

Initial Evaluation Note

Business License Simplification Municipality of Lima, Peru

IFC ADVISORY SERVICES IN LATIN AMERICA AND THE CARIBBEAN

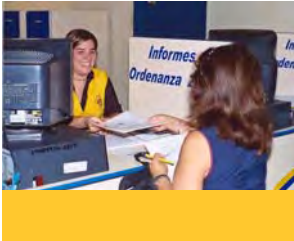


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I. Business Licensing Before the Reform

In 2005, Peru had some of the most burdensome administrative procedures for starting a formal business (ranked 106 among 155 countries)¹. Although the municipal government was tied to only three of the ten procedures, it accounted for most (60%) of the time spent in the licensing process.²

For that reason, the International Finance Corporation (IFC) and Foreign Investment Advisory Services (FIAS) decided to work with the Municipality of Lima to reform the administrative process for obtaining a business license in *Cercado de Lima*,³ which is one of 44 districts that comprise metropolitan Lima. According to the Municipality, 64% of the businesses in this district lacked a business license in 2005, and most of them were micro enterprises.⁴

Compared with the other districts prior to the reform, *Cercado de Lima* had one of the most costly (US\$170) and complex licensing procedures, due to insufficient inter-agency coordination that resulted in extensive paperwork and superfluous requirements, complicating the application process for entrepreneurs. In 2004, the Municipality of Lima and FIAS conducted a study that identified municipal bureaucracy as the primary obstacle to the formalization of small and medium enterprises (SMEs).⁵ In the four years preceding the reform, the average dropout rate for the licensing process was around 70%, indicating significant obstacles to formalization. The district had records for 13,948 business licenses, but cadastral survey records

¹ According to DB 2006, starting a business in Peru in 2005 involved 102 days, ten steps and a cost of 38% of the GDP per capita.

² This calculation includes zoning and inspection procedures; the latter are administered by the National Institute of Civil Defense (INDECI).

³ *Cercado de Lima* is Lima's historic center with an estimated population of 289,855 (2005 census; www.inei.gob.pe). Unlike other districts in the Lima Metropolitan Area, this district has a special importance as the provincial capital.

⁴ Source: Municipality of Lima, 2005.

⁵ Evaluation of Business License Simplification in Lima, Peru – MIT Poverty Action Lab, p.5.

identified more than 50,000 sites pursuing economic activities. This discrepancy suggests that about three-quarters of businesses in the district were operating without a municipal business license.

II. The Reform and the Initial Benefit/Cost Analysis

All planning and preparation for the reform took place in 2005, and the reform was implemented in January 2006. The objective was to reduce the transaction costs for starting a business by decreasing the time, requirements and cost associated with obtaining a business license. Obtaining a business license before the reform required, on average, 60 days, 11 visits to municipal government offices, and five separate inspections.

The reform focused on the municipal procedures to obtain three documents: the certificate of compatibility (zoning), technical clearance (the inspection), and the business license. Regarding inspections, it is important to note that the reform addressed tasks that are partially the responsibility of the Municipal Institute for Civil Defense (INDECI), which deals with low-risk businesses with facilities that are less than 100 m² (i.e., Groups 1 and 2; see footnote 10 for the definition of these groups). Having INDECI intervene in specific cases improved the efficiency of the licensing process. A decree promulgated in 2007 granted power for the national INDECI office to intervene in exceptional cases falling under Groups 1 and 2. For example, if a small, low-risk business is close to a school, church, or government office, the national INDECI office must inspect it and decide whether to approve the business license. In the post-reform period, inspections for Groups 1 and 2 should take place after the license has been issued, but currently the national office of INDECI has special authorization to conduct ex-ante inspections. The significant and burdensome role of the national INDECI office has led to current discussions about reforming this agency's role in the licensing process, too.

Given the paucity of available data, IFC estimated the initial benefit/costs analysis (BCA) one year into the implementation of the reform. It was calculated for a five-year period using an annual discount rate of 10%.

The BCA considered two benefits: (i) the reduction in the cost (fee) of obtaining a license and (ii) the

reduction in the amount of the entrepreneurs' time required to obtain a license, which is the sum of the total number of days and the number of visits to municipal government offices. The reform was expected to reduce the number of days by 50% (from 60 to 30) and the number of visits to municipal government offices by 40% (from 11 to 7).

To assign a dollar figure to the reduction in the amount of time required, the analysis multiplied the decrease in the number of days by the minimum daily salary determined by the government and a factor of 0.2⁶. To assign a dollar figure to reduction in the time spent visiting municipal government offices, the decrease in the number of visits is multiplied by the minimum daily salary and a factor 0.5⁷. The reduction in the cost (fee) was added to these two results to yield a dollar figure for the total benefits accruing to the entrepreneur. The analysis considered the project cost to be equal to the overall investment of US\$207,718 (i.e., total costs,⁸ including funds spent by IFC and donor and client contributions).

The BCA also assumed that the number of licenses would increase by 20% in the first year after the reform, decline by 10% in the second year, and level off in the third year and beyond.⁹ In retrospect, those assumptions were very conservative.

The project's net present value (NPV) was estimated at US\$1.26 million, equivalent to an internal rate of return (IRR) of 166% and a benefit/cost ratio of 7.0, as summarized below.

Year	0	2006	2007	2008	2009	2010	NPV
Benefits (Reduction in Price and Time)		325,606	374,426	397,574	417,452	438,325	1,461,442
Costs	207,718	0	0	0	0	0	207,718
Benefits-Cost	-207,718	325,606	374,426	397,574	417,452	438,325	1,253,724
IRR	166.3%						
B/C	7.0						

Baseline year 2005 = 1,711 new licenses
 Cost or investment = US\$207,718
 Source of basic data: Municipality of Lima

⁶ The BCA assumed that an entrepreneur would spend 20% of his/her time in the process of obtaining a license.
⁷ The BCA assumed that an entrepreneur would spend 50% of his/her day in the process of obtaining a license.
⁸ Costs include staff, travel, consultants, and an 18% IFC overhead rate, but do not include in-kind contributions.
⁹ Based on the results of a previous IFC reform in La Paz, Bolivia.

III. Project Results and Ex-Post Benefit/Cost Analysis

The reform yielded the following results:

Indicators (I)	BEFORE THE REFORM 2005	AFTER THE REFORM		
		2006	2007	2008
Outcome Indicators:				
Time (days)	60	5	10	5
Visits	11	2	2	2
Official cost/fee (US\$)	170	45	52	52
No. of requirements	33	4	4	4
No. of licenses issued	1,711	8,457	4,171	1,978
Impact indicator:				
Aggregate savings for the entrepreneurs (US\$)	-	1,738,759	801,103	415,050

(i) Source: Municipality of Lima, official records, January 2009.

1. Time¹⁰ and Visits to Municipal Government Offices

The increase in the number of days from 2006 to 2007 (see table above) was mainly due to a 2007 INDECI decree and a reduction in personnel¹¹ that affected the efficiency of the process. According to the decree, a business categorized as being low risk but operating in a high-risk area is automatically considered a high-risk business by INDECI and must undergo a detailed inspection that can last up to 45 days. In 2008, the number of personnel increased somewhat and significant improvements were made in the Municipality's information system (SISLIC).

The number of visits to municipal government offices was reduced from 11 to only two, and that reduction has been maintained to date.

¹⁰ The time indicator (days) is the weighted average for the four business categories: Group 1 (general economic activities in facilities smaller than 100 m² that do not involve the production of goods), Group 2 (activities involving the preparation and sale of food and drinks), Group 3 (general services and economic activities that involve some risks not included in Group 4), and Group 4 (manufacturing and economic activities involving hazardous products). In the post-reform period, a business in Groups 1 or 2 (collectively representing 80% of businesses) can obtain a license in as little as four hours or up to one day, whereas a business in Groups 3 or 4 needs 10-15 days, due to ex-ante inspections.

¹¹ This occurred in the Municipality's Civil Defense and the Licensing Division, due to the enactment of Business License Framework No. 28976 and the more stringent demands of a new decree (D.S.N. 066-2007-PCM) issued by INDECI.



2. Licensing Requirements

The reform reduced the number of requirements in the licensing process from 33 to four. However, subsequent work has shown that some informal entrepreneurs perceive an increase in the number of requirements, due to confusion surrounding the requirements for obtaining a business license versus those for sector-specific approvals, as explained by Maria Teresa Portal, manager of the customer service department for the Municipality of Lima in November 2008. National agencies have established specific, nationwide requirements for these sector-specific approvals. Depending on the sector (natural resources, heavy industry, etc.) approval is a prerequisite for obtaining the operational license. These requirements apply only to firms that operate in specific sectors, and they cannot be modified at a sub-national level by the municipalities. Only the national authorities responsible for each sector have the power to modify the requirements.

3. Official Cost of a License

Before the reform, the central government set an upper limit on the fee that municipalities could collect for licenses¹². Under the reform, the license fee was set at the real cost incurred by the Municipality. The previously fixed fee of US\$170 has become four different fees, depending on which business group is involved.¹³ For example, a low-risk business pays a lower fee.

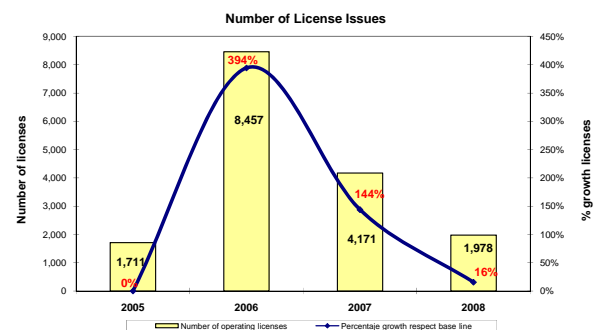
In 2006, the weighted average official cost had been reduced to US\$45. Because this fee is tied to the inflation-indexed monetary value (UIT; see footnote 12), the fee undergoes are slight nominal adjustments, but no real increases. The failure to communicate this properly to the beneficiaries has resulted in confusion and false perceptions.

¹² This value was calculated at 10% of the *Unidad Impositiva Tributaria* (UIT), which is a value used to calculate administrative fees.

¹³ As part of the reform, businesses were classified in one of four groups according to the nature of the business activity and the level of risk involved; see footnote 10.

4. Number of Licenses Issued

In 2006, the number of licenses issued increased by 394%, primarily as a result of the fee reduction and a more streamlined process. In 2007, this number declined and was “only” 144% greater than the number of licenses issued in 2005. This relatively lower increase was partially due to the enactment of Business License Framework No. 28976 in August 2007, which eliminated the need for provisional permits and permits for businesses located in shopping centers.¹⁴ Of the 8,457 licenses issued in 2006, 5,393 were provisional. In 2007, the number of licenses issued included only permanent licenses. In 2008, the number of licenses issued decreased to 1,978. This decrease is attributed primarily to: (i) the transition in the Directing Manager position in the Municipality’s Business License Office, which was expected to have a temporary effect on performance, and (ii) enforcement of the decree requiring the national INDECI office to intervene in exceptional cases as described in section II.



This trend is expected in cases such as that of the Municipality of Lima, where licenses are permanent and do not have to be renewed annually. If licenses had to be renewed annually, a sustainable reform would result in an upward trend, with a larger number of licenses being renewed or issued with each passing year. In the three years after the reform, 14,606 licenses were granted; this was more than the 13,948 licenses granted prior to the reform. Of the approximately 36,000 businesses that lacked a license before the

¹⁴ This law permits a single corporate license for a shopping center instead of requiring individual licenses for each business located therein, and it eliminates provisional permits.

reform (see section I), approximately 40% now have a license.

Businesses constantly enter and exit the market, so the total number of businesses fluctuates and is not limited to the estimated 50,000 businesses in *Cercado de Lima*. In addition, not all businesses want to obtain a license, as will be shown in section V.2. Purchasing the *Certificado de Aptitud de Establecimiento* (CAE) (Business Aptitude/Eligibility Certificate) is the first step in the licensing process. Considering that 3,916 and 3,668 copies were purchased in 2004 and 2005, respectively,¹⁵ there may be annual demand for about 3,800 licenses, *ceteris paribus*. In those same years, only 1,343 and 1,398 applications were actually filled out, implying that issuing approximately 1,350 licenses could maintain the total number of businesses. Ideally, with the reform, the number of licenses issued will exceed that number to the greatest extent possible.

5. Cost Savings for the Entrepreneur

Savings estimates come from primarily two sources. First, the reduction in time is estimated to have saved US\$0.69 million in 2006, US\$0.37 million in 2007, and US\$0.17 million in 2008 (*savings from reduction in time US\$ * number of licenses*). Second, the decrease in the fee from US\$170 to a weighted average of US\$45 represented additional savings of US\$1.06 million in 2006, US\$0.49 million in 2007, and US\$0.23 million in 2008 (*reduction in fee * number of licenses*). Thus, the total savings for informal entrepreneurs who obtained a license were US\$1.74 million in 2006, US\$0.86 million in 2007, and US\$0.42 million in 2008.

6. Ex-Post Benefit/Cost Analysis

Based on the Municipality's official data through December 2008, the project's NPV is estimated at US\$2.98 million, which is equivalent to an IRR of 786.7% over a five-year period. This represents a B/C ratio of 13.9.

Year	2005	2006	2007	2008	2009	2010	NPV
Benefits (Reduction in Price and Time)		0 1,738,759	861,103	415,050	435,803	457,593	2,896,324
Costs/Investment	207,718	0	0	0	0	0	207,718
Benefit-Cost	-207,718	1,738,759	861,103	415,050	435,803	457,593	2,978,249
IRR	786.7%						
B/C	13.9						

Additional assumptions: The expected annual growth rate between 2008 and 2010 of the number of licenses issued is 5%.

Source: Municipality of Lima

The estimated cost savings and the ex-post BCA strongly suggest that the reform yielded economic benefits for the entrepreneurs. Presumably, having a successful business improves their welfare and that of their families.

IV. Lessons Learned from the Reform

Based on the previous findings and an evaluation of business license simplification project carried out in 2007 by the MIT Poverty Action Lab,¹⁶ the following lessons should be considered in designing future reforms.

- The project clearly defined the scope of the reform, but the importance of national or "horizontal" procedures and requirements under the control of other government authorities must not be underestimated.
- Follow-up is critical to the sustainability of the reform, even after the project has been completed. For example, in October 2008, the LAC M&E and BEE teams organized a workshop to discuss the preliminary results of the baseline of an impact evaluation (see section V) with municipal authorities.
- Key data, such as the number of licenses issued, must be tracked to assess the reform's performance and sustainability and to continue learning, enhancing and improving this and other similar reforms.
- To avoid confusion and manage expectations, up-to-date information about the reform must be

¹⁵ Evaluation of Business Licensing Simplification in Lima, Peru, MIT 2007, pg. 12.

¹⁶ Evaluation of Business License Simplification in Lima, Peru, MIT Poverty Action Lab, 2007.



communicated to informal entrepreneurs more effectively and accurately on an ongoing basis.

V. So What? An Impact Evaluation of the Reform

The aforementioned 2007 MIT study assessed the outcome and “impact” achievements of the IFC reform project. It validated the performance of the project and provided useful insights before and after the reform.

Under the direction of the Business Regulation Evaluation Group (BREG)¹⁷, IFC decided to implement a three-year experimental evaluation to measure the impact of having a business license in terms of greater SME economic activity, greater access to credit, and other considerations. Although this impact evaluation was designed in September 2007, the first survey and information-gathering took place between the second and third years (July 2008) after implementation of the reform in the Municipality of Lima. As stated in section III.4, almost 8,500 licenses were issued after the reform in 2006 and more than 4,000 were issued in 2007.

Clearly, this evaluation missed the approximately 12,500 SMEs that obtained their license before the baseline survey was conducted. Therefore, this evaluation cannot and will not measure the impact of the reform itself (i.e., its impact in terms of improved economic activity, access to credit, and other considerations). It could be argued that the most entrepreneurial businesses – the “gazelles” – obtained their licenses soon after the reform and no longer are within the scope of this study. The evaluation may be capturing only those businesses that were not very interested in getting their license – the “slugs”. On the other hand, if business entry and exit to the sector is dynamic, the evaluation may be capturing new “gazelles” as well, but in a more “steady state” of the reform.

1. Objective

The objective of this evaluation, henceforth referred to as the Lima Tracer, is to analyze (i) the impact of possessing a business license on the businesses’ performance as measured by

¹⁷ BREG is a network of international cooperation and development organizations working together to evaluate projects related to administrative simplification and business regulation in Latin America. Its members include CAF, CIDA, CIDES/IDRC, DFID, FUNDES, IDB/FOMIN, IFC and SECO.

productivity, employment, profitability, access to credit, and other factors, (ii) the institutional factors that affect SMEs’ improved economic activities, and (iii) the perceived negative and positive incentives for obtaining a business license.

2. Methodology: *Encouragement Approach*

Although the scope of the reform included informal businesses in all four groups, the evaluation focused on businesses in Groups 1 and 2 (see footnote 10), since they represent the majority (approximately 80%) of businesses operating in *Cercado de Lima*.

The evaluation is based on a randomly selected sample of businesses in *Cercado de Lima* that do (treatment group) and do not (control group) have a business license. Their performance was measured twice a year for three years (six rounds) in order to infer the impact and benefits of obtaining a business license.

The study began by conducting a baseline (BL) study of informal businesses, or businesses without a business license, in areas identified by the Municipality as having many informal businesses. The BL study was based on a sample of 600 informal businesses, but we do not know whether it is truly representative of all non-licensed enterprises¹⁸. However, given the sample size, the evaluation can provide statistically valid results with an attrition rate of up to two-thirds (400 businesses). In other words, if the last round has a sample of at least 200 businesses (100 in the treatment group and 100 in the control group), the evaluation can statistically identify the 10% effect. Any change of less than 10% in the value of a variable will not be captured with this sample size.

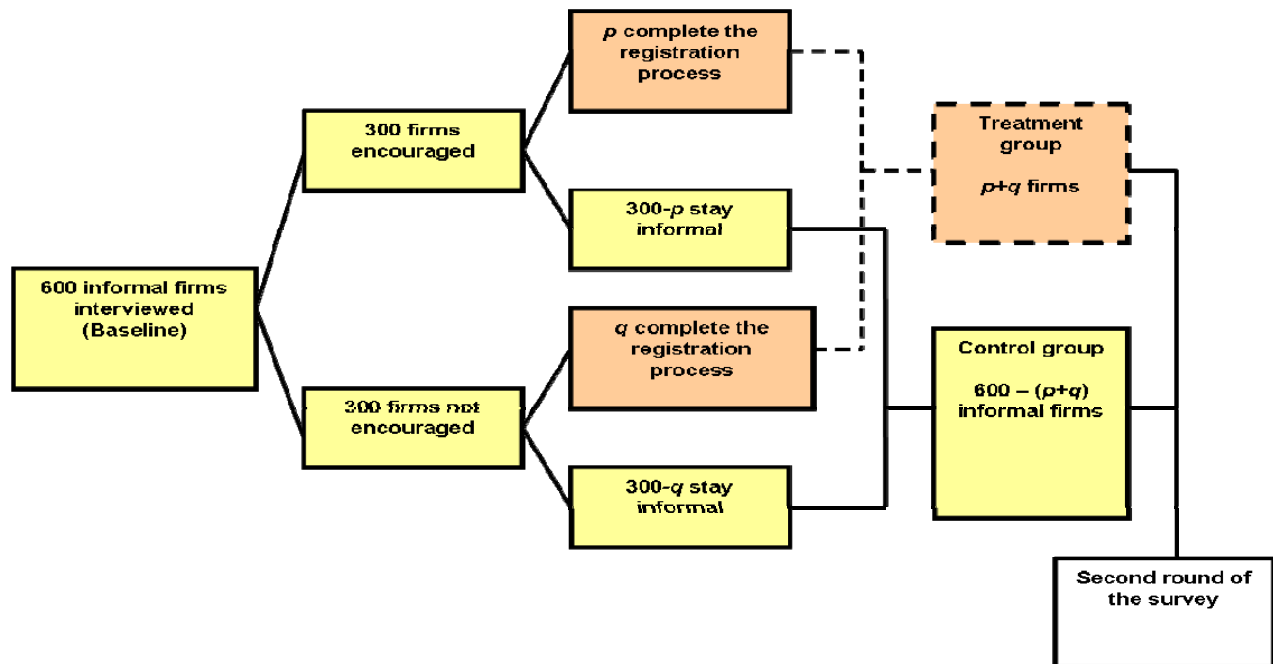
After the baseline study was completed, the evaluation had to overcome the selection bias in creating treatment and control groups for the study. Therefore, an incentive was given randomly to half of the BL sample of informal businesses (300 businesses). For this study, the incentive was a monetary voucher partially covering the fee

¹⁸ The Municipality of Lima did not have systematic, reliable records of the number and location of informal businesses.

for obtaining a business license. Random selection ensured that the treatment group was representative of all the businesses being studied (i.e., companies that had a relatively high or low inclination to obtain a business license). Thus, after receiving the incentive, the treatment group

should be similar to the control group (companies that lack a business license).

The following figure illustrates the design of the incentive.



• **The Encouragement Approach in Practice**

The initial incentive was a monetary voucher (40 Peruvian soles) to help pay for the license. It was equivalent to 1-14% of the total cost of the license, depending on the type of business. Of the 300 businesses that were randomly selected to receive the voucher, 60 (20%) were very interested, 127 (42%) were somewhat interested, and 113 (38%) were not interested in using the voucher. Only 23 businesses used the 40-sole voucher to complete the registration process and obtain the license.

To try to generate more positive responses, the voucher amount was increased to 80 soles for businesses that had showed interest in the first voucher and 100 soles for businesses that had showed no interest in the first voucher. These

monetary incentives represented 21-35% of the cost of getting a license. Ten new licenses were obtained. It is important to note that in 39 cases the offered voucher would have covered the total cost of obtaining the business license, yet 23 of those businesses did not act on the incentive.

A number of businesses with a “positive” profile were offered assistance in gathering the necessary documentation and accompanying the entrepreneur to the municipal government offices to apply for the license. An additional 35 licenses were obtained.

In total, 68 businesses used the voucher and obtained a license; 27 (9%) additional businesses that received the incentive did not use the voucher, but completed the registration process on their own. Therefore, of the 300 businesses that received the incentive, 95 completed the registration process.



Business License Simplification - Municipality of Lima, Peru

Although the number of businesses with licenses is less than ideal, it is sufficiently large to permit valid statistical inferences.

Finally, it is important to note that the 9% of businesses (27 out of 300) that received the voucher and obtained a business license without using it could be the new “gazelles”. This would imply that these SMEs have higher entrepreneurial tendencies than their counterparts do.

• **Lessons Learned from the Encouragement Approach**

- Informal businesses that do not perceive the advantage of the reform assign a very low importance to having a business license. The Municipality’s enforcement of the regulations seems to be ineffective, and businesses apparently do not anticipate receiving benefits from having a license.
 - Safety and health regulations usually require modifying buildings’ physical infrastructure, such as bathrooms and emergency exits. Some businesses are not willing to make the additional investments needed to comply with these regulations.
 - The municipal officers who are responsible for accepting and evaluating license applications have significant discretion in issuing or denying licenses. The information provided about zoning rules changed from one visit to the next, and some businesses were asked to meet additional requirements.
 - Personal assistance may be a more effective incentive than monetary vouchers, particularly if the fee for obtaining a license is relatively low.
- Size: A typical business has one or two workers in a small store area (30 m² on average), was opened quite recently (2.6 years ago, on average), is run by an entrepreneur with only three years of experience, and operates in a rented facility.
 - Credit: A typical business is unlikely to request formal credit, but larger and more experienced businesses that request credit are likely to obtain it. Credit from the informal sector is more common and more likely to be granted.
 - Profitability: Profits vary widely with the characteristics of the business. Businesses that have been operating for more than one year have higher revenues than younger businesses, as do those with three or more workers and those in Group 2. These differences in profitability are not necessarily due to lower total costs. In the sample, average monthly costs are US\$1,195 and average monthly revenues are US\$1,700.
 - Wages: The average monthly wage for a full-time worker is between US\$172 and US\$199. The average monthly wage for a part-time worker is US\$122. These figures are higher than the average wage (US\$110²⁰) for a micro-entrepreneur and also very close to the minimum wage (US\$178).
 - Investment: In the six months preceding the survey, 23% of the businesses had invested in equipment and 19% had invested in physical infrastructure. Businesses that had been operating for one year or less, had three or more workers, and were classified in Group 2 had invested more in equipment and physical infrastructure, averaging US\$1,444 and US\$538, respectively.

3. **Baseline Characteristics**¹⁹

The baseline survey was conducted during April and May of 2008, with 604 completed surveys. Informal businesses in Groups 1 and 2 operating in the streets of *Cercado de Lima* (not in shopping centers) were characterized as follows:

Entrepreneurs’ perceptions of the reform are as follows:

¹⁹ All results reflect a 95% confidence level.

²⁰ Peruvian Household Survey, Encuesta Nacional de Hogares (ENAHOG) 2007.

- Forty-five percent of the survey respondents indicated that their primary reason for not getting a license was that *“the process is lengthy and tedious.”* This is surprising, since the reform aimed to tackle precisely those issues. One possible explanation for this is that the respondents may not have had complete or accurate information and this has been identified as one of the lessons learned from the reform (see section IV).
- Thirty-six percent of the survey respondents indicated that *“the license is very expensive.”* As explained earlier, the fees vary depending on the businesses’ size and risk. The cost for a business in Group 1 is US\$79 (US\$50 for the license, plus US\$29 for INDECI for businesses of up to 50 m²). The cost for a business in Group 2 is US\$130 (US\$89 for the license, plus US\$41 for INDECI for businesses between 51 m² and 100 m²).
- Thirty-two percent of the survey respondents indicated that they didn’t obtain a license because *“my business is new, so I have not had time to get the license.”*
- Sixty-three percent of the survey respondents indicated that they perceive “no advantage” in having a license. On the other hand, 68% believe that the main disadvantage of not having a license is the *“risk of paying fines”* and 36% believe it is the *“risk of paying bribes.”*

4. Preliminary Hypothesis

Having a business license does not have a statistically significant impact on the economic activity of the SME groups under study, as long as the informal entrepreneurs do not perceive predictable benefits.

Licenses are a form of government regulation that generally is justified on the grounds of addressing market failures that generate inefficiencies and inhibit economic growth. The authority, in this case the municipal government, seeks order and regulates the provision of services to the community. Using this rationale, municipal authorities establish

zoning regulations that contribute to orderly urban development. Municipal authorities have the power to impose sanctions, such as fines or mandatory business closure, to enforce these regulations.

The administrative simplification projects aim to facilitate licensing processes that entail transaction costs that are usually financial. These reforms are seldom complemented with tangible benefits. It is only assumed that a business license will facilitate business activity, and that is precisely what this evaluation tries to demonstrate. Thus, if informal entrepreneurs perceive and receive benefits that are higher than the costs (B>C), then in theory they will be readily willing to obtain a license.

Entrepreneurs may have positive or negative incentives for complying. Positive incentives arise if the license is an instrument for obtaining a tangible benefit. Negative incentives arise if the entrepreneurs want to avoid actual or potential detrimental effects on their business or economic wellbeing, such as having to pay fines.

As stated in the previous section, the majority (63%) of the survey respondents indicate that *“there is no advantage”* in obtaining a business license. This means that they perceive no benefit from obtaining a license. If this is the case, then the cost of the license will always be greater than the benefit (C>B). When asked which factors at the municipal level would influence business expansion, 67% indicated simplification of the process for obtaining a business license. Institutional factors under the control of the central government, such as lower taxes, and macroeconomic factors, such as economic growth, are also perceived as being influential. Nevertheless, the reported perceived lack of benefits is supported by the fact that even though the incentive approach offered to pay 100% of the cost of the license for 39 small entrepreneurs, only 16 of them accepted the offer.

Furthermore, 12% of the respondents indicated that *“the main advantage of obtaining the license is to avoid paying fines and bribes.”* Sixty-eight percent indicated that the *“risk of paying fines”* was the primary disadvantage of not having a business license. These are negative incentives and it remains to be seen whether the benefit (not paying



finer and bribes) is greater than the cost of getting the license and complying with the regulation. If the benefit is lower than the cost, entrepreneurs will not get the license ($B < C$). There is also the possibility that if the enforcement of licensing regulations is very effective, the negative incentives may become higher, along with the benefits of avoiding fines and bribes.

The magnitude of the benefits may be related to the size of the business. Relatively large businesses that obtain a license may have a higher probability of reaping the expected benefits (e.g., increased access to credit, better possibilities of serving as suppliers to larger companies), and thus these benefits could be greater than the costs. Since this analysis studied businesses in Groups 1 and 2 that have an average of only 1.4 and 2.1 employees, respectively, the benefits of having a license may not be greater than the costs.

VI. Conclusions

1. To date, the project's performance has been satisfactory. The results of the reform show that obtaining a license has become less expensive and less burdensome, and the number of businesses that lack licenses has decreased by about 40% over three years. Furthermore, the BCA demonstrates considerable net benefits accruing to both the SMEs and the Municipality of Lima. However, continued close monitoring is still needed to assess the sustainability of the reform.
2. The Lima Tracer clearly will not capture the impact of the reform in its entirety, since 12,500 "gazelles" were missed in the baseline survey and thus are outside the scope of the evaluation. IFC and BREG are considering a qualitative survey of a sample of those businesses to determine whether the business license has helped them obtain credit, expand their economic activity, or reap other benefits. IFC and BREG will conduct a more in-depth analysis of the database for the MIT Study, which took place after the reform was implemented, to determine the feasibility of a simple before-and-after evaluation. Finally, the database for the incentive approach will be analyzed in greater detail to attempt to determine whether there is a significant relationship between the age of a business and its predisposition to obtain a business license.
3. So far, the evaluation seems to suggest that SMEs in Groups 1 and 2 do not perceive predictable benefits that are greater than the financial and other transaction costs of obtaining a license.
4. A more integrated approach that considers reforming the licensing process at the sector and national levels may be necessary in order to minimize the costs and help the entrepreneurs perceive a significant advantage in obtaining a license.
5. Finally, even when the costs to obtain a license are close to zero (there is no fee to obtain the license and the bureaucratic procedures are performed at the business's location), the actual costs of improved safety, security, and other measures may be significantly higher than the perceived benefits. In addition to these costs, there may be negative incentives, such as being registered with the municipality for taxes and other purposes, which may inhibit SMEs from obtaining a business license. Strict law enforcement may be the only way to make SMEs obtain a business license with the risk of having social unrest in the sector.

