d in other taxes</td>
</tr>
<tr>
<td>Stamp duty</td>
<td>1</td>
<td>BTN 10</td>
<td></td>
<td></td>
<td>per signature</td>
<td>0</td>
<td>small amount</td>
</tr>
<tr>
<td>Employee paid - Health insurance</td>
<td>0</td>
<td>jointly</td>
<td>1%</td>
<td>gross salaries</td>
<td></td>
<td>0</td>
<td>withheld</td>
</tr>
<tr>
<td>Personal income tax</td>
<td>12</td>
<td>30</td>
<td>various rates</td>
<td>gross salaries</td>
<td></td>
<td>0</td>
<td>withheld</td>
</tr>
<tr>
<td>Totals</td>
<td>18</td>
<td>52</td>
<td></td>
<td></td>
<td></td>
<td>35.3</td>
<td></td>
</tr>
</tbody>
</table>

*Source: Doing Business 2020*

**Paying taxes over time**

In 2017, the Royal Government of Bhutan rolled an online system for filing and payment of income tax has been working properly and majority of taxpayers used the platform for filing of the corporate income tax and personal income tax returns. Payment of the two taxes is still done in physically at the tax office. Despite these efforts, Bhutan still has room to improve to align with global best practices.

**Short-term recommendations:**

1. **Encourage use of electronic systems through outreach campaign and trainings.**

While online filing and payment are available in Bhutan through the RAMIS system, the majority of companies still prefer to submit the payment in person. The Department of Revenues and Customs (DRC) is stepping up efforts to improve communications and taxpayer education. The online portal is very informative, including legislation, guidance and tutorials of how to use the electronic systems as well as help centers to assist the public. This is particularly important following significant recent reforms of the tax system such as improvements of electronic filing and payment systems. The simple fact that an electronic system is available does not of itself guarantee that taxpayers will feel a reduction in compliance time. Often, taxpayers can experience issues with using electronic filing and payment systems, either due
to glitches and errors in the system, or due to lack of taxpayer training and guidance. Any changes to the tax filing and payment systems should be combined with an outreach campaign to encourage broader usage of the electronic systems, including by small and medium-sized companies. *Doing business* only records online filing and payment systems if those are used by most of such companies. Promotion to encourage widespread use of the system is an essential component in using technology effectively to streamline procedures. For example, while Belize, Colombia, Costa Rica and Nicaragua had made online filing and payment available since the beginning of 2000, their new systems were not fully implemented until 2010 because taxpayers did not make use of the new technology.

To avoid the same lack of implementation in Bhutan, the tax officials could run a promotion campaign to educate taxpayers on how to use the system. Educational training and collaboration between the tax authority and SMEs has proven to be useful in increasing awareness of the initiatives being implemented by the tax authority. Lack of understanding of the system from the small and medium size companies and taxpayers in general might lead to delays to file and pay taxes. Improved dialogue and communication with taxpayers can also contribute to shifting their perception of the tax administration. This is particularly important following significant reforms of the tax system implemented during the last years, such as improvements of electronic filing and payment systems and changes in rates of some taxes/contributions. Taxpayer’s education and communication campaigns plays an important role before, during and after policy reforms are introduced, systems are upgraded, and processes streamlined. All such measures should be showcased/publicized through a national government website, national investment department, associations of small and medium size enterprises and chamber/s of commerce.

Two of the world’s largest economies – India and China, have continually reformed and improved their online systems. For example, in India tax authority’s website published detailed help manuals and instructions on the tax forms and how to complete them, provided free software for preparing tax returns on its website and on CDs, established a call center to answer taxpayers’ queries by phone and e-mail, set up help centers at all field office headquarters, organized regular meetings and seminars with taxpayers and tax practitioners. In China, the tax authority introduced a taxpayer service hotline back in 2005 to explain tax policies and rules. Since then the center was systematically upgraded over the years. Starting in 2013, Chinese tax authorities introduced several campaigns aimed at informing the tax payers and helping to publicize initiatives to reduce the number of tax filings and use technology to reduce time and burden for both the taxpayers and the tax collectors. Most recently, in 2017, China introduced a tax consultation and tutorship system, simplified declaration forms for corporate income tax and value-added tax and enabled e-invoices issuance and delivery.

**Medium to Long-term reform recommendations:**

2. **Streamline and automate the process of amending tax returns.**

The DRC could allow taxpayers who self-report an error in the calculation of their income tax liabilities to submit an amended return supported by any relevant documentation (typically a letter explaining the error and, in some cases, amended financial statements) and pay the difference immediately – without triggering an audit of the income tax return in the majority of cases. In the medium term, Bhutan should also consider allowing taxpayers to submit an amended corporate income tax return electronically. Recently, other economies have introduced online systems for submission of documents and payment of the income tax liability electronically. Mauritius and Slovak Republic are such examples. In the Slovak Republic, for instance, it takes taxpayers one hour to correct the error in the return, half an hour to submit the amended return online and half an hour to make the additional payment online. In the Slovak Republic, a minor mistake in the income tax return is not likely to trigger an audit. This brings the total compliance time to two hours. In Portugal and Estonia, taxpayers must only submit an amended tax return and make the
necessary payment at the moment of submission. It takes taxpayers half an hour to prepare the amended return and another half an hour to submit it electronically. The payment is also made online.

3. Implement a robust risk-management system for corporate income tax audit.

*Doing Business* records that the likelihood of corporate income tax audits in the case of a minor error in the corporate income tax return and an underpayment of tax liability due is high in Bhutan. According to *Doing Business 2020* report, most companies that amended the annual corporate income tax return and underpaid their tax liability due to error would be included in the pool of businesses exposed to a comprehensive audit of their corporate income tax returns. Complying with a corporate income tax audit per *Doing Business* case scenario takes 3.5 hours, while 2 weeks are needed to complete the audit.

To reduce the average length of tax audits, the criteria used to select cases for audit should be redefined. A risk-based approach takes into consideration different aspects of a business such as historical compliance, industry characteristics and firm size. Characteristics of firms are also used to better assess which businesses are most prone to tax evasion. One study showed that data-mining techniques for auditing, regardless of the technique, captured more noncompliant taxpayers than random audits.\(^{92}\) In a risk-based approach the exact criteria used to capture noncompliant firms, however, should be concealed to prevent taxpayers from purposefully planning how to avoid detection and to allow for a degree of uncertainty to drive voluntary compliance. Despite being a post-filing procedure, audit strategies set by tax authorities can have a fundamental impact on the way businesses file and pay taxes.

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\(^{92}\) Gupta and Nagadevara 2007
8. Trading Across Borders

In today’s globalized world, making cross border trade between economies easier is increasingly important for business and heavily influences many investment and product sourcing decisions. Excessive use of paper documents, burdensome customs and border management procedures, inefficient port operations and inadequate infrastructure adversely affect a country’s competitiveness by raising the cost of imported inputs and saddling exports with dead weight inefficiencies. Countries that facilitate trade are more likely to attract investment and help their private sector participate and compete in the international trading system93.

The performance of customs and other government agencies that regulate cross border trade, the quality of trade related infrastructure, the availability and quality of private sector logistics service providers, and the existence and administration of non-tariff barriers, all impact the ease of trading across borders and the competitiveness of the trading community. A firm’s ability to trade internationally can be impeded by a range of factors, including inadequate infrastructure, excessive documentation requirements, burdensome customs and border management procedures, poor competition and investment policies, excessive inspection regimes and difficulty in accessing the right information to comply. By simplifying and rationalizing border management systems and procedures, governments can contribute to creating a business environment conducive to trade that enables entrepreneurs to expand business opportunities beyond their national borders.

The Doing Business Trading across Borders indicator measures the time and cost (excluding tariffs) required to import and export goods, as reported by domestic business entities. Since its 2016 edition, Doing Business has used an updated methodology for measuring the Trading Across Borders indicator. Specifically, the updated indicator reports the time and cost associated with the process of importing and exporting two sets of procedures – documentary compliance and border compliance94. The time and cost associated with transporting a shipment between a warehouse and the seaport/land border most widely used by traders located in the main business city of the economy (domestic transport time and costs) is still being reported and published in the report but no longer affects the ranking or the ease of doing business score. The main reason for this is that the time and cost for domestic transport are affected by many external factors, such as the geography and topography of the transit territory, road capacity and general infrastructure, proximity to the nearest port or border and the location of warehouses where the traded goods are stored and so are not directly influenced by and economy’s trade policies and reforms. Likewise, the number of documents required to comply with regulations is reported but no longer contributes to the Trading Across Borders ranking. The case study assumptions have also been updated. The export product is now defined based on the country’s comparative advantage determined by value of exports (in the case of Bhutan, the export product used is HS 72: Iron and steel. The import product is HS 8708: Parts and accessories of motor vehicles) for the 190 economies measured by Doing Business. The import and export case studies assume different traded products. It is assumed that each economy imports a standardized shipment of 15 metric tons of containerized auto parts (HS 8708) from its natural import partner – the economy from which it imports the largest value (price times quantity) of auto parts. It is

94 Documentary compliance captures the time and cost associated with compliance with the documentary requirements of all government agencies of the origin economy, the destination economy and any transit economies. The aim is to measure the total burden of preparing the bundle of documents that will enable completion of the international trade for the product and partner pair assumed in the case study.
Border compliance captures the time and cost associated with the economy’s customs regulations and with regulations relating to other inspections that are mandatory in order for the shipment to cross the economy’s border, as well as the time and cost for handling that takes place at its port or border. The time and cost for this segment include time and cost for customs clearance and inspection procedures conducted by other agencies. For example: the time and cost for conducting a phytosanitary inspection would be included here.
assumed that each economy exports the product of its comparative advantage (defined by the largest export value) to its natural export partner – the economy that is the largest purchaser of this product. The route and mode of transport are defined based on the most widely used trade pattern for the selected product and the partner. Simultaneity of processes is also taken into account while measuring time spent on document preparation, customs and other border control inspections, port and border handling. Due to these recent changes, Doing Business data for this indicator in 2016, 2017, 2018, 2019 and 2020 cannot be directly compared to results from previous years.

Globally, Bhutan ranks 30th out of 190 economies on the ease of trading across borders in Doing Business 2020, and 1st out of 8 economies in the South Asia region, while the economy scores 94.2 points on the ease of doing business score. It takes exporters 9 hours and US$50 to prepare, obtain, submit and process the required export documents, and 5 hours and US$59 to comply with border compliance export procedures. It takes importers 8 hours and US$50 to prepare, obtain, submit and process the necessary import documents, and 5 hours and US$110 to complete border compliance import procedures. In keeping with Bhutan’s trade patterns, the Doing Business case study measures the time and cost for exporting and importing to India, through the Jaigaon land border crossing. Across all the indicators, Bhutan’s figures are significantly lower than the regional averages for imports and exports. This is partially explained by the fact that Bhutan trades through a land border crossing while other economies in South Asia (i.e. India, Pakistan) trade through seaports (Table 8.1).

Table 8.1 Doing Business Trading Across Borders ranking and best performers

<table>
<thead>
<tr>
<th>Doing Business Trading Across Borders Indicator</th>
<th>Across</th>
<th>Unit</th>
<th>Rank / Score</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Ease of Trading Across Borders</td>
<td>Rank</td>
<td>30</td>
<td>109</td>
<td>30 (Bhutan)</td>
</tr>
<tr>
<td>Time to export</td>
<td>Hours</td>
<td>9</td>
<td>73.7</td>
<td>9 (Bhutan)</td>
</tr>
<tr>
<td>Cost to export</td>
<td>Hours</td>
<td>5</td>
<td>53.4</td>
<td>5 (Bhutan)</td>
</tr>
<tr>
<td>Time to import</td>
<td>Hours</td>
<td>8</td>
<td>93.7</td>
<td>8 (Bhutan)</td>
</tr>
<tr>
<td>Cost to import</td>
<td>Hours</td>
<td>5</td>
<td>85.7</td>
<td>5 (Bhutan)</td>
</tr>
<tr>
<td>Documentary compliance</td>
<td>US$</td>
<td>50</td>
<td>157.9</td>
<td>50 (Bhutan)</td>
</tr>
<tr>
<td>Border compliance</td>
<td>US$</td>
<td>59</td>
<td>310.6</td>
<td>59.2 (Bhutan)</td>
</tr>
<tr>
<td>Documentary compliance</td>
<td>Hours</td>
<td>8</td>
<td>93.7</td>
<td>8 (Bhutan)</td>
</tr>
<tr>
<td>Border compliance</td>
<td>Hours</td>
<td>5</td>
<td>85.7</td>
<td>5 (Bhutan)</td>
</tr>
</tbody>
</table>

95 To identify the trading partners and export product for each economy, Doing Business collected data on trade flows for the most recent four-year period from international databases such as United Nations Commodity Trade Statistics Database (UN Comtrade). For economies for which trade flow data were not available, data from ancillary government sources (various ministries and departments) and World Bank Group country offices were used to identify the export product and natural trading partners.

96 Austria; Belgium; Czech Republic; Denmark; France; Italy; Luxembourg; Netherlands; Poland; Portugal; Slovak Republic; Slovenia; Spain; Hungary; Croatia; Romania.
According to the *Doing Business* 2020 report, traders routinely submit 8 documents to export iron and steel to India. These reflect legal and in-practice requirements by authorities of Bhutan and destination economies (India). The documents include the Commercial invoice; Certificate of origin; Customs export declaration; Insurance certificate; Packing list; Purchase order; Shipping bill and Report quality certificate. Six documents are commonly prepared to import a container of auto-parts to Bhutan from India, including the Commercial invoice; Customs import declaration; Insurance certificate; Packing list; Certificate of origin and Purchase order (Table 8.2). The time and costs of trading across borders are outcomes of the existing legal and regulatory framework and *de facto* practices of all involved authorities.

**Table 8.2. Documents required for Trading across Borders in Bhutan**

<table>
<thead>
<tr>
<th>Export</th>
<th>Import</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commercial invoice</td>
<td>Commercial invoice</td>
</tr>
<tr>
<td>Certificate of origin</td>
<td>Customs import declaration</td>
</tr>
<tr>
<td>Customs export declaration</td>
<td>Insurance certificate</td>
</tr>
<tr>
<td>Insurance certificate</td>
<td>Packing list</td>
</tr>
<tr>
<td>Packing list</td>
<td>Certificate of origin</td>
</tr>
<tr>
<td>Purchase order</td>
<td>Purchase order</td>
</tr>
<tr>
<td>Shipping bill</td>
<td></td>
</tr>
<tr>
<td>Report quality certificate</td>
<td></td>
</tr>
</tbody>
</table>

*Source: World Bank, Doing Business 2020 data*

**Table 8.3. Components of Border Compliance in Bhutan**

<table>
<thead>
<tr>
<th></th>
<th>Time to Complete (hours)</th>
<th>Associated Costs (USD)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Export: Clearance and inspections required by customs authorities</td>
<td>5.2</td>
<td>12.7</td>
</tr>
<tr>
<td>Export: Clearance and inspections required by agencies other than customs</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Export: Port or border handling</td>
<td>1.9</td>
<td>46.5</td>
</tr>
<tr>
<td>Import: Clearance and inspections required by customs authorities</td>
<td>2.7</td>
<td>13.6</td>
</tr>
<tr>
<td>Import: Clearance and inspections required by agencies other than customs</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Import: Port or border handling</td>
<td>5.0</td>
<td>96.5</td>
</tr>
</tbody>
</table>

*Source: World Bank, Doing Business 2020 data*

Bhutan’s performance on the Trading across borders indicator over time

The government of Bhutan has undertaken several initiatives in the past few years in the areas of trade facilitation and logistics. Bhutan’s National Trade Facilitation Committee (NTFC) was established by executive order in February 2013 in response to a policy action of the South Asia Sub-regional Economic Cooperation (SASEC) Trade Facilitation Program (TFP). The TFP was designed to serve as the primary mechanism through which interagency coordination will eventually move to a national single window (NSW) environment in Bhutan. In August 2015, the Ministry of Finance reconstituted the NTFC as the National Transport and Trade Facilitation Committee (NTTFC) to enable this committee to address...
transport-related matters. In addition, the Department of Revenue and Customs in Bhutan has been engaged in improving the customs procedures in line with the Revised Kyoto Convention and building in-house capacity in support of simplifying and harmonizing customs procedures. Other important trade and transport facilitation projects include development of a mini dry port in Phuentsholing; a bypass road from Phuentsholing to Rinchending via Dhoti Khola; a new road to connect Pasakha directly to India across the border; and a customs post at Alay. Recently, the Department of Trade carried out a feasibility study for the establishment of a Trade Information Portal.

However, a range of specific trade facilitation challenges remain before the border (particularly through automation and streamlining of certain licensing requirements), at the border (regulatory and procedural rationalization, harmonization and simplification, further automation of trade procedures, institutional reform of key agencies and improved collaboration between Customs and other border management agencies), and behind the border (enhanced trade and transport related infrastructure). Doing Business has not recorded any major reform in Bhutan on this topic during the last 10 years.

**Short-term reform recommendations**

1. Identify opportunities to reduce the administrative and procedural costs linked to importing and exporting.

Bhutan does considerably well-compared to the regional average for costs associated with documentary and border compliance for import and export procedures; however, there is still room for improvement when compared to international best practices. The costs needed to comply with border requirements for import and export procedures stand out to be more burdensome than the costs associated with documentary compliance. Specifically, the costs associated with border handling for import and exports are higher than the associated costs for customs clearance and inspections required by customs authorities. (Table 8.3).

This indicates that there may still be room to lower the administrative and procedural costs associated to importing and exporting both at customs and at the border. The majority of the cost for importing and exporting is due to inland transportation and handling (for example, truck rentals), therefore, an assessment of the procedures at the Jaigaon border crossing will be necessary to identify potential areas for cost reduction. Meanwhile, in order to lower the administrative costs of trade, the Bhutanese authorities could develop an inventory of the fees required at each step of the trading process to identify high fees that could be reduced. These measures could lead to further trade facilitation and help boost imports and exports. A study using data from 167 countries finds that every US$1 reduction in the cost to export a 20ft container could increase exports by up to US$11,000 and a decrease of US$1 in the cost to import a 20 ft container can yield an increase in imports of almost US$1,000.  

2. Improve information availability, particularly on procedures and fees for trading across borders.

Currently, Bhutan is in the process creating a Trade Information Portal. A feasibility study was conducted already. Bhutan should ensure that the new trade portal include information on export and import procedures and associated fees in order to increase efficiency and predictability. Transparency implies making information on border requirements and documentary compliance systematically available and easily accessible to the public, including the cost associated with those procedures. Publishing information on all fee schedules could improve the prospects of compliance, while at the same time allowing traders to take informed decisions on their economic activity. Freight forwarders and trading companies spend time locating information and validating the border and terminal fees to calculate their expenses.

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A Trade Information Portal will assist in complying with Bhutan trade requirements, as they are today and as they change in time. In many developing countries, government agency-specific websites may not exist and even when they do, they are often incomplete, out of date, or the content may not cover the entire spectrum of information that a trader may wish to obtain to ensure compliance with import, export, or transit requirements. It is therefore desirable that in the new trade portal all the information relating to trade from all the various agencies is aggregated and readily available for searching and viewing. Easy access to fee structures of all entities involved in the process – customs, borders, terminal, other government agencies – allows traders to anticipate costs and reduce unpredictability. Some of the costs associated with the unavailability of information are the incurrence of penalties for non-compliance and additional clearance times. In addition, any changes to fees or charges should be published in advance, giving parties an opportunity for comment, and should not take effect until such information has been made publicly available.

Medium to Long-term reform recommendations

3. Modernize the customs legislation.

Bhutan should consider improving its legal framework by updating their Customs Act. In the last decade, there has been an enormous increase in volume and complexity of trade, use of information technology, improving in trade logistics infrastructure, among other factors. All these developments should be taken into consideration in updating the customs legislation.

A new modern customs legislation should incorporate the essential elements of modernized customs legislation. It should be written in style, structure and language that is more easily accessible to Customs and economic operators, who are the main users of the law. It should also include legal provisions necessary to:

- fully enable risk management as the principal basis for customs control;
- allow Customs processing and controls to be conducted away from the border, before or after the goods arrive;
- enable implementation of simplified or alternative entry processing and controls;
- define customs procedures for the storage, processing, and movement of goods without payment of duty and tax, consistent with the WCO Revised Kyoto Convention;
- require transparency, stakeholder consultation, and publication of draft rules and regulations for public comment;
- enable coordinated border management, with the relevant Department of Customs taking the lead role;
- permit fully electronic exchange of information between Customs and economic operators and other border authorities;
- include a provision regarding the Authorized Economic Operators regime (eligibility criteria, benefits and application procedures for private sector companies);
- provide sanctions for customs violations that are “effective, dissuasive and proportionate”; 
- provide remote clearance procedure;
- allow periodic review of formalities and documentation requirements;
- advance rulings;
- comply with WTO customs valuation procedures; and,
- protect confidential information and data security.
4. Consider establishing a national single window for trade.

Currently, Bhutan lacks a one-stop shop (electronic or physical) for trade-related transactions. The level of interconnectivity and automation for Government agencies involved in the trading process is still very low. In order to establish a National Single Window for Trade Facilitation in the country, Bhutan needs as a first step to identify and eliminate challenges in the process of electronic import and export declarations, manifests and other trade related documents, such as technical certificates and permits, and improve data sharing between the regulatory agencies. As a second step, the data sharing between the regulatory agencies and the central database need to become fully electronic (sharing raw data instead of scanned documents). Oftentimes, countries first introduce a single location where all the agencies involved in the trading process have a representative. Rather than dealing with different agencies/ministries to submit and process the necessary documentations, the best single windows systems will link banks, licensing agencies and trade clearance agencies into a unique platform (electronic or physical), and allows exchange of information in real time, speeding up approvals.

Among other measures to enable fully functional electronic single window may be:

- Connect all relevant agencies to the system
- Eliminate the paper-based submission of documents
- Introduce or increase the use of risk management techniques
- Improve the existing laws and regulations to support the exchange of such documents.

The electronic transmission of documents not only speeds the clearance of goods; it often reduces the incidents of corruption as for example, informal payments. Time spent on document preparation and cargo release could be cut substantially by enabling importers and exporters to submit their documents electronically prior to the arrival of the cargo, rather than in hard copy upon arrival of the vessel. The electronic submission of customs declarations and the manifest allow customs to reconcile both documents prior to cargo arrival, and, based on this, complete clearance of the vast majority of cargo even before the arrival of the vessel. This will save traders’ time and it will reduce the cost of trading given that cargo is manipulated less and released faster. In best practice countries, e-submission of customs declaration is sufficient for clearance, unless there are suspicions that justify additional controls, in which case the supporting documents are checked. The strongest incentive in this respect is shorter processing times and lower costs. The electronic Single Window should allow traders to upload all documentation and receive approvals online and it should also introduce online payment systems in the Single Window to limit the number of physical interactions and time spent at the border. Information campaigns and education seminars can help raise awareness about available options. At a final stage, submissions in hard copies should be eliminated completely and replaced with fully automated procedures.
Table 8.4. Successful National Single Window Systems in Asia.

<table>
<thead>
<tr>
<th>Name of the Customs Administration</th>
<th>Singapore</th>
<th>Korea</th>
<th>Japan</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Singapore Customs</td>
<td>Korea Customs Service</td>
<td>Customs and Tariff Bureau, Ministry of Finance</td>
</tr>
<tr>
<td>Organization Type</td>
<td>Customs Agency</td>
<td>Customs Agency</td>
<td>Ministry Department</td>
</tr>
<tr>
<td>Approximate staff strength</td>
<td>987</td>
<td>5,058</td>
<td>9,808</td>
</tr>
<tr>
<td>Name of the Customs ICT System</td>
<td>Network Trade Platform (NTP)</td>
<td>UNIPASS</td>
<td>NACCS (Nippon Automated Cargo and Port Consolidated System)</td>
</tr>
<tr>
<td>Import</td>
<td>5,538,609</td>
<td>21,560,000</td>
<td>7,075,000</td>
</tr>
<tr>
<td>Number of Declarations</td>
<td>Export</td>
<td>Import</td>
<td>Export</td>
</tr>
<tr>
<td>------------------------</td>
<td>--------</td>
<td>--------</td>
<td>--------</td>
</tr>
<tr>
<td></td>
<td>3,687,070</td>
<td>9,235,092</td>
<td>8,418,000</td>
</tr>
<tr>
<td>Percentage of electronic declarations</td>
<td>100%</td>
<td>92%</td>
<td>100%</td>
</tr>
<tr>
<td></td>
<td>100%</td>
<td>94%</td>
<td>100%</td>
</tr>
<tr>
<td>Number of authorities issuing import or export permits</td>
<td>11</td>
<td>41</td>
<td>11</td>
</tr>
<tr>
<td>Number of authorities connected to National Single Window System</td>
<td>11</td>
<td>27</td>
<td>6</td>
</tr>
</tbody>
</table>

Source: Annual Report 2018-2019 – World Customs Organization

International examples abound. Singapore, for instance, has been a global leader in the implementation of a single window platform. Singapore has a unique customs clearance and trade facilitation regime in place, designed primarily to match the needs of the port community with less attention on revenue collection and other regulatory matters. The country rolled out a new national trade information management platform, the Networked Trade Platform (NTP), in September 2018. Replacing the previous TradeNet system for trade-related applications and the TradeXchange system for connecting the trade and logistics community, the NTP was designed to be a fully integrated digital ecosystem for the interface of trade and logistics actors and government systems. The NTP provides a single location for government certification services required for trading in and out of Singapore, as well as a digital marketplace for value-added trade and logistics services by third-party firms. By becoming a completely paperless system, the government estimates up to S$600 million worth of man-hour savings annually for the private sector. The NTP was developed by the Singapore Customs and the Government Technology Agency of Singapore (GovTech) and is a completely open source. Revamping the system took four years and over 100 million Singaporean dollars. The process involved more than 20 ministries, government agencies, and working groups. By being an open-source platform, the government envisions more rapid innovation and through a “Developer Zone” co-designed by government and industry. This serves as a platform for industry entrepreneurs to build innovative ICT applications using the data tools provided by the NTP for their onboarded users.

Korea also operates a fully integrated trade and logistics platform: UNI-PASS. The platform is the backbone of international trade in Korea and serves as the information hub for the entire trading community. UNI-PASS connects all stakeholders involved in trade clearance processes, and provides automated end-to-end processing of all trade transactions, including payment. The most recent available data states UNI-PASS connects 169 government entities, including Customs, ports, warehouses, banks and 27 OGAs, and a total of 260,000 different private sector entities covering importers, exporters, customs brokers, shipping lines, etc. Information on the platform is shared among relevant stakeholders and regulators. Through UNI-PASS some 21 million import declarations are processed annually, and revenue collection of USD 52 billion. Moreover, 25 million TEUs of cargo are handled, and, through the platform’s intelligent risk management features, some USD 7 billion of illegal trade is prevented. Since 2016, the 4th generation of UNI-PASS has been deemed a “Smart Customs System.” To that end, Korea Customs Service (KCS) established an ICT Development Division in 2017 to explore the potential application of new science and technologies for improving UNI-PASS and related systems. The Division began this effort by joining the public-private maritime export logistics consortium, led by Samsung SDS Co., to determine the feasibility of a blockchain solution for data exchange among public and private entities. Building on the success of this initiative, KCS launched the “Fourth Industrial Revolution and Smart Customs” project in 2018, with
the aim of designing and implementing Artificial Intelligence (AI), blockchain, and big data solutions to Customs systems and procedures.

**Japan’s experience with trade facilitation and Customs automation dates back to the late 1970s, when it introduced the Nippon Automated Cargo and port Consolidated System (NACCS).** Initially focusing on airports, ‘Air-NACCS’ was first rolled out at Narita International Airport in 1978. Today, NACCS is a fully integrated system, serving all stakeholders involved in international trade. It connects some 14,000 entities, including Customs, ports, warehouses, banks, shipping companies and their agents, terminal operators, airlines, 7 other governmental agencies (OGAs), and some 8,600 companies. NACCS provides complete end-to-end automation and processing of all trade transactions, and allows information sharing, payment and performance oversight for all but a few OGAs. The most recent update to NACCS in 2017 liberalized the Customs declaration policy so that Authorized Economic Operators (AEO) importers and exporters can declare goods at any customs office, not only at the customs office with jurisdiction over the bonded area where goods are stored. The latest version also digitized the administrative system for tariff quotas and centralized the vessel booking system on the NACCS platform.

5. **Consider reduced or joint physical examinations and adopt the use of risk management in all border agencies, including risk-based inspections.**

In Bhutan, as of 2017, all imports and exports are subject to 100 percent physical inspections although the officer in charge makes the decision for inspection at an informal level. The use of risk management techniques must be realized by all controlling bodies represented at the border. Introduction of Risk Management System facilitates the controlling agencies focus on high-risk goods while providing free movement for low-risk goods. WCO Framework of Standards to Secure and Facilitate Global Trade states that “Customs administration must create risk management system to reveal potentially hazardous cargo and automate such system. The system must include mechanism of risk validation and decisions on tracing the cargo as well as determining the most effective methods of work”. The risk management process is usually based on a cycle which starts with assessing the environment. Risks are then identified, followed by assessment and prioritization, analyzed, determined and strategies developed to tackle the risks. Throughout the process, the monitoring and evaluation takes place. Use of X-ray machines could further expedite the process.

In best practice economies, inspections are risk-based and coordinated where more than one agency is involved. This increases efficiency at the border for both government agencies and traders. Bhutan’s agencies should adopt a risk-based approach to inspections and other control measures and continue efforts to reduce the level of physical inspections, which has the potential to significantly impact the time and cost saving on the Doing Business performance.

Another measure that could help reduce time and costs at the border in Bhutan is implementing the Trusted traders or Authorized Economic Operator regime. Trusted traders or Authorized Economic Operators are persons or companies that meet criteria specified by customs, including having an appropriate record of customs compliance, financial viability, and satisfactory system for managing commercial records. The status of trusted trader provides access to simplified procedures—such as pre-arrival processing of information; simplified declaration, valuation, clearance at locations convenient for the trader; payment of duties after release—where the Custom Agency reduces the level of controls and relies more on internal controls applied by the trader to ensure compliance with all relevant laws and regulations.

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Uruguay is one of the countries that successfully implemented a risk-based approach to inspections. Building on the Uruguayan Customs Modernization Plan launched by the Government in 2007, the National Customs Directorate rolled out a new risk-based system that became fully operational by 2014. Inspections have therefore become faster, as has the time required to complete the process of export and import customs clearance. Albania also implemented an electronic risk-based inspection system, which reduced the time for border compliance. As part of the Western Balkans Trade Logistics Project completed by Albanian Government and UNCTAD in January 2015, Albanian Customs introduced an effective electronic risk-based inspection system at the Port of Durres. The new system establishes risk profiles, which allow to apply physical inspections in proportion to the potential risk of consignments. The risk-based inspection system has been facilitated by the upgrade of the existing ASYCUDA Customs Processing system, which now allows electronic assignation of green channels. The risk-based inspection system is fully operational, and the majority of exports go through green channels which do not require either physical or documents inspection, thus decreasing the time of export customs clearance.

6. Enhance cross-border cooperation with neighboring countries.

Bhutan, like many other landlocked economies face special challenges in competing globally because of the greater inland distances and multiple border crossings involved in their trade. These economies can accelerate trade through efforts to increase border cooperation agreements and reduce the number of checkpoints so that cargo can move freely—without being stopped for customs or other inspections—until it reaches its destination.

Bhutan and India established a free-trade regime in 1972 (The India-Bhutan Trade and Transit Agreement). Since then, the agreement has been renewed five times. The last Agreement was renewed on November 2016. The Agreement also provides for duty-free transit of Bhutanese exports to third countries. In 2018, bilateral trade reached Rs/Nu. 9288 Cr. (imports from India were Rs/Nu. 6011 Cr., accounting for 84 percent of Bhutan’s total imports, whereas Bhutan’s exports to India stood at Rs/Nu. 3217 Cr. and constituted 78 percent of its total exports).

To achieve significant progress in improving the efficiency of its customs clearance procedures and reduce border delays, Bhutan needs to further engage with its neighboring countries and main trading partners – especially India – to secure effective customs cooperation/harmonization, transit, as well as data-exchange agreements. For instance, Bhutan could harmonize working hours of the custom station of Jaigaon with India and simplify transshipment procedures. Bhutan could also ensure real-time information exchange with the neighboring countries’; speed-up release; remove the need for duplicate checks; and, foster compliance. Transit agreements also help in avoiding unnecessary unloading and reloading operations at the border.

In recent years, several countries in the East African Community have adopted the concept of a one-stop border post (OSBP) which combines the border control agencies of two countries into one single facility, often eliminating the need to repeat clearance procedures on the other side of the border. In 2017 the Malaba OSBP, which is shared between Uganda and Kenya, became operational. The Malaba OSBP houses a number of government agencies from both countries in a single facility at the border, including customs officials. As a result of this cooperation, both countries experienced increased efficiency at the border. One-stop border posts also became operational in Rwanda and Tanzania in 2017.

Another example is the case of US and Canada. The US exports HS 84: Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof to Canada by truck. Being the US and Canada part of the North American Free Trade Agreement (NAFTA), physical nor non-intrusive inspections (such as scanning) are very rare at the border. Not only that: all border clearance happens on the Canadian side of the border, where the Canada Border Services Agency (CBSA) accepts either a commercial invoice or a Canada
Customs Invoice for clearance purposes. Consequently, US exporters sending shipments to Canada do not need to prepare a customs export declaration and they don’t need to fill the Electronic Export Information (EEI) with U.S. Customs and Border Protection (CBP) through the Automated Export System (AES). Nevertheless, there are certain exceptions in which US traders are required to complete the EEI, mostly related to security.
9. Enforcing Contracts

Research in various countries around the world suggests that, in the absence of efficient courts, firms make fewer investments while informal transactions become more attractive. A study of 27 economies found that the informal sector’s share in overall economic activity decreased with better contract enforcement quality, evaluated by a country-wide measure of rule of law, as well as by the firm’s perception of the fairness of courts. Improvements in court efficiency are associated with a lower share of the informal sector in the overall economic activity, increased investor confidence and with increased bank financing of firms for new investment. For example, reforms in other areas, such as creditors’ rights, can increase bank lending only if contracts can be enforced before the courts.

Efficient contract enforcement is essential to economic development and sustained growth. Economic and social progress cannot be achieved without respect for the rule of law and effective protection of rights, both of which require a well-functioning judiciary that resolves cases in a reasonable time and is predictable and accessible to the public. Economies with a more efficient judiciary, in which courts can effectively enforce contractual obligations, have more developed credit markets and a higher level of development overall. A stronger judiciary is also associated with more rapid growth of small firms. Overall, enhancing the efficiency and quality of the judicial system can improve the business climate, foster innovation, attract foreign direct investment and secure tax revenues.

Doing Business measures the efficiency (time and cost) of the judicial system in resolving a standardized commercial dispute before the Thimphu District Court, Commercial Bench, as well as the quality of judicial processes. Globally, Bhutan ranks 29th on the ease of enforcing contracts among 190 economies, and 1st out of 8 economies in the South Asia region, with an overall Ease of Doing Business score of 70.00 percentage points. On average, resolving a standardized commercial dispute at the Thimphu District Court, Commercial Bench takes 225 days and costs 23.1 percent of the case study claim value (BTN 391,120). Enforcing Contracts in Bhutan is one of the fastest in the world. Bhutan’s results in the time and cost indicators are below regional averages. (Table 9.1).

In addition, Bhutan scores 8 out of 18 possible points in the Quality of judicial processes index, above the regional average. According to Doing Business 2020, Bhutan follows some of the good practices tested in the areas of case management and alternative dispute resolution. However, there is a complete lack of court automation in the courts in Bhutan, including the Thimphu District Court, Commercial Bench (Table 9.2).

Table 9.1. Enforcing contracts ranking and best performers

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102 Esposito, Lanau and Pompe 2014; Dakolias 1999; Ball and Kesan 2010; Klerman 2006; Dam 2006; Rosales-López 2008.
103 Dakolias 1999; Sherwood, Shepherd and De Souza 1994.
104 Dam 2006.
106 Esposito, Lanau and Pompe 2014; Dakolias 1999; Ball and Kesan 2010; Klerman 2006; Dam 2006; Rosales-López 2008.
107 Singapore 164 days; New Zealand 216 days and Uzbekistan and Bhutan 225 days.
<table>
<thead>
<tr>
<th>Doing Business Indicator</th>
<th>Bhutan</th>
<th>South Asia average</th>
<th>Regional best performer</th>
<th>Global best performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Time (days)</td>
<td>225</td>
<td>1101.6</td>
<td>225 (Bhutan)</td>
<td>164 (Singapore)</td>
</tr>
<tr>
<td>Cost (% of claim)</td>
<td>23.1</td>
<td>29.9</td>
<td>18.5 (Maldives)</td>
<td>9 (Iceland)</td>
</tr>
<tr>
<td>Quality of judicial Processes index (0-18)</td>
<td>8.0</td>
<td>7.1</td>
<td>10.5 (India)</td>
<td>17 (China)</td>
</tr>
</tbody>
</table>

Source: Doing Business 2020 database

**Table 9.2. Details on the Time, Cost and Quality of judicial processes indexes**

<table>
<thead>
<tr>
<th>Time Sub-index (days)</th>
<th>225 days</th>
</tr>
</thead>
<tbody>
<tr>
<td>Filing and service</td>
<td>20 days</td>
</tr>
<tr>
<td>Trial and Judgment</td>
<td>90 days</td>
</tr>
<tr>
<td>Enforcement of judgment</td>
<td>115 days</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Cost Sub-index (% of claim value)</th>
<th>23.1%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Attorney fees</td>
<td>23%</td>
</tr>
<tr>
<td>Court fees</td>
<td>0.1%</td>
</tr>
<tr>
<td>Enforcement fees</td>
<td>0%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Quality of judicial processes index (0-18)</th>
<th>8.0</th>
</tr>
</thead>
<tbody>
<tr>
<td>Court structure and proceedings (-1-5)</td>
<td>2.5</td>
</tr>
<tr>
<td>Case management (0-6)</td>
<td>3.0</td>
</tr>
<tr>
<td>Court automation (0-4)</td>
<td>0.0</td>
</tr>
<tr>
<td>Alternative dispute resolution (0-3)</td>
<td>2.5</td>
</tr>
</tbody>
</table>

Source: Doing Business 2020 database

**Bhutan’s performance on the Enforcing Contracts indicator over time**

*Doing Business* has recorded two major reforms in Bhutan on this topic in the last ten years. In 2007/2008 Bhutan eased the caseload of district courts by creating a land commission to handle property transfers (previously about 30 percent of all district court cases), thereby reducing the time required to enforce contracts through the courts. In addition, in 2016/2017, Bhutan made enforcing contracts easier by creating a dedicated bench to resolve commercial cases.

Despite Bhutan’s overall good performance on this indicator, the Judiciary of Bhutan still faces some challenges. The scarce use of electronic case management tools and the lack of court automation in the Thimphu District Court, Commercial Bench are some of the challenges to be overcome.

**Short-term reform recommendations**

1. **Make publicly available judgments in commercial cases at all levels.** Currently, few Supreme Court judgments are published in Bhutan ([http://www.judiciary.gov.bt/index.php](http://www.judiciary.gov.bt/index.php)). Efforts should be put into making judgments rendered by local courts at all levels systematically available to the public through publication in official gazettes, newspapers, and/or online. Making court decisions publicly available is a common practice worldwide to promote transparency and discourage corruption in the judicial system. It creates incentives for courts to adhere to decision making principles and higher court guidance, to write judgments concisely and clearly, increases public accountability and promotes the likelihood of receiving
fair trials. It also supports judicial certainty and promotes a greater public understanding of court reasoning for both firms and individuals by clarifying the scope and interpretation of the law. Access to the results of commercial cases benefits companies that invest in a particular jurisdiction, clarifying the scope of their rights and duties.

To build public understanding and confidence in the courts, courts need to make efforts to publish regularly all court decisions. Initially, courts that lack the capacities for continuous online posting have opted for making key decisions in commercial cases available in paper format (Official Gazette) and then online. Doing so will not only increase transparency but improve the public’s confidence in the court and provide predictability for the legal community. Another aspect of this reform is publishing additional information about the ruling – such as the timeliness and the specific judge – which further increases public accountability. This can highlight inefficiencies or inconsistencies in the productivity of particular courts or judges, who must then be held accountable through social pressure and healthy competition.

The effectiveness of this policy is strengthened even further when the court rulings are freely available online, such as in the Republic of Korea. Maintaining a well classified, searchable electronic database of these decisions is also beneficial for reliable record-keeping of decisions (there is less chance of papers being misfiled) and allows interested parties to search a particular topic more efficiently. If lawyers and litigants understand how courts generally decide certain type of cases and when appeals are successful or not, appeals tend to be better justified and litigant satisfaction tends to increase.

Recently, many countries, such as Kazakhstan, Turkey and Vietnam, made enforcing contracts easier by making judgments rendered at all levels in commercial cases available to the public online. Some countries in South Asia region, such as India and Maldives, also make publicly available all judgements rendered in commercial cases at all levels (first instance, appellate and supreme courts).

**Medium and long-term reform recommendations**

**2. Strengthen limits on adjournments by linking the granting of adjournments to performance management systems and setting and monitoring time limits.**

The Civil and Criminal Procedure Code of Bhutan 2001 neither regulates the number of adjournments and continuances that can be granted, nor does it limit adjournments to unforeseen and exceptional circumstances. The main reference to court adjournments in the Code is mentioned in Section 76.1, which provides that the court may grant a motion for adjournment or stay of proceedings in several different circumstances, for instance: in the absence of a crucial witness summoned by the Court; if an opposing party requires time to study/consider court admissible evidence not previously available which may have an impact on his/her legal strategy or plea; if a party needs time to prepare for the cross-examination of a new witness of the opposing party not previously scheduled to appear in the proceedings; if a respondent/defendant wishes to change his/her plea; if the witness or party in the suit, excluding an imprisoned defendant has to attend another Court provided that the summons from that Court was issued earlier to the institution of this suit; if the parties jointly agree to pursue an out-of-Court settlement in accordance with this Code; if a party is sick or mentally unsound and furnishes a medical certificate; if a member of the family of either party is critically ill; if there has been a death in the family of either party; if the participation of a litigant in farm activities during planting or harvesting seasons is necessary and if a national emergency has arisen directly affecting the parties or other key parties to the suit. In addition to those circumstances, the same Section mentions that the court may grant a motion for adjournment for any other judicially valid reasons or purposes as may be determined by the Court.

To reduce the total time of proceedings and to prevent abuse by the litigants, it is recommended to regulate the maximum amount of adjournments that can be granted, and to limit them to unforeseen and exceptional
circumstances. The liberal granting of adjournments, especially if requested by litigants as a delaying tactic, can slow down court proceedings, increase caseloads and, in turn, may strain court resources. Clarity on when, why and for how long adjournments should be granted will help keep cases on track. In addition, establishing time frames favors timely flow of cases through the court from initial filing to disposition. Both techniques enhance processing efficiency and promote early court control of cases. When well implemented, case management techniques can enhance record-keeping, reduce delays and case backlogs and provide information to support strategic allocation of time and resources—all of which encourage generally better services from courts. They can also improve the predictability of court events, which can ensure accountability, increase public trust, reduce opportunities for corruption and enhance the transparency of court administration.

Regulating the maximum number of adjournments that can be granted and limit them to unforeseen and exceptional circumstances will also reduce the total time of proceedings and prevent abuse by the litigants. Those provisions need to be respected by the court.

In Doing Business 2020 report, amending civil procedure rules to limit adjournments to unforeseen and exceptional circumstances was a popular reform. For instance, China, Mauritania and Nigeria, implemented this reform.

3. Consider creating a small claims court or a fast track procedure for small claims.

Currently, Bhutan does not have a small claims court or a fast track procedure in place for the expeditious resolution of disputes involving small claims. Dispute resolution can be expensive and time-consuming for micro, small and medium size businesses. Small claims courts help expedite the resolution of minor disputes of a relatively low value. They do so by setting aside many legal formalities and using simplified or fast-track procedures. Simpler processes and more relaxed rules lower costs for claimants, who may also be able to file and present their own cases before the court. In addition, filing fees are lower and judges issue decisions rapidly. Because they have lower costs and faster turn-around times, small claims courts can provide an easier alternative for resolving simple disputes. In addition, they tend to reduce backlogs and caseloads in higher courts. Small claims courts usually use informal hearings, simplified rules of evidence and more streamlined rules of civil procedure—and typically allow the parties to represent themselves.

Faster and less costly dispute resolution matters to micro, small and medium-size enterprises, which may not have the resources to stay in business during long, costly litigation. If a claim could not be enforced because the relative cost is prohibitive, there would be a denial of justice. By providing a venue for resolving claims with costs and procedures that are realistic and proportionate to the size of the dispute, small claims courts and simplified procedures for small claims increase access to justice for businesses and individuals.

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According to *Doing Business 2020* data, 131 economies have either a stand-alone small claims court or a simplified procedure for small claims within the first-instance courts. Of these 131 economies, 119 allow parties to represent themselves during the proceedings. In the South Asia region, Bangladesh, India, Nepal, Pakistan and Sri Lanka follow this international best practice.

4. **Introduce fully-automated random assignment of cases to judges at the Thimphu District Court, Commercial Bench.**

Today, when a case is filed at the Thimphu District Court, Commercial Bench, the basic consideration when a court registrar assigns a case manually is assuring an equitable distribution of caseload. However, by law, a case shall be assigned to a Bench in an order of precedence\(^\text{112}\). Courts also checks if a judge who is assigned a case may be reasonably construed to have conflict of interest, which would make it improper for this Judge to preside over a particular case.

A credible system for random assignment of cases fosters trust in the courts and can play an important role in ensuring that judges are assigned similar workloads.\(^\text{113}\) Making the assignment of cases random through an automated process diminishes the possibility for the parties or lawyers to influence the assignment.

While almost all economies worldwide (163) provide for random assignment of cases, only 53 have a fully automated process. In Bhutan, this currently does not exist. According to *Doing Business 2020* data, case assignment is neither random nor automated. Measures should be taken to align the country to international best practices in this area of business regulation.

5. **Consider developing an electronic case management system for judges and lawyers in the Thimphu District Court, Commercial Bench.**

The Thimphu District Court, Commercial Bench does not have an electronic case management system for the use of judges or lawyers. A case management system is the aggregate of the processes and resources used to facilitate the progress of a case from filing through to its ultimate disposition. Electronic case management systems can help reducing procedural delays and parties’ non-compliance with judicial orders and deadlines. It also enhances record-keeping, reduce case backlogs and provide information to support strategic allocation of time and resources – all of which encourage generally better services from courts.

The main features of an advanced electronic case management system may include access to laws, regulations and case law; access to forms to be submitted to the court; automatic generation of a hearing schedule; management of electronic notifications; tracking of the status of a case; management of case documents; electronic filing of briefs and motions; and access to court orders and decisions. Such systems may be available to a range of users, from judges to lawyers, court administrators and court users.

Worldwide, there has been an increase in the implementation of case management systems in courts, especially in commercial courts\(^\text{114}\). In the South Asia region, only the courts in Karachi, Pakistan have a well-advanced electronic case management system in their courts for the use of judges.

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\(^{112}\) Article 71 of the Civil and Criminal Procedure Code.
\(^{113}\) USAID 2009.
\(^{114}\) 53 economies out of the 190 economies covered by Doing Business have a well-advanced electronic case management system in their courts for the use of judges. 43 out of those 53 economies also have a well-advanced electronic case management system for the use of lawyers.
6. Consider introducing court automation features, such as electronic filing of the initial complaint, electronic service of process and electronic payment of court fees.

Courts in Bhutan lack automation. To further reduce the cost and time to enforce a contract, the adoption of court automation features such as electronic filing of the initial summons, electronic service of process and electronic payment of court fees is recommended. Electronic records tend to be more convenient and reliable than paper-based ones. Reducing in-person interactions with court officers—facilitated by electronic systems—decreases the chances for corruption and results in speedier trials, better access to courts and more reliable service of process. These features reduce the cost to enforce a contract as court users save in reproduction costs and courthouse visits, while courts save in storage costs, archiving costs and court officers’ costs. Studies show that after electronic filing is introduced in courts, the accessibility of information increases and access to and delivery of justice improve considerably.115

The best performing economies have several features of court automation. For example: The Republic of Korea and Singapore. In the South Asia region, only India allows for electronic payment of court fees.

The Republic of Korea and Singapore are two of only eight economies worldwide that receive full points on the court automation index; they also score points for the availability of electronic case management systems for both judges and lawyers. Unsurprisingly, both of these economies introduced improvements in this area in the past few years. Korea launched an electronic case filing system in 2010 that allows electronic document submission, registration, service notification and access to court documents (Box 9.1). Singapore introduced a new electronic litigation system in 2014. The system allows litigants to file cases online—and it enables courts to keep litigants and lawyers informed about their cases through e-mail, text alerts and text messages; to manage hearing dates; and even to hold certain hearings by video conference.

7. Consider financial incentives for parties to attempt mediation or conciliation (e.g. refund of court filing fees).

While mediation services are available in Bhutan and widely used and encourage by judges, there are no financial incentives for parties to participate in such services. Mediation is an important part of the dispute resolution process and allows parties to settle their claims without intervention from a judge or another official, but rather with the assistance of a mediator, who helps the parties reach their settlement voluntarily through negotiations. This can be the most cost-effective and speedy way to settle a dispute. However,

parties, who are already at odds and in an adversarial position, will rarely attempt mediation, unless they see an immediate financial benefit beyond a potential settlement. Financial incentives that can be used to encourage use of mediation services include, for example, tax waivers for mediated settlements, income tax credit, and refund of court fees when the case is resolved through mediation.

Worldwide, 31 economies follow this international best practice, including Bangladesh, India and Nepal in the South Asia region. In Doing Business 2020, Serbia and Uzbekistan made enforcing contracts easier by establishing financial incentives for the parties to attempt mediation.
10. Resolving Insolvency

A well-functioning insolvency framework is essential for the healthy circulation of credit. Where insolvency regimes are effective, creditors are more likely to lend, both in higher volumes and at lower interest rates. A balanced insolvency system also operates as a filter that promotes economic efficiency by providing a framework for the rehabilitation of viable companies and the swift liquidation of unviable ones, thereby preserving jobs and enterprise value in the former situations and freeing up capital and assets in the latter cases to be put to better use elsewhere. By facilitating the efficient business exit and liquidation of nonviable companies, an insolvency framework supports the efficient reallocation of resources across the economy.\(^\text{116}\) Improvements to insolvency systems however require sustained and continuous efforts. Often, the effects of reforms are not immediately evident, and several years may pass before they can be quantified.

The Doing Business resolving insolvency indicator measures the time, cost and outcome of insolvency proceedings for domestic companies as well as the strength of the legal framework applicable to the liquidation and reorganization proceedings. The rankings are based on two equally weighted indicators—the recovery rate (recorded as cents on the dollar recouped by secured creditors through reorganization, liquidation or debt collection—foreclosure or receivership—procedures) and the strength of insolvency framework index. The recovery rate is influenced by the time, cost and outcome of resolving an insolvency case, as well as the lending rate in the country. The indicator does not deal with situations where a business owner voluntarily winds up a company, but rather where businesses face financial distress. The strength of insolvency framework index is based on the provisions of the insolvency law and includes four indices: commencement of proceedings index, management of debtor’s assets index, reorganization proceedings index and creditor participation index. The data are based on feedback from local experts who extensively practice in the area of resolving insolvency, as well as on the readings of the law.

Resolving insolvency in Bhutan is scored as No Practice, which means that globally, Bhutan ranks, together with other 23 economies, 168th out of 190 economies. The Doing Business methodology explains that “If an economy had zero completed cases a year over the past five years involving a judicial reorganization, judicial liquidation or debt enforcement procedure (foreclosure or receivership), the economy receives a ‘no practice’ mark on the time, cost and outcome indicators”\(^\text{117}\). This means that creditors are unlikely to recover their money through a formal legal process. The recovery rate for “no practice” economies is zero. In addition, a “no practice” economy receives a score of 0 on the strength of insolvency framework index even if its legal framework includes provisions related to insolvency proceedings (liquidation or reorganization). Bhutan, as a No Practice economy, scores 0.00 percent on the Ease of resolving insolvency score. Bhutan ranks 8th out of 8 economies in the South Asia region on the resolving insolvency indicator. Bhutan is the only economy in the region that scored as “no practice”.

For this reason (being a “No Practice” economy), Bhutan compares unfavorably when looking at other countries in the region. While Table 10.1 shows Bhutan relative to its peer and best performers at the regional and global scale, it should change if Bhutan starts processing insolvency cases and becomes a Practice country. The best regional performers in terms of costs to the bankruptcy estate are Pakistan and the Maldives at 4 percent, a substantial improvement over the regional average (9.9 percent) but still short of the overall best international performer -Norway at just 1 percent-. In turn, it takes 2.2 years on average to work out an insolvency case in the South Asian economies. This average duration is more than the time it takes to work out an insolvency case in the regional best performer, the Maldives (1.5 years). In turn, the


\(^{117}\) www.doingbusiness.org/en/methodology/resolving-insolvency
insolvency cases in Ireland, the global best performer just take 4 months. Finally, the average recovery rate in South Asia region is 38.1 cents on the dollar. This recovery rate is lower than the regional best performer (India, 71.6 cents on the dollar). In comparison, the recovery rate of Japan, the global best performer in this area, is 92.1 cents on the dollar.

Table 10.1 Resolving insolvency ranking and best performers

<table>
<thead>
<tr>
<th>Doing Business Indicator</th>
<th>Bhutan</th>
<th>Regional Average</th>
<th>Regional best performer</th>
<th>Global best performer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Time (years)</td>
<td>No practice</td>
<td>2.2</td>
<td>1.5 (Maldives)</td>
<td>0.4 (Ireland)</td>
</tr>
<tr>
<td>Cost (percent of estate)</td>
<td>No practice</td>
<td>9.9</td>
<td>4.0 (Maldives; Pakistan)</td>
<td>1.0 (Norway)</td>
</tr>
<tr>
<td>Outcome (0 as piecemeal sale and 1 as going concern)</td>
<td>0</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Recovery rate (cents on the dollar)</td>
<td>No practice</td>
<td>38.1</td>
<td>71.6 (India)</td>
<td>92.1 (Japan)</td>
</tr>
<tr>
<td>Strength of insolvency framework index (0-16)</td>
<td>No practice</td>
<td>6.5</td>
<td>12 (Afghanistan)</td>
<td>15.5 (Serbia)</td>
</tr>
</tbody>
</table>

Source: Doing Business 2020 database

For the same reasons indicated above, the legal framework for resolving insolvency in Bhutan has been 0 out of 16 in the strength of insolvency framework index.

Bhutan’s performance on the Resolvency Insolvency indicator over time.

No reforms have been recorded by Doing Business in the past 10 years on this indicator in Bhutan. In Bhutan, the legal underpinnings for insolvency can be found in the Bankruptcy Act of the Kingdom of Bhutan of 1999 and the Companies Act of 2016. Currently, Bhutan is reviewing the Bankruptcy Act to strengthen legal rights for creditors and borrowers. As noted earlier, it often takes time before one can perceive the impact of an insolvency reform in practice. The absence of instant results should not discourage economies from continuing to improve the insolvency framework. A good example is Slovenia, which determined to improve its insolvency framework in the 2000s. In 2007, Slovenia adopted a new insolvency law, but, following the global financial crisis, revised again its corporate restructuring framework in 2013. These efforts gradually paid off: while in Doing Business 2010 the recovery rate in Slovenia was equal to 45.5 cents on the dollar, with the most likely outcome for insolvent businesses being a piecemeal sale, in Doing Business 2016 the recovery rate rose to 88.1 cents and the outcome changed to going concern. In Doing Business 2020, Slovenia’s recovery rate was 90.0 cents and the most likely outcome of proceedings remained going concern.

Short-term reform recommendations:

1. Encourage the use of insolvency and debt collection proceedings.

Current reform efforts should focus on the incentives of the parties to initiate and participate in formal judicial mechanisms to settle debts, particularly in collective insolvency proceedings. A reform in this domain would have to be firmly rooted in the realities of the existing legal system and take into account religious, constitutional, and political sensitivities.

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118 The recovery rate calculates how many cents on the dollar secured creditors recover from an insolvent firm at the end of insolvency proceedings.
The difference between black letter law and legal practice is well known in legal circles. While legal institutions are based on rules, their implementation requires more than the rules themselves. A key aspect in this regard, is the uptake of legal rules by litigants and their legal representation. If for any reason those individuals choose not to make use of certain tools provided by the legal system, the objectives set out under the laws containing those tools may become unfulfilled. Legal institutions, especially shortly after legal reforms, tend to face those challenges.

According to the Doing Business 2020 report, there has been little if any insolvency practice in Bhutan, which can be attributed to the shortcomings of the current insolvency regime. In order to break with the existing inertia in this area of law, socialization efforts should be strongly pursued to raise awareness among stakeholders of the benefits and possibilities arising from the procedures available. As with other socialization efforts, the outreach should be directed to potential users and their representatives, including (but not limited to) the business and banking communities and the tax authority.

In addition, the existing institutional framework could be bolstered by creating a bankruptcy court or a division within the civil court to ensure effective specialization of judges. Capacity building should include training of judges, stakeholders (for instance, commercial banks) and court personnel.

Same measures should be implemented after amending the current insolvency framework to introduce effective reorganization procedures; provisions dealing with administration of the debtor’s assets during insolvency proceedings; and, increase creditors’ rights in insolvency proceedings, among other important measures in this area.

Medium to long-term reform recommendations:

2. Ensure that the new Bankruptcy Act Draft and/or amendments to the Companies Act of 2016 address the gaps identified in the current legislation. The current Bhutanese insolvency framework is regulated by the Bankruptcy Act of the Kingdom of Bhutan of 1999 and the Companies Act of 2016. It should be noted that the Bankruptcy Act was enacted in 1999, well before international standards crystallized into the World Bank Principles (2011) or the UNCITRAL Legislative Guide (2004). Because of this gap of several years, international standards could not be included in the bankruptcy act at the time it was enacted. Bhutan should consider conducting a timely review of the current corporate insolvency regime and work on fully aligning it with international standards. A number of technical reforms would be useful in this regard, including the following:

a. Introduce provisions allowing the continuation of contracts supplying essential goods and services to the debtor (goods and services necessary for the survival of the business) after commencement of insolvency procedures. Under the current insolvency regime in Bhutan there are no specific provisions that would allow the debtor to continue contracts essential to business survival. As a consequence, if the other contractual party requires to cancel the contract, there is nothing the debtor can do, even though the contract may make the difference between business survival and failure. Currently, the insolvency regime in Bhutan does not provide for the possibility to allow continuation of contracts as described. In most countries with best practices, the relevant provision will authorize the insolvency representative to confirm or disclaim contracts within a specific period of time depending on their usefulness to the business activity of the debtor. Continuation of contracts, where appropriate, can be necessary to achieve the maximization of the value of the debtor’s assets. Additionally, the law should provide that contracts cannot be terminated by the other party solely on the grounds of the debtor’s insolvency. In that sense, it is advisable to include explicit and direct provisions authorizing continuation of contracts after
commencement of insolvency proceedings (by either the debtor or the insolvency representative) if such contracts are for goods and services essential to the debtor’s business continuation.

b. Include explicit and direct provisions authorizing avoidance (invalidation) of undervalued transactions concluded before the commencement of insolvency proceedings. Allowing the avoidance (invalidation) of undervalued transactions, which were made as a gift or in exchange for less than equivalent value and which occurred when the debtor was insolvent or resulted in the debtor becoming insolvent, is of paramount importance because they prevent the debtor from distributing the assets that can otherwise be used to pay off the creditors or to preserve the business so that it can be sold as a going concern. There are no provisions under the Bankruptcy Act of 1999 allowing invalidation of undervalued transactions as described above. The Bankruptcy Act of 1999 allows avoidance of preferential transactions. The law should allow courts to invalidate both preferential and undervalued transactions on the request of the administrator or creditors. Usually there should be a time limit, meaning that only transactions that were concluded within a specific period prior to commencement of insolvency proceedings can be invalidated. This time period is called the suspect period and it can vary widely between countries, from several months to several years.

c. Establish the possibility for the insolvency representative to request new financing after commencement of insolvency proceedings and grant creditors who provide post-commencement financing with priority over claims of existing creditors. Availability of new funding is especially important in the period between commencement of proceedings and approval of the reorganization plan and should be specifically addressed by the insolvency framework. The insolvency framework should recognize the need for post-commencement financing, authorize its use and create priority of repayment for lenders who agree to supply such financing. Additionally, post-commencement creditors should rank above ordinary unsecured creditors. Regular post-commencement credit provisions should allow new loans with or without security.

d. Allow creditors to select or appoint an insolvency representative. Creditors are key participants of insolvency proceedings, because the maximized value of the assets is closely tied to the recovery of creditors, whether financial lenders, employees or trade creditors. Thus, it is key that creditors play an important role in insolvency proceedings, which requires specifying their powers, rights and liabilities. Because the insolvency representative’s fees are taken out of creditors’ returns, they are highly motivated to seek out a professional who is familiar with the nature of the debtor’s business, activities or type of assets, or who has special knowledge to handle the particular circumstances of the case. The risk that an insolvency practitioner might favor the creditor who nominated him or her can be mitigated by provisions that allow other creditors to move to replace the insolvency representative, for example at the first creditor’s meeting. Moreover, once a strong framework for regulating insolvency representatives is in place, an insolvency representative could be held accountable for his or her professional conduct. One approach is to allow creditors filing an application (and perhaps debtors, in the case of debtor-initiated proceedings) to appoint the company administrator or liquidator, as long as they meet all other legal requirements. Alternatively, the court could make the initial appointment as long as creditors are entitled to review the appointment within a reasonable amount of time, such as by the first creditors meeting.

e. Require the creditors’ approval for the sale of substantial assets of the debtor. The insolvency framework should incorporate a number of procedural safeguards to make sure that the procedures are fair, transparent, well publicized and that the manner of sale chosen maximizes the

119 Section 97 of the Bankruptcy Act of the Kingdom of Bhutan of 1999.
value for the estate. To that end, where a substantial part of the insolvency estate is to be sold, the insolvency framework should require the creditors’ approval. Best practices suggest that creditors should be allowed to challenge the sale of the assets (either with the insolvency representative or the court, as appropriate) if they disapprove, to ensure that their interests are also protected. In such a way the creditors will be able to require that the assets will be valued by neutral, independent professionals and that collusion between the debtor and prospective bidders will be discouraged.

f. Establish the right of individual creditors to request at any time information from the insolvency representative on the debtor's business and financial affairs. Best practices suggest that individual creditors should have the right to request information about the financial state of the debtor on a continuous basis throughout the insolvency proceedings without significant impediments. The most common way to gain access to such information is through a request to the insolvency representative who manages the business affairs of the debtor.

g. Provide for a trained, licensed and regulated cadre of insolvency professionals to advise courts, creditors, and debtors, and in the appropriate case, to oversee the conduct of collective insolvency proceedings. The law should also provide a clear statement of the powers and duties of such professionals. This can be supplemented with developing a profession of insolvency practitioner. It is essential to include provisions setting out clear rules for the qualifications, training, supervision, sanctions, and regulation of the creditors’ representatives. Such provisions would help establish a cadre of well-trained and qualified insolvency practitioners – which is crucial for increasing the number of companies that can be successfully reorganized and efficiently liquidated.

h. Introduce effective reorganization provisions in the corporate legal framework of Bhutan. Currently Bhutan does not have any rescue procedures aimed at rescuing insolvent companies. As it is evident that a reorganization procedure, although complex, has been intended to achieve specific purposes which are absolutely vital in the context of commerce and corporate sectors, the possibility of introducing similar concepts in Bhutan’s jurisdiction may be considered. Keeping viable businesses operating is among the most important goals of bankruptcy systems. A good insolvency regime should inhibit premature liquidation of sustainable businesses. Research has shown that insolvency reforms that implement reorganization reduce both failure rates among small and medium-size enterprises and the liquidation of profitable businesses. The purpose of an in-court reorganization procedure is that the financial well-being and viability of a debtor's business may be restored based on a reorganization plan, so that the business can continue to operate through means that may include debt forgiveness, debt rescheduling, debt equity conversions and sale of the business (or parts of it) as a going concern. Provisions governing the administration and management of reorganization procedures should focus on timeliness, efficiency and impartiality. It is important that the provisions governing reorganization include the following elements:

- The possibility for both the debtor and the creditors to initiate reorganization procedures and a concrete mechanism to commence reorganization proceedings, identifying parties who can apply for reorganization, establishing a procedure for submitting the application as well as the timing of the application;
- A mechanism to manage the property of the debtor while reorganization proceedings are ongoing, this usually involves appointment of an administrator or a manager to oversee the debtor’s assets and operation and a moratorium preventing creditors from enforcing their rights outside the reorganization process;

• Minimum standards for a reorganization plan, including its content and treatment of creditors;
• A mechanism for implementation of a reorganization plan and equity considerations for approval of a reorganization plan. In that sense, when voting rehabilitation plan, only creditors whose rights are affected by the plan should vote. The rights of certain secured creditors may be unaffected by a given reorganization plan. If that is the case, those creditors should not vote to approve the reorganization plan.
• Enable creditors to vote reorganization plan in classes and establish that creditors of the same class receive the same treatment under the reorganization plan. Good international practice recommends dividing creditors into classes and having each class vote separately to approve a rehabilitation plan. This approach helps in preparation of the reorganization (rescue) plan and ensure fair voting procedures.
• Based on the possibility that the majority of creditors can impose a plan on the dissenting minority, a generally accepted principle is that dissenting creditors must receive at least as much under the reorganization plan imposed on them as they would have received in liquidation proceedings.
• An element of restructuring. The debtor’s business undergoes a change based on the approved reorganization plan, whereby some restrictions are imposed on the debtor as to how its assets and business should be managed or structured until the debts are repaid in accordance with the plan.
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